GENERAL AGREEMENT ON TARIFFS AND TRADE

Working Party on Border Tax Adjustments

SUBMISSION BY THE EUROPEAN COMMUNITIES

RESTRICTED
Spec(69)89
1 July 1969

Original: English/French
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I. Border Adjustment of Indirect Taxes

1. The grounds for offsetting indirect taxes at frontiers

The most important taxes referred to in this chapter are selective taxes on certain products (droits d'accise) and the general taxes, such as sales taxes and turnover taxes, which affect all or at least most products.

The common feature of these two kinds of tax is their identity of purpose, namely taxation of the expenditure of final consumers, i.e. usually of households. The economic aim of these taxes is to enable the State to tap the resources of the nation at the stage of and in proportion to consumption—a procedure which results in restricting the purchasing power of households. In laying down the methods of levying these taxes, the legislator is really seeking to ensure that the actual burden will be borne by the final consumer and will fall entirely on him.

Thus, the point at which these taxes are levied is determined according to the principle of taxation in the country of destination, in other words of consumption, for it would appear to be contrary to international rules on the delimitation of fiscal sovereignty that, by taxing consumption, a State should affect the purchasing power of nationals of other States.

As for the effects of this principle, special attention should be drawn to the fact that, since it is domestic consumption which is subject to indirect taxes, these must be levied on all commodities no matter whether their origin is domestic or foreign. Consequently, taxation on the import of goods of a type not produced within a country is also justified. For the same reason, exports must be exempt from taxation and any taxes already paid must be refunded. This tax relief on exports is moreover necessary to avoid double taxation in countries which also levy an indirect tax.

In addition, the adjustment of taxes on imports ensures economic balance on the competitive plane, since foreign and domestic products are treated equally; there is therefore no need to treat it as a non-tariff barrier.

The reasons set out above for applying the destination principle to these taxes mean conversely that the goods should not be taxed under the legislation applicable in the country of origin, that is, where they are produced. If this were done, it would not be possible to delimit the tax sovereignty of the
two States, to avoid double taxation (in practice) and so to avoid distortion of competition between States.

Studies of taxation practices in both GATT and OECD have shown that all countries arrange for these indirect taxes to be offset at some point, either by adjustment at the frontier when goods are imported or exported or else at a stage closer to the consumer or to those producing for export.

2. The passing on of indirect taxes in prices

The extent to which indirect taxes are effectively passed on forward in prices is a matter of controversy. There do not appear to be any writers who maintain that there is no passing on. Most of them seem to accept that any change in prices linked with a change in indirect taxes results from the interplay between the change in taxation and the earlier market situation. The passing on of the tax change may go beyond or fall short of the straight impact it should have; what in fact happens will depend on whether the economy, the industry concerned or the particular firm is expanding or contracting.

The practical conclusion to be drawn from this controversy is that normally the full tax is passed on. There may be exceptional cases and temporary situations in which the change in prices does not correspond to the full amount of the tax; but since, for better for worse, the tax will have been paid, it will be other price formation factors that have undergone compression. In other words, it will really be a case of price reduction and not of the seller deciding to bear the tax himself. It is always the consumer who pays the tax. Business circles themselves tend to confirm that passing on in full is the rule.

In practice, however, if allowance were to be made for the fact that the amount passed on in prices may sometimes be greater and sometimes smaller than it normally should be, it might be and sometimes is considered, that border adjustments for indirect taxes are justified only if and to the extent that these taxes are in fact passed on in the prices of goods and that the practical conclusions should be drawn from this argument.

The argument must, however, be rejected for the following reasons:

From the economic point of view it seems difficult to accept that, if the domestic producer were to bear part of the tax, the legislator should exempt the supplier in the other country from this same burden. A sound competition policy requires that starting conditions should be equal.
With regard to exports, it is difficult to understand why - assuming that, as an exception and contrary to the aim pursued, these taxes were not passed on to the domestic consumer - the legislator should at the export stage levy that part of the consumption tax which it had not been possible to pass on in prices at home. It is, incidentally, a moot point whether competitive conditions on the external market would be more favourable for, if it is conceded that the taxes are not fully passed on, this must also be conceded in relation to indirect taxes in the country of destination.

If it were desired to reduce border tax adjustments, by what practical method could an overall assessment (or - and this would be more justifiable in this hypothesis - an assessment for certain classes of products) be made of that part of the indirect tax burden which is not passed on?

