Put another way, a value-added tax is carefully structured to pass the tax along in an accounting sense. Its effect on international trade, however, depends on whether the economic effects follow the accounting structure. If the tax is not fully shifted forward in an economic sense, then the international trade of the country using the tax will be favored regardless of the accounting structure.

It is not the levels of rebates per se and the differentials between them that measure the competitive effects of border tax adjustments. If Country A has a value-added tax of 10 percent and rebates to an exporter the total of the taxes, at a 10 percent level, that he has paid on his purchases it is because Country A does not want his tax costs, which are real, to enter into export prices. If Country B has no value-added tax or other sales tax, then there are in this respect no comparable tax costs to rebate to its exporters. But knowing only these facts does not really inform us about trade competitiveness between these countries. We cannot conclude that Country A grants a 10 percent subsidy to exporters while Country B has no subsidy. Nor can we conclude that the goods of Country A have a great advantage entering into Country B because they face no import charge in the latter country whereas the goods of Country B face a 10 percent charge on entering Country A and hence are a great disadvantage in Country A. If sales taxes were fully shifted forward, then the goods of both countries would, as respects sales taxes and border adjustments, be on an equal competitive plane despite the different levels of adjustment. But if such taxes are not fully shifted, then in this regard the exporters of Country A have been advantaged as against the exporters of Country B—not necessarily to the full extent of the differentials in border adjustments but only to the extent to which the tax in Country A is not shifted forward.

Of course, questions of incidence can be raised as to other taxes. The working assumption of legislators for domestic legislation when they consider a corporate income tax is that it is borne by shareholders and not passed forward in higher prices or backward in lower wages or lower raw materials prices. Again, as a working assumption this view of the incidence of the corporate tax is a useful generality. But if it is only a generality and if there is some forward shifting in prices, an exporter has added costs, due to the corporate tax entering into product costs, which are not being rebated and hence which affect his export prices and his external competitive position. Of course, this would be true for an exporter in any country with a corporate tax, including European countries. We should note that the effective rates of corporate income tax in major European countries do not appear to be significantly different from the United States effective rate. Certainly, if a differential does exist between European corporate taxes in relation to the United States corporate tax, it is far less than the differential between European indirect taxes and our indirect taxes. In addition—though there may be no studies on this point—the conditions that may influence a shift forward of the corporate tax into prices, if such shifting does occur, would presumably not differ between Europe and the United States.[8]

These are difficult, intriguing—and highly important—questions. This matter of tax incidence and tax shifting is murky, and it has kept economists busy for decades. Their papers have contributed many volumes to the economic literature—and nevertheless I suspect that the summaries in Economics I are still inconclusive and uncertain. Moreover, one may have to move from incidence and shifting on to levels of taxation and then to levels and allocation of Government expenditures. But clearly the area requires exploration and analysis beyond the generalities.

The problem will become more acute if the Europeans take the next step of harmonizing their indirect tax rates, for this could mean an increase in the value-added taxes—perhaps to 15 percent or more—for all countries except France, which today is at 20 percent (on the value of the product excluding tax).

Certainly, to the extent that the generalities are not fully valid, the disparity in indirect tax levels can only be working to the disadvantage of the United States in world trade. The extent of that disadvantage and the extent to which it has been adjusted for in prior exchange rates and devaluations may be difficult to measure, but the direction is that of disadvantage for the United States.

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[8] For a discussion of the possible effects, considering the various theories of tax incidence, on the balance of payments of a shift in the United States to greater reliance on indirect taxes and less on direct taxes, and the relationship of those effects to the effects on domestic policies and conditions, see Salant, the Balance of Payments Deficit and the Tax Structure (Brookings Institutin, Reprint 80), 1964.