encompasses all and several combinations of the possibilities shown in table 1. Consequently, in modern economies the instances of trade neutrality consistent with GATT assumptions constitute only a special rather than the general case.

Practical Issues

If the current system of border adjustments neutralizes tax effects on international trade in special cases only, how serious are trade diverting effects in the remaining instances?

Trade distorting effects of existing border adjustments probably have been largely compensated by past changes in relative rates of exchange, tariffs or price levels. But, under present conditions, exchange rate or tariff changes no longer are flexible instruments of adjustment to changes in competitive position among industrial countries. Consequently, possible trade distorting effects of new border adjustments now are of much greater concern than they were in the past, although even past changes—with the greater adjustment possibilities then available—probably have produced a world trade pattern rather different from that which would have come about under systems which truly neutralized the international trade effects of differential national tax systems.

To remedy the situation one could, first, consider fundamental changes in the basic system of border adjustments. These might range from elimination of the entire practice to a broadening of the practice to include various taxes now considered ineligible for adjustment. Complete elimination of current practices clearly is not a practical possibility, partly because adjustments to earlier trade distorting effects—such as may have occurred in relative rates of exchange for example—would need to be unwound. But more importantly, in the absence of border tax adjustments, countries with a high degree of trade involvement and a close tie to world prices would find forward shifting of indirect taxes (i.e., full reflection of the tax in export prices) virtually impossible. Thus their basic tax structure might have to be modified to the extent that it relied heavily on indirect taxation.

Inclusion of a broader range of taxes, such as the corporate profits tax and social security charges, would meet with considerable administrative problems. Even if the degree of shifting, which to complicate matters may actually vary from product to product and from country to country as well as over time, could be accurately determined, it would be virtually impossible to determine the precise amount of tax embodied in the price of a specific product. This problem is analogous to that encountered in rebating cumulative turnover—or so-called cascade—taxes, where "average" rates are being rebated, which leads to over- or under-rebating in individual instances and to distortions of the competitive position among individual firms. The elimination of this problem is one of the advantages cited in favor of the value-added tax system which is to replace the cascade type systems in Germany, Italy and the Benelux countries by 1970.

In any event, as shown in table 2, extension of border tax adjustments to virtually all types of taxes, except the personal income tax, would not redress the balance of competitive advantage in favor of countries, such as the United States, now having no or few border