From the point of view of general economic theory, it might be asked why, among all the many constituents of a cost price, the indirect tax should be singled out as the marginal element when the possibilities of passing on changes are considered.

Under the TVA system, moreover, the passing on of the tax in prices occurs in a special way. Here, as in many other respects, the effect of the TVA is no different from that of a sales tax levied solely at the retail stage (see section 3 below).

3. The mechanism of TVA and its effect on trade

TVA is an indirect tax which affects consumers' expenditure in just the same way as single phase taxes. It is a single ad valorem tax which, at the final stage of consumption, adds an identical charge to the price of products or services, whether of domestic or foreign origin and no matter what the method of manufacture (integrated or not), how long the distribution circuit or how often and at what rates taxes have been levied on the intermediate transactions.

The only essential difference between this tax and a sales tax levied solely at the final stage of the field of application of a TVA is one of method, TVA being paid step by step at every stage through which the product or the service passes. Nevertheless, the total TVA paid at a certain stage may be deducted or reimbursed at the following one. This is why the TVA is shown separately on the invoice so that the latter comprises the net price (without tax) and an amount of TVA which consists of a kind of transfer to the customer of a tax credit with the Exchequer. Thus, the TVA shown on the invoice is not an element of the cost price as long as the purchaser (who may be

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1 See the statement, made to the GATT Working Party, in document Spec(69)5 of 10 February 1969, page 33.
a producer, a dealer or a provider of services) is himself subject to TVA. Through this levying mechanism complete and precise "passing on" is ensured right to the final stage at which the goods or services are delivered to the ultimate consumer. It is only at this stage that the TVA is incorporated in the price. However, as the amount of TVA due at the final stage is known exactly, this transparency of taxation again works in favour of full passing on, just as with a single phase tax.

With regard to imports, a distinction should be drawn between imports by parties not subject to TVA (usually private persons and certain State organizations not engaged in commercial or industrial activity) and those subject to TVA (usually producers, dealers and persons supplying services):

(a) **Imports by parties not subject to TVA**

Where an item is imported by a party not subject to TVA - this will of course be only a minority of cases - the levying of tax at the frontier constitutes a real and final adjustment. The tax is applied to imports in just the same way as to similar supplies furnished from within the country (the same rate is applied to the real purchase price). It should be observed that the domestic supplier may be at a disadvantage in cases where the deduction of TVA paid at previous stages is not complete. This may occur during the transitional periods which usually accompany introduction of the tax.

(b) **Imports by taxable parties**

In this case the tax levied at the frontier does not constitute the genuine and final adjustment, which occurs only at the final stage in the field where TVA is applicable. The whole point of taxing imports is to put foreign and domestic suppliers on an equal footing, since the TVA paid on imports, like that paid on home-produced goods, may be deducted at the end of the period specified for tax return purposes (usually at the end of the month).

Although the rate applied to imports is the same as that applied to similar products within the country, its level is hardly of concern to the importer because a higher or lower rate on goods imported is aligned on the level applying within the country at the next taxation stage. It follows from this that - provided the tax authorities possess adequate means of control - tax adjustment on imports would not even be indispensable. However, non-payment of TVA upon importation might, in certain cases, entail a financing advantage in relation to goods supplied from within the country.
As far as exports are concerned, the tax adjustment is not effected by means of a refund on the export as such. It is not in fact a matter of reimbursement on export grounds and, consequently, not of a refund due to the fact that a particular product is being exported, either. Under the TVA system, goods purchased or produced, no matter whether they are intended for export or sale on the domestic market, are in the enterprise without any TVA charge on them, since the TVA paid at the time of purchase has in principle been deducted or, as the case may be, refunded. If the goods are subsequently exported the tax adjustment is carried out simply by granting exemption. If, on the other hand, the goods are delivered to the domestic market, the TVA is again levied.

Thus there is complete and neutral remission of tax without any special reimbursement on export grounds.

The above description of the mechanism of the TVA system should elucidate the effects of this type of taxation on trade.

4. Conclusions

The various points concerning border adjustments for indirect taxes lead to the conclusion that there are very good grounds for the GATT rules which allow the burden of indirect taxes on products to be fully offset at the frontier in accordance with the rules and methods of the several States. Such action enables the differences in indirect taxes from country to country to be eliminated when the principle of taxation in the country of destination is consistently applied. The application of these rules makes it possible to balance the incidence of consumer taxation on domestic and foreign products, and world trade can thus develop untrammelled by distortions of competition due to indirect taxation.

