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**REPORT OF THE
COMMONWEALTH CARIBBEAN
REGIONAL WORKSHOP ON
HARMONIZATION OF FISCAL
INCENTIVES TO INDUSTRIES**



PORT-OF-SPAIN, TRINIDAD & TOBAGO

8-12 September 1969

UNITED NATIONS

ECONOMIC COMMISSION FOR LATIN AMERICA

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OFFICE FOR THE CARIBBEAN

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CHAPTER I: INTRODUCTION

1. A Workshop on Harmonization of Fiscal Incentives to the Manufacturing Industry within the CARIFTA region was held at Port of Spain, Trinidad and Tobago, from 8-12 September 1969. The Workshop was sponsored by the United Nations Technical Assistance Programme. It was organized jointly by the Economic Commission for Latin America (Office for the Caribbean) and the Government of Trinidad and Tobago with the cooperation of the Division of Public Finance and Financial Institutions of the Department of Economic and Social Affairs, United Nations, New York; Permanent Secretariat for Central American Economic Integration (SIECA); and the University of the West Indies. It was attended by 29 participants from 12 countries. The Secretariat of the Caribbean Free Trade Association as well as the University of the West Indies had each sent a representative to the meeting. The participants attended the Workshop in their individual capacities and the views expressed by them did not necessarily represent those of their Governments.

2. The Workshop was formally opened by Dr. the Rt. Hon. Eric Williams, Prime Minister of Trinidad & Tobago. At the inaugural session Mr. Frank Rampersad, Chairman of the Session and a Director of the Workshop, welcomed the Prime Minister and participants to the Workshop, and outlined the broad framework within which the Workshop was conceived. Mr. George Rampersad, Acting Director of the ECLA Office for the Caribbean, read a statement on behalf of the ECLA Executive Secretary in which were outlined the objectives of the Workshop and ECLA's approach to some of the development problems facing Commonwealth Caribbean countries.

3. The Prime Minister, in his opening address, emphasized the need for formulating a regional incentive policy for the member countries of CARIFTA and stressed its significance in attaining the objectives and goals of economic integration within the area. He urged the participants to pursue co-operative rather than competitive economic strategies in the dynamics of international relations both at the level of the outside government or the outside firm. "We are" he said "now in mid-stream in the perilous

waters which we must cross in order to achieve West Indian economic integration" and he added "let us not falter, now that we are encountering the tricky current of the harmonization of fiscal incentives." In conclusion, he wished all the participants success in their deliberations. Mr. Iqbal Gulati, a Director of the Workshop, thanked the Prime Minister for his opening address and the Government of Trinidad and Tobago for providing all the host facilities.

4. The Workshop had before it the Report on Harmonization of Fiscal Incentives to Industries in the CARIFTA Territories (E/CN.12/845), in its draft form, prepared by a team of experts appointed by the Economic Commission for Latin America to study this question.^{1/} The Workshop discussed principally the role of incentives in industrial development and of harmonization in economic integration, evaluation of existing incentives and various elements of a regional incentive policy.

5. Messrs. H. Walker of Jamaica, Charles Cadet of St. Lucia, Bernard Primus of Trinidad and Tobago, and Steve De Castro of the University of the West Indies were elected Chairmen to chair various Plenary Sessions of the Workshop. A Drafting Committee was also appointed to draft the Report of the Workshop. Mr. Frank Thompson of Trinidad and Tobago and Dr. Paul Chen-Young of Jamaica were respectively elected Chairman and Rapporteur of the Drafting Committee. Mr. Frank Rampersad, Acting Permanent Secretary, Ministry of Finance, Trinidad and Tobago and Mr. Iqbal Gulati, Regional Economic Adviser attached to the ECLA Office for the Caribbean, served as Directors of the Workshop.

6. At the concluding Plenary Session of the Workshop, Mr. Donald Augustin of Guyana and Mr. H. Walker of Jamaica thanked ECLA for organizing the Workshop and also expressed

^{1/} Referred to hereinafter as the Expert Team's Report.

their gratitude, on behalf of all the participants, to the Government of Trinidad and Tobago for providing all the host facilities and particularly to the Prime Minister for opening the Workshop.

CHAPTER II: THE ROLE OF INCENTIVES IN INDUSTRIAL DEVELOPMENT AND OF HARMONIZATION IN ECONOMIC INTEGRATION

7. The Workshop considered the role of incentives in industrial development and their harmonization in the context of economic integration of the CARIFTA countries. It was clearly recognized that incentives were only