A COMPARATIVE STUDY OF THE RECENT
USE OF CORPORATE INCOME TAXATION IN CANADA
AND SINGAPORE AS A MEANS TO STIMULATE
INDUSTRIAL DEVELOPMENT

by

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We accept this thesis as conforming
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ABSTRACT

Providing incentives to foster industrialization has been much in vogue in the developing countries in recent years. It is felt that, in the spree of enthusiasm to provide incentives to industries, the question of whether these incentives are appropriate to the economic problems at hand may not always be considered by the national government to the extent they desired.

This study deals specifically with the tax incentives by way of corporate income taxation in Canada and Singapore. The purpose of this comparative study is to draw out the significant similarities and differences in the economic backgrounds and approaches by a system of tax incentives to assist in solving the underlying economic difficulties.

It appears that in Canada incentives by way of corporate income taxation may not have had the anticipated impact on the Canadian economy. Many of the Canadian tax incentives seem to be too short-lived to influence long-term business investment decisions. In Singapore, possibly because of the urgency of its economic problems, the tax incentive legislation permits a long term use of the incentives which may therefore have a greater impact in influencing the long-term structure of the economy.
The conclusion has been reached that in spite of the vastly marked social, economic and geographic differences between the two countries they have, however, employed substantially similar incentives to varying extent to stimulate the economies toward industrial development, although the economic environments of the two countries seem to require different approaches.
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CHAPTER I

INTRODUCTION

It is perhaps not an over-emphasis to suggest that economic development has been the key economic issue in the 20th century. Economic growth is defined by S. Kuznets to be "a sustained increase in per capita or per worker product, most often accompanied by an increase in population and usually by sweeping structural changes"(1). The criterion of development or underdevelopment of a country is the extent to which it has achieved structural transformation. The indices of transformation are the shares of manufacturing and services in the Gross Domestic Product and in employment and the degree of structural interdependence in the economy. A country can of course have a high per capita income without having to undergo structural transformation, for example, a small country relying on the export of some valuable natural resource product. But this is the exception rather than the rule.

It is possible for a very large country like Canada with extensive natural resources to achieve self-sustained growth. But in a small country like Singapore, the degree of self-sustenance of the growth process is less because of greater external dependence. A small country can achieve economic growth only with a high ratio of foreign trade to its gross national product. For an understanding of the
analysis that is to follow it is important to bear in mind the structural differences in the economies of the two countries and hence the approaches to solving the economic problems differ.

In a continental country like Canada, economic growth involves a balanced pattern of development with exports and imports playing a marginal balancing role. In a small country, there are limits to import substitutions and economic development usually involves the export of manufactured goods unless the country has primary resources for export.

Economic development will not however, be achieved through a mere desire to improve the per capita income of the people. It implies "a determined effort to increase their productivity through structural changes both economic and other-wise". Increasingly, it is felt that for most underdeveloped countries to develop, a positive role on the part of the national governments is unavoidable. The extent of government participation however, differs from country to country, depending upon the social philosophy of the populace and the state of the economy and may range from state ownership of business enterprises on the one hand to private enterprise on the other. In the discussion that is to follow we shall accept the proposition that a certain degree of government intervention in the price mechanism is not inimical to economic growth. "In the future, as in the past, government
action will be needed in certain spheres of activity to supplement the role of private initiative and enterprise"(3). The fields where government action may be desirable to remove obstacles to growth are extensive and differ among countries. However, it is possible to single out particular government measures for special consideration. Accordingly, the tax policy of each of the two countries is singled out for particular attention in this study. Tax policy, it is believed, if used intelligently, can influence materially the direction and extent of economic growth. It is recognised that all tax systems have certain anti-growth biases and may also distort the efficient allocation of a country's resources. But some of the anti-growth features of the tax system can be compensated for within the tax system, as the Royal Commission on Taxation rightly points out, "reforming the tax base and rate structure should therefore not reduce the rate of growth and may increase it".(4)

In the light of the discussion above we may proceed to discuss the nature of the analysis in this thesis. The writer is faced with the problem of evaluating the fiscal incentives that have been introduced in Singapore with the objective of transforming the structure of the economy. As with most developing countries, fiscal incentives take the form of manipulating the corporate tax structure.

In this process of evaluation an attempt will be made to compare the tax incentive systems of Singapore and
Canada. It is hoped that by this comparative study, using Canada as the counterpart, one may comprehend more fully the implications of the incentives introduced in Singapore.

In recognition of the need for a systematic evaluation of the tax policy of Singapore as an instrument of economic growth the differences in the corporate tax systems of Singapore and Canada and particularly the special incentives introduced to stimulate the growth of the manufacturing industry will be examined. Tax provisions can influence capital formation, research and development, export, business savings and the application of new technology in production. These factors affect manufacturing industry more than the primary and service industries. The emphasis in this thesis will be the growth of the manufacturing sector of the economy since it is believed that it has assumed, and will continue to assume, an important role in economic development. It will be shown later, that fostering the growth of the manufacturing industry is to all intents and purposes, synonymous with fostering economic development in Singapore.\(^{(5)}\)

As is true with all public policy, the desirability or otherwise of a tax policy depends upon the objectives it is to serve. It is not the intention of this thesis to judge the choice of particular objectives—a choice that involves a considerable amount of value judgment and is made at the political level. We shall however, analyse and ascertain the extent to which similar company income taxation
measures have been employed or are in the course of being employed in both Singapore and Canada and the extent to which these measures have been promulgated for similar objectives and the likely implications of such measures.

Broadly speaking, the primary objectives of the Canadian fiscal policy in general and the fiscal incentives in particular are conceived to be one of promoting STABLE growth and the reduction of unfavourable swings in the business cycle. But for Singapore, the objectives are to stimulate growth itself. It is therefore a mistake to assume that the "economic objectives of tax and budgetary policy in underdeveloped countries which are to promote investment, to maintain stability, and to reduce extreme inequalities in wealth and income"(6) are "not basically different from the economic goals of allocation efficiency, economic growth, stability, and optimum income distribution which guide fiscal policy in advanced country on a free enterprise basis"(7).

It is against this background that the study is undertaken. It should be realised that conditions in Singapore differ vastly from those of Canada and a realistic and sound system of fiscal incentives operating through the company taxation structure can be laid down only in relation to the economic conditions in Singapore and Canada and the objectives that are to be achieved. The formulation of such an incentive scheme for Singapore and Canada must take into account the stage of economic development of the two countries, "the
degree of elasticity of response of the system to (fiscal) stimuli, and the state of the economy at any given time". With the above general introduction a scheme of study may be formulated. First, an attempt will be made to review the main features of the Singapore and Canadian economy in 1959 and 1960 respectively. This will be done in Chapter II. This serves to bring out the objectives of the incentive schemes introduced in the 1960's. Chapter III will undertake to review first, the corporate tax structure as it would operate without incentives in Singapore. This serves as a base upon which the incentive provisions of the 1960's were added. Chapter IV will similarly discuss the corporate tax structure of Canada without incentive provisions before introducing the incentive legislations. Chapter V will be devoted to a discussion of the differences in the approaches to incentive provisions in the two countries, bearing in mind the objectives underlying such measures. Chapter VI will attempt to assess and evaluate the implications of the incentives with respect to the objectives and the shortcomings of the tax incentive measures as devices to stimulate industrial development.


(5) The Royal Commission on Canada's Economic Prospects classified Canadian economy into the following sectors:

(a) Primary industries which comprise fishing, agriculture, forestry and mineral extraction.

(b) Manufacturing industries which comprise of:
   (i) Primary manufacturing, i.e. processing of mineral ore, petroleum refinery etc.
   (ii) Secondary manufacturing, which comprises the manufacturing of products to the final "consumable" stage.

(c) Service industries, e.g. government service and energy.

The above scheme is also adopted by W. F. Lougheed in his book "Secondary Manufacturing Industries in the Canadian Economy". The above classification is in accordance with international practice. In this thesis we are concerned primarily with (b).


(9) It is coincidental that both countries introduced incentive provision in their income tax structures to stimulate the growth of manufacturing industry.
at about the same time. For Canada for instance, speaking of the "Baby Budget" of December 1960, J. R. Petrie said, "three tax incentives, rare in federal fiscal history, were promulgated".
CHAPTER II  
THE ECONOMIC BACKGROUNDS

This chapter is an attempt to review the economic environment of Singapore and Canada in 1959 and 1960 respectively with a view to introduce to the reader the underlying objectives and policy orientation of the fiscal incentives that will be discussed in Chapters III and IV.

I. SINGAPORE

1. Traditional Source of Income

Situated at the cross-roads of international sea and air routes Singapore has been a major trading centre for South East Asia for the past years. The contribution of entrepot trade\(^1\) to her economy can best be seen by the fact that in recent years earnings from this source accounts for 20\(^\circ\)/o of the national income of Singapore and directly accounts for 15\(^\circ\)/o of the employment in 1957\(^2\). These figures do not include the indirect contributions of trade. It may be said that the key to Singapore's development and prosperity lies with the provision of services. The extent to which Singapore relies on trade is shown by the fact that during 1960 trade per capita was $M 4,625\(^3\) (vs. Canada's $M 1,680\(^4\)).
But entrepot trade "has very limited possibility of expansion. The danger is that there may be some decline in the future"(5). This, foreseen in 1950's, is born out by the trend of total trade in recent years:

<table>
<thead>
<tr>
<th>Year</th>
<th>Imports</th>
<th>Exports</th>
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<tbody>
<tr>
<td>1961</td>
<td>3,963.3</td>
<td>3,308.5</td>
</tr>
<tr>
<td>1962</td>
<td>4,035.9</td>
<td>3,416.7</td>
</tr>
<tr>
<td>1963</td>
<td>4,279.0</td>
<td>3,474.5</td>
</tr>
<tr>
<td>1964</td>
<td>3,478.7</td>
<td>2,771.9</td>
</tr>
<tr>
<td>1965</td>
<td>3,807.2</td>
<td>3,004.1</td>
</tr>
<tr>
<td>1966</td>
<td>4,065.7</td>
<td>3,375.6</td>
</tr>
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Besides, two other factors that would affect Singapore's trade in the future were becoming obvious by 1959.

(a) The world demand for natural rubber, which accounted for 33°/o of the value of total imports of Singapore and 41°/o of its exports would not expand substantially due to the decline in demand particularly in the U.S.

(b) The trend towards direct trade among Singapore's traditional customers. The First Four-year Plan observed: "It is however, an inescapable fact that irrespective of improved facilities
to encourage trade expansion there are factors controlling the extent of entrepot trade which are beyond this country's influence. Of these the two most important are the general desire of all countries of the region to develop manufacturing industries and thus reduce imports and secondly trade directly with the countries using the raw materials they produce and thus by-pass Singapore" and concluded that "even if the usual volume of trade could be maintained or even slightly increased trade and allied activities alone could not provide the required opportunities for Singapore's fast growing population, of which larger and larger numbers are entering the labour market every year"(7).

2. Population Growth and Employment

The unemployment situation is at best to be described as serious. With a total population of 1.6 million in 1959 living on an island of 224.5 sq. miles and with very little natural resources in the generally accepted meaning of the term Singapore cannot hope to develop on the line of many developing countries by relying on agriculture or resource industries in the early stages of development. Besides, population growth between 1947 and 1957 was 4.3% annually—a rate which
is the highest known in the world.

Chronic unemployment in 1957 was 24,000 and in 1959, 31,000 (or about 9% of the labour force). Net additions to the labour force for 1961-1964 was estimated in the Four-year Plan to be as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Net Additions</th>
</tr>
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<tbody>
<tr>
<td>1961</td>
<td>10,400</td>
</tr>
<tr>
<td>1962</td>
<td>14,100</td>
</tr>
<tr>
<td>1963</td>
<td>14,400</td>
</tr>
<tr>
<td>1964</td>
<td>13,700</td>
</tr>
<tr>
<td>Total</td>
<td>52,600</td>
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In aggregate terms, if the backlog of the unemployment, plus the new entrants into the labour market is to be absorbed, 84,000 new jobs must be created between 1961-1964 or 21,000 per year. It was also envisaged by the Plan that public service, construction and employment due to normal growth in the economy would absorb some 40,000 during the period. This still leaves 44,000 or about 7% of the labour force unemployed. "Hence, unless unemployment in manufacturing industry expanded, there would still be 44,000 chronically unemployed in 1964" (8).

The prospect in 1959 then was that unemployment would increase substantially unless a structural transformation of the economy takes place.

3. **Industrial Development**

Industrial development is commonly used to
denote (a) primary manufacturing and (b) secondary manufacturing. In the context of Singapore, industrial development specifically refers to the latter. It was recognised by the end of the 1950's that Singapore had to seek alternative sources of employment for the growing population. Because of the population pressure and the limited expansion possible in the traditional sector described earlier, it was felt that greater emphasis would have to be placed on industrialization while at the same time there should be no reduction in Singapore's reliance on entrepot trade, at least in the short run.

By 1960 Singapore's secondary manufacturing sector contributed some $M 1\,143 or about 7.1\% of the gross domestic expenditure.\(^9\)

The secondary manufacturing sector of Singapore in 1960 was characterised by a large number of small establishments which made up 70\% of the total manufacturing establishments. Small establishment is defined to be firms employing less than ten workers each. If these small establishments are included, total value added by the secondary manufacturing sector should account for 9.1\% of the GNE. Small establishments are estimated to have contributed only 1/5 of the employment and output in the secondary manufacturing sector. In any event, it is obvious that Singapore's
secondary manufacturing industry was relatively "underdeveloped". On the other hand almost 48% of the output of this sector was exported in 1956.(10) Most part of it comprised of food stuff and crude materials.

4. **Capital Formation**

Another yardstick used to assess the adequacy of economic development is the percentage of saving out of national income to be devoted to capital formation. It is generally agreed that most developing countries channel less than 10% of their income into net investment every year. In 1959, Singapore's gross capital formation amounted to only 7.6% of the gross national income.(11) This is very low by any standard. Furthermore if we deduct depreciation and capital formation in the trade sector, the net investment in industries will be very low indeed. The Four-year Development Plan of 1961-1964 envisaged a gross capital formation of close to 20% if the Plan was to achieve its target. As matters stand in 1960, there was an urgent need to increase the level of capital formation. This is an inescapable economic fact.

Hence a review of the economic environment of Singapore in the late 1950's does not offer much grounds for complacency. For ease of reference we
summarize below the main characteristics:

(a) The source of Singapore's prosperity, the entrepot trade sector offered limited opportunities for growth.

(b) The unemployment, standing at 9% in 1959 would worsen unless a structural transformation of the economy take place. The unemployment situation is described by E.L. Wheelwright to be "critical".

(c) Gross capital formation was inadequate when compared with the industrially advanced nations. The need to increase the share of national income devoted to capital formation is particularly obvious.

(d) Because of the lack of natural resources, the only possible solution to the unemployment problem is through industrialization which lends itself most easily to expansion if it is given the proper inducement.

(e) The growth in manufacturing slackened considerably in 1959-1960 as IBRD report stated, "In Singapore, recent growth in manufacturing has been less spectacular after buoyant progress had been experienced in the 1950-1957 period. Although comprehensive industrial statistics are lacking, it appears that the increase in
output stagnated after 1957 until 1960". \((f)\)

"Rapid industrialization is the only solution to Singapore's problems, as the Development Plan recognizes and drastic action is called for if the unemployment situation is not to deteriorate further. What is needed in Singapore is nothing less than a transformation of the economy in the shortest possible time from a predominantly commercial trading basis, to a predominantly industrial basis". \((g)\)

Given the economic environment in 1959, one can readily realize the urgency of the problem. It was then decided that special incentives must be given to induce investors to establish manufacturing enterprises in Singapore. Because of Singapore's very great dependence on international trade and the government's basic philosophy of free enterprise, the government's task was confined to creating the conditions which would induce substantial private capital (both local and foreign) into industries. The industrial promotion aspect however, was totally neglected until 1959 when a series of promotional effort began to take shape to be effective from 1960. The promotional policies took two directions: (a) fiscal incentives by way of company income tax and (b) provision of industrial estates to industrialists. Since the central idea
of this thesis is fiscal incentives, subsequent chapters will highlight this aspect. However, other aspects of promotional work will be mentioned briefly wherever necessary.

II. CANADA

1. Canadian Economic Background up to 1960

   It is not possible in this short review to discuss in detail the Canadian economy. The primary intention of this section is to focus upon the economic environment of Canada in 1959-1960 with the objective of discerning the basic structure of the economy which would suggest the direction of the fiscal policy orientation in the 1960's.

   Canadian economic growth and development since 1939 was determined by a few causal factors among which are: (a) the world war effect, (b) foreign investment, (c) ample supply of natural resources, and (d) proximity to the U.S. These features will be brought out in the discussion to follow.

   Before the war in 1939 Canadian economy recovered, like most other industrially advanced nations, sluggishly from the depression of 1932. In 1939, ten years after the last period of prosperity, unemployment was 11% of the labour force. Between 1940 and
1945 Canada, with ample raw material and capital resources responded readily to a war demand. Industrial capital stock was brought to capacity operation. The manufacturing sector, measured by the volume of output expanded 1\frac{1}{2} times during 1939 and 1944 to become the largest sector in the Canadian economy. Relatively little expansion took place in the agriculture and service sectors. No detail capital investment statistics are available for this period, but it was obvious that Canadian manufacturing capacity increased and became more diversified.

1944-1949 were the years of adjustment to a civil economy. The initial vigour of the postwar demand was felt. This facilitated the adjustment process. The large liquid savings during the war were released for consumption. This, coupled with the initiation of a period of mass consumption, gave strength to the Canadian economy. The economy was further boosted by intense world demand for both manufactured products and raw materials for reconstruction. During the period major price indexes turned sharply upward—a natural consequence of the rapid growth.

J.D. Gibson summed up the period as follows:

"Given the upset state of the world, Canadians as a people have tried to do too much too quickly. In addition to the aid which we provided as a nation to overseas friends and customers, we attempted to maintain a higher level
of consumption than ever before and embarked on a tremendous program of capital replacement and expansion. Though Canadian production was in the aggregate some 50% over pre-war it was by no means sufficient to meet the combined demands of exports, consumption and investment. Something had to give way.\(^{(14)}\)

The foreign exchange reserve skidded alarmingly and measures were taken to control imports of consumption goods and the suspension of U.K. drawings on the Canadian loan advanced early in the post war year. A budget surplus in 1949 was effected to fight inflation. The Bank of Canada on the other hand maintained an easy money policy and this was essentially stimulating to investment and capital expenditure. Resource export industries also expanded rapidly during the period. The manufacturing industries as reported by the Department of Reconstruction and Supply, "a large measure of industrial diversification is accompanying the process of conversion, modernization and expansion of Canadian factories". Thus by 1949, the Canadian economy had adjusted to a peace time economy without undue stress and strain.

1950's began with a period of full employment. In June 1950 the stimulation given by the Korean War took its course in the Canadian economy. Three sectors of the Canadian economy were affected: (a) consumer spending (b) defence outlays and (c) export, especially industrial materials. The first component was
already high then and the increased consumption added further to the buoyant economy. Items (b) and (c) showed an immediate sharp upturn. Canadian export components showed a change from that of immediate post-war. The political and economic implications of the cold war called upon Canada to perform its historical role as raw material supplier and primary manufacturer. In Europe, recovery from the war was almost completed and the stage set for economic expansion and growth. Elsewhere in Japan and Australia the process of industrialization was gaining momentum. These trends in world demand for raw materials were powerful sources of stimulation for Canada's resource export industries and through them the economy in general. With the expansion in Canada's resource industries in-flowed American capital. From 1946 to 1955 the growth in general manufacturing and resource-export industries had been very similar in size and "although a more rapid rate of investment occurred in the resource industries immediately after Korea, the general similarity of two investment trends (by the two industries) is striking. Both industry groups have undergone rapid expansion—one in response to external demands, the other primarily in response to domestic demand. The resultant picture is one of growth and development on a broad front and this was further stimulated by a high
level of population growth.

1955-1960 witnessed intense American investment in Canada's resource and manufacturing industries. The extent of American involvement is seen by the following comment by W.F. Lougheed in 1961 "in manufacturing and the resource industries the American influence is really apparent. Based on book value, U.S. control—which is more important than ownership—is present to the extent of 42 per cent in manufacturing as a whole, 71 per cent in petroleum and natural gas, and 52 per cent in mining and smelting. These are frightening figures to apply to key sectors of Canadian industry. The degree of control is also understated in that in many industries the American firms in Canada are the largest in their respective sectors, with the result that the more numerous but smaller Canadian companies very often are swept along by the American-made industry policy decisions". (17)

There can be no doubt therefore, that American capital had contributed immensely to Canada's economic growth since the war. However, public concern is widespread as to the desirability of this economic fact. A few of the criticisms against American capital may be cited:

(a) By dominating the key sectors of the Canadian economy, many Canadian owned companies suffer
competitive-wise. This was becoming apparent in the late 1950's.

(b) The American subsidiaries, backed up by immense financial resources at home, technological development and the negligible amount of research undertaken in Canada tend to widen the technological gap between U.S. and Canada.

(c) The competition posed by U.S. resulted in excess capacity in the Canadian corporations. This was especially so in the manufacturing industry. Because of this competitive advantage on the part of U.S. (and other countries) they now enjoy, coupled with the new and modern equipment many of them installed threatened to undermine the position of Canadian companies even in their own home market as well(18).

It is not easy to assess the logic of these arguments. It is certainly true that without American capital the Canadian economy would not have developed to this stage. Furthermore the adverse effects may be small compared with the benefits direct investment conferred by way of capital, markets, technology and skills. A.E. Safarians, for instance, concluded that the faults ascribed to foreign ownership may often be not due to ownership as such but to the basic structure of the Canadian economy--e.g. tariffs and the absence of adequate legislation designed to increase
efficiency or to spur development.\(^{(19)}\)

It is not the intention of the writer to delve in detail the "reasonableness" of such conclusions. Suffice to note here that a number of tax legislations introduced in 1960's had been aimed at correcting this feature of the Canadian economy. The more relevant question in hand is to determine the causes of such inflow, which can be traced largely to the Canadian monetary, fiscal and exchange policies in the post war year. Briefly, the premium on the Canadian dollars in the second half of the 1950's had a stimulating effect to American capital inflow. The inflow of funds further raised the Canadian dollar from par in late 1955 to a premium of 6\(^{0}/_{o}\) in the autumn of 1957. The increase in the value of the Canadian dollar helped to induce a rapid increase in imports and discourage the expansion of exports (except raw material export) and thus produced current account deficits in the balance of payments equal in size to the annual inflow of foreign funds.\(^{(20)}\)

Meanwhile, monetary policy moved from a condition of relative ease to one of increasing restriction. For a prolonge period interest rates in Canada were higher than that of the U.S. During the whole of the late 1950's C.L. Barber noted that there had been an upward movement in interest rates in a number of major countries. His data showed that the
rate had risen more in Canada during this period than was true for any of the other countries cited except U.K.