While the TVA system, like the system of a single-stage sales tax, makes it possible for any tax levied to be offset in full and so to achieve balance from the angle of competition, this is practically ruled out with the system of multi-stage turnover taxes and with certain systems of droits d'accise. The recent report by the OECD Secretariat shows that in the States which apply the latter systems, there is more often than not a tendency to under-adjustment.

II. Direct Taxes

1. Grounds for not offsetting direct taxes at frontiers

The only direct taxes likely to be eligible for border adjustment would be those which actually fall on companies in particular those on profits and on company assets.
As taxes on profits are levied neither at the time of supply nor on the consumption of products, the legislator is not interested in the price, the origin or the destination of the products sold, but purely in the net profit which the producer or dealer has realized, no matter whether he operates entirely within the country or internationally. From the angle of these taxes, location is of significance only in relation to international law on double taxation. There is therefore no correlation between the field of application of the tax on profits and the circumstances in which goods traded on the international market are taxed.

This is even more true of the tax on assets. In view of their nature, it seems perfectly logical that the rules of international law in force should on principle confer no right to offset the burden of these taxes in the field of international trade.

Moreover, a system of this kind would run into almost insuperable difficulties. Whereas indirect taxes usually constitute fixed values corresponding to a certain percentage of the price of goods or to the other precisely determined criteria (weight, number, etc.) the direct tax burden is related to more or less variable parameters. The effect of these taxes will, owing to their very nature, differ from firm to firm; there may even be no tax at all when profits are nil or a loss has been sustained. Furthermore, the basis of assessment for taxes on profits is not fixed until after the operations in connexion with which action would be taken to offset the tax. It therefore appears to be impossible to offset them satisfactorily. There might even be reason to fear that the introduction of adjustments of this kind might disturb competition and international trade since they could not be carried out in proper fashion.

2. The passing on of direct taxes in prices

Studies on the possible effect on international trade of taxes which cannot be offset often attribute to them the same effect on costs and prices as to those which can be offset. However, as far as can be judged, this premise has no conclusive foundation. One may well wonder whether direct taxes, especially those that are levied on a firm's profits or assets, can normally and systematically be passed on in prices. As a rule - and the point is confirmed by industrialists - the market situation places on firms strict limits to what they can do in passing on the impact of these taxes.

3. Conclusions

If only for reasons of tax method, then, there can be no easy method of offsetting direct taxes at the frontier. Normally firms will not, because of their position on the market, try to pass on taxes levied on profits and assets in the form of higher prices, so there is no reason for including such taxes in border adjustments. It is even debatable whether the incidence of direct taxation is of any great importance. It would seem more important to know whether there are essential differences from one State to another in the taxes levied on profits and assets (see Chapter III).
III. The Effects Resulting from Differences in Tax Structures

1. The thesis of divergences in tax structures

After the conclusions drawn in Chapters I and II, an opinion should be given on a thesis frequently put forward in discussions on border tax adjustments, namely the "thesis of tax structures". This establishes a direct relationship between international competition and the structure of a country's tax revenue, and is based on the idea that countries where revenue from taxation comprises a relatively large proportion of taxes that can be offset (and a correspondingly small proportion of taxes that cannot) enjoy an advantage in international competition. The offsetting of taxes at the frontier would constantly induce a tendency to run surpluses in the balance of trade. On the other hand, countries with a high percentage of taxes that cannot be offset would, generally speaking, run a deficit on trade as a result of the offsetting from which their competitors benefited.

As can be seen, for example, from Table 12 of the OECD Secretariat's fact-finding report [C(68)47, 19 April 1968], the tax structures of the different countries show not inconsiderable disparities. In view of this, the thesis of tax structure warrants detailed examination.

This examination shows the thesis to be invalid for the following reasons:

2. The methodological errors of this thesis

(a) The fiscal structure thesis improperly mixes macro-economic and micro-economic factors. The ratio between taxes that cannot be offset and those which can is based on total values that are purely fiscal in origin. Such factors could not be indiscriminately brought into a discussion on international competition. Like competition on the domestic market, international competition is a micro-economic, not a macro-economic process. This requires that only appropriate micro-economic data should be used if a realistic analysis of the fiscal conditions of this process is to be obtained. An opinion concerning the effect of taxation on competition and international trade should not be based on aggregate figures of tax receipts; the only thing to do is to note and compare the fiscal data relevant to each particular case.

