

A. Border Taxes

In meetings of chemical industry representatives with the Department of Commerce on non-tariff barriers in 1963, the effect of border taxes was reported. In February 1966 the MCA provided the STR a report on border taxes. In this report prepared by Horace J. De Podwin Associates, Inc., the effect of European border taxes on U.S. chemical exports were detailed.

Early in 1967, the U.S. negotiators in Europe were given an updated summary of the effect of border taxes on U.S. chemical exports. Also, the expected damage to U.S. exports from the expected increase to 14.7 percent of the Common Market border tax was stressed.

The Common Market countries are in the process of harmonizing their border taxes and export rebates, first by shifting from the "cascade" types of turnover tax systems to a uniform value-added turnover tax (TVA) system, and second, by harmonizing at a single rate for the entire EEC. At least one non-Common Market country has already changed to a TVA system (Denmark) and others are seriously studying similar changes (U.K. and Sweden). The adverse effect upon our trade of the adoption of the TVA system is a most immediate problem as demonstrated by the changes recently implemented by Germany.

Before January 1 of this year, Germany had a cascade-type turnover tax system under which each sale of a product in Germany, either domestic or imported, was assessed a tax at the regular rate of 4 percent of the selling price including the tariff. Products of U.S. manufacture imported into Germany were therefore subject to an initial tax of approximately 4 percent at the border and additional tax each time the product was sold in Germany. On January 1, Germany switched to a TVA system under which a tax of 10 percent of the value added is charged instead of the 4 percent tax on the entire value as had been charged under the "cascade" system each time the goods were sold. Products of U.S. manufacture imported into Germany are now burdened with an initial tax of 10 percent at the border. The additional tax burden attracted by subsequent sales in Germany is limited to 10 percent of the value added after importation. On July 1, 1968, the rate will be increased to 11 percent.

France has for years employed a type of TVA system. Ultimately all EEC countries will agree on a uniform TVA tax rate estimated at approximately 15 percent. The German border tax adjustments are used as the reference framework for the comments which follow.

It has been argued that American manufacturers are not disadvantaged by border adjustments under the TVA system. We submit this is not so.

B. Disadvantage of Tax Systems Changes

The switch from the cascade-type turnover tax system to the TVA system in Germany has adversely affected American chemical exporters in several ways. MCA members have found that for many major product exports, the border tax adjustment, under the previous system, was less for both imports and exports than the higher cumulative tax cost reflected in the German producers' domestic price for a given product. Under the new system, the tax is no longer an element of cost to the German producer since he can pass it on in the same way as does an importer. As a consequence, he has been under pressure from German customers to reduce his selling price to reflect the tax saving.

MCA members have reported that, when the switch to TVA was made, the German chemical manufacturers, in many cases, had in fact reduced his selling price. To compete, the American company frequently found it necessary to reduce its selling price to the German customer by a like amount.

When the amount of the price reduction of the German chemical manufacturer exceeds the theoretical turnover tax burden of approximately 4 percent¹ and to the extent the American exporter finds it necessary to match the price reduction, he suffers a loss of profit, the exact amount varying with each product. Many MCA members have confirmed that in Germany, for many products, this is what has happened.²

C. The Theory of Tax Shifting

All turnover taxes, such as value-added taxes, are indirect taxes, and under the GATT it has been assumed that their burden is always shifted completely

¹ Often the tax base for the imported merchandise was the price to the German distributor rather than the distributor's price to its German customer and the sale to the German customer would involve only one transfer. When this was the case, the turnover tax burden of the imported merchandise was less than that of domestically produced merchandise. MCA members report that for some imported chemicals the actual burden was as low as 2 percent.

² See Appendix A for statement by Stanley S. Surrey, Asst. Sec. of Treasury.