Tight money did little to damper the investment climate in Canada. Instead of resorting to internal source of funds, corporation borrowed abroad. The effect was a shift to foreign sources of funds. Fiscal policy was lenient during the period, as is shown by the level of fiscal budget deficit. The overall effects of the fiscal, monetary and exchange policies of the Canadian government may be summarised as follows:

(a) The persistently high interest rate in Canada as compared with that of U.S. induced large amount of capital inflow during this period under review. This was reflected in the high level of investment as a percentage of gross national product, amounting to over 20% annually. This rate cannot be sustained without American capital.

(b) The high level of demand for Canadian dollar led to a premium on Canadian dollar vis-a-vis the U.S. dollar. This served to divert consumer demand from domestic to imported goods. By 1959 the excess capacity in the Canadian economy was becoming apparent. Unemployment was at a level of 7%.
(c) The premium on Canadian dollar also discouraged export of Canadian manufactured goods, particularly secondary manufactured goods.

(d) No step was taken to reduce the premium on Canadian dollar and the high interest rate. Furthermore the fiscal policy as noted earlier, was lenient.

(e) There was no slackening in final demand, but rather it was directed to foreign imports.

(f) The upshot of these developments was that output and employment in Canada were depressed. If only part of the final demand could be directed to domestic manufactures, Canadian economic growth would have been different.

Hence the problem of Canadian economy is largely induced by the rather unco-ordinated monetary, fiscal and exchange policy. By the end of the 1950's it was becoming evident that the objectives of any Canadian economic policy should be directed to putting the Canadian economy back on its pre-1953 long-term growth line. Not only was Canadian manufactures unable to compete effectively in the world market, development of new sources of supply and substitutes for the natural resource exports were also beginning to be felt by 1960.
Taking a long term view it was also recognised that by 1965, one million jobs would have to be created to cater for the entrants into the labour market and the reduction of employment in the agricultural sector. This could be achieved only when there is economic growth, which is associated with new capital investment.

But as noted earlier the Canadian economy exhibited certain amount of excess capacity due to inadequate—domestic and foreign—demand. Hence, "in a modern industrial economy like Canada, securing and maintain a large and growing volume of market demand is the single most important problem to face"(21) and not a lack of productive capacities.

It was also becoming obvious that the secondary manufacturing sector was most in need of stimulation, first to reduce the excess capacity and secondly to create employment opportunities for the new entrants to the labour market. Full employment cannot be achieved through primary and service industries. A strong manufacturing base was clearly needed. It is only in secondary manufacturing industry that the latest equipment, management and research can make themselves felt in the Canadian economy—requirements if Canada is to offset world competitive conditions.

A few features of the Canadian secondary manufacturing industry may be observed.
2. Employment by Industry

Table II shows the trend of employment in the Canadian economy.

<table>
<thead>
<tr>
<th>TABLE II</th>
</tr>
</thead>
<tbody>
<tr>
<td>EMPLOYMENT BY INDUSTRY IN CANADA(22)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>1941</th>
<th>1951</th>
<th>1960</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>1,084</td>
<td>939</td>
<td>675</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>709</td>
<td>1,350</td>
<td>1,470</td>
</tr>
<tr>
<td>Services</td>
<td>1,722</td>
<td>1,576</td>
<td>1,722</td>
</tr>
<tr>
<td>Others</td>
<td>682</td>
<td>1,290</td>
<td>1,088</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>4,196</td>
<td>5,155</td>
<td>5,955</td>
</tr>
</tbody>
</table>

In percentage terms, manufacturing (both primary and secondary) provided 16.9, 26.0 and 24.6 per cent of the jobs to the labour force in respective years. It can be seen that (a) agricultural employment declined rapidly in 1951-1960, (b) total employment in other non-manufacturing industries had not grown by any substantial number in 1957-1960 and appeared to have reached the maximum as a percentage of the total labour force, and (c) future employment will have to be created largely in the secondary manufacturing sector.

3. Contribution of Manufacturing to Gross Domestic Product

Table III below shows the importance of
of manufacturing industries in the Canadian economy.

**TABLE III**

**VALUE-ADDED BY MANUFACTURING INDUSTRY AS PERCENTAGE OF GDP IN CANADA**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Manufacturing</th>
<th>Secondary Manufacturing only</th>
</tr>
</thead>
<tbody>
<tr>
<td>1953</td>
<td>36.4</td>
<td>20.2</td>
</tr>
<tr>
<td>1954</td>
<td>35.6</td>
<td>19.5</td>
</tr>
<tr>
<td>1955</td>
<td>36.0</td>
<td>19.5</td>
</tr>
<tr>
<td>1956</td>
<td>35.3</td>
<td>19.5</td>
</tr>
<tr>
<td>1957</td>
<td>34.6</td>
<td>19.4</td>
</tr>
<tr>
<td>1958</td>
<td>34.6</td>
<td>18.7</td>
</tr>
<tr>
<td>1959</td>
<td>33.0</td>
<td>18.3</td>
</tr>
</tbody>
</table>

It can be seen that since 1953 height, the contribution of manufacturing as a whole to GDP had shown considerable drop. The contribution of the secondary manufacturing sector also decline relatively. What these figures imply is that the growth in the manufacturing sector had not kept pace with the growth in the economy.

4. **Export of Manufactures**

Table IV below shows the importance of export of manufacturing products.

Total export as a percentage of GDP declined from 1952 to 1960. Manufactured export increased nominally as a percentage of the total
### TABLE IV

**EXPORT OF MANUFACTURES IN CANADA**

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Domestic Product</th>
<th>Total Export</th>
<th>% of GDP</th>
<th>Export of Manu. as % of GDP</th>
<th>Export of Manu. as % of Total Export</th>
<th>Secondary Manu. as % of Total Export</th>
</tr>
</thead>
<tbody>
<tr>
<td>1952</td>
<td>21,344</td>
<td>4,337</td>
<td>20.3</td>
<td>726</td>
<td>3.41</td>
<td>12.5</td>
</tr>
<tr>
<td>1955</td>
<td>24,326</td>
<td>4,330</td>
<td>17.9</td>
<td>708</td>
<td>2.92</td>
<td>9.9</td>
</tr>
<tr>
<td>1958</td>
<td>29,318</td>
<td>4,894</td>
<td>16.7</td>
<td>851</td>
<td>2.90</td>
<td>11.6</td>
</tr>
<tr>
<td>1960</td>
<td>32,146</td>
<td>5,395</td>
<td>16.8</td>
<td>999</td>
<td>3.11</td>
<td>11.1</td>
</tr>
</tbody>
</table>

**Source:** See footnote (22) page
export while export of secondary manufactures declined slightly in its contribution to total manufactured products exported. The only conclusion one can draw from these statistics is that Canadian manufacturing industry had not fared well in the export market.

5. **Import of Manufactures**

Table V shows the imports of manufactured products.

The last two columns of the table are significant. Import of secondary manufactures have not shown any decrease as a proportion of GDP, which implies that import substitution had not play a great part in the decade. But it is also true to say that as some of the imports are being manufactured in Canada, more are demanded of goods not produced in Canada. Import of manufactured goods as a percentage of import in fact shows some increase during the years. In any case it is expected that as economic development advances, the proportion of import of manufactures as a percentage of the GDP and total import should decrease.

From all indications therefore Canada's manufacturing industry had not grown at the same rate as the economy grew both in terms of export, value-added and employment.

6. **Regional Development**

Another aspect of the Canadian economy is
<table>
<thead>
<tr>
<th>Year</th>
<th>GDP ($m)</th>
<th>Total Import ($m)</th>
<th>Import of Manu. ($m)</th>
<th>Import of Manu. as a % of GDP</th>
<th>Import of Manu. as a % of GNP</th>
<th>Import of Manu. as a % of total import</th>
</tr>
</thead>
<tbody>
<tr>
<td>1952</td>
<td>21,344</td>
<td>3,916</td>
<td>2,348</td>
<td>18.3</td>
<td>11.00</td>
<td>60.00</td>
</tr>
<tr>
<td>1955</td>
<td>24,324</td>
<td>4,568</td>
<td>2,848</td>
<td>18.9</td>
<td>11.65</td>
<td>62.50</td>
</tr>
<tr>
<td>1958</td>
<td>29,318</td>
<td>5,050</td>
<td>3,136</td>
<td>17.2</td>
<td>10.62</td>
<td>62.25</td>
</tr>
<tr>
<td>1959</td>
<td>31,293</td>
<td>5,509</td>
<td>3,497</td>
<td>17.6</td>
<td>11.20</td>
<td>63.50</td>
</tr>
</tbody>
</table>

Source: See footnote (22), page
the difference in growth in the different regions of Canada. Space does not allow us to go into detail this aspect of the Canadian economy. Nevertheless, any policy directed toward economic growth cannot neglect this aspect of the Canadian economy. The Commission on Canada's Economic Prospects notes that "the evidence suggests that much greater caution is required in attributing to these regions a similar rate of economic growth, and that the pace of economic development will likely be less rapid there than elsewhere unless special measures of a far-reaching nature are implemented. This does not imply that progress will be automatic in the regions other than North and the Atlantic Provinces". (24)

III POLICY IMPLICATIONS

This chapter serves to illustrate the backgrounds to any economic policy in the 1960's. In short, any policy aimed at fostering economic development in the two countries must be made in the light of the economic environment and objectives. The following might be considered to be the prime objectives of any policy directed toward economic growth in the early 1960's.

Singapore

(1) Effort was to be made to increase the rate of domestic savings and the channelling of these
savings to productive manufacturing sector.

(ii) Because of competition from Hong Kong and Japan which have achieved an early start, emphasis in manufacturing should be on goods of high quality and skill content.

(iii) Given two investment projects, equal in every aspect except in employment, preference should be given to that one which is more labour intensive. In other words, labour-intensive industries should be encouraged.

(iv) Policy should be aimed at inducing foreign direct investment.

(v) Policy should be orientated to supporting export industries. The reason being that because of a complete lack of natural resources, and as the pace of industrialization gathers momentum, considerable foreign exchange would have to be needed for the import of machinery and raw materials.

Canada

(i) Effort was to be made to increase capital expenditure. But it is also important that the slack in the economy be eliminated.

(ii) Although the exact impact of foreign ownership and control in the Canadian economy cannot be ascertained with any degree of certainty, effort was to be made to moderate the dependence on
foreign capital and to foster domestic capital investment.

(iii) To eliminate the slack in the Canadian economy considerable effort must be made to export manufactured goods.

(iv) To reduce the technological gap it behoved on Canadians to do more scientific research at home.

(v) To eliminate the persistent balance of payments deficits.

(iv) To eliminate undue cyclical swings in unemployment.

Any fiscal and monetary measures must be directed to the above objectives which, because of the differences in economic environment, tend to differ in certain aspects in the two countries.

Singapore needs a long term transformation of the structure of the economy and hence policy must be directed to long term aspect. Furthermore measures must be substantial and even drastic.

For Canada, the economy had reached a high level of development. The adjustment is more marginal and regulatory in nature.

The above analysis reviewed the economic structures underlying the two economies up to 1960. Chapter III will discuss in detail the tax measures in so far as they operate through the corporate income tax structure to effect
the objectives listed for Singapore, while Chapter IV will discuss the corporate tax structure of Canada.
CHAPTER REFERENCE

(1) Entrepot trade is the provision of transit services to international trade transactions. The term includes processing of raw materials and water transport activities associated with this trade.


(3) Singapore shared with Malaysia and Brunei a common Malayan currency until June 1967. In 1967 separate currencies were introduced. The exchange value of the present Singapore and Malaysian dollar however are on par. For statistics up to 1967, the Malayan dollar is used. The old Malayan dollar and the new Singapore dollar equal 35.7 cents Canadian.


(6) Monthly Digest of Statistics, Department of Statistics Singapore Vol. VI No. 12, December 1967, page 40. The drop in value in 1964 and 1965 is largely accounted for by Indonesian boycotting trade with Singapore during confrontation, 1963-1965. Singapore imported from Indonesia some $M700m or 16.3 o/o of the total import exported $M400m or 11.5 o/o of Singapore's total export in 1963. Almost the entire trade was entrepot in nature.


The employment statistics of Singapore leaves much much to be desired. No up-to-date records are kept. The Labour Department keeps a record of those who registered with it for employments. But this is not comprehensive in its coverage. Speaking of the unemployment situation in his 1967 budget speech the Minister of Finance says: "All this strengthens my belief that there
should be established in the government machinery a system for the period estimation of unemployed persons by some reliable statistical method. This is the one key economic variable in Singapore and yet it cannot be known with certainty simply because of the absence of a machinery to collect information" (page 10, Official copy, Budget Speech, Ministry of Finance, Singapore, 1967, December).

(9) The value of $M143m is estimated by taking the value of output by secondary manufacturing sector of $M428m and taking 30 o/o of which to be the value added. (See Economic Development Board, Annual Report 1966, pages 3 and 4).

(10) Four-year Development Plan, op cit, page 15.


(13) E. L. Wheelwright, Industrialization in Malaysia, op cit, page 120.


(16) Op cit, page 49.


(20) See C. L. Barber, op cit, page 60.

(21) C. L. Barber, op cit, page 37.


(23) For a study of the regional aspect of Canadian economy, the reader may refer to Some Regional Aspects of Canada's Economy Development by R. D. Howland, Queen's Printer, Ottawa 1957, Royal Commission on Canada Economic Prospects.

(24) op cit, page 3.
CHAPTER III
SINGAPORE CORPORATE INCOME TAX

I. BROAD OUTLINE OF SINGAPORE CORPORATE INCOME TAX

This section serves as a review of the corporate tax legislation in Singapore as it would apply to a normal company without any forms of incentives. This discussion is necessary for an understanding of the significance of the incentive legislations introduced in the 1960's which are to be discussed below.

First, a short review of the sources of revenue of the Singapore government may be helpful. This is given in Table VI below.

TABLE VI

SOURCES OF REVENUE OF
THE SINGAPORE GOVERNMENT (1959)

<table>
<thead>
<tr>
<th>Source</th>
<th>$M mill.</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate income tax</td>
<td>47.0(1)</td>
<td>17.1</td>
</tr>
<tr>
<td>Personal income tax</td>
<td>29.7</td>
<td>10.8</td>
</tr>
<tr>
<td>Sales tax</td>
<td>nil</td>
<td>--</td>
</tr>
<tr>
<td>Customs Duties</td>
<td>95.3</td>
<td>34.6</td>
</tr>
<tr>
<td>Excise Duties</td>
<td>nil</td>
<td>--</td>
</tr>
<tr>
<td>Excise Tax</td>
<td>nil</td>
<td>--</td>
</tr>
<tr>
<td>Other Tax</td>
<td>25.5</td>
<td>9.3</td>
</tr>
<tr>
<td>Non-tax revenue</td>
<td>77.4(2)</td>
<td>28.1</td>
</tr>
<tr>
<td>Total</td>
<td>274.9</td>
<td>100</td>
</tr>
</tbody>
</table>
In comparison with Canada the Singapore government relies heavily on custom duties and non-tax items for its revenue. The bulk of the custom duties was collected from three categories of goods: tobacco, petroleum and liquors which account for 13.5, 12.4 and 8.7 per cent respectively of the total revenue.

As can be seen from the percentage distribution, corporate income tax accounts for only 10.8\% of the total revenue. Since partnerships are taxed as personal income, total tax from business enterprises as a whole should be around 20\% although the annual report of the Inland Revenue did not undertake to give a breakdown.

The figures given in page 38 represent the entire revenue of the government of Singapore in 1959. There are no provincial taxes like those of Canada. Largely because of the size of the economy, and land area, the tax structure (both direct and indirect taxes) is relatively unsophisticated. There is also no sales tax. Excise tax is minimal and is levied only on locally produced stout and beer. This is in contrast to a country like Canada where a review of the sources of Federal government revenue shows that more than 27.1\% of the total revenue is derived from sales and excise taxes in 1966-67.

The heavy reliance on import duties on three products may be due to ethical reasons or to the fact that it is easier and administratively less burdensome to collect.
In any event, the revenue structure shows that the introduction of the incentive schemes to be discussed later in the chapter will have relatively less impact on total government revenue than otherwise might be the case since company tax accounts for a relatively small share of the total revenue. This is true at least in the short-run.

Income tax in Singapore is levied under the provisions of the Income Tax Ordinance (Chap 166 of 1948) which has been amended by various amendment ordinances in the course of the years. The following account refers to the provisions up to 1967 as they affect a company without any form of incentives.

Income tax is levied on income accruing in or derived from the State or received in the State from outside sources. Tax is imposed on items normally included in the income tax base, e.g. profits, salary, dividends, rents, interest, discounts, royalties and premiums.

In computing the taxable income of a company, the Ordinance permits deductions incurred to earn the income. Section 14 (1) states:

"there shall be deducted all outgoings and expenses wholly and exclusively incurred during that period by such person in the production of the income"

which includes interest payment, rent, repairs of premises, bad debts which became bad during the year, contributions to pension funds (with certain limitations). Other expenses not specifically mentioned presumably come
within the general provision of S14 (1). There is consequently no detailed listing of deductible expenses as in the case of the Canadian tax act. A great deal of the expenses, including advertising, automobile expenses, research, would presumably be decided by the comptroller. There is, further, no published regulations and explanations to the Ordinance governing the deductibility of many expenses commonly encountered in business operations. S15 ss1(b) lists a few items not deductible; the most important of which are "disbursements or expenses not being money wholly and exclusively laid out or expended for the purpose of acquiring the income". As a whole therefore, the deductibility of business expenses, except those most common items, are subject to whether it falls within the general provisions of S(14)(a) and S15 ss1(b). "Reasonableness" seems to be the test for deductibility. This is further substantiated by S33(1) which reads:

"Where the comptroller is of the opinion that any transaction which reduces or would reduce the amount of tax payable by any person is artificial or fictitious or that any disposition is not in fact given effect to, he may disregard any such transaction or disposition and the persons concerned shall be assessable accordingly".

The only deductible item that is laid out in considerable detail is the capital cost allowance of which the following is a summary (Sections 16 and 19).

(a) **Industrial Buildings**

(i) An initial allowance equals to one-tenth
(10°/o) of the capital expenditure incurred on the construction is allowed in the first year when income is earned.

(ii) An annual allowance of 2°/o of the expenditure incurred for a total period of 50 years. Total deduction in the first year is 12°/o and 2°/o straight line for the remaining 49 years.

(b) **Machinery and Plant**

(i) an initial allowance equals to one-fifth of the capital expenditure incurred in the first year when income is earned.

(ii) An annual allowance calculated at prescribed rates for different types of machinery and equipment. Deduction is computed on a diminishing balance basis on the reduced purchased price of the asset.

The rates differ for different types of assets and range from 5°/o to 20°/o. For the first year, for an asset with a permissible rate of 10°/o, total deduction allowed is 30°/o. Throughout the life time of the asset total deduction is 120°/o of the purchase price of the asset. Similarly for an industrial building the total deduction is 110°/o of the purchase price. It is perhaps true to say that this feature has provided a certain amount of incentive to invest in manufacturing industry since this
sector can reap most from the 120°/o and 110°/o capital allowance. Otherwise, it is true to say that until the first special incentive was introduced in 1959, no special tax incentives existed in the tax structure.

The different rates for different types of assets require the keeping of separate accounts and this, as will be seen in Chapter V is one of the unsatisfactory features in the treatment of capital cost allowance in Singapore.

Section 23 provided for the carrying forward of allowances if in any year of assessment full effect cannot, by reason of an insufficiency of profits, chargeable for that year of assessment, be so deducted during the year. Otherwise, there is no provision for voluntary carrying forward of allowances.

The net balance after deducting what are allowed under the Ordinance is termed assessable income. From this is deducted

(a) "the amount of a loss incurred by him during the year of assessment in any trade, business, profession or vocation, which, if it had been a profit, would have been assessable under this Ordinance" and "the amount of a loss similarly incurred by him in any such trade, business, profession or vocation during any year preceding the year of assessment which has not been allowed against his statutory income of a prior year".(4)

Although the pronoun "he" is used, nothing in the Ordinance precludes a company from deducting losses from its income. In fact this is true in practice. Another
point which is worth noting is that "any trade, business, profession or vocation" in which the taxpayer had sustained a loss is deductible. There is no rule in the Ordinance which forbids a company (incorporated) from taking advantage of this section. However, it is not obvious if this in fact is the case.

(b) gift to approved institutions of a public character.

For a corporated enterprise, after deducting the above items, the balance is taxable income and upon this a tax of 40/o is levied.

Although personal income tax is not within the purview of this thesis, a brief review of it is necessary because of the "integration" of corporate and personal income tax. There is strictly speaking no corporate tax for Singapore residents. The following provisions govern this rule:

"Every company which is resident in Singapore shall be entitled to deduct from the amount of any dividend paid to any shareholder tax at the rate of forty per cent on every dollar of such dividend (5)",

and

"The income of a person from a dividend paid by a company liable to tax under this Ordinance...shall, where any such tax has been deducted therefrom, be the gross amount before making such deduction; where no such deduction has been made the income shall be deemed to be such a gross amount as after deduction of tax at the maximum rate deductible at the date of payment would be equal to the amount received (5)."
The operation of the above provisions is best illustrated by an example.

Assuming that a company has income before tax of $100,000 then:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income before tax</td>
<td>$100,000</td>
</tr>
<tr>
<td>Tax at 40%</td>
<td>$40,000</td>
</tr>
<tr>
<td>Income after tax</td>
<td>$60,000</td>
</tr>
</tbody>
</table>

When the after-tax income is distributed the company would notify the shareholders thus:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividend</td>
<td>$100,000</td>
</tr>
<tr>
<td>Less tax paid at source</td>
<td>$40,000</td>
</tr>
<tr>
<td>Net dividend</td>
<td>$60,000</td>
</tr>
</tbody>
</table>

For simplicity, assume that the shareholder operates the company with his wife as the other shareholder and in managing the business he draws $10,000 as salary during the year. His tax liability would be as follows, assuming he has no other dependents than his wife:
Salary  
Gross up dividend  
Total income  
Less allowance:  
  Personal  
  Earned income  
Assessable income  
Tax payable  
Tax paid at source  
Balance of tax to be paid  

The above feature will have an influence on the incentive provision to be discussed later in this chapter.

It should be noted that the total amount of tax the taxpayer paid is independent of the corporate tax rate. If the marginal rate of the shareholder is between 41 and 50 percent (50% is the maximum personal income tax rate) there is an incentive to retain profits in the corporation. Section 30, however, allows the comptroller to treat certain undistributed profits as distributed if distribution can be made "without detriment to the company's business". However, unless the company is a family affair, management is unlikely to be able to take into consideration the marginal tax rates of the individual shareholders.

Non-resident individuals are taxed at the rate
of 40\% without personal allowance although British subjects or British Protected Persons may be entitled to a deduction of a proportionate allowance. This rule apparently does not apply to dividends since the deductibility of the amount of tax paid at source discussed earlier renders the total tax liability of a non-resident equal to a maximum of 40\% of income.

The above discussion is the operation of the company income tax law that is applicable to an ordinary manufacturing and trading company. All the companies established up to 1959 and all non-pioneer companies (to be discussed later) still operate under these general provisions of the tax law.

One important feature of the Singapore legislation is that a great deal of the definitions are left to the comptroller. The rules as a whole are extremely general in nature. This is rather unsatisfactory because it can easily lead to a wide divergence of opinion, and interpretation. Furthermore, the Inland Revenue Department has thought fit to keep all disputed cases confidential. As a result, a useful source of information on the interpretation of some of the important provisions is not forthcoming.

II. INCENTIVE LEGISLATIONS INTRODUCED IN 1959 AND 1960's

For ease of exposition the legislations will
be discussed in the following order:

(a) Legislation that affects the computation of taxable income:

(i) accelerated depreciation allowance
(ii) Double deduction of market development expenditure

(b) Legislation that exempts wholly or partly the tax assessed:

(i) Pioneer Industries Ordinance
(ii) Foreign loans for productive equipment
(iii) Royalties and technical assistance
(iv) Expansion of established enterprises
(v) Production for export

These will be discussed in turn in the order outlined above.

(1) Legislation that affects the computation of taxable income

(1) Accelerated depreciation allowance

This provision was introduced in 1965 immediately after Singapore ceased to be a state in the Federation of Malaysia. The economic conditions then were not particularly conducive to investment. With the prospect of a common market with Malaysia vanished into thin air, the government introduced a series of incentive legislation in 1965-1967 to attract capital into manufacturing
industry to supplement the Pioneer Industries Ordinance (1959) to be discussed below.

An accelerated depreciation allowance (which in effect means capital cost allowance) was introduced in 1965 to assist any industry that utilise "prescribed plant and machinery". This Section (Section 19A), is not applicable to pioneer industries. Under this section if a person proves to the satisfaction of the comptroller that he is carrying on an industrial enterprise (exclusive of pioneer industries, utilities, storage and trade) he can be entitled, for a period of three years to an annual allowance of 33 1/3% in respect of the capital expenditure incurred, on or after the first day of January 1965, on the provision of machinery or plant for the purposes of that industrial enterprise in lieu of the normal initial and annual allowances discussed earlier.

It is not clear what industries will qualify under this provision. To the writer's knowledge only one firm had been granted this privilege by 1966. Furthermore, since most industries that can profitably be established in Singapore, can qualify for pioneer status, this provision cannot be of general applicability. It appears that this provision is meant for a company that cannot qualify under any other incentive provisions but
needs nonetheless some form of inducement or assistance. It is also to be noted that the capital cost allowance is limited to 100\% of the cost of the asset. The benefit is a complete write off of the cost of machinery and equipment in three years. This provision as a whole needs elaboration. Its benefit to an investor depends on the person proving "to the satisfaction of the comptroller" that he is operating an industrial enterprise, which is not difficult. But to prove that he qualifies for such concession is not easy for there is a total lack of a definition of what industries can qualify—a rather unsatisfactory state of affairs.

Section 19, subsection 2 provided further that the comptroller may, in his discretion allow a higher rate than that prescribed. Referring to this section the Minister of Finance said in his budget speech of December 1966: "The government may approve on application special accelerated initial depreciation (allowance) up to 100\% in one year."(7) Again it is not known what industries are likely to qualify. It appears that the extent of the benefit under the accelerated depreciation allowance provision depends on the merit of individual cases. Unless the circumstances under which
these provisions are operative are specified, at least broadly, the incentive effect will be minimal.

Section 23 of the Income Tax Ordinance allows the carrying over of the uncharged allowance to future year(s) if in the year of assessment the profit or gain is insufficient to permit the total allowance for the year to be charged off completely. Hence to get the best out of this incentive, a company must earn sufficient profits in the first three years.

(ii) Double deduction of market development expenditure

In recognition of the fact that the Singapore domestic market is limited and of the need to export, Section 14B was enacted. The purpose of this section may perhaps be best understood if a few points about Singapore's economy are recapitulated:

(a) a population of two million can hardly be considered adequate to provide a sufficiently large market for efficient utilisation of modern technology in production.

(b) Being new to the field of industrialization and having to compete with the industrially advanced countries in the export market, Sing-
apore companies face competitive disadvantages.

(c) Because of a lack of domestic natural resources, Singapore must import the necessary raw materials for the expanding industrial sector (besides machinery and equipment). The need to earn foreign exchange and to maintain its international balance of payments healthy is therefore obvious.

It was under the shadow of these economic conditions that Section 14B was introduced together with the accelerated capital cost allowance discussed earlier.

Section 14B states that where a market development expenditure is incurred on or after January 1966 by an "approved market development enterprise" it shall be entitled to "a further deduction equal to the amount of such market development expenditure in addition to the deduction allowable under Section 14 of this Ordinance"\(^{(8)}\) (Section 14 permits the deduction of expenses incurred in the production of the income). This amounts to a 200 per cent deduction of the market development expenditure.

"Approved market development enterprise" means an enterprise approved by "an order made by the Minister". The amount of the market develop-
ment expenditure allowed for double deduction is to be the average sum "incurred in direct advertising in recognised media for the three years immediately preceding the basis period for the year of assessment in which the deduction is claimed". For an enterprise that has been in operation for less than three years the amount deductible is to be calculated on a pro rata basis.

To qualify for double deduction, the expenditure should have been incurred "primarily and principally for the purposes of seeking opportunities or in creating a demand "for goods which have been manufactured, produced or assembled in Singapore either for local consumption or for export. However, for an expenditure for local consumption the deduction allowed is limited to 50% of the excess of expenditure in a year in question over the average of the preceding three years or $M 100,000 which ever is less. For an expenditure on export promotion, which includes sample, advertising, travel expenses and market research the additional amount is limited to 100% of the expenditure.

It appears that for local promotion no double allowance will be given to expenditures on samples or market research since these expenditures
for export promotion are specifically mentioned where for local promotion only advertising is mentioned.

The time period during which the approval will be operative is subject to what the minister "may think fit to impose".

This provision can be seen to be an attempt to promote locally manufactured products. The provision is quite generous for any export promotion for double deduction can be claimed for advertising of goods "which have been manufactured, produced, assembled, processed, packed, graded or sorted in Singapore". Hence this double deduction is not confined to goods manufactured in Singapore. For local promotion, however, the double deduction is limited to locally manufactured or processed goods.

(2) Legislation that exempts wholly or partly the tax assessed

(1) Pioneer Industries Ordinance 1959(9)

The first legislation to provide incentive to manufacturing industries. The purpose of the Ordinance is succinctly summarised as follows:

"An Ordinance to make provision for encouraging the establishment and development in Singapore of industrial enterprises by way of relief from income tax". (10)
This was the first major step taken to offer tax concessions to attract foreign and domestic capital into manufacturing industries. When it was first introduced in 1959, a company operating under this Ordinance receives full tax exemption for five years. The Minister may declare any industry a "pioneer industry if he is satisfied that such an "industry is not being carried on in Singapore on a scale adequate to the economic needs of Singapore and that there are favourable prospects for the establishment of such industry". Since the industrial base of Singapore in 1959 was very small, products declared pioneer have been rather extensive and undiscriminating at times. Few studies were made to determine if a particular product truly possess "favourable prospects" for this industry to be established. Since 1959, a total of some 100 industries and 347 products have been declared pioneer. Products covered ranged from ready-made garments to shipbuilding and petroleum products. Any firm producing a pioneer product may be considered for pioneer status regardless of the country of incorporation and regardless of ownership. A breakdown of the total pioneer firms established up to 1965 shows that 21 of the 114 firms established have complete foreign ownership and control while
have foreign participation\(^{(12)}\) to a certain extent. In all, 65\(^{0}/\)\(^{0}\) of the firms have foreign participation either wholly or partly.

From 1959 to 1965 the tax exemption for any firm qualified for pioneer status was five years regardless of the amount of capital expenditure and regardless of other conditions. In 1965, in conformity with the existing Malaysian legislation\(^{(13)}\) the tax exemption period was amended as follows:

(a) Two years where a firm's fixed capital expenditure is less than $M 250,000.

(b) Three years if the fixed capital expenditure exceeds $M 250,000 but not more than $M 500,000.

(c) Four years if the fixed capital expenditure exceeds $M 500,000 but not exceeding $M 1 million.

(d) Five years if the fixed capital expenditure exceeds $M 1 million.

The exemption period is to commence from the day the firm begins to produce the pioneer product in "commercial quantity", and will continue for the period as stated above.

Further, the income of the pioneer enterprise in respect of its exempted income is to be ascertained without making any deductions with respect to capital cost allowance. Capital cost allowance (both initial and annual) will be avail-
able to reduce tax payable after the tax exemption period, though this was not spelled out in the Ordinance of 1959. In effect therefore, the benefit of pioneer status is extended to the first few taxable years of the enterprise.

It should also be noted that because of the integration of the corporate and personal income tax discussed earlier (pages 44 to 46) such tax exemption under pioneer status would be nullified if the dividend from such pioneer enterprise is included in the personal income of the individual shareholders and taxed at the personal rates. To achieve complete exemption Section 13 of the Pioneer Industries Ordinance rules that the tax exempt income need not be included in the income of the shareholder when computing his total income. This provision applies to both resident and non-resident shareholders.

Lastly, if a pioneer enterprise incurs losses during the tax relief period, such losses shall be allowed to be carried forward to be set off against profits in after-tax relief periods. The effect of this provision is to reduce further the tax burden of a new enterprise even after the tax exemption period. The total losses for the tax exemption period is the amount by which total
loss exceeds income in the exemption period.

(ii) **Foreign loans for productive equipment** *(14)*

This provision introduced an exemption from tax on non-residents deriving income from a loan to a resident company. A resident may apply for such special concession if the following conditions are fulfilled:

(a) That it engages in any manufacturing industry.

(b) That the amount of loan (which should not be less than $820,000) be raised from a non-resident and used to purchase production equipment for the purpose of the company's trade or business.

If the above conditions are met and if the comptroller is satisfied that the exemption of tax on the interest paid to a non-resident would not result in an increase in his tax liability in his country of residence, the interest so paid on the loan is to be exempted from tax.

Where this exemption applies, the company concerned, when it pays such interest, will not, in computing its income, deduct the interest so paid, but will only have to submit to the comptroller a statement of the amount which would otherwise be deductible.

(iii) **Royalties and technical assistance** *(15)*

The question of royalties and technical
assistance was brought into the income tax law in 1967 for the first time. This section introduced in 1967 applies to companies that rely on foreign technical assistance and research. Traditionally royalties and technical assistance payments are deductible in computing income. Under this section only formal agreements between a resident company and a non-resident are qualified. If approved, the non-resident on receiving the payment shall be taxed at 20% on such approved royalties fees or contribution against 40% payable by non-residents not accorded such privilege.

This provision again does not specify what kind of royalties or technical assistance payments will qualify except those where the Minister is satisfied that "it is expedient in the public interest to do so". Furthermore, relief is given only if the comptroller is satisfied that such relief or exemption in respect of approved royalties, fees or contributions does not result in an increase in liability for tax by the non-resident person in his country of residence.

Section 43(2) further extends such privilege to total tax exemption on some royalties, fees or contributions if the Minister is satisfied that
"it is expedient in the public interest to do so". Also, if the fees so received by the non-resident are invested in shares of the resident company, either wholly or partly, that part so invested will be exempt from tax.

(iv) Expansion of established enterprises

Under this provision, if "the Minister is satisfied that the increased manufacture of the product of any industry would be of economic benefit to Singapore" he may declare an industry to be an approved industry and the production of such products of an approved industry may entitle its firms to favourable treatment. Only established companies in such an industry that intend to incur new capital expenditure of either:

(a) More than one million dollar or
(b) where the expenditure is less than $1 million, but exceeds $100,000 and is not less than a 30% increase in value at original cost of all production equipment of the company, are eligible. The tax exemption period on increased profits will be as follows:

(a) three years where the expenditure is less than $250,000 and
(b) five years where the expenditure exceeds $250,000.
The exempted income is to be computed without deducting capital cost allowance. Besides, whether tax relief is forthcoming or otherwise depends on the extent of the new income due to expansion in comparison with the pre-expansion income.

(a) Where the pre-expansion (or pre-relief) income equals or exceed the expansion income no relief will be given.

(b) Where the expansion income exceeds the pre-relief income the amount of the excess shall be allowed as a deduction but the deduction allowable shall not exceed the sum which bears the same proportion to the expansion income as the new capital expenditure on productive equipment expenditure and the value at original cost of the productive equipment owned and used by the expanding enterprise prior to its expansion (Section 19 (5) (b)).

An example will perhaps clarify this second condition. Assume the following:

- Pre-expansion productive equipment owned by the firm at original cost: $1,000,000
- Pre-expansion income: 500,000
- New equipment added: 800,000
- Total income after expansion: 1,000,000
Then (i) the income eligible for exemption

\[ = 1,000,000 - 500,000 = 500,000 \]

(ii) New capital expenditure as a proportion of existing capital

\[ \text{equals} \frac{800,000}{1,000,000} = \frac{4}{5} \]

(iii) Therefore exemption limited to

\[ 500,000 \times \frac{4}{5} = 400,000 \]

Clearly, the lower the pre-expansion capital investment and income the larger will be the tax exemption.

Section 6 limits the total amount of exemption to 100\(^\circ\)/o of the expansion income if the company qualifies under other incentives (e.g. under pioneer status, or export incentives (to be discussed below).

(v) Production for Export

The Minister may under this provision declare a product manufactured in Singapore or deep-sea fisheries to be an export product if it is deemed "to be in the interest of the public".

To qualify the export sale of an enterprise (value at f.o.b.) should in the first year be not less than:

(a) 20\(^\circ\)/o of the total value of its sales and
(b) in any case not less than $8100,000.

The tax relief period on export profit is to continue for:

(a) 15 years for an enterprise that is not a pioneer enterprise or,

(b) where the enterprise is a pioneer enterprise, the period commences from its export year\(^{(16)}\) or, if the export year falls within the period of tax relief under pioneer status, the start is from the commencement of the taxable year (i.e. the first year after the tax exemption period under pioneer status) and is to continue for such period which together with its tax relief period under pioneer status, extend in the aggregate to fifteen years\(^{(17)}\).

In other words the total exemption period is limited to 15 years. The income of an export enterprise to which the provision applies is to be computed without making a deduction of a capital cost allowance.

To reduce the problems of allocation of expenses between the export and domestic markets, Section 28 (2) in essence defines profit on export to be:

\[
\text{Export profit} = \text{total profit} \times \frac{\text{total export sales by value (fob)}}{\text{total sales by value}}
\]
Sections 29(3) and (4) limits the amount of export profit qualified for exemption. The limit is based on the principle of (a) established export market and (b) new export market. For a company exporting to a "established market" the preferential treatment is extended to only the excess of such profit over a fixed sum to be determined in the following way:

(a) in the case of a company which has been previously exporting to this established market the average annual export profit of the company for the five years ending 31st December 1965.

(b) In the case of a company which has not been exporting prior to 31st December 1965 the fixed sum will be determined by the Minister as he thinks fit having regard to the total sales of the company and the performance of other companies that had exported to this established market.

For a firm exporting to a country which is not established market the whole of its export profit arising out of the export of such approved products will qualify for relief.

Section 29 (1) further limits the tax relief by the following conditions:
(a) For the first year of assessment the export sales in the basis period should amount to not less than $20\%$ of the total sale in value and in any case not less than $3100,000.

(b) For each subsequent year of assessment the export sales should not be less than $5100,000 in value.

The first year in which the tax relief is to begin (called the export year) will be when the minimum requirement of (a) and (b) are met. In subsequent years, relief is given only when (b) is met. However, the Minister has the power to grant such relief even if (a) alone is met, if after consideration on application he is satisfied that such relief is "reasonable and expedient in the public interest to do so" (Section 29(2)).

When the relief is established, $90\%$ of the export profit will be exempted from tax and only the balance of $10\%$ is taxable.

For all the tax exempt income qualified under the various schemes, (pages 54 to 65) any dividend declared out of the tax exempt profit is not taxable in the hands of the shareholders.

III. SUMMARY

The above is a brief review of the Singapore corporate income tax legislation. In the course of
exposition it is noted that many of the items in the
tax legislation were not well defined. The definitions
of some of the important provisions are left to the
comp’reller and the Minister for whom the guiding prin­
ciple is "public interest". This appears to be a rather
nebulous concept. This feature prevails in practically
all the incentive legislation. In Chapter VI there
will be a discussion in detail of what are thought to
be some of the short-comings and implications of the
incentive provisions.
CHAPTER REFERENCE


(2) Includes $20.0m from government undertaking of a commercial nature and $17.7m rental of government properties and investment.

(3) All disputed cases are referred to an Appeal Board which conducts hearings in private and keeps its findings confidential. Consequently, it is not possible to learn how the two sections are applied in practice. See Part XII, Section 78, Income Tax Ordinance.

(4) Section 37(2)(a) and (b).

(5) Section 44, op cit.

(6) Section 29, op cit.


(10) Op cit.


(12) Participation is taken to mean share ownership.

(13) Income taxation was a federal matter when Singapore was a state in Malaysia from September, 1963 to August, 1965.

(14) Economic Expansion Incentives (Relief from Income Tax), Bill Supplement, Republic of Singapore, Government Gazette, No. 8, November, 1967, Section 36.
This provision, besides all the remainder in this chapter has yet to be incorporated into the Income Tax Ordinance. However, these provisions are made retroactive to January 1966.

(15) Section 40, op cit.

(16) Export year means the first year the company meets conditions (a) and (b) above.

(17) Section 23(1)(b), op cit.

(18) Established export market is taken to mean a country to which any approved export product has been exported continuously by any Singapore manufacturers in such volume as the Minister may determine for a period of five years immediately preceding 1966.

(19) The year in which the tax liability is assessed is the assessment year and the basis year is the year in which the income is derived. Hence tax assessed for 1968 will be on the income of 1967, the basis year of assessment 1968.
CHAPTER IV

CANADIAN FEDERAL CORPORATE INCOME TAX

The Canadian Federal income taxes are levied on individuals and corporations. As the central theme of this thesis is corporate income tax no detailed discussion on personal income tax will be entered into except in so far as it affects the analysis of particular corporate tax incentives. Briefly, the following topics will be discussed in this chapter:

(I) A general introduction to Canadian corporate income tax legislation without any specific attention being given to incentive provisions.

(II) Incentive measures operating through an increase in deductible expenses, e.g. accelerated depreciation, double deduction of depreciation, etc.

(III) Incentive measures which operate through an exemption of tax on taxable income or lower rate of tax on taxable income.

(IV) Incentive measures by way of financial assistance in the form of grants.

(V) Withholding tax.

and

(VI) Some "disincentive" legislations.

I. A GENERAL INTRODUCTION TO CANADIAN CORPORATE INCOME TAXATION

The Canadian corporate income tax is charged against total profit "wherever earned". Income for a
taxation year from a business is the profit therefrom for the year. Generally speaking the rules in the Income Tax Act for the determination of the profit to be used as a base to determine an income tax liability follow quite closely the accounting concept of profit determination.

For an understanding of the items of expenses that are deductible, and those that are not, it is important to distinguish between items that may be deducted in computing income and those that are deductible from taxable income. The incentive provisions that were introduced in the 1960's operate through both categories of deduction, namely as expenses and as tax exemptions.

Generally, deduction from revenue to compute taxable income of a business must meet three conditions:

(i) No outlay will be allowed if it is "an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by the other section of the Act". (1)

(ii) No deductions will be allowed in computing income except "an outlay or expense... to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer" (2) and

(iii) "In computing income, no deductions shall be made in respect of an outlay or expense otherwise
deductible except to the extent that the outlay or expense was reasonable in the circumstance."(3)

Paragraph (i) above specifically prohibits therefore a company to deduct capital outlay except depreciation and depletion which are expressly permitted under Section 11 and Part XII of Income Tax Regulations.

Paragraphs (ii) and (iii) are general tests of deductibility of a business expense and the ordinary rule is "reasonableness" in the circumstances.

Section 11 of the Act specifically allows a list of items of business expense to be deducted. However, through the passage of time and practice, normal expenses of a business constitute proper deductions and the moot point are confined to a few items which are singled out for consideration below largely because it is through these special items that legislated incentives were implemented.

(i) Depreciation allowances

It must be noted that the amount deductible under the Act differs from the accounting concept of depreciation. For tax purposes, the term "capital cost allowance" is used. The deduction permitted under Section 11(1)(a) does not follow the common business practice of calculating depreciation for computation of the business income. The Income Tax Regulations Schedule B divides the
various assets of a company into a comparatively small groups or classes. It further specifies the maximum rates of allowance for assets of designated classes. Generally the rates appear quite generous and range from 4°/o for Class 1 (largely fixed long-lasting properties like bridges and roads) to 100°/o for Class 24, (an incentive item for the elimination of industrial wastes). Classes 19 to 22 are incentive items to be discussed below. The highest rate for an ordinary company without incentive is class 12 (100°/o) which covers fragile items and small tools. For an industrial company, the diminishing balance method must be used to compute the maximum amount of depreciation allowed in a given year. It is computed on the balance outstanding (undepreciated) in the class concerned. The class system eliminates the necessity to keep a separate account for each asset. The following classes are of special interest in this study:

Class 3 (5°/o) which covers industrial buildings of brick.
Class 6 (10°/o) which covers buildings of light material like log, galvanised iron etc.
Class 8 (20°/o) which covers tangible capital assets and other assets not included in other classes. Most machinery and equipment for manufacturing industry fall within this class.
As mentioned earlier the annual charge for capital cost allowance is calculated on the basis of the balance in a pool at the end of the year. The amount in the pool for a particular year is increased by new purchase and reduced by sales of assets. Each pool corresponds to each class of asset. The percentage is applied to the undepreciated balance to determine the maximum amount deductible for the year. But a company has the option not to claim the maximum amount for any one year. The amount a taxpayer refrains from claiming in any one year is automatically carried forward to be deductible in subsequent years. Furthermore, the taxpayer is not required to equate the deduction to the useful productive life of the assets except that total deduction is limited to the cost of the asset.

Apart from the rates structure for allowances, which are considered to be reasonably generous, no specific allowances were in force prior to 1960 to encourage the development of secondary manufacturing industry. As matters stand in 1960 only the extractive industries were given special incentives. Although oil, gas and mineral extraction proper is not considered to be manufacturing, the processing of such materials is however included under primary manufacturing and hence require our attention. Also, many oil, gas and mineral refining companies are in fact the operators of oil and gas wells, and as such receive concessions that are available
to oil, gas and mining companies.

The above analysis represents the broad structure of the Canadian corporate income taxation in so far as it affects the central theme of the thesis. It will be helpful at this stage to see how the income of a corporation is treated by the tax authorities in the hand of the shareholders.

Assume that a company has an income before tax of $100,000, then:

Income before tax $100,000

Tax at
21°/o on first 35,000 7,350
51°/o on 65,000 13,150 41,500

58,500

Let us further assume that all the after tax income of the corporation is distributed to the shareholder and his wife, the only two shareholders in the corporation. Further, assume that during the year the shareholder drew $10,000 as salary. His tax liability can be determined as follows:

Salary $10,000
Dividend 58,500
Total income 68,500
Less personal allowance 2,000 66,500

Tax thereon 30,970
Less dividend credit (20°/o) 11,700

Net tax $19,270
It can be seen that the dividend of credit does not compensate fully the tax paid at corporate level. If however, the corporate income is $35,000 or less a higher proportion of the tax paid at corporate level is credited as the following example will show.

Let us assume that the conditions of the shareholder is as above except that the corporate income before tax is $35,000.

Then

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate income before tax</td>
<td>$35,000</td>
</tr>
<tr>
<td>Tax at 21°/o</td>
<td>7,350</td>
</tr>
<tr>
<td>Income after tax</td>
<td>27,650</td>
</tr>
</tbody>
</table>

When the shareholder receives the dividend his net tax liability is as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salary</td>
<td>$10,000</td>
</tr>
<tr>
<td>Dividend</td>
<td>27,650</td>
</tr>
<tr>
<td>Total income</td>
<td>37,650</td>
</tr>
<tr>
<td>Less personal allowance</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td>35,650</td>
</tr>
<tr>
<td>Tax thereon</td>
<td>13,895</td>
</tr>
<tr>
<td>Dividend credit (20°/o)</td>
<td>5,530</td>
</tr>
<tr>
<td>Net tax</td>
<td>$ 8,365</td>
</tr>
</tbody>
</table>

Hence in the first case dividend credit is 27.6°/o of the corporate tax. In the second case it is 75°/o.
II. INCENTIVE MEASURES OPERATING THROUGH AN INCREASE IN DEDUCTIBLE EXPENSES

(1) Accelerated write-off of expense of resource industries

The concessions to the resource industries operating through accelerated deduction are contained in Section 83A of the Act.

Section 83A allows, in the computation of the income of a mine or gas or oil company, certain accelerated deductions with respect to exploration, prospecting and development expenses which would normally constitute capital expenditure and would not therefore be allowed under Section 12(1)(b).

(a) Oil and gas company

For an integrated oil or gas company whose business includes the production and refining of, as well as exploring or drilling for, petroleum or gas, allowance is made to deduct, in computing income:

(1) "An amount up to the aggregate of its drilling and exploration costs, including all general geographical and geophysical expenses incurred during and after 1949 on or in respect of exploring or drilling for petroleum or natural gas in Canada" and

(2) Prospecting, exploration and development expenses in search of minerals in Canada.

A company may also deduct expenses incurred in prior years to the extent that they were not previously deducted. The limit deductible in a given year is the income of the year.

In 1959, the concession was extended to
companies marketing the product of these resources. Further, it is worth noting that since 1953, oil and gas companies are allowed to deduct expenses incurred in search for minerals in Canada and vice versa for mineral companies\(^6\).

Income for purposes of determining the amount deductible is computed before depletion allowance (to be discussed, see pages 91-93) and net of any non-taxable dividend received from other corporations. Similarly, by using the term "income" rather than "taxable income" the law precludes in effect the deduction of losses sustained in prior or future year(s) until income equals or exceeds the drilling, exploration and development expenses are met.

(b) **Mining Companies**

For a company whose principal business is mining, exploring for minerals or the prospecting of mineral and metals, the general rule is that such a company may deduct such exploration, prospecting and development expenses in the year of occurrence. Since it is unlikely that a company can produce an income in its earlier years of operation such expenses may be postponed for several years until there exists sufficient income to enable these expenses to be deducted. Hence, the deduction
in a given year may have been incurred in prior years or in the current year. Such concession is applied to all prospecting, exploring and development expenses incurred by a company in Canada.

A 1956 amendment allows a company to deduct a predecessor's expenditure on exploration, drilling and development expenses provided its principal business is as defined above.

For companies whose principal business is not mining or exploring for minerals but the working of coal-mines and other non-bedded deposits the above allowance does not apply. However, concessions are granted by Section 1205 of the Income Tax Regulations which allows a 25\% deduction of the preproduction expenses reasonably attributable to prospecting, exploring for, and development of a mine that later came into production in commercial quantities.

The total allowance is to be calculated as the aggregate of all outlays reasonably attributed to prospecting, exploring and development prior to production less

(i) any outlay in respect of which a deduction is allowed under Section 83A,

(ii) any expenditure deductible in the year of occurrence,
(iii) cost of property which capital cost is allowed under Section 11 of the Act, and

(iv) the cost of leasehold interest.

The total deduction is spread over four years.

(2) Accelerated depreciation to assist new industry with a degree of Canadian ownership and industry established in designated areas.

The accelerated depreciation provisions introduced in the 1960's were meant to meet the economic conditions of the 1960's. As was noted in Chapter II the rate of growth in the Canadian economy slowed down considerably in the late 1950's. Unemployment had increased to 7% by the end of 1960, and excess capacity existed in manufacturing industry largely due to foreign competition and lack of export opportunities. As noted earlier a great deal of the difficulties of the Canadian manufacturers can be traced to an excessive premium on the Canadian dollar. In any event, in the supplementary budget of December 1960, a few incentive provisions, rare in Canadian tax history were introduced. One of these measures was the accelerated depreciation allowance for new industries in designated area.

(a) Accelerated depreciation for industry in designated area (1960 enactment)

In the supplementary budget of December
1960, the Minister for Finance observed that the purpose of this incentive measure was first "to assist new industries in areas where there is a substantial degree of continued unemployment over the years, second, to aid the development of new products from processing operations not hitherto carried on in Canada, and third, to encourage the production of new types of goods." Double depreciation will, at the option of the taxpayer be allowed in respect of capital expenditure incurred in the first year for these purposes but may be applied in any of the first three years. The program is to run for 2 years commencing January 1 1961."(7)

The Minister was criticised for not specifying the types of industries and the "designated areas" he had in mind. In any event the concession was not extensive. Double depreciation was available only in the first year, though it might be taken in subsequent year(s). For most manufacturing industry, hence, the first year's rate of capital allowance was 40% for machinery and equipment. Presumably for the second year the rate reverts back to 20% on the balance of cost incurred. Investors must invest in the two years period to be eligible and total depreciation was limited to the cost of the capital asset. It is, in other words, a speed up in timing of depreciation.

(b) Acceleration depreciation for re-equipment and modernization of machinery and building (1961)

In 1961 special legislation was introduced
to encourage the re-equipment and modernization of machinery, equipment and buildings. Under the new legislation there was allowed a 50% increase in the first year in the rates of capital cost allowance. These rates were to be applied to the excess of the company's expenditure in a fiscal period over that of the average of the two immediately preceding years. The Minister, in moving the bill in the House of Commons contended that only expenditures in excess of those in a recent base should be eligible because he was "attempting to establish a rule by which to make this valuable concession available to those who are genuinely increasing the level of their investment in new depreciable assets but not to that large total of depreciable assets most of which would have been acquired in any event". But the question is how the government can distinguish between those genuinely increasing the level of investment and those that "would have been acquired in any event". Also, the total depreciation was limited to the cost of the machinery. The only benefit is the timing of deduction of depreciation. It is difficult to discern from this argument of the Minister for Finance the extent of the application of this new proposal. Further, this provision was to last for two years to March 31, 1963, but subsequently
extended to January 1, 1964.

(c) Accelerated depreciation for industry with a degree of Canadian Ownership (1963)

In 1963 a new accelerated depreciation allowance was introduced to replace the allowance discussed above. This new concession was to be effective from June 14, 1963 to January 1, 1967—a period of three and a half years. Classes 19, 20 and 21 were subsequently created in the Income Tax Regulations to effect this new feature in the Canadian income tax law.

Part XI of the Regulations states that

(a) where the taxpayer is a corporation that had had a degree of Canadian ownership in the taxation year, or is an individual who was resident in Canada in the taxation year for not less than 183 days, such an amount as he may claim in respect of property of class 19 in Schedule B that was acquired in a particular taxation year not exceeding the lesser of

(i) 50% of the capital cost thereof to him or
(ii) the amount by which the capital cost thereof to him exceeds the aggregate of the amounts deducted in respect thereof in computing his income for previous taxation years but the aggregate of amounts deductible for a taxation year in respect of property acquired
in each of the particular taxation years, under this paragraph, shall not exceed the underpreciated capital cost to him as of the end of the taxation year (before making any deduction under this subsection for the taxation year) of property on the class.

Schedule B clarifies the conditions for such concessionary rates (besides the Canadian ownership requirements) to be:

(a) The property must be acquired by the taxpayer between the period June 14, 1963 and December 31, 1966.

(b) The property must be those assets falling within Class 8 of depreciable property which refers specifically to machinery and equipment.

(c) The property must be new.

(d) The property must be acquired for use in Canada by a company whose business must not be the operation of a gas or oil well, logging, mining or concentration or any combination of these businesses. In other words the privilege was available to only secondary manufacturing industry.

(e) Furthermore, the business must

   (i) for the fiscal period in which the property is acquired or

   (ii) for the fiscal period in which the business
first commenced selling goods in reasonable commercial quantities
be in a business with net sales or rent of goods processed, manufactured plus revenue derived from advertising of at least not less than \(\frac{2}{3}\) of the total gross sales less returns and rebates of the business.

If a corporation cannot fulfill the Canadian ownership requirements, the amount it may claim is of course limited to \(20\%\) of the undepreciated capital cost. It should be noted that if a company qualifies for \(50\%\) deduction, such deduction is \(50\%\) of the capital cost whereas for companies not fulfilling the requirements it is \(20\%\) of the undepreciated asset cost. Hence in the first case, the cost of the asset can be written off in two years on a straight line method of calculation.

(d) Accelerated depreciation for industry in designated areas (1963 enactment)

The above provision applies specifically to Canadian manufacturing companies with a degree of Canadian ownership. But the same privilege is extended to a new manufacturing or processing business operating in a designated area. A designated area is defined in the Area Development Incentives Act (1963). This Act was enacted to assist industry
by way of financial grants if they are established in a designated area (to be discussed later. See page 95). The definition of designated areas in the Area Development Incentive Act is equally applicable to this accelerated depreciation provision. This concessionary depreciation allowance is applicable to new assets acquired between the period December 5, 1963 and April 1, 1967—a period of almost 3½ years. Manufacturing or processing business in the context of the Area Development Incentives Act is taken to mean

"A business that had net sales for the fiscal period in respect of which the expression is being applied from the sale of goods processed or manufactured in Canada by the business, the amount of which was at least 95% of the amount by which the gross revenue from the business for the period exceeds the aggregate of each amount paid or credited in the period to a customer of the business as a bonus, rebate or discount or for returned or damaged goods"

and new manufacturing or processing business is meant,

"a manufacturing or processing business that commences manufacturing or processing in reasonable commercial quantities after December 4, 1963 and before April, 1967"(11)

However, the Minister of Industry may allow this privilege to be granted to a firm, for reasons of an event beyond its control, if manufacturing or processing cannot commence during the stated period, provided reasonable preparations had been
made in the stated period for production.

With respect to accelerated depreciation for property falling under Class 3 or 6 (industrial building) Class 20 provides that a taxpayer is permitted to deduct, in computing income, 20% on a straight line method, of the capital cost of a new building or a substantial extension to an existing building in a designated area and acquired in a particular taxation year within the period commencing December 6, 1963 and ending March 31, 1967—a period of approximately 3½ years.

To qualify the following conditions must be fulfilled, besides the date of acquisition:

1. It must be a building or an extension of building and that the aggregate cost of the extension exceeds the lesser of
   a. $100,000 or
   b. 25% of the capital cost to the taxpayer of the building on December 5, 1963

and must be certified by the Minister

3. to be situated in an area that was a designated area and must have not have been used for any other purpose whatever before and

4. the capital cost must be those approved by the Minister under the Area Development Incentives Act.
As noted above the acceleration provisions for machinery and building were introduced in 1963 when the Canadian economy had not shown sufficient resilience to recover from the depression of the later 1950's and early 1960's. Unemployment was still high. The Minister contended that the tax measures were "to encourage employment by reviving private capital expenditures which have lagged so conspicuously for the past six years". These incentives were directed at solving the unemployment problem by encouraging investments in areas of slower growth and surplus manpower.

(3) **Accelerated deduction of scientific research expenditure**

It has been noted in Chapter II that to increase the productivity of the Canadian manufacturing industry more research has to be done in Canada. This was emphasised by the Minister of Finance in 1961. Prior to 1961, for a manufacturing company, deduction was allowed for scientific research expenditures incurred in Canada subject to certain limitations. The law relating to the deduction of scientific research expenditures was spelt out in Section 72 11(1) of the Act. Briefly, expenditures are classified under two categories:

(a) Research expenditure of a "current nature" and
(b) Research expenditure of a "capital nature".

For (a) deduction was allowed in full in the year in which the expenditure was incurred. Item (b) excluded land and cost of acquisition of right, such as patent rights accruing out of a research project. The legislation for the deduction of expenditure of a capital nature was summarised by the Minister of Finance as follows:

"The income tax act now provides that expenditure of a capital nature made on scientific research in Canada may be fully written off in three years. The Act now provides that amounts deducted under the provision dealing with scientific research, shall be limited to 5% of the taxpayer's previous year's taxable income unless the research program has been approved by the Minister of National Revenue with the advice of the National Research Council. Although in practice approval is normally given, I believe that a modification of this requirement will give encouragement and certainty to taxpayers who are planning to increase their scientific research program"(12)

Accordingly, the first modification in the Act to promote scientific research was enacted to allow

(a) a taxpayer to deduct, if he wishes, such capital expenditure in full in the year in which the expenditure was incurred, and

(b) to remove the 5% ceiling on the taxpayer's previous year's taxable income.
Section 72 of the Act was amended to read broadly as follows:

(a) all expenditures of a current nature made in Canada on

(i) scientific research relating to the business of the taxpayer

(ii) payments to approved research institutions on research related to the business of the taxpayer

(iii) payment to a corporation resident in Canada for scientific research and

(b) all expenditure of capital nature related to the business of the taxpayer less any amount of grant paid to the taxpayer under the various grant programs (to be discussed. See pages 96-101) are deductible in the year of occurrence.

Section 72(la) allows expenditures made in the year in respect of scientific research carried out outside Canada if it is expenditure of a current nature made on scientific research related to the business of the taxpayer or payments to approved research institutions to be used for scientific research relating to the class of business of the taxpayer.

In brief, therefore, Section 72 allows all approved expenditures incurred in Canada to be
deductible. But for foreign expenditure Section 72(1a) limits it to current expenditure only, and that in either case, it is not necessary for the taxpayers to conduct scientific research themselves. Payment made to acquire rights resulting from the scientific research such as patent or copyrights are not deductible.

To encourage scientific research in industry, the Minister of Finance introduced in the House of Commons in 1962 an amendment to the Income Tax Act. This subsequently appeared as Section 72A which provides that in addition to the deduction described above under Section 72, a corporation, carrying on a business in Canada, may claim an additional deduction equal to 50% of the increase in expenditure made in Canada over the base scientific expenditure of the corporation. To qualify, such expenditure must have been incurred in the period April 11, 1962 to December 31, 1966. Thus in effect a taxpayer is permitted to deduct 150% of their increased expenditure in scientific research for industrial purpose in the year in which the expenditure is incurred. The use of a base year is, according to the Minister, to "provide a taxpayer with scope to earn substantial tax benefits through increased research". This provision however, excludes market
research. The additional 50% of the increase in research expenditure is equivalent to making a cash grant in support of such research.

The eligibility for deduction of expenditure on research outside Canada was explained by the Minister in 1964 thus:

"For many years companies in Canada have made payments to their parent companies abroad, or to other non-residents for the right to share in the results of research and development programs carried on outside Canada. These long standing arrangements under which Canadian companies have obtained the results of research carried on abroad have provided Canadian industry with valuable process, techniques and know-how and denial of the right to deduct payments for this information would restrict this flow of information with detrimental results for the Canadian economy."

Consequently Section 72(1a) was introduced to clarify the position of firms which had made payments on scientific research abroad. The law was made retroactive to 1962, and applied to only expenditure of a current nature. The double deduction allowance however, was not allowed for payment on scientific research abroad.

III. INCENTIVE MEASURES OPERATING THROUGH AN EXEMPTION OF TAX ON TAXABLE INCOME OR LOWER RATE OF TAX ON TAXABLE INCOME

This group of tax incentive comprise the following:

(1) Depletion allowance for gas, oil and mineral
industries

(2) Three-year exemption on income from new mines

(3) Tax exemption for new industry established in designated areas.

(1) **Depletion allowance for gas, oil and mineral industries**

The depletion allowance with respect to oil and gas and metal mines operate through Section 11(1)(b) of the Act and Part XII of the Regulations. This section applies specifically to what may be termed "wasting asset" industries. The difficulty in applying the concept of depreciation to extractive industry is due to two reasons:

(a) the cost to a company of its ore body or oil or gas reserves is difficult to determine because of the present day practice of paying a modest amount in cash and a block of shares to the prospectors in consideration of the ore body,

and

(b) the absence of data concerning the actual volume of the mineral or reserve under ground or the expected life of the mine.

The depletion allowance is deducted, not for the computation of income as in the case of depreciation, but rather from taxable income itself. The tax authorities
discard completely the idea of relating depletion allowance to the actual amount spent on acquiring the ore body or reserve. A mining company for instance, is given an outright perpetual exemption from tax on a percentage of its profits. The Income Tax Regulations Part XII section 1201 (2) states that for taxpayers in 1960, the depletion was to be related to "the aggregate of his profits for the taxation year reasonably attributable to the production of oil, gas, prime metal or industrial minerals from all of the resources operated by him" rather than to the actual expenditures of the taxpayer. The deduction amounts to 33 1/3\% of the aggregate of the profits less the aggregate of the losses of the taxpayer sustained through the operation of the said mines or wells. The allowance for gold mines being the greater of

(a) 40\% of aggregate profit less the aggregate of the losses of the taxpayer reasonably attributed to the production of mine, oil or gas of the class qualified for depletion allowance or

(b) $4 per oz of the output of gold for the year from the mines operated

if the aggregate output of a mine from which output of gold is not less than 70\% of the total output by value.

The above depletion allowances constitute the few important provisions in the Canadian tax structure and
were designed to make investment in mines, oil wells and gas wells more attractive. Furthermore, in the computation of the income of a mine or gas or oil well, certain deductions are also allowed with respect to exploration, prospecting and development expenses (see pages 76-79) which would normally constitute capital expenditures and are not therefore deductible under Section 12(1)(b).

(2) Three-year exemption of tax on income from new mines

A three-year tax exemption is given to a mine operator for the operation of a new mine. The exemption period begins on the day the mine comes into production in reasonable commercial quantities. (See Chapter VI for a criticism of this provision).

(3) Exemption of tax for new industry established in designated areas

The conditions for tax exemption under this program are identical to that for a grant given to new manufacturing or processing industries in designated areas and the accelerated depreciation allowance for such industries discussed earlier. (see pages 84-87 for accelerated depreciation provisions and pages 95-96 for the provision of grants under the Area Development Incentives Act). The exemption was effective for a fiscal period (or periods) of the new business occuring within the 36 months and commences on the day the new enterprise begins operation in commercial quantities. The program was to run for three
years from June 13, 1963 to June 1966. The machinery and equipment, of which 95% must be situated in the designated area, must be acquired before June 18, 1965.

One important feature must be noted: the effective period of exemption to a new enterprise was a maximum of 36 months. An enterprise which began operation in June 1965 for instance would have only one year of its income exempted from tax.

IV. INCENTIVE MEASURES BY WAY OF FINANCIAL ASSISTANCE IN THE FORM OF GRANTS

With respect to assistance to manufacturing industry the following grant programmes are important:

(1) grants made under the Area Development Incentive Act of 1963.

(2) grants for scientific research under various assistance programs.

(1) Grants to industry under the Area Development Incentive Act

This Act does not form part of the Income Tax Act. Effective July 1, 1965 to March 31, 1971, any industry located in a designated area may apply for such grant in lieu of tax holidays (see page 94).

To qualify, the taxpayer must commence commercial production before the expiration of the program on March 31, 1971. The grant is available to both new industry and the expansion of existing facilities. For
the establishment of new facilities the following formula apply:

(a) $\frac{1}{3}$ of the approved capital cost if it does not exceed $250,000.

(b) Where the approved capital cost exceeds $250,000 but less than $1M the grant is $\frac{1}{3}$ of $250,000 plus $\frac{1}{4}$ on the excess.

(c) Where the approved capital cost exceeds $1M the grant is as (2) above plus $\frac{1}{5}$ of any amount in excess of $1M or $5M which ever is less.

For an expansion of an existing facility the amount of grant is the lesser of

(a) $\frac{1}{3}$ of the capital cost less 10% of the value as determined by the Minister of the existing facility being expanded or $10,000 which ever is greater,

or

(b) $5M.

Such grants are exempt from income tax and a taxpayer may apply the grant against his tax liability. As a condition for the grant the taxpayer must keep the National Employment Service informed of his manpower requirements for a period of five years from the date the last payment of the grant is made.

(2.) Grants for scientific research under the Industrial Research and Development Incentives Act, 1965
Under the IRDI Act industries are given financial assistance in the form of grants for scientific research. These grants are available to resident Canadian companies doing business in Canada. Regulations issued in compliance with this Act stated that "a corporation that applies for a grant shall certify with respect to any scientific research and development...(that)

(a) it carried on all of such scientific research and development for the purpose of strengthening the business of the corporation or facilitating an extension of such business.

(b) It is free to exploit in Canada the result of all of such scientific research and development and

(c) The corporation is free to exploit the results of all of such scientific research and development in all export markets other than the countries referred to in paragraph (d) of Section 3" (16) (which requires the corporation to state the countries in which the corporation is not free to exploit the results of the scientific research and development).

The payment, if approved, will be an amount equal to 25% of the aggregate of

(a) the approved capital expenditure in the period on scientific research and development relating to the business undertaking by or on behalf of the
applicant

and

(b) the amount of eligible current expenditure incurred in the grant period exceeds the average eligible current expenditure by the applicant in its base period\(^{(17)}\)

This incentive by the government was to replace the concessionary rate on writing off of scientific research expenditure discussed on pages 87-91. An approved applicant can utilise the grant or part of it towards settling his tax liabilities.

Section 804 of the Regulation spelt out the items of capital expenditure qualified for grants and items of current expenditure that are not to be included. As a whole, replacement of damaged properties are not included. Eligible capital expenditure is not dependent on an increase in expenditure over the base year. This approach recognises the fact that capital expenditure fluctuates widely from year to year and a grant based on some base period would do injustice to companies incurring heavy capital expenditure in the base year.

(3) Grants for scientific research under the Defence Development Sharing Program and the Defence Industrial Research Program

These two grant programs are of interest to us largely in the indirect effect of the scientific
research projects in promoting the growth of the Canadian manufacturing industry. Grants are normally awarded on the basis of government and industry each sharing equally in the cost expended on research facilities. Firms receiving grants under these two programs must deduct such an amount from the total expenditure on research in computing income under Section 72(1) of the Income Tax Act. Hence only the portion of expenditure incurred by the firm itself is deductible as expenses in computing income.

(4) Grants for scientific research under the Industrial Research Assistance Program

Differs from the preceding program, this program is more relevant to this study as it affects manufacturing industry directly.

Established in 1962 by the National Research Council of Canada. The aim of the IRAP is "to stimulate interest of Canadian industry in scientific research by promoting the establishment of new industrial research teams or the expansion of existing research groups". Its aim is to promote long term research projects in science and engineering. Two important qualifications for approval are:

(a) Only companies incorporated in Canada and doing research in Canada are eligible.

(2) Details of research projects, including the manufacturing and research facilities of the company must be submitted for approval.
Grants may also be given in special circumstances to companies subcontracting approved project to other commercial research organizations. In normal circumstances the share of cost is on the basis of the National Research Council paying for the costs entailed in expenditure on overhead and purchase of equipment and the company paying for remuneration of the scientific and technical staff engaged on the project. For tax purposes, only the excess of the expenditure on research over and above the grants is deductible. Furthermore, such excess also qualifies for a grant under the Industrial Research and Development Incentives Act discussed earlier (see pages 96-98).

(5) Grants for scientific research under the Program for the Advancement of Industrial Technology

Established in 1965 to provide financial assistance to industries for upgrading their technology this program aims at the development of products and process developed, for example, under the preceding program. Only companies incorporated in Canada are qualified for this grant. The research program must be carried out and exploited in Canada to be eligible. It is also required that the applicant company show evidence that it has the capacity and facilities to undertake the development work and also to provide for the manufacture and marketing of the resulting processes.
Subcontracting of research work in special cases are allowed and assistance takes the form of the Department of Industry shouldering 50% of the cost of resources used directly in the project exclusive of any general-purpose capital facilities or facilities in setting up production.

The objectives of the special incentive programs to assist industry in scientific research may be summarised as follows:

(a) to encourage new or small firms to engage in specific research and development;
(b) to assist established firms to expand their scientific research and development activities;
(c) to foster projects which involve high technical risks;
(d) to help obsolescent industry to diversify into more sophisticated forms of production

and

(e) to support co-operative research and development program

IV NON-RESIDENT WITHHOLDING TAX

The taxation of incomes of non-resident earned in Canada has an indirect influence on industrial development. As was noted in Chapter II, Canadian resource and manufacturing industries have considerable foreign parti-
icipation. The treatment of non-resident's income in a country's tax structure is influenced by the tax agreement entered into between the country in which the income is derived and the non-resident's home country. It is not possible to enumerate all the tax agreements Canada has with foreign countries in this thesis. However, because of the overwhelming importance of U.S. capital in Canadian industries the following analysis will refer largely to the treatment of U.S. residents in the Canadian tax structure. In the following study, because of the limitation of space, only factors that are relevant to the development of Canadian industrial potential will be discussed.

It cannot be denied that Canada has benefited substantially from foreign investment. Official pronouncement on this issue has been conflicting at time. Suffice to note here, however, that any changes in the treatment of non-resident withholding tax is bound to affect Canadian manufacturing industry both in terms of capital inflow as well as in terms of technical knowhow and market.

The following was broadly the treatment of non-resident income from industrial undertaking in 1960\(^{(20)}\)

1. **Dividends**
   
   A withholding tax of 15\(^{\circ}/o\) was levied on dividend paid to a non-resident. Dividends of a personal corporation were however, not subject to the 15\(^{\circ}/o\) withholding tax since it was contended that the
total income of a personal corporation was taxed as deemed dividends to the shareholders in the year in which the income was earned and so to levy another tax of 15°/o at the time the earning was distributed would render the same income liable to double taxation.

(2) **Management fee**
Management fees were not subject to withholding tax if they were paid to a non-resident.

(3) **Interest, rents, and royalties**
These items of payment were subject to 15°/o withholding tax.

Hence in 1960 withholding taxes on foreign residents were relatively simple and straightforward. However, with the belief that it is in Canada's interest to moderate the foreign control of Canadian industries, the government introduced a few "disincentives" to foreign investments. In 1961 the following changes were made to the treatment of non-resident income:

(1) The exemption of withholding tax on distribution of branch profit was withdrawn and henceforth all distributions of branch profit would be subject to the 15°/o withholding tax.

(2) Corporate borrowing abroad was made less attractive by the imposition of a uniform withholding tax of 15°/o on interest and the concessionary rate
for some classes of securities were eliminated.

(3) 5°/o special concessionary rate on dividend paid by a Canadian resident corporation to non-resident shareholders who control all the shares of the corporation was eliminated and then 15°/o rate was substituted.

In 1963, further changes were made as follows:

(1) A management or administration fee paid by a resident to a non-resident is taxed at the rate of 15°/o.

(2) The rate of a withholding tax on dividend is to depend on whether a corporation has a degree of Canadian ownership or otherwise. For a corporation which has a degree of Canadian ownership the withholding tax is 10°/o. Otherwise it is 15°/o.

VI DISINCENTIVE MEASURES

As the Canadian economy turned into a boom condition in 1966 the need to curb inflation arouse. Two disincentive measures were consequently introduced in March 1966 with a view to take off the heat in the economy.

(1) Reduction in capital cost allowance

Under this provision, the normal rate of capital cost allowance was made applicable to only part of the capital cost of the asset for the three-years following the acquisition of the asset if it is acquired during the
period between March 1966 and October 1967. This provision affects largely manufacturing industries but does not apply to assets which were acquired for installation and use in designated areas, or those covered by the special temporary classes established as incentives.

(2) Refundable tax

Section 105E was introduced in March 1966 to be effective from March 1966 to March 1967. Under this provision

"Every corporation and trust shall pay a special refundable tax in an amount equal to 5% of its corporate tax base or trust tax base, as the case may be, for each taxation year of the corporation or trust included in whole or in part in the tax period".

The refundable tax was to be paid in monthly installments. The tax collected under this section was to be repaid to the paying corporation between 18 months and 36 months after the later of

(a) the day on which the payment of tax to be so refunded was due or
(b) the day on which such payment of tax was made.

The tax so paid was to bear an interest rate of 5% per annum.

These two taxes therefore serve to discourage investment. The first provision reduces the amount of capital cost allowance for initial years and hence increases the amount of tax in these years while the refundable tax
reduces the amount of cash available to the corporation without reducing its profitability. It is more like a forced saving.

V. SUMMARY

The above analysis represents the broad structure of the Canadian corporate income taxation in so far as it affects the central theme of the thesis. Admittedly, to extract the essential, considerable details have been left out. Chapter V will be devoted to a discussion of the similarities and differences in the tax structures of Singapore and Canada in so far as they affect the theme of the thesis.
CHAPTER REFERENCE


(2) Op cit, Section 12(1)(a).

(3) Op cit, Section 12(2).

(4) See Royal Commission on Taxation, Queen's Printer, 1967, Vol. IV, Page 239.


(6) See Section 83A.


In this chapter only the incentive legislations will be discussed. Any criticism of these measures will be reserved to Chapter VI.


(9) The question of the degree of Canadian ownership is governed by Section 139A of the Act. It was introduced in 1963 and briefly a company is said to have the required degree of Canadian ownership if

(a) It has issued and outstanding equity share of a type that fit the rigid definitions of the Act, and

(b) equity shares representing at least 25% or more of the total paid-up value of all equity shares outstanding be owned by Canadian residents, or by companies which can be said to be controlled in Canada, under the definition of the Act.


(11) Canadian Income Tax Act, Section 71A(2).


(15) A criticism of this generous incentive provision is reserved to Chapter VI.

(16) Section 4(1) and (2) Industrial Research and Development Incentives Regulations, reprinted in Incentives for Industrial Scientific Research and Development in Canada, CCH, 1967, page 47.

(17) Op cit, Section 4, page 29.


(20) This date is chosen because it represents the last year before the introduction of a series of changes to the withholding tax.
Chapter V

A COMPARISON

In this chapter the corporate income tax systems with respect to incentive provisions for industrial development of Singapore and Canada will be drawn together. The purpose of this comparison is to observe the similarities and differences in the incentive systems. If they differ we shall examine the reasons for such differences.

An incentive by way of corporate income taxation must serve a set of objectives. These objectives may be implicitly or explicitly stated. Hence firstly, this chapter will compare the objectives of the incentive measures in Singapore and Canada. Secondly, the approaches to the objectives may differ, by which is meant the means to the objectives. Broadly therefore the following points will be the subject of comparative study.

(I) A comparison with respect to the broad structure of corporate income taxation.

(II) A comparison of the main objectives of the incentive measures introduced in the 1960's.

(III) A comparison of the approaches to these objectives.

(IV) A general observation of the burden of taxation on companies of the two countries.

(V) Conclusion.
I. A COMPARISON WITH RESPECT TO THE BROAD STRUCTURE OF CORPORATE INCOME TAXATION

Chart I shows in a summary way the broad structure of the determination of income and the tax thereon in the two countries under the normal circumstance. An examination of the table would show that there is basically no difference in the computation of taxable income between the two countries. The major differences appear to be the following:

(a) In the computation of expenses deductible the Canadian tax law is more thorough. Section 11 listed all the items deductible and Section 12 those not deductible. As for Singapore, as noted in Chapter III, all expenses that may be deducted are judged in the light of the circumstances and depend a great deal upon the view of the comptroller of what may be considered reasonable, though Section 14 listed in a general way a few items of expenditure that are deductible.

(b) A Singapore corporation which receives a dividend from another corporation must include the grossed up amount of such dividend in its income for tax purposes. This springs from the integration of personal and corporate income tax discussed in Chapter III. It may be noted that this integration
SINGAPORE

Gross revenue less cost of goods sold plus grossed up dividend and net interest income

Expenses to earn income

Capital cost allowance

Business losses (carry backward one year & carry forward indefinitely)

Rate of tax - 40%

Less tax paid at source,
Less foreign tax credit

CANADA

Gross revenue less cost of goods sold plus interest and other income but exclude dividend income

Expenses to earn income

Capital cost allowance

Business losses (carry backward one year & carry forward indefinitely)

Rate of federal tax: 21 or 51 percent

Less provincial tax credit & foreign tax credit

Provincial taxes
feature was one of the major recommendations of the Royal Commission on Taxation for Canada. In the existing income tax law of Canada a Canadian corporation need not include the amount of dividend it receives from another corporation in its income for tax purposes. (c) The Singapore Income Tax Ordinance provides for an initial capital cost allowance of 20% and 10% respectively for machinery and equipment and building. In effect, the total amount deductible is 120 and 110 per cent of the cost of a machinery and industrial building respectively. There is therefore a certain amount of built-in incentive. The Canadian Tax Act provide for no initial allowance. But the rates on building and machinery are generally higher. One important difference in the treatment of capital cost allowance lies in the provision in the Canadian Tax Regulations to group assets into different classes. This facilitates considerably account keeping. Under this system only a maximum of 24 accounts need to be kept for depreciable assets. In Singapore an account must be kept for every depreciable asset. The Canadian system provides a distinct advantage over the Singapore system. Generally the capital cost allowances are higher in Singapore in the first year, but in subsequent
years they are lower. In both cases capital cost allowances are deferrable. But in the Canadian case, deferral is at the option of the taxpayer, whereas in Singapore it may be deferred only when income is insufficient to meet the capital cost allowance for the year.

(d) Normally a corporation in Singapore pays a standard rate of 40% tax on profit regardless of the amount of the profit. For the Canadian case the dual rates of 21 and 51 per cent apply. This was claimed to provide assistance to small businesses. Since in Singapore a majority of the enterprises are in fact small units employing less than 10 workers each, it is felt that the high flat rate of 40 per cent may impose undue hardship on these small enterprises. The Canadian rates are decidedly preferred.

(e) On the other hand it must be remembered that, in Singapore, because of the "integration feature", a shareholder pays no extra tax on the dividend received if his marginal personal rate is below 40 per cent. In this case, if he receives only dividend, he may in fact get a refund of a portion of the tax paid at source. If however, the marginal tax rate of the individual is between 41 and 50 per cent (the maximum personal rate) he will have to pay the marginal amount --- the difference between the personal
and corporate rates (assuming for simplicity that he has no other sources of income). The Canadian case, however, provides for a dividend credit of 20 per cent. But this credit normally does not compensate fully the tax paid at corporate level.

(f) Both countries allow credit to foreign tax paid to overseas authorities. This general provision is however, much modified by the individual tax treaties entered into by the respective countries.

(g) Singapore is a unitary state and hence no complications arise from the federal-provincial tax arrangement, a perennial source of conflict between the Federal and Provincial governments in Canada (1)

(h) The Singapore tax rate of 40 per cent on non-resident deriving income from Singapore appears very high in comparison with the Canadian withholding tax of 15 per cent. But it must be remembered that dividend payments overseas are allowed full credit for tax already paid at source. Hence a non-resident receiving a dividend from a Singapore corporation need not pay any extra tax. But if he receives an interest income or payments on account of technical knowhow he pays the full 40 per cent.

For a non-resident deriving a dividend from Canada the rate depends upon whether the paying corporation has a degree of Canadian ownership. If it has, the
rate is 10 per cent. Otherwise it is 15 per cent. No credit however is given to the corporate tax paid at source. Hence in this case it can be said that the same income is taxed twice, the total rate is 66 per cent for large corporations. For interest income however, the rate is 15 per cent.

It is not possible therefore, to conclude from the above discussion the relative burden of taxation on business in the two countries. Furthermore for industrial enterprises, the burden is very much influenced by the incentive provisions discussed in Chapters III and IV. Also, this comparison is partial. Writing on the tax aspects of Canada's international competitive position M. R. Robertson observed that "it is impossible in the space of a few pages to compare the tax system of Canada's competition in home and world markets. Nor, for that matter, is it certain that a detailed treatise would be of value since meaningful comparison of tax structures are obviously difficult, and must by their very nature become entangled in extremely intricate and technical matters". And for various technical reasons, "no satisfactory methods have yet been devised for making accurate comparison of the actual tax burdens borne by different industries or the same industries in different countries".

Furthermore the overall tax burden of an industry must include the general excise and sales taxes which unfortunate-
ly cannot be included in this study. Moreover, especially in Canada, there is the complication of the provincial taxes. Because of these difficulties it is not at all easy to compare the tax incidence of Singapore and Canada. We can at best attempt a rough comparison by deducing the facts from comparative general statistics. This attempt is deferred to a later section after an attempt is made to compare the incentive provisions of the two countries.

II. A COMPARISON WITH RESPECT TO THE OBJECTIVES OF THE TAX INCENTIVES

To observe the objectives of a tax incentive is equivalent to observing the underlying economic structure of the country. In Chapter II, the underlying economic conditions of Singapore and Canada were discussed in some detail. The objectives of the fiscal incentives introduced in the 1960's can therefore be observed to be purported means to solve the underlying economic difficulties. Implicitly or explicitly, the economic conditions of the two countries at the end of the 1950's may be recapitulated to be as follows:

Singapore

(a) The traditional source of income, the entrepot trade sector, had been shown in Chapter II to have limited growth potential.

(b) A high population pressure, coupled with a high level of unemployment necessitate a determined effort
to increase job opportunities by industrialization. Because of the small industrial base in the 1950's and early 1960's, this means a structural change in the economy from a traditionally trading one to an industrial one.

(c) Because of the immobility of capital from the traditional trading sector effort had to be made to channel more savings into industrial enterprises.

(d) Because of the predominately trading economy, technical and industrial know-how even for some of the simplest manufacturing process were not available.

(e) Hence to industrialise, Singapore needed capital, technical knowhow, and market. In all these Singapore was poorly endowed in the late fifties and even in the sixties.

Canada

For Canada, the basic economic conditions differ substantially. The following may be noted to be the causes of the economic slowdown of the Canadian economy in the late fifties and early sixties:

(a) As noted in Chapter II there was considerable inflow of foreign investment into Canada in the fifties, particularly into the resource industries and certain categories of the manufacturing industries. The
following table indicates the extent of the inflow. (See Table VI).

Since 1952 therefore Canada had been experiencing a persistent deficit in its international payments on current account at an ever widening magnitude. The current account deficits were financed by heavy capital inflows. These unprecedented capital inflows exerted pressure on the Canadian dollar with the result that the Canadian dollar was at a premium of about 5% over the U.S. dollar in 1959.

(b) The premium on the Canadian dollar raised considerably the price of Canadian export and lower the price of foreign imports. As a result Canadian manufacturers faced considerable difficulties in the export market, and even in the domestic market, the Canadian manufacturers were at a disadvantage. Considerable excess capacities occurred in the Canadian economy and employment reached a level of 7% in 1959.

(c) The share of manufacturers in the total export declined as a percentage of total export while import of manufacturers rose as a percentage of total import. (See Chapter II).

(d) It is also felt that the inability of the Canadian manufacturers to compete internationally was also due to a slackening in the level of scientific
TABLE VI(b)

FOREIGN INVESTMENT IN CANADA

<table>
<thead>
<tr>
<th>Year</th>
<th>Net Current Account</th>
<th>Direct Foreign Investment</th>
<th>Net Foreign Purchase of Canadian Portfolio Securities</th>
</tr>
</thead>
<tbody>
<tr>
<td>1952</td>
<td>-164</td>
<td>346</td>
<td>133</td>
</tr>
<tr>
<td>1953</td>
<td>-443</td>
<td>426</td>
<td>158</td>
</tr>
<tr>
<td>1954</td>
<td>-432</td>
<td>392</td>
<td>191</td>
</tr>
<tr>
<td>1955</td>
<td>-698</td>
<td>417</td>
<td>-45</td>
</tr>
<tr>
<td>1956</td>
<td>-1,366</td>
<td>583</td>
<td>725</td>
</tr>
<tr>
<td>1957</td>
<td>-1,455</td>
<td>514</td>
<td>757</td>
</tr>
<tr>
<td>1958</td>
<td>-1,131</td>
<td>420</td>
<td>607</td>
</tr>
<tr>
<td>1959</td>
<td>-1,504</td>
<td>550</td>
<td>650</td>
</tr>
<tr>
<td>1960</td>
<td>-1,243</td>
<td>650</td>
<td>236</td>
</tr>
<tr>
<td>1961</td>
<td>-982</td>
<td>520</td>
<td>339</td>
</tr>
<tr>
<td>1962</td>
<td>-848</td>
<td>495</td>
<td>361</td>
</tr>
<tr>
<td>1963</td>
<td>-542</td>
<td>280</td>
<td>357</td>
</tr>
<tr>
<td>1964</td>
<td>-424</td>
<td>255</td>
<td>398</td>
</tr>
<tr>
<td>1965</td>
<td>-1,083</td>
<td>390</td>
<td>218</td>
</tr>
<tr>
<td>1966</td>
<td>983</td>
<td>660</td>
<td>323</td>
</tr>
</tbody>
</table>

research activities being undertaken in Canada.

(e) Lastly, there is considerable inequality in economic development across Canada.

The problems of the Singapore and Canadian economies appear similar at the surface. But one should not be misled to believe that they could be solved by similar methods. The causes of the economic difficulties differ. As noted in Chapter I, for a developed economy like that of Canada, with tremendous reserves of natural resources the adjustments needed to bring about economic revival are marginal in nature. It is rather a symptom of depression and is a feature of a short-run slack in the economy. Given the proper dose of fiscal, monetary and exchange policy, a revival is not especially difficult. But for an economy which requires a structural transformation a different policy will have to be adopted. Briefly, the differences in the two economies may be summarised as follows:

(a) Canada's problems are probably short-run whereas Singapore's are long-run in nature.

(b) Singapore does not have a balance of payments problem, whereas Canada depends on foreign capital inflows to finance its trade deficits.

(c) Singapore is in need of foreign capital because of the fact that domestic capital has not been suffi-
ciently mobile and furthermore, foreign capital brings with it technical knowhow. Canada is dependent on foreign capital not so much for its industrial development as for balancing its international balance on current account.

(d) Because of the differences in the stage of industrial development in the two countries, Singapore needs not basic scientific research, but more the applications of the results of scientific research conducted in other countries.

(e) Because of a small domestic market and the lack of natural resources, export of manufactures is the only possible way out for Singapore if it wants to industrialise. Canada, on the other hand, has a sufficiently large domestic market and export of manufactures can play a less important role.

(f) Canada had excess capacity in the late fifties, but Singapore needs to create the capacity itself.

For the above reasons we may expect more differences than similarities in the objectives.

In all the budget speeches in Singapore since 1960, the question of unemployment appears to be uppermost in the mind of the Finance Minister. Unemployment supercedes all other economic considerations. The Minister of Finance,
speaking in the 1966 budget session stressed that Singapore "must make every effort to increase the rate of expansion to provide sufficient primary jobs in the industry to absorb the growing army of unemployed... The provision of employment opportunities has become even more urgent"(4) and in the 1967 speech: "unemployment has always been the central economic problem of Singapore" and that "the primary objective of the Peoples' Action Party government since 1959 had been to create new jobs for Singapore's growing population". Reviewing the progress made in the past years the Minister says in December 1967: "It is a sobering thought that with the prodigious effort put in and the vast amounts of money and resources which the government had been channelling towards increasing the growth of the manufacturing industries all that had been achieved is a 5,000 net increase in employment in these industries each year. The rate of increase is clearly inadequate to meet our needs. It has not even absorbed the increasing numbers of the young people looking for jobs though, no doubt, without the effort we put in, the unemployment situation may well have passed the critical point at which social discontent may severely disrupt all the prospects of political stability and economic growth. This element, the rate of net increases in jobs in the larger manufacturing industries is a critical economic variable."(5)
The unemployment situation is expected to get worse after the withdrawal of British forces from Singapore. British military spending accounts for some 20% of the Gross National Product of Singapore. When withdrawal is completed by 1971, some 40,000 or 8% of the labour force will be added to the unemployment register making some 18% of the labour force unemployed, unless there is accelerated growth in the economy.

It can be seen without doubt that the provision of additional job opportunities is the most critical economic factor in Singapore. Measures must be taken to bring about sufficient industrial growth. The question is what sectors of the economy can be stimulated to produce growth. The trade and agriculture sectors had been ruled out. Construction is a good provider of jobs, but this is dependent on other sectors expanding to produce a buoyant economy. Industrialization is the overall objective of the fiscal incentive ---- not industrialization for its own sake, but rather to provide employment opportunities. It is because of the above objectives that fiscal incentives were introduced in 1959, 1965 and 1967, and the measures discussed in Chapter III are meant to serve the objectives listed.

With respect to Canada the objectives may be gathered from the speeches of the Finance Minister. A
few of which are as follows:

"Our rate of growth over the past years as a whole has been quite inadequate. We have had a falling rate of new investment. We have had chronic deficits in our international balance of payments.

And most important we have had chronic unemployment."(6)

"It is important that the new employment we are seeking to achieve in the Canadian economy, and the new investment required to produce it, be directed wherever practicable to areas of slower growth and surplus manpower."(7)

"But the need for increasing efficiency and productivity is equally great in the private sector. To increase our employment and decrease our dependence on foreign capital we must compete successfully for markets, both at home and abroad".(8)

and that the tax incentive were meant

"to encourage private capital expenditures, which have lagged so conspicuously for the past six years".(9)

And that the alteration of the withholding tax was introduced

"with a view to promote a growing partnership between Canadian and non-resident investors in Canadian corporations".(10)

The objectives of the Canadian tax incentives can therefore be summarised as follows:

(a) to reduce the persistent balance of payments deficit on current account

(b) to induce greater Canadian participation in Canadian industries.
(c) to foster growth in areas where growth had not matched the national average, and in areas with surplus manpower;

(d) to improve the efficiency and productivity in Canadian industries through scientific research and

(e) to promote demand for Canadian products both at home and abroad.

Basically these objectives are different and requires different approaches from those of Singapore. It is also clear that because of the basic differences in the economies of the two countries the objectives of the tax incentives inevitably differ. It is worth repeating that the duration of the Canadian recessions are of short-run in nature. This is further illustrated by the introduction of the refundable tax in 1966 when the Canadian economy revived to a boom condition and with it the need to curb investment and inflationary pressure. This suggests that Canadian fiscal incentives play a more regulatory role rather than a role as agents of growth. This seems basically different from that of Singapore which needs a sustained effort to stimulate a transformation of the economy.

The Minister of Finance of Canada in introducing the refundable tax and reduced capital cost allowance said that these measures were meant to

"provide prompt pressures upon the inducements for
business to defer capital expenditures, they will not add to the costs of production and they will help business to maintain capital expenditures in future years".\(^{(11)}\)

and

"that (Canada had) for many years used increased rates of capital cost allowances as inducements for accelerating business investments. Indeed (it) has been using them recently. It is logical that Canada should now use reductions in these allowances to induce business to defer a part of the investment".\(^{(12)}\)

It is concluded therefore that the objectives of the Canadian and Singapore fiscal incentives are different although both had the overriding objective of promoting growth. But the details differ. As a whole Canadian fiscal incentives (and disincentives) aim at accelerating the economy along the right track. But in Singapore a new track has to be laid.

III. A COMPARISON WITH RESPECT TO THE APPROACHES

Because of the basic differences as observed above it is not very meaningful to compare the approaches in any great detail. In this section only the broad differences in approach will be discussed.

Singapore approaches the problem through a series of tax incentives that aim at reducing the burden of corporate tax by:
(a) an acceleration in certain deductible expenses
(b) exemption of income from tax; and
(c) reduction in the rate of tax.

These are the three basic approaches in its fiscal incentives. For a detailed listing of the individual incentives under each category, the reader may refer to the CONTENT.

One noticeable feature of the approach is that there is a total absence of incentive by way of a financial grant or subsidy. All the approaches listed in Chapter III require that the tax paying company earn a profit before they are of real benefit. A detailed discussion on this issue is postponed to Chapter VI.

Canada approaches the problem from a slightly different angle. The following summarises the incentives into broad groups: \(^{(13)}\)

(a) an acceleration or double deduction in allowable expenses, particularly capital cost allowance;
(b) an exemption of income from tax;
(c) reduction in the rate of tax payable;
(d) financial grants;
and lastly there are the disincentive provisions in the form of:
(e) refundable tax and
(f) reduction in the rates of capital cost allowance.
One important difference between the two systems lies in the duration of the incentives. For Singapore there is no specification of the time period in which the incentives will be effective. Presumably these incentives are to be withdrawn only when the conditions are right. The Canadian incentives, apart from the incentives to the resource industries, are short-lived, so short that it is doubtful if they are of any significance to most new enterprises particularly in influencing their investment decisions.

Another difference is the financial grants available to firms doing scientific research in Canada. There is no corresponding provision for Singapore. The absence of this method may be said to be one of the short-comings of the Singapore system of incentives.

Singapore includes an incentive specifically to promote export, but Canadian authorities hope to promote export by giving general incentives to manufacturing by way of research grants and to promote employment by encouraging investment in areas of slow growth and surplus manpower.

As a whole, the Canadian incentive provisions, apart from the incentives to the extractive industries and the research grants for approved scientific research, appear to be given more for psychological reasons than for genuine assistance. Singapore is more definite. The feature springs perhaps from the basic differences in the
degree of need for assistance by the manufacturing industries and the urgency of the problems involved.

IV. A GENERAL OBSERVATION REGARDING THE BURDEN OF TAXATION UPON COMPANIES IN THE TWO COUNTRIES

A measure of the burden of taxation upon companies would show the competitive advantage or disadvantage of the domestic manufacturers vis-a-vis foreign competition. It would however, be unrealistic to believe that the burden of income tax is the sole criterion of a manufacturer's competitive position. Not only is comparison difficult, but the total burden a company bears is complicated by other taxes, e.g. property tax, excise tax and also import taxes of various kinds. Subject to the foregoing reservations the following comparative measures are intended to give some broad indication of the burden of taxes upon companies in the two countries.

(1) A comparison of total taxes

Table VI below compares the total taxes as a percentage of Gross National Product in the respective countries in 1963.\(^{(14)}\)

The data in the table show that Canadians as a whole are not over-taxed in comparison with the U.S. and U.K. Other comparisons on the same basis show that West Germany's percentage is 34.0\(^{0/o}\) in 1960 and France's is 33.2\(^{0/o}\). Obviously, Singaporeans'
### TABLE VI (c)

**TOTAL TAXES AS A PERCENTAGE OF GNP IN DIFFERENT COUNTRIES**

<table>
<thead>
<tr>
<th>Country</th>
<th>Total tax as a percent of GNP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada</td>
<td>25.8</td>
</tr>
<tr>
<td>U.K.</td>
<td>29.1</td>
</tr>
<tr>
<td>U.S.</td>
<td>28.8</td>
</tr>
<tr>
<td>Malaysia</td>
<td>19.5</td>
</tr>
<tr>
<td>Singapore</td>
<td>10.9</td>
</tr>
</tbody>
</table>

*Source: Computed from U.N. Statistical Office, Year Book of National Accounts Statistics 1964 except for Singapore which, because it was not an independent state then, did not lodge its accounts with the U.N. The Singapore figure is obtained from Singapore Year Book, 1965, Ministry of Culture, Singapore.*

The tax burden is considerably lower as compared with that of the Canadians. Even Malaysian tax is relatively higher than that of Singapore. On the other hand Singapore is relatively heavily taxed when compared with other developing countries, including Taiwan and India. Although these figures refer to the total taxes of the countries, they reflect the burden of the corporations. Comparative figures for total tax burden...
tend to show that the more advanced a country is economically, the larger the role of government and hence the higher the percentage of taxes to national income. This comparison is at best a general indication. But it shows that Singapore is not among the relatively heavily-taxed nations.

(2) A comparison of trend of taxes as a percentage of Gross National Expenditure in Canada and Singapore

The following statistics show the trend of total taxes (both direct and indirect at all levels of government) as a percentage of GNE for Canada and Singapore.

**TABLE VII**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Taxes as a Percentage of GNE</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Canada</td>
</tr>
<tr>
<td>1960</td>
<td>24.0</td>
</tr>
<tr>
<td>1961</td>
<td>24.2</td>
</tr>
<tr>
<td>1962</td>
<td>24.6</td>
</tr>
<tr>
<td>1963</td>
<td>24.2</td>
</tr>
<tr>
<td>1964</td>
<td>25.4</td>
</tr>
<tr>
<td>1965</td>
<td>25.5</td>
</tr>
<tr>
<td>1966</td>
<td>25.6</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Taxes as a Percentage of GNE</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Singapore</td>
</tr>
<tr>
<td>1960</td>
<td>10.4</td>
</tr>
<tr>
<td>1961</td>
<td>11.4</td>
</tr>
<tr>
<td>1962</td>
<td>12.0</td>
</tr>
<tr>
<td>1963</td>
<td>10.9</td>
</tr>
<tr>
<td>1964</td>
<td>11.6</td>
</tr>
<tr>
<td>1965</td>
<td>11.3</td>
</tr>
<tr>
<td>1966</td>
<td>n.a.</td>
</tr>
</tbody>
</table>

Source: See footnote to Table VI
Certainly in Singapore, the level of tax cannot be considered high by Canadian standard. The Canadian rates have shown some increase during the past six years. For Singapore such a trend is less obvious and except in 1962, there is no apparent upward trend in spite of the increasing volume of government activities. This is obvious when one realises that since 1960 there has been no change in the personal and corporate tax rate structure except the incentives provisions discussed earlier.

(3) A comparison of corporate tax as a percent of Gross National Expenditure in Canada and Singapore

Table VIII shows the corporate tax as a percentage of Gross National Expenditure.

**TABLE VIII**

**CORPORATE TAX AS PERCENTAGE OF GNE IN CANADA AND SINGAPORE**

<table>
<thead>
<tr>
<th></th>
<th>Canada</th>
<th>Singapore</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960</td>
<td>4.30%</td>
<td>2.25%</td>
</tr>
<tr>
<td>1961</td>
<td>4.25</td>
<td>2.10</td>
</tr>
<tr>
<td>1962</td>
<td>4.25</td>
<td>2.16</td>
</tr>
<tr>
<td>1963</td>
<td>4.10</td>
<td>1.85</td>
</tr>
<tr>
<td>1964</td>
<td>4.15</td>
<td>2.04</td>
</tr>
<tr>
<td>1965</td>
<td>3.76</td>
<td>1.97</td>
</tr>
<tr>
<td>1966</td>
<td>3.72</td>
<td>n.a.</td>
</tr>
</tbody>
</table>

It can be seen that Singapore corporations are not overtaxed as compared with Canadian corporations. In both countries the trend seems to be a declining one. In terms of contribution to government revenue, 1963 figures shows that corporate income tax contributed some 13\% of the total revenue of the governments of Canada. In Singapore it is only 10.6\%.

In conclusion then it can be said that the tax incentive policies of the two countries are essentially different. This springs largely from the political, social and economic differences. Furthermore, corporations in Singapore bear less tax than Canadian Corporations. This should give a greater competitive advantage in the case of Singapore. But it would be unrealistic to draw any strong conclusion out of this analysis. For a comparison of this nature is at best approximate. It does show however, that with respect to incentive provisions Singapore is more generous and "determinant". This difference as aforementioned, can only be explained by the basic economic, social and political differences in the two countries.
CHAPTER REFERENCE

(1) The only occasion this problem arose was when Singapore was state in Malaysia between August 1963 and August 1965.


(3) Op cit, page 2.


(7) Op cit, page 997.

(8) Op cit, page 999.

(9) Op cit, page 1004.

(10) Op cit, page 1004.


(12) Op cit, page 3388.

(13) For a detailed listing of the individual incentives under each group please see CONTENT.

(14) Total taxes comprise federal and provincial taxes both direct and indirect.

A CRITIQUE OF THE FISCAL INCENTIVES

I. GENERAL INTRODUCTION

Chapter V discussed the main differences in the objectives and approaches to incentive legislation in the light of the economic environment of Singapore and Canada. It was found that because of the differences in political, economic and social characteristics of the two countries the objectives and approaches tend to differ. The question that inevitably follow is the reality of such fiscal incentives—specifically, it seems desirable to assess the likely effect of such policies upon the economies of the countries particularly with respect to their economic objectives.

It is important to make clear at the outset of this chapter that it is not intended to evaluate the result of the policies adopted. It is believed that tax experts tend to overstate the beneficial effect of incentives on economic growth in general, and on investment by individual firms in particular. Economic growth presupposes the interaction of many factors including research, education, capital formation, market and not the least government investment, fiscal, monetary and exchange policies. There is still much to be learned about the growth process itself and the
extent it can be influenced by tax policy. It would therefore be naive to believe that the fiscal incentives introduced in the 1960's can fully explain the economic growth of Singapore and Canada in the 1960's. We can at best make an attempt to assess the likely implications of the policies.

Before we look into the implications of such measures with respect to Singapore and Canada, a brief review of the opinion of some tax experts on fiscal incentives in other countries may be useful. The following excerpts from the conclusions of a conference on tax policies and economic growth sponsored by the National Bureau of Economic Research in 1966 is helpful.\(^{(1)}\)

The Japanese representative in examining his country's policy on tax exemptions granted on income from new products and from exports conceded that:

"these provisions like those on accelerated depreciation, may have had significant differential impact, he doubts whether they have been very effective in increasing aggregate saving or investment. He also suggests that the discriminatory character of many of these provisions may have resulted in some mis-direction of resources within the Japanese economy"\(^{(2)}\)

The German representative attributed his country's growth to growth-promoting tax policies. This was a tax system that favoured the wealthy. "Undistributed profits represented more than 40 per cent of total capital formation right after the war and between 30-40 per cent in 1953-
1960. This in his opinion was due in large part to the preferential tax treatment given to retained earnings.\(^{(3)}\)

The conclusion one may draw from the German's experience is that a policy to induce a higher level of retained earning has a favourable effect on investment and growth.

The Italian representatives "observed that the Italian experience seemed to suggest that there was very little connection between the rationality of a country's tax system and its rate of growth".\(^{(4)}\) Furthermore, another of their representatives was even more pessimistic about the effectiveness of tax exemption in promoting regional development. They concluded that if some form of government intervention is needed to achieve a more balanced growth of the Italian economy they would favour the use of direct subsidies, which would be administered more flexibly and with more telling effect on investment decisions.

The Netherlands representative expressed "some skepticism about the effects which the various special provision (incentive taxation) have had on the level of investment and wondered whether a generally lower level of taxation might not accomplish about as much.\(^{(5)}\)

The other countries that participated in the conference expressed substantially similar conclusions and
it is generally agreed that special tax incentives are not important considerations for economic growth. The overall conclusions of the conference are as follows:

(a) There are considerable difficulties in trying to relate differences in growth rates of various countries to differences in specific tax policies. It is far from clear and easy to attribute economic growth to any specific factor.

(b) It cannot be denied however, that tax policies had some influence on the postwar rates of growth of the countries participating in the conference; but even in these countries where the influence of tax policies was believed to be greatest, there were other important contributing factors.

(c) Tax policies that can influence growth most are provisions that sought to promote growth by spurring capital formation, which means an increase in aggregate savings and investment in relation to the Gross National Product.

(d) On the other hand, a general tax reduction may not contribute as much to economic growth as selective and discriminatory measures.

(e) Other considerations are important determinants of investment.
(f) No quantitative statistics are available to support any contention.

(g) In any case it was agreed that the price a country might have to pay for growth promoted by tax incentives could be very high mainly from the standpoint of equity and also from that of an optimal allocation of resources.

Having reviewed the implications of tax incentives in other countries, we may proceed to evaluate the measures adopted by Singapore and Canada.

II. SINGAPORE

(1) Economic growth since 1960

(a) Growth of the manufacturing sector in terms of contribution to Gross Domestic Expenditure

It was seen in Chapter V that the tax incentive provisions in Singapore were meant to achieve industrial growth. It was also noted that the incentives operated through two categories:

(i) An acceleration or double deduction in certain expenditures especially capital cost allowances and market development expenditures.

(ii) An exemption, partly or wholly, on income earned if the company earning the income meets certain sets of conditions.
The most important legislation is the Pioneer Industries Ordinance of 1959 which had been in operation for seven years by the end of 1957. The others are relatively new, and, as noted in Chapter III, some of them have yet to be formally enacted. Hence more can be said about the pioneer industries. The following statistics would be useful as a starting point. They summarise the achievement in the pioneer industries up to December 1966.(6)

<table>
<thead>
<tr>
<th>Number of pioneer firms</th>
<th>165</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total issued capital</td>
<td>$M291m</td>
</tr>
<tr>
<td>Total paid up capital</td>
<td>$M190m</td>
</tr>
<tr>
<td>Capital outlay in fixed assets</td>
<td>$M327m</td>
</tr>
<tr>
<td>Employment created</td>
<td>11,102</td>
</tr>
<tr>
<td>Contribution to national income as a percentage of Gross Domestic Product (1966)</td>
<td>8.5 per cent</td>
</tr>
</tbody>
</table>

Total contribution to national income by the manufacturing sector 12.3 per cent

Compared with 1959, the manufacturing sector contribution to national income has shown considerable improvement. In 1959 the contribution by this sector was 7.1 per cent. There is therefore a substantial increase from 7.1 per cent to 12.3 per cent. The following series would show the pattern of growth in this sector as a percentage of Gross Domestic Expenditure:(7)
Year | Contribution of manufacturing to Gross Domestic Expenditure (Per Cent)
--- | ---
1959 | 7.1
1960 | 6.4
1961 | 6.7
1962 | 8.3
1964 | 10.1
1965 | 10.6
1966 | 12.3

From the above data we note the steadily increasing contribution of manufacturing to the GDP and hence to the economy of Singapore. For a comparison of the growth of the manufacturing sector and the growth of the Gross Domestic Expenditure the following data is useful:

<table>
<thead>
<tr>
<th>Year</th>
<th>Growth in GDE</th>
<th>Growth in value added by manufactures</th>
</tr>
</thead>
<tbody>
<tr>
<td>1961</td>
<td>14.4</td>
<td>21.0</td>
</tr>
<tr>
<td>1962</td>
<td>4.5</td>
<td>28.0</td>
</tr>
<tr>
<td>1963</td>
<td>14.1</td>
<td>28.0</td>
</tr>
<tr>
<td>1964</td>
<td>2.1</td>
<td>19.8</td>
</tr>
<tr>
<td>1965</td>
<td>7.2</td>
<td>13.1</td>
</tr>
<tr>
<td>1966</td>
<td>5.8</td>
<td>22.0</td>
</tr>
</tbody>
</table>

It can be seen that in all years the growth of the manufacturing sector outstripped the growth of the economy. It is not possible, however, to say with any degree of certainty whether this rate of growth is satisfactory, for there is no objective standard of the desired target. Recourse will therefore have to be made to other yardsticks discussed below.
(b) Employment created

The Four-year Development Plan envisaged an increase of employment in the manufacturing sector of 30,000 between 1961-1964. The employments in the pioneer industries established up to 1966 represent about 95% of the total increase in employment in the manufacturing industries. For 1961-1964 the total increase was about 6,000 for the whole period. This is only 20% of the target and is clearly below the estimate. Even by the end of 1966 only 11,000 new jobs were created in manufacturing industries. Together with the growth in employment in the old established industries an average of less than 5,000 new jobs were created each year for the period 1961-1966.

(c) Capital formation

The Plan estimated that through government expenditure under the Plan and the fiscal incentives discussed in Chapter III a Gross Capital Formation of 20% of Gross Domestic Product is feasible. Table IX below shows the trend of gross capital formation as a percentage of Gross Domestic Expenditure in recent years.\(^{(9)}\)
TABLE IX
GROSS CAPITAL FORMATION IN SINGAPORE

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Capital Formation</th>
<th>As of Gross Domestic Expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960</td>
<td>$M 138.5m</td>
<td>6.9</td>
</tr>
<tr>
<td>1961</td>
<td>226.6</td>
<td>9.8</td>
</tr>
<tr>
<td>1962</td>
<td>255.1</td>
<td>10.6</td>
</tr>
<tr>
<td>1963</td>
<td>323.2</td>
<td>11.8</td>
</tr>
<tr>
<td>1964</td>
<td>414.7</td>
<td>14.8</td>
</tr>
<tr>
<td>1965</td>
<td>463.8</td>
<td>15.4</td>
</tr>
<tr>
<td>1966</td>
<td>454.1</td>
<td>14.2</td>
</tr>
</tbody>
</table>

Clearly, therefore gross capital formation has not reached the target level of 20% envisaged by the Plan, and this accounts for the short fall in employment discussed in the last section. The almost complete dependence on tax incentives to achieve the rate of capital formation should be viewed with a degree of skepticism. The government expenditure in infrastructure development under the Plan was 90% of the target. It is believed that the short fall occurred largely in the private sector. This leads us to a discussion of the likely implications of the tax legislations particularly the pioneer industries provision.

(2) A critique of Singapore's tax incentives

(a) As was seen in Chapter II and the preceding section that Singapore must raise its level of capital formation and to industrialise to provide jobs for the unemployed. It may be contended therefore that any tax incentives should encourage labour-
intensive industries. The tax incentives introduced so far however, do not aim at this. In fact it is the reverse. For, by giving a longer period of tax exemption to enterprises with larger capital investments this in fact encourages capital intensive industries.

(b) From the conclusions of the conference on tax policies and economic growth discussed earlier, it was noted that encouragement of reinvestment of earnings represents the best means to raise the saving and investment of a country. Singapore does not appear to aim at this method of raising the level of capital formation. Further, no provision is made to encourage foreign reinvestment. This together with the ease of transferring of funds overseas would not encourage internal saving and reinvestment of profits. The lack of incentive to provide for a reinvestment of profits is further induced by the completely tax-free dividend declared out of pioneer firm profits. It is contended therefore that some measures should be introduced to encourage re-investment of earnings.

(c) All the tax incentive measures introduced are of benefit only to those enterprises that are in a position to make a profit in the first five years
years of operation. From experience, it is noticed that a manufacturing enterprise normally does not make a profit in the first three years of operation. One can conclude therefore that the tax exemption on pioneer firms with less than a $M500,000 investment seems not at all helpful to such small scale industries, or as indicated above it, may not encourage industries that are labour-intensive. Table XII shows the classification of capital investment and employment of the pioneer industries up to December 1966.

It can be seen from Table X that petroleum and petroleum products group of industry require the largest investment per worker. This group of companies is 90% foreign owned and controlled. They also are companies that are capable of making profit in the first five years of operation. The contribution of this industry to the economy of Singapore is marginal, as was noted by the Minister of Finance on the export of petroleum to Vietnam:
### TABLE X

CAPITAL INVESTMENT AND EMPLOYMENT IN PIONEER FIRMS

<table>
<thead>
<tr>
<th>Industry Group</th>
<th>Capital Investment in fixed assets $M'000</th>
<th>Employment at full production</th>
<th>Capital per Worker</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food Beverages</td>
<td>46,042</td>
<td>2,071</td>
<td>25,200</td>
</tr>
<tr>
<td>Textile, garment leather</td>
<td>12,653</td>
<td>5,938</td>
<td>2,230</td>
</tr>
<tr>
<td>Wood and paper</td>
<td>15,112</td>
<td>1,926</td>
<td>7,840</td>
</tr>
<tr>
<td>Rubber products</td>
<td>16,496</td>
<td>652</td>
<td>25,300</td>
</tr>
<tr>
<td>Chemical products</td>
<td>18,376</td>
<td>1,392</td>
<td>13,250</td>
</tr>
<tr>
<td>Petroleum and Petroleum product</td>
<td>126,485</td>
<td>610</td>
<td>206,200</td>
</tr>
<tr>
<td>Non-metallic mineral product</td>
<td>12,761</td>
<td>907</td>
<td>14,050</td>
</tr>
<tr>
<td>Metal and engineering</td>
<td>62,963</td>
<td>3,542</td>
<td>17,760</td>
</tr>
<tr>
<td>Electrical products</td>
<td>5,907</td>
<td>941</td>
<td>6,350</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>9,907</td>
<td>949</td>
<td>10,440</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>326,756</strong></td>
<td><strong>18,930</strong></td>
<td><strong>17,290</strong></td>
</tr>
</tbody>
</table>


"However, most of the products exported to Vietnam consist of petroleum and petroleum products. These no doubt have been useful to our refineries and to business connected with tanker operations, the benefit accruing to our manufacturing industry are much less(10)

The policy of granting five years exemption to this industry is questionable. The benefit to Singapore in terms of employment and national income may be outweighed by the revenue forgone. Tax holidays will be neutral with respect to capital (labour) intensity only when the exemption period is the same for any amount of capital investment."
"As capital is ordinary scarcer than labour in the less developed countries, an incentive scheme offering special inducements to the use of capital-intensive methods is questionable. (11)

(d) Another criticism that may be levied against the pioneer ordinance is that under normal circumstances a firm has an unlimited period in which to deduct losses, and since few pioneer companies can make any substantial profit in the initial years, the benefit in the first three years to a new enterprise is nominal since in any case a new company is not likely to be taxed. Furthermore, under normal condition a new company can write off some 30% of the cost of machinery in its first year of operation and hence the effective tax rate is considerably lowered. For the pioneer company, on the other hand, is not entitled to deduct any capital cost allowance in its tax relief period.

(e) The pioneer ordinance provides for no limit to the maximum amount of tax to be exempted during the tax holidays. The benefit to the investor (and conversely the revenue loss to the State) under a tax holiday depends on the amount of profits realised and there may be a possibility of a windfall to the investor. To reduce the cost to the public treasury it is believed that this
"open-end" feature of the Singapore tax holiday should be avoided by limiting the tax exemption to earnings that bear some fixed ratio to the investment.

(3) The reliance on foreign capital

With respect to unlimited dividend payment overseas to induce foreign investment, it may be noted that most developing countries offer tax incentives of one form or another. Malaysia's Pioneer Certificate Ordinance, for instance, is almost identical to that of Singapore. Competitive exemption among developing countries seems to be the order of the day. This is not to argue that Singapore should not provide a scheme of tax incentives. Rather, it is to be realised that under this competitive environment consideration other than tax incentives should play a greater part in promoting industrialization.

Foreign capital has played a great part in Singapore's industrialization so far. In the pioneer industries for instance, 44.4% of the capital are from foreign sources. The distribution of foreign capital differs among industries, with the petroleum industry almost 90% foreign owned. About one-half of the companies established up to 1966 have foreign capital participation. Except under special conditions, complete foreign ownership is not the rule.
There is no doubt that without foreign investment the growth in the manufacturing industries in Singapore would have been considerably lower. The incentives formulated are intended to a large extent to induce foreign capital inflow. Because of the institutional barriers as discussed in Chapter II, foreign capital is needed to supplement local capital. It would however, be an over simplification to believe that foreign capital will always be forthcoming to the extent required by Singapore. This leads us to discuss two important considerations with respect to foreign capital (i) What are the after tax returns to a foreign investor, and (ii) what has been the actual pattern of foreign capital investment in developing countries. The first question can be answered only in the light of the tax law in the investor's home country and for which a summary review is necessary for an understanding of the common practice and the necessary steps Singapore has to take to render its tax incentives effective.

Foreign capital inflow depends on several important variables, among which is the treatment of foreign income in the tax structure of the investor's country or his country of residence. This problem deserves closer attention as the relative volume and mobility of capital increased.
A theoretical aspect of taxation of foreign income

The return to an investor in a foreign country depends on (a) the tax rate in the country in which the investment is made, (b) the tax rate in his country and (c) the extent he repatriates his earnings. For the investor who intends to consume or accumulate his income in his country of residence we must measure the after-tax return from foreign investment against after-tax return from domestic investment. For an investor who intends to consume or accumulate income in the country of the investment, we have to measure his after-tax return abroad, (assuming that only income repatriated is taxed in his country of residence).

Since 1918 U.S. and other capital exporting countries have adopted the principle of a foreign tax credit. Under this system an investor is allowed a credit on tax paid abroad. The taxpayer is however subject to his domestic rate. This gives his total tax payable in his country of residence and against this a credit is allowed for the tax paid abroad. His total tax liability depends therefore, not on his foreign tax
rate, but on that of his country of residence. The country of the source of income is therefore given the prior claim to tax and the foreign tax is credited against the domestic tax liability of the individual in full so long as the foreign rate does not exceed the domestic rate. The total tax liability does not depend on the foreign tax rate and the lower the rate in the capital-import country the greater will be the tax to be paid at home, and vice versa. In allowing a tax credit the capital-export country sacrifices a great part of the tax payable to its own treasury in the interest of removing an unduly large tax burden on the foreign investor. If there is no tax credit (which may happen in cases where there are no tax agreements) the investor may have to pay tax twice on the same income. By eliminating double-taxation would, presumably, facilitate international movements of capital.

The above discussion assumes that the definition of foreign income in the country of residence is all income whether repatriated or otherwise. The situation would change considerably if the definition
of foreign income is altered to include only income repatriated. In this latter case, an incentive is provided to induce the investor to reinvest his profits abroad. If however, the first case holds the capital-export country would apply its domestic rate to all investment income wherever it arises and wherever it is deposited, and the tax concession granted by a developing country would be completely nullified. The treatment of foreign income apparently has an important bearing on the rate of return to the foreign investor and the effectiveness of the tax incentive offered by the developing countries.

Perhaps the only possible way for a developing country to make effective use of a tax incentive to induce foreign investment is to conclude with the capital export countries international tax agreements with "tax sparing" clauses. Incentive laws in developing countries are most typically associated with relief from income taxes. The present system of taxation in the U.S. and other countries receiving foreign source income decidedly appears to cancel the effectiveness of tax
concessions offered by developing countries to attract foreign investment. To a large extent the effectiveness of tax incentives of developing countries depends on the measure taken by the capital-exporting countries. To assist a developing country a capital-export country can take either of two courses of action, (a) defer to the developing country the total tax rate, or (b) retain control of the strength and distribution of the incentives.

Under (a) there is a complete exemption of foreign source income and hence defers to the capital-import country full control of its tax rate and structure. Tax-sparing is the most common form of such deferral system. Under (b) would be policies which allow a lower rate on foreign source income. Under this system, the control of a developing country's tax incentives again lie in the hands of the capital-exporting country. Generously applied, this system is said to have the advantage of precluding competitive tax rate reductions on the part of the capital-import countries. (12)
However, (a) is seldom available to developing countries while (b) is maintained by some countries. Without going into detail it is obvious that given the economic conditions in the important capital-export countries, the U.K. and the U.S. it is most unlikely that (a) will ever be of any significance and even for system (b), the extent of its application cannot be gauged. It is also to be noted that the U.S. Interest Equalization Tax introduced in 1963 too has an adverse effect on tax incentives offered by the developing countries.

In the light of the above discussion it would be appropriate to see where Singapore stands with respect to foreign tax structures. Singapore had by the end of 1967 double taxation treaties with Japan, Malaysia and the U.K. In each of these treaties special allowance is given by each country to Singapore's tax exemption provision under the pioneer ordinance. The treaty with Japan is typical:
"For the purpose of the credit referred to ... where the taxpayer in Japan receives a dividend from Singapore corporation which is exempted under the provisions of Section 13 of the Pioneer Industries (Relief from Income Tax) Ordinance 1959, these shall be deemed to have been paid by the taxpayer in Japan the amount of Singapore tax so exempted under the provision of the said Ordinance."(13)

But for most capital-exporting countries, Singapore has no double taxation agreements. It is believed therefore that it is in the interest of Singapore to conclude more agreements so that its tax incentives can be rendered more effective.

Even if other capital-export countries are prepared to conclude tax agreements with a tax sparing clause, it still depends on the initiative of private investors to invest their money in Singapore. This leads us to the second question. What is the likely extent of foreign investment in industries?

(ii) What is the actual pattern of foreign capital investment in developing countries?

Even if foreign capital is forthcoming and desirable to Singapore, the question is whether it will be forthcoming to the extent required by Singapore. For the period
1961-1967, it was stressed earlier that capital formation has been below that in the planned estimate. The incentives are meant to induce both local and foreign capital into industries and as such one should look at the extent to which one can rely on foreign sources of capital. A few observations by some writers may be illuminating.

"The flow of foreign capital which had declined substantially after 1930 had always been very unevenly distributed over the world. Asia is receiving a minor share now as well as during the 20's and 30's. In post-war years the U.S. has emerged as a major capital exporting country. ...These investments are concentrated in a few countries and selected industries in which Asia's share has declined to still lower level. The flow of capital is directed either to countries where capital investments are already high or to extractive industries which have to be operated at the source. These phenomena are highly significant for the countries of South and South-east Asia where much reliance is being placed on the external sources of capital for development.\(^{(14)}\)

and

"The extent to which the capital needs of the underdeveloped countries are likely to be met by private foreign investment is exceedingly limited.\(^{(15)}\)

Other observations to the same effect can also be noted. However, the
above argument would suffice to show that too heavy an expectation on the positive role of foreign capital is unwarranted. In the context of Singapore, one may conclude that it is very unlikely that foreign investment can be counted on to make any large quantitative contribution to bridging the investment gap which the national development programs estimate as necessary.

It is also not clear to what extent a tax reduction on income might not be simply a subsidy to one particular investment group rather than a quantitatively significant stimulus to economic development. There is a need for a more precise study of the "tax elasticity" of foreign investment in Singapore, or at least the probable effect of a given percentage reduction in corporate tax rates on the percentage increase in foreign investment. The conclusion one may draw is that an undue dependence on foreign capital may be unrealistic and may not even be desirable.

To conclude this subsection on Singapore, it needs to be mentioned that an analysis of the "effectiveness" of the
tax incentives is further complicated by the fact that during the period under review the government participated in no small measure in establishing industrial estates complete with all amenities. Although the government does not participate directly in manufacturing industries, its extensive development of the economic and social infrastructure plays a great part in furthering the growth of the manufacturing industries in Singapore. The chief measures, besides the establishment of industrial estates are:

(a) The introduction of protective duties in 1965.

(b) The effort of the Economic Development Board in promoting industrial growth.

(c) The financial participation of the Economic Development Board in manufacturing industries which amounted to some 27% of the total investment in fixed assets of the pioneer industries by 1966.

These are no small measures and it is believed that they play a more positive role in fostering industrial development than the tax incentives although it cannot
be disputed that the tax incentives do play a considerable part. This no doubt was in the mind of the Finance Minister when he declared that "merely providing incentives would not produce the results we want, unless it is backed by the right policy implemented by an effective administrative agency. In this second phase of our industrialization programme, it will be necessary for us to make increasingly large outlays on selected growth industries."(16) In other words, a more positive role on the government is required. This means that the government should initiate and participate more extensive in worthwhile manufacturing industries.

III. CANADA

(1) General observations

In the last section it was found that there are some short-comings in the Singapore tax incentives. It is concluded that the growth in the economy in 1960-1967 is a result of a combination of factors, and that tax incentives by way of corporate income tax cannot be considered the dominant factor, although it might have played a differential role. If the tax incentives in Singapore cannot be considered the most
important factor in stimulating growth, much less can be said about the Canadian system. Chapters II and V discussed the economic conditions in Canada in the late 1950's and early 1960's. Specifically, it was noted that the economic slowdown in the late 1950's and early 1960's were a result of the monetary, fiscal and exchange policies pursued by the government. (see Chapter II).

Given the background as outlined in Chapter II, certain tax incentives were introduced. These were discussed in Chapter IV. The intention of the tax incentive measures by way of corporate income tax was to remedy the economic ills in the Canadian economy in the early 1960's. Given the basic problems, it behoves on us to make an attempt to analyse the likely effect of these measures and whether in fact they were necessary at all. This study is divided into two parts. Part one will discuss some short-comings of the incentives while part two will be given to an analysis of what is believed to be the factors that brought about the recovery in the Canadian economy in the 1960's.

(2) Some observations on the short-comings of the tax incentives (on measures introduced in the 1960's).

The incentive provisions, noble though their intent, have a number of short-comings.
(a) Firstly, the duration of most of the incentives (except the research grants and the incentives to the extractive industries) may be too short to be of much benefit to many new firms. The most complete set of incentives are those provided under the Area Development Incentive Act (with its associated accelerated capital cost allowance). But an examination of the provisions show that for tax exemption, a firm must initiate, plan, execute and make a profit within three years to be able to take advantage of the provision. Even then, it would not qualify for exemption for all the three years of exemption since only incomes earned within the three-year period are exempted. It is furthermore highly improbable that a new firm can make a profit within such a short time.

(b) Secondly, incentive capital cost allowance is designed to bring marginal projects within the range of profitability. It not only reduces the effective tax rate in the early years of a particular asset's life, but the reduced rate may be a permanent feature depending on the firm's rate of expansion. This however, is of avail to only large firms which have the capital resources to make continuous commitments in assets. As was seen in Chapter IV all the incentives by way of
accelerated depreciation are too short-lived to make this method of incentive really effective even to large firms. It was also noted earlier in this chapter that the experience of some of the countries that participated in the conference on tax policies and economic growth did not show that there was a correlation between accelerated depreciation and investment. With respect to Canada R.P. Mendels said:

"Unfortunately, there is little evidence to support the claim that the incentive has the desired effects... It is undoubtedly true that many factors were responsible, for (the) slowing down of Canada's rate of growth and that these factors probably more than offset the incentive to expansion give by a liberal capital cost allowance."(17)

Conversely, other considerations very likely more than supplement the tax incentives in accounting for the rapid rate of growth in the Canadian economy in 1964-1966.

(c) Thirdly, accelerated capital cost allowance is desirable when there is an urgent need for additional capacity. But this was not the case in the early 1960's. The view of the Economic Council of Canada in its Fourth Annual Report was that earlier recovery in the 1960's was made possible both by the strong underlying productive capacities of the economy, notably the rapidly
expanding labour force, and by the drawing in of economic slack which existed in the early 1960's. Under the economic conditions as they existed in the 1960-1963 period at least, more investment was not the cure of the economic ills. Rather a strong demand for Canadian products was required. If there is excess capacity, there is little reason to expect that there would be a favourable response to the incentives.

(d) Fourthly, incentive capital cost allowance is a highly discriminatory fiscal measure. It benefits only established and diversified firm with sufficient taxable income against which to charge the additional capital cost allowance. Furthermore it favours capital-intensive industry, and may interfere with the economic allocation of resources among firms and industries. The wisdom and equity of giving special concession to new firms in designated areas is also questionable when established ones have been located in or near the same locality on their own initiative.

(e) Fifthly, investment is a time-consuming process. To be effective the incentive would have to be introduced before the turning point of the business cycle. However, it is not easy to forecast this turning point.
For the above reasons, it is believed that the tax incentives by way of accelerated capital-cost allowance and tax exemption are unlikely to have much impact on investment in secondary manufacturing industries. It is almost impossible to attribute the amount of increase in investment to incentive provisions by way of tax exemption and accelerated capital cost allowance and if incentive is necessary, a more direct approach may be more desirable than by way of accelerated depreciation.

"Given alternative policy choices, it is usually true that the most direct approach is the best, too... . The cost of incentive depreciation is high in terms of revenue loss to the Treasury. What is more, the true cost of the measure is not readily ascertainable since it carries over a number of fiscal years and since it is a function of the businessman's response to the incentive. Direct subsidies or reductions in the corporate income tax rate would therefore seem to be a preferable means to stimulate investment."(18)

(f) Lastly, the incentive provision by way of grant deserve some comment. This form of incentive should prove more effective to stimulate industrial scientific research; for it does not depend on the earning of a profit to be eligible. This should have the effect of providing almost equal benefit to all firms undertaking research, even to those making a loss. The 1962 legislation which allowed
an 150% write-off of the increase in research expenditure of a current nature give a benefit to only corporations with substantial profits. The introduction of research grants therefore is a substantial step forward. Also the 150% deduction is based on an increase in expenditure over a base year. Hence a corporation which undertook no research expenditure before 1962 was put in a preferred position. This appeared inequitable. The change to a three year moving average expenditure on current nature in the Industrial Research and Development Incentive Act removes this inequity. As a whole, it must be conceded that the financial grants for scientific research are of considerable benefit to industries, particularly the secondary manufacturing industries.

(3) A criticism of the incentives to the extractive industries

The next group of incentives that should be reviewed is the incentives to the extractive industries. Specifically it refers to (a) 100% write-off of exploration, prospecting and development expenses in the years of occurrence (b) depletion allowance and (c) three-year exemption of tax on new mines. These provisions have been subject to controversy over the years. Two strains of arguments are put forward. There are those who believe that these concessions
are made to take account of the peculiar features of the extractive industries. Others, however, contend that these provisions give an unwarranted concession to one particular type of economic activity. The first category, which of course includes largely those companies with a vested interest contend that such concessions are meant to counter the following characteristics of the extractive industries.(19)

(i) because of the uncertainty of the return on outlays incurred an immediate write off of such costs would achieved interindustry neutrality.

(ii) the nature of the resource industries is risky and special concessions must be allowed to compensate for this risk especially when present tax legislation does not provide for full loss-offsets.

(iii) the capital market is biased against risk and hence against risky extractive industries.

(iv) that the present system of company income taxation discriminates against extractive industries. A tax on exhaustable resources is a tax on capital and tax concessions are necessary to compensate for this non-neutral feature in the income tax law.

(v) investments in resource industries confer economic and social benefit.
It is however difficult to assess the logic of these arguments. Individual firms differ in their size and financial strength. To use a few firms to represent the industries is questionable. In this thesis we can do no more than to cite a few criticisms advanced by the Royal Commission on Taxation.

The desirability of the incentives can only be assessed in rather broad terms and must be based on a number of general criteria, the most important ones are: (20)

(i) the relative degree of risk attached to investment in resource industry vis-a-vis other industries.
(ii) the degree of capital market bias against risk taking if any and
(iii) the extent to which extractive industries divert funds, from the other industries e.g. secondary manufacturing industries.

These are not easy to answer. The Royal Commission-on-Taxation dismissed most of the arguments for existing concessions. Specifically the commission argued that

(1) though it is difficult to determine just how fast the write-off of expenses should achieve interindustry neutrality to compensate for the alleged risk attached to extractive industries, it is felt that "to focus attention on the undeniably high risk attached to a particular exploratory venture grossly overstates the degree of risk of investments in the mining and petroleum industries relative to other industries" and that even for small firms they are not "subject to
greater risks than small firms in some other industries characterised by rapid technological and product changes"(21)

and

(ii) the diversion of resources to extractive industry may be at the expense of other industries. Furthermore, recent trends in the development of the resource industries have shown some excess capacity.

The Commission concluded that

"the only ground for special tax concessions to the extractive industries would be to compensate for the possible discrimination against risk taking in the Canadian capital market. In other words to the extent that there was a bias in the capital market against risk taking, and to the extent that mineral and petroleum extraction was unusually risky, a deviation from a neutral tax system would be justified to compensate for this bias, assuming that more efficient methods of compensation were not available."(22)

But its study showed that

"the need for special encouragement to mineral and petroleum exploration to compensate for a capital market bias against risky venture is small, if it exists at all."

and that it is convinced that

"there are fiscal methods available that would be as efficient as, or more efficient than, tax concessions in encouraging exploration if this was deemed to be in the public interest."(23)

It recommended, in return that wherever possible, if incentives are needed, subsidies should be granted rather than tax concessions. The cost of subsidies is more readily measured and could be applied to exploration programmes, transportation,
or geological surveys.

A review of Chapter II would tend to show that there is much reason in the Commission's view. It was noted that the extractive industries expanded markedly in the 1950's but for the well being of the Canadian economy, the development of the secondary manufacturing industries could confer many benefits which are not forthcoming from extractive industries. And any excessive concession to induce the flow of funds to the extractive industries tends in the long run to reduce that available to the secondary manufacturing industries. Also, the concessionary tax benefit given to the resource industries may partly account for the excessive inflow of foreign capital with the result that considerable upward pressure was put on the Canadian dollar.

The Commission also recommended the abolition of the depletion allowance; and for immediate write-off of exploration and development expenses, it recommended that exploration expenditures be given immediate write off, but the development expenses be spread over a number of years, and, if an incentive is needed it could be achieved more effectively through subsidies.

The Commission next dealt more specifically on the depletion allowance and the three-year exemption of tax for new mines. These aspects of the incentive
system came under searching criticism by the Commission. It contended that "percentage depletion is an extremely expensive incentive for encouraging mineral and petroleum exploration" (25) for the following reasons:

(i) the incentive is related to current profit and not to costs. Incentive to encourage exploration could be done by relating it to the additional exploration expenditure "so that exploration that would have taken place without the incentive would not be unduly rewarded". (26)

(ii) because exploration expenses must be deducted before the depletion allowance, the less a corporation spends on exploration the larger will be the depletion benefit. This may discourage exploration. In any event, the impact is uncertain. (27)

(iii) depletion allowances are of benefit to only established corporations with operating income. Small corporations receive little direct benefits. (28)

The Commission regarded the three year exemption for new mines to be more efficient than the depletion allowance since it is selective and therefore less costly. However, it involves a large element of waste since the exemption is applied to all regardless of whether their development would have taken place in its absence. Also it provides the greatest benefit to those who need it least. --- i.e. the large mining companies. (29)

The overall view of the Commission on the depletion allowance and the three-year exemption for new mines is summed up as follows:
"The present depletion allowance for both mining and petroleum and the three-year exemption for new mines appear to us to be not only more generous than is necessary to compensate for any risk factor but are, in addition, inappropriate and inefficient incentives. In our view, to the extent that there is to be a divergence from a neutral tax treatment, it would be better to permit an accelerated write-off of all costs, including the cost of properties, development costs, and the cost of properties, development costs, and the cost of depreciable assets which are useful only for a particular exploration or development project or for production from a particular mine or oil or gas well (but not the cost of smelters and refineries). When combined with the more liberal treatment of business losses, such treatment should be quite adequate to offset any bias in the capital markets that might exist against the mining and petroleum industries. (30)

(4) Some observations on the factors that contributed to the Canadian economic recovery in the 1960's.

The short-comings of the tax incentives discussed earlier are but one aspect of the criticism of the whole tax incentive scheme. The other aspect which is also relevant is the question whether the tax incentives especially those which aim at the development of secondary manufacturing industries, are appropriate in the context of the Canadian economy in the 1960's and whether these measures served the objectives.

The Canadian economy riding on the slack of the late 1950's made a remarkable recovery in the 1960's. It can almost be said at the outset that this upswing in the economy is due to factors other than
tax incentives. The following paragraphs will attempt to show that other economic factors tend to overshadow tax incentives in bringing about the economic recovery.

In Chapter II it was noted that the problem in the Canadian economy was due not to a lack of investment. Rather, investment was directed, to a large extent, to the extractive industries. The persistently high interest rate in Canada vis-a-vis the U.S. rates and the premium on the Canadian dollar were contributory factors to the inability of the Canadian manufacturers to compete in both in the domestic and international market. This was especially true for the secondary manufacturing industries and not for the extractive industries. If these were the causes then it appears that the proper policy should have been to adopt an easy money policy to reduce the rate of interest. This will, firstly, encourage domestic investment while at the same time discourage foreign investment which will in turn bring down the premium on the Canadian dollar. (This is true only when the foreign exchange is allowed to fluctuate according to supply and demand, as the Canadian dollar was in the pre-1962 period). The monetary and exchange policies in the 1961-1966 period in fact followed this desirable course.

Credit conditions in Canada eased considerably
in 1961. Interest rates were lower in the second half of the year and substantially lower than that of 1959 and 1960. In the words of the governor of the Bank of Canada:

"Yields on long term government of Canada bonds moved around an average level of close to 5-1/4 per cent during the first five months of 1961. In June they fell to slightly below 5 per cent and remained close to this level through the remainder of the year. Yields on medium-term government bonds fluctuated around a level of about 4-1/2 to 4-3/4 per cent in the first five months fell in June and continued to decline through most of the second half of the year. Yields on 91-day treasury bills fluctuated around an average level of roughly 3-1/4 per cent during the first five months of the year, declined to about 2-1/2 per cent in June and were relatively stable thereafter until they rose in the closing weeks of the year to a level of about 3 per cent."(31)

This easy money condition was brought to an abrupt end with the foreign exchange crisis of June 1962. The drain on the Canadian foreign exchange reserve necessitated a tight monetary policy to induce an inflow of foreign funds. This led to a policy of tight money and high interest rates. In the early months of 1963 foreign capital inflow was sufficient to warrant a policy "to continue to encourage credit conditions that facilitate sound domestic economic expansion"(32) and the Bank Rate which was fixed at 6 per cent in June 1962 was lowered to 5-1/2 per cent in September, to 5 per cent in October, 4 per cent in November and 3-1/2 per cent in May 1963. This trend
was interrupted again in the middle of 1963 when the U.S. announced the introduction of the Interest Equalization Tax. In August, 1963 long and short-term rate differentials between the U.S. and Canada narrowed. Following the measures taken by the U.S. in 1965 to improve its balance of payments, both long and short term rates began to move up and continued through 1966. The yield on long-term government of Canada bonds reached a peak of about 6 per cent. The rate of economic growth also slackened in the course of 1966 and continued through 1967. "The rate of advance in total product was exceptionally high during the closing months of 1965 and in the first quarter of 1966, after which it showed more moderate gains."(33)

The above resume of the course of the Canadian monetary policies seems to indicate a few interesting features of the Canadian economy.

(i) Canada cannot adopt unilaterally monetary policy measures to stimulate investment.

(ii) that any tax measure to discourage foreign investment is at best marginal.

(iii) the attempt in the 1960's to lower the interest rates had a more substantial impact on the course of Canadian economic growth than the tax incentive measures. (See below)
It was also noted in Chapter II that the Canadian manufacturers (i.e. the secondary manufacturers) faced considerable difficulties in both domestic and international markets largely because of the premium on the Canadian dollar. It appears therefore that the right policy measure should be towards removing this feature of the exchange rate.

The Canadian dollar was at a premium right up to about June 1961. As a result of the government's intention to use its exchange funds to reduce the value of the Canadian dollar, its value fell to a discount of 3\% in terms of U.S. funds. But the Canadian dollar gradually weakened until the exchange crisis of 1962. Thereupon the exchange rate was fixed at 92.5 U.S. cents per Canadian dollar. The premium on the Canadian dollar ceased to be important.

To sum up briefly, "basically the cause of the slowdown in the growth of the Canadian economy in the years 1958 to 1961 was an undesirably restrictive monetary policy (which) sharply increased the level of interest in Canada. This encouraged an unnecessarily large inflow of capital funds. The capital inflow raised the value of the Canadian dollar and reduced the competitive power of Canadian business firms in relation to foreign firms.... Had the government
taken steps as early as 1958 to attain a more favourable exchange rate the economy would have enjoyed higher levels of output and employment and a better rate of growth." (35)

In any event the lower exchange rate may be regarded as one of the most important contributing factors accounting for the growth of manufacturing industries in Canada.

The Economic Council of Canada also attributed Canada's recovery to a decline in the exchange rate of the Canadian dollar. "The exchange rate declined from early 1960 to mid 1962, which amounted to 13. per cent, gave a powerful competitive lift to Canada's international economic position." (36)

(5) Some indications of the growth of the Canadian manufacturing industry

The growth in the export of manufactured products can be shown by the total export of manufactures as a percentage of Gross National Product and total export as given by Table XI below. It can be seen that export as a percentage of Gross National Product increased from 15.8°/o in 1961 to 18.0 per cent in 1966 while export of manufactures increased from 19.2°/o to 30.6°/o of the total export.

Table XII shows the import of manufactured goods as a percentage of Gross National Product and
### TABLE XI

**EXPORT OF MANUFACTURED PRODUCTS IN CANADA**

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross National Product ($m)</th>
<th>Total Export of Manu. ($m)</th>
<th>Percent Export of GNP</th>
<th>Export of Manu. as % of GNP</th>
<th>Export of Manu. as % of Export</th>
</tr>
</thead>
<tbody>
<tr>
<td>1961</td>
<td>37,471</td>
<td>5,903</td>
<td>15.8</td>
<td>1,127</td>
<td>3.1</td>
</tr>
<tr>
<td>1962</td>
<td>40,575</td>
<td>6,357</td>
<td>15.7</td>
<td>1,312</td>
<td>3.2</td>
</tr>
<tr>
<td>1963</td>
<td>43,424</td>
<td>6,990</td>
<td>16.1</td>
<td>1,537</td>
<td>3.5</td>
</tr>
<tr>
<td>1964</td>
<td>47,403</td>
<td>8,304</td>
<td>17.5</td>
<td>1,998</td>
<td>4.2</td>
</tr>
<tr>
<td>1965</td>
<td>52,109</td>
<td>8,767</td>
<td>16.9</td>
<td>2,239</td>
<td>4.3</td>
</tr>
<tr>
<td>1966</td>
<td>57,781</td>
<td>10,325</td>
<td>18.0</td>
<td>3,148</td>
<td>5.4</td>
</tr>
</tbody>
</table>

**Note:** The statistics in this table do not form a series with that of Table IV (page 25) because of the change in classification of many of the items. Also it is not possible to retrace the sources of information used by W.F. Lougheed in his book, Secondary Manufacturing Industry in the Canadian Economy from which the statistics are derived. This however, does not impair the analysis above since in themselves, these statistics form series.

**Source:** Compiled from Dominion Bureau of Statistics, Trade of Canada and Canadian Statistical Review.
### TABLE XII

**EXPORT OF MANUFACTURED PRODUCTS IN CANADA**

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross National Product ($m)</th>
<th>Total Import ($m)</th>
<th>Percent of GNP</th>
<th>Import of Manuf. ($m)</th>
<th>Manuf. import as % of GNP</th>
<th>Import of Manuf. as % of total import</th>
</tr>
</thead>
<tbody>
<tr>
<td>1961</td>
<td>37,471</td>
<td>5,771</td>
<td>15.4</td>
<td>3,693</td>
<td>9.8</td>
<td>64.8</td>
</tr>
<tr>
<td>1962</td>
<td>40,575</td>
<td>6,294</td>
<td>15.5</td>
<td>3,889</td>
<td>9.5</td>
<td>62.0</td>
</tr>
<tr>
<td>1963</td>
<td>43,424</td>
<td>6,578</td>
<td>15.2</td>
<td>4,032</td>
<td>9.3</td>
<td>61.2</td>
</tr>
<tr>
<td>1964</td>
<td>47,403</td>
<td>7,488</td>
<td>15.8</td>
<td>4,645</td>
<td>9.8</td>
<td>62.0</td>
</tr>
<tr>
<td>1965</td>
<td>52,109</td>
<td>8,633</td>
<td>16.6</td>
<td>5,412</td>
<td>10.0</td>
<td>62.5</td>
</tr>
<tr>
<td>1966</td>
<td>57,781</td>
<td>9,867</td>
<td>17.1</td>
<td>6,431</td>
<td>11.1</td>
<td>64.8</td>
</tr>
</tbody>
</table>

**Source:** Compiled from Dominion Bureau of Statistics, *Trade of Canada* and Canadian Statistical Review.
total import. From 1961 to 1965, import of manufactures as a percentage of Gross National Product increased only slightly. In fact it is only in later years that there is some increase. But the import of manufactures as a percentage of total import did not show much change until 1966, when it reverted back to the 1961 percentage.

Other economic indicators also show that there was considerable growth in the Canadian manufacturing industries, especially the secondary manufacturing. In terms of correcting Canada's balance of payments deficits Table XIII shows that its current account balance improved markedly from 1961 to 1966, except in 1965. The improvement is due largely to the merchandise trade surplus, caused principally by the decline in the exchange rate.
### TABLE XIII

<table>
<thead>
<tr>
<th>Year</th>
<th>Merchandise Trade</th>
<th>Non-merchandise Trade</th>
<th>Current Account Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1956</td>
<td>-725</td>
<td>-644</td>
<td>-1,372</td>
</tr>
<tr>
<td>1957</td>
<td>-594</td>
<td>-857</td>
<td>-1,451</td>
</tr>
<tr>
<td>1958</td>
<td>-176</td>
<td>-961</td>
<td>-1,137</td>
</tr>
<tr>
<td>1959</td>
<td>-421</td>
<td>-1,066</td>
<td>-1,487</td>
</tr>
<tr>
<td>1960</td>
<td>-148</td>
<td>-1,085</td>
<td>-1,233</td>
</tr>
<tr>
<td>1961</td>
<td>+173</td>
<td>-1,101</td>
<td>-928</td>
</tr>
<tr>
<td>1962</td>
<td>+184</td>
<td>-1,014</td>
<td>-830</td>
</tr>
<tr>
<td>1963</td>
<td>+503</td>
<td>-1,124</td>
<td>-521</td>
</tr>
<tr>
<td>1964</td>
<td>+701</td>
<td>-1,125</td>
<td>-424</td>
</tr>
<tr>
<td>1965</td>
<td>+118</td>
<td>-1,201</td>
<td>-1,083</td>
</tr>
<tr>
<td>1966</td>
<td>+380</td>
<td>-1,363</td>
<td>-983</td>
</tr>
</tbody>
</table>


With respect to the incentive provisions to foster development in the underdeveloped areas in Canada, no statistics are available. However, since most of the "designated areas" are in fact in the Atlantic and Quebec Provinces a comparison of the unemployment rates of these provinces with that of the national average may throw some light on the success of the scheme.
TABLE XIV

UNEMPLOYMENT RATES BY REGION
(Unemployment as a per cent of the labour force)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Atlantic</td>
<td>10.7</td>
<td>11.2</td>
<td>10.7</td>
<td>9.5</td>
<td>7.8</td>
<td>7.5</td>
<td>6.5</td>
</tr>
<tr>
<td>Quebec</td>
<td>9.1</td>
<td>9.2</td>
<td>7.5</td>
<td>7.5</td>
<td>6.4</td>
<td>5.5</td>
<td>4.8</td>
</tr>
<tr>
<td>Ontario</td>
<td>5.4</td>
<td>5.2</td>
<td>4.3</td>
<td>3.8</td>
<td>3.2</td>
<td>2.6</td>
<td>2.5</td>
</tr>
<tr>
<td>Prairie</td>
<td>4.2</td>
<td>4.6</td>
<td>3.9</td>
<td>3.7</td>
<td>3.1</td>
<td>2.6</td>
<td>2.1</td>
</tr>
<tr>
<td>B. Columbia</td>
<td>8.5</td>
<td>8.5</td>
<td>6.6</td>
<td>6.4</td>
<td>5.3</td>
<td>4.2</td>
<td>4.6</td>
</tr>
<tr>
<td>Canada</td>
<td>7.0</td>
<td>7.1</td>
<td>5.9</td>
<td>5.5</td>
<td>4.7</td>
<td>3.9</td>
<td>3.6</td>
</tr>
</tbody>
</table>


Table XIV shows the unemployment rates in the different provinces in Canada.

From 1963 to 1966 the national unemployment rate drops by 48.5% whereas in the Atlantic and Quebec provinces it dropped by 31.6 and 36.0 per cent respectively. It may be inferred that the drop in unemployment rate in the two provinces had not been in the same degree of magnitude as the national average.

With respect to the grants for scientific research it is still too early to assess their effect on research. Furthermore, an assessment is again difficult, for research is influenced by many variables.
As for foreign investment, Table VI in Chapter IV shows that direct and indirect foreign investment dropped considerably in 1963, a result of the Interest Equalization Tax in U.S. rather than the change in the withholding tax since the maximum rate of 15% was not changed. However, the proposed 20% for corporations without a degree of Canadian ownership might have caused the drop in foreign direct investment in 1963.

IV. SUMMARY

To conclude this chapter one can observe that Singapore's Pioneer Industries Ordinance, was in a way successful in attracting industries to Singapore, although the extent of its success cannot be assessed. For it is not possible to determine conclusively the success or failure of any country's investment incentive program since there is no record of what would have been in its absence. But based on the expected capital formation in Singapore and the employment target, it is believed that the incentives have not been as successful as was originally envisaged. It is also noticed that Singapore has utilised only two fiscal incentive measures, namely, an acceleration in write off of allowable expenses of certain types and tax exemption on profits. There is no incentive operating through subsidy or grant, and to this extent, the tax incentive scheme could be improved. Furthermore, it was observed that the rate
of growth in Singapore still leaves much to be desired. It is believed therefore that the government may have to take a more direct role in industries if it wants to achieve the employment target. Also, Singapore should not rely unduly on foreign capital for the reason that experience in other countries has been disappointing.

As for Canada, it is believed that the tax incentives played relatively a small part in the economic recovery in the 1960's. It is believed that the monetary and exchange policies were more important. With respect to the incentives it is believed that the incentives given to the extractive industries are too generous and this may partly explain the lack of development in the secondary manufacturing industries in the 1950's.

It is also believed that the financial grants given to research should prove more useful than tax exemption or accelerated capital allowances and hence should be advocated if future tax incentives are required.

Lastly, this chapter serves to show the difficulties of relating tax incentives to industrial growth, or other objectives. It also serves to show that if any tax incentive is to be introduced, a cost and benefit analysis should be undertaken. Only then may the possible impact of particular measures be assessed.
CHAPTER REFERENCE


The countries which participated in this conference are: Japan, West Germany, Italy, The Netherlands, France, Sweden and Great Britain.

(2) Op cit, page 4

(3) Op cit, page 8

(4) Op cit, page 15

(5) Op cit, page 19


(9) Op cit, page 1


(14) S.A. Abbas, Capital Requirements for the Development of South and South-east Asia. J.B. Welters-Groningen (Netherlands) 1956, page 27.


(21) See op cit, page 308-309.

(22) Op cit, page 309.

(23) Op cit, page 309.


(30) Op cit, page 333.


Chapter VII

CONCLUSION

The corporate tax structures of Singapore and Canada were reviewed in Chapters III to VI. In the course of this comparative study it is noted that there are certain similarities. However, it is also obvious that there are major differences. This is expected.

The similarity lies mainly in the determination of the taxable income. It is worth noting that in both countries, items that are reasonably attributable to the earning of income are deductible although many of these items are not explicitly stated in the income tax law of the respective countries. On the other hand, it is true to say that Singapore's tax legislation leaves much to be desired in terms of clarity of definition. Many of the items commonly encountered in business are left to the direction of the comptroller. In this respect, one may say that Singapore's legislations relative to that of Canada need improvements.

Turning to the incentive provisions, it was noted in Chapter II that Singapore's economic structure differs vastly from that of Canada and hence incentive measures must essentially differ. It was noted that in Singapore the problem of industrialization is great and urgent, largely
because of the high population pressure and high level of unemployment. Canada, on the other hand, is a country endowed with extensive resources. Industrialization, namely the growth of a secondary manufacturing industry, though necessary is less pressing as compared with Singapore.

Furthermore it was noted that Canada's problems which the incentive measures were intended to alleviate, seem to be more a result of the uncoordinated nature of the fiscal, monetary and exchange policies pursued during the late 1950's. The economic growth problem in the economy may possibly therefore be removed by better coordinated monetary, fiscal and exchange policies without bringing in some of the incentives which tend to complicate the tax legislation unnecessarily. The Canadian economic problem in the late 1950's and the early 1960's may be said to be short-run in nature as compared with that of Singapore where a structural transformation of the economy is required.

With respect to the incentives introduced in the 1960's in Canada by way of an accelerated capital cost allowance and a tax exemption, one may say that because they are short-lived they are unlikely to be of much value in influencing capital investment. Also, the incentive provisions for the extractive industries which date back to the 1950's might have induced an excessive flow of capital to these industries at the expense of the secondary manufacturing industries.
On the other hand, in Singapore, because of the urgency of the problem, incentive legislation with respect to secondary manufacturing industry is more extensive and generally there is no specification of the duration of the incentives. It was noted that Singapore is in need of a higher level of capital investment, and this need has been and is being approached by fostering both foreign and domestic capital investment in industry. But the study shows that though foreign capital is desirable it is likely that it will not be forthcoming to the extent needed by Singapore to fulfill the investment gap. It is suggested therefore that direct government participation in manufacturing industries may be required since private capital (both local and foreign) has not been forthcoming to the extent required in the past few years.

In examining the detailed approach to tax incentives it was found that Singapore's legislation operates through two principal means, (a) a tax exemption on income and (b) an increase in deductible expenses. It is recommended that incentives should preferably operate through grants or subsidies. The cost of these approaches may at least be measurable.

Lastly, it is recognised that because of the differences in political, social, culture and economic characteristics of the two countries differences with respect to tax incentive provisions must inevitably exist.
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GENERAL