(b) Furthermore, the hypothesis in question is wrong in that it generalizes the economic effects of all classes of direct and all classes of indirect taxes. Of the various kinds of direct taxes, there are only a few which are likely to affect significantly the cost of sales prices of goods. For example, the following could hardly be included in this category: taxes on personal income and wealth, estate duty, etc. (cf. Chapter II, Section 1). As far as the indirect tax heading is concerned, it should also be observed that it covers taxes that differ widely in their influence on the conditions of competition in international trade.
It must therefore be recognized that the fiscal structure thesis lacks realism, if only in its methodological starting point.

(c) The fiscal structure thesis makes no allowance (and this is no doubt its principal defect) for the fact that, apart from simple differences between the taxation systems of the countries, a certain number of other factors make the ratio between receipts from taxes that can be offset and from those that cannot vary from one country to another. Only a few of these non-fiscal factors will be mentioned below.

(i) One is the economic structure of the countries, which is reflected in the relative importance of the various branches of activity in a national economy. The example of the industry/agriculture ratio in the various countries provides an illustration of the influence of this factor. In countries where industry makes the greater contribution to gross national product, incomes and capital are generally greater than in countries where greater contribution is made by agriculture. Given similarity of tax systems, the proportion of taxes that cannot be offset is in relatively more industrialized countries necessarily higher than in countries where agriculture plays a more important part in the national economy.

(ii) Furthermore, the country's standard of living has a considerable effect on the ratio between taxes that can and those that cannot be offset. It is well-known that income per head presents quite significant differences from one industrialized country to another. Given identical systems for taxing incomes and assets, the share of taxes that cannot be offset in total tax receipts will necessarily be higher in the "affluent" than in the "poorer" countries, since in the former the numbers liable to taxation is much greater.

(iii) Lastly, the structure of a country's tax receipts depends on the predominant form of the market, which determines how keen competition shall be. If, in a given country, the structure of the market tends towards the formation of oligopolies, enterprises in that country will, as experience shows, obtain higher revenues than those in countries where forms of markets have developed which are marked by keen competition or where there is permanent pressure on incomes. Given similar tax systems, the proportion of taxes that cannot be offset in countries with oligopolies (where incomes are fairly high) will be greater than in countries where competition cuts profit margins.
These factors, together with others of a non-fiscal nature, influence not only the structure of central government revenue from taxation, but also that of the various regions within a country. Thus, in regions which are highly industrialized and where levels of income and wealth are high, the proportion of taxes which cannot be offset is, as a general rule, considerably greater than in predominantly agricultural regions, where incomes and wealth are relatively modest. This factual situation - which at national level usually leads, for social and economic reasons, to a policy of financial equalization between regions - must of course also be taken into consideration when discussing revenue yields in the various countries.

The fiscal structure thesis is therefore based on fundamental data that leave completely out of account factors which, along with tax law, are the main factors determining the structure of national tax receipts. To this extent it is impossible not to criticize the thesis for a certain lack of profoundness.

3. Conclusions

The necessary inference from these considerations is that the fiscal structure thesis does not allow of any valid conclusion.

Briefly, the fact that the respective proportions in revenue yield from taxes which can be offset and from those which cannot differ from country to country does not justify conclusions being drawn, especially with regard to the effects on international trade of the current rules and practices governing border tax adjustment. More particularly, these disparities in the structure of receipts do not mean that countries where the tax yield consists of a relatively high share of taxes which cannot be offset are handicapped in international trade, whereas countries with a high share of taxes that can, have an advantage. To solve this problem another line needs to be followed.

IV. Real Effects of Border Tax Adjustment

1. The real effects on trade of present rules governing adjustment

In order to understand this subject it is necessary to grasp more closely than hitherto the economic reality of competition and trade between the various countries. It then becomes apparent that, apart from the special case of State trading, international trade is not the responsibility of the countries, but that the individual firms are the operators in economic transactions. Nor, then, is international competition to be looked on as competition between national economies, but as competition between firms and their products. In other words (as mentioned above in Chapter III, section 2) international competition can be understood and analyzed as a process at micro-economic level.
This is the economic fact which should be the starting point. It will be necessary to examine the conditions created by countries, through their tax systems, for the different enterprises and products when these enter the cycle of international competition. This is the only way to get a real insight into the tax problem raised and to try to give a satisfactory answer to the question of the effect these adjustments have on trade, a question asked in point 1(c) of the terms of reference of the GATT Working Party.

It should be added that this way of looking at the tax problems arising in international trade is not the result of recent observations. The notion that in international trade it is the tax conditions applicable to the various products which come into play in the border tax adjustment is already present in the General Agreement on Tariffs and Trade. Thus, under Articles III and XVI of GATT the prohibition of all tax discrimination with regard to imports and of all fiscal subsidies on exports is applied to the various products and precedence is thus given to the micro-economic view.

If the tax conditions under which competition and trade between States must be carried on are studied from this angle, taxes on the various products can as a start be left out of account. According to the provisions of GATT, these taxes can be offset and any differences in this respect between one country and another are consequently neutralized when the countries apply in a consistent manner the principle of taxation according to the legislation of the country of destination (cf. Chapter I, Section 5).

From this angle, the essential need is to know how international competition is affected by the GATT rule under which direct taxes - i.e. especially taxes levied on the incomes, wealth and other similar economic assets of firms - are not to be offset in international commodities trade.

If, for a moment, it is assumed that the enterprises located in a country where the pressure of these taxes is fairly heavy are consequently at a disadvantage in international competition compared with enterprises which in their own countries are subject to similar but lighter taxation, then it is essential, in order to appraise the position of such enterprises with regard to this point, to know whether, among the various Contracting Parties to the General Agreement, there are any considerable disparities in the burden of taxes on income and capital. Unfortunately, an answer to this question cannot be given for all GATT countries, for lack of the necessary documentation. According to the information available, a reply to this question can be given (again subject to certain provisos) only in respect of a few GATT countries in the "industrialized countries" category, but these account for the major part of the world's trading activity.
Various analyses of the taxation of joint-stock companies of these countries, as for example the study entitled "Report of the Committee on Turnover Taxation" made by British experts in 1964, show that, on the whole, the burden imposed on these firms by taxes that cannot be offset does not greatly vary among the principal trading powers. During recent years, taxation of joint-stock companies appears to have reached a level at which the differences in tax burden still existing among these countries are probably no longer great enough to influence capital movements.

Starting from the fact that there are no essential differences between the States in the tax burden falling on those companies which play the major rôle in international trade, it can be concluded that, whatever may be thought of passing on these taxes in prices, the elimination of border tax adjustments in this field cannot influence trade or be prejudicial to international competition.

If then, the theoretical arguments in favour of excluding direct taxes from adjustment at frontiers (see Chapter II) are left on one side and the situation as it is today is taken as a basis, it may well be concluded that the introduction of a special border adjustment system covering taxes on the capital and profits of enterprises would be inadvisable.

Nevertheless, when comparing the tax burden on the profits and capital of firms in the various countries, it should not be forgotten that certain particular differences may arise when a government resorts to special tax measures to attain specific short-term economic policy objectives. If, for example, in order to help its enterprises to overcome a cyclical crisis, a country adopts efficacious tax measures involving more rapid depreciation allowances or facilities for exceptional depreciation allowances, perhaps exceeding 100 per cent, these enterprises have, when they compete on the international market, a measure of advantage (due to the taxation system) over enterprises in countries not granting a similar tax concession. As a general rule, however, these fiscal privileges, and others of the same type which affect the taxation of enterprises, are granted only for a limited period. Usually, as soon as the economy enters a period of expansion, the States lose no time in withdrawing these concessions. This may also hold, by and large, for tax measures adopted by some countries for structural policy reasons. There remain, however, certain differences between the tax burdens on enterprises in the various countries, because the latter do not apply the same principles in determining the basis of assessment. In practice, it is probably impossible to rule out the possibility that certain differences may appear in the impact of those taxes for which no adjustment can be made.

2. The effects on trade of a change in adjustment

The special case of a change in border tax adjustments not accompanied by identical change in the rates of domestic taxation needs to be examined.
According to current international rules and practices, the principle of the country of destination is applied generally in all countries to indirect taxes on commodities. These taxes may therefore be offset either at frontiers or at a subsequent or prior stage and, as a general rule, this is in fact done in every country. In view of these universal rules and practices of international trade, any failure to offset such taxes in full at the frontier is, from the point of view of international competition, a competitive handicap for goods produced in the country concerned, as it puts domestic production at a disadvantage compared with international competitors: when action is taken to have the taxes offset in full, the handicap and the distortion are simply removed. The adjustment cannot therefore confer any right to a quid pro quo for goods from other countries.

Again, conversely, any excess in offsetting, such as inevitably occurs at times under a system of flat rate tax adjustments, gives rise to an unwarranted commercial advantage; normal competitive conditions can be established only where there is no such excess. Nor should the abolition of such excess entitle a country effecting it to any quid pro quo from other countries. The international rules treat excess offsetting as equivalent to the imposition of a customs duty on imports or a subsidy on exports.

Owing to the methods used to determine them, the tax adjustments made in certain countries which apply multi-stage systems do not always provide the complete offsetting of the turnover tax which is the aim of the adjustment system. It is not, therefore, improbable that the changeover from this tax system to a value added system (the most frequent case) might have a favourable effect on the trade balance, provided and to the extent that the new system eliminates the previous disadvantage suffered by domestic products.

It is, however, apparent that offsetting in the multi-stage tax systems is usually almost complete. Where there is a shortfall, it does not exceed one or two per cent, as the countries in question have usually not allowed any shortfall to assume significant proportions. This is true of the multi-stage systems of the EEC States. The commercial effect stemming from its elimination when the TVA system is adopted is therefore not very great, and when they occur may be, indeed frequently are, appreciably attenuated by transitional arrangements restricting the deductibility of taxes levied on stocks and earlier investments or fresh investments. Sometimes, too, there are tax residues under the TVA system, caused by limits placed - usually for budgetary or economic reasons - on the facilities available upstream for deduction of taxes, and these residues form a further obstacle, to full adjustment at the frontier. Furthermore, firms which benefited from too high a refund, owing to the application of the flat rates typical of the multi-stage tax system, lose their advantage. This very often happens with the products of highly integrated firms, a type which in many countries accounts for a large part of total exports.
In addition, a great deal depends on the impact which the adoption of TVA has on domestic prices (cf. section 2 above); for this is a very far-reaching tax reform which involves alteration of all rates and other tax procedures, its main purpose being to guarantee that tax revenue shall be at least equal to that obtained under the previous system; this changeover, in its turn, compels firms completely to revise the structure of all prices. In certain business situations, too, the change in method of taxation may be looked upon by firms as an opportunity to bring prices up-to-date by incorporating rising costs which they had not so far passed on in their prices. In this way the reform may intensify and accelerate an upward movement which was already affecting prices. Any favourable effect which the change in the tax system might in certain cases still have would be not merely wiped out by such an inflationary development, it might even be reversed.

Moreover, the possible impact of a change in the arrangements for border tax adjustments in international trade needs to be assessed in the light of the fact that the operation cannot be repeated, and that in addition it is just one of the constant and distinctly more significant changes which occur in the other factors which determine the terms of trade.

V. General Conclusions

In any realistic assessment of the present situation in the field of border tax adjustments it should be noted that no perfect fiscal balance between States exists or can be attained. This holds not only for taxation of a firm's earnings but also for taxes levied on goods.

The effects which the differences between one State and another in respect of these two classes of tax may have on international competition and trade should, in our opinion, not be over-estimated. Although from a strictly economic point of view these disparities might prevent international trade from reaching an optimum level, it should not be forgotten that, apart perhaps from a few isolated cases, these differences of fiscal origin are unlikely to give rise to more than very slight disturbances in international competition. In this connexion, it should be remembered that the economic ideal of absolute fiscal equality from the point of view of competition has not been achieved even in internal markets, in most of which special fiscal regulations of a local and regional character have produced certain differences in the taxation of goods and enterprises. Generally speaking, competition is nevertheless normal in these markets, as the differences are slight. This state of affairs, noted in practice, probably also holds good in international competition. The slight differences found between countries in those commodity taxes which cannot be offset and in the taxation of profits and capital of enterprises should hardly impair international competition. In our opinion, it is just this aspect of scale which deserves special attention when the effects which may be exerted by differences of a fiscal nature between States are being assessed.
From all the considerations set out in this paper it may be concluded that:

(i) The border adjustments to taxes on commodities which States make in accordance with GATT rules are justified. Although these adjustments are not always complete, the residual elements of taxation not subject to border adjustment are, on the whole, probably not large enough to prevent international trade from expanding under substantially fair conditions of competition.

(ii) There may, it is true, be certain differences between States as far as taxes on firms' profits and capital are concerned and in respect of which the GATT rules rightly do not allow any border tax adjustments. But here again those differences, as regards the industrialized countries, are not great enough to have a harmful effect on competition and international trade.

(iii) Consequently, the few disparities of a fiscal nature between States are unlikely to perturb international competition and to affect the development of trade balances in such a way as to warrant any change in the GATT rules on border tax adjustments.