

EEC member state tax evolution

Traditionally, the Member States of EEC have made considerably greater use of indirect taxes than the U.S. These taxes are refunded on exports and collected as border taxes on imports. This became accepted practice when tax rates were much lower than in the 1960's and has been included in the GATT arrangements. VAT (TVA) as developed by France during the past ten years has been accepted by GATT as an indirect tax and therefore refundable on exports. Also, the tax can be levied as a border tax on imports.

The taxes collected by all levels of government of European nations divert to government use about as large a portion of GNP as is the case in the U.S. The impact on the balance of international payments of tax differences is not in the relative level of taxation. It lies in the types of taxes used to raise this level of government revenue, and the manner of taxation expected to exist in the future.

The EEC is now deeply involved in carrying out Article 99 of the Treaty of Rome. On April 5, 1960, under the provision of Article 99, The EEC Commission established a Fiscal and Financial Committee (FFC) to work towards "establishment of a common market through creating and insuring conditions similar to those of an internal market" in the area of taxation. The report of the FFC was completed in July, 1962, and adopted by the Economic and Social Committee of EEC on July 2, 1963, and by the European Parliament on October 17, 1963.

A substantial portion of the FFC report is a recommendation for a common EEC value-added tax along the lines of the very successful French TVA. The timing provides for passing and promulgating a VAT (TVA) system before December 31, 1967, and the entry of the system into force cannot be delayed beyond December 31, 1969. The draft of structure and implementing details were completed on schedule and submitted in April 1965. In February 1967, the EEC Member States gave final approval to adoption of a VAT (TVA) system on industrial goods. The system will be in effect not later than 1970. On January 1, 1968, the German VAT (Mehrwertsteuer) went into effect. The remaining EEC Member States are developing appropriate legislation. However, the Italian VAT is not expected to become effective until 1971.⁵ VAT is being used by Denmark, and Norway and Sweden have adopted legislation to introduce it.

EEC is well on its way to establishing a common VAT. Under the rules of GATT the VAT possesses the capability of providing a powerful export stimulus through rebate to the exporter of all tax attributable to the production of the product exported. It also can be the basis for restricting imports as the full rate of the tax can be applied to imports as border taxes. It is very doubtful if a tax possessing these international trade "advantages" can be realistically abandoned or turned down once introduced and used by a major group of trading nations. Current U.S. discussions to attempt to minimize the advantages are therefore unlikely to produce results.⁶

GATT's acceptance of VAT as an indirect tax seems to have developed originally from the conditions out of which it arose and the method of French administration. The correctness of this decision can be the subject of an honest difference of opinion. But this is all water over the dam, and TVA, and therefore VAT, are considered to be indirect taxes by GATT under Article XVI-4 and implementing amendments. This GATT position combined with proven effectiveness of VAT in France points to a very nearly inevitable continued spread of the use of the tax.

It is a multi-level tax, and therefore can be a major revenue raiser with relatively low rates. Its use permits reduction of taxes on profits and incomes. It will also be the basis for an additional protective trade wall increasing the difficulty for firms outside EEC to compete in EEC with producers located in EEC Member States. The attraction of VAT to EEC Member States and other European nations as a substitute for their cascade turnover taxes is nearly irresistible. The tax does not violate the basic theory of turnover taxation while it eliminates most of the weaknesses of this tax.

The VAT approach to taxation has proven itself in France and has been adopted by Germany. The generalization of the procedure will permit EEC Member

⁵ *European Taxation*, April 1966, pp. 92-95, February 1967, pp. 44-45, and *Common Market*, April 1968, pp. 85-88.

⁶ Richard W. Lindholm, "Adjusting the Posture of the U.S. Economy to Facilitate Corporate Freedom in International Actions," *The Journal of Finance*, (1966), pp. 253-265 and *Maintaining the Strength of the United States Dollar in a Strong Free World*, U.S. Treasury, January 1968, p. 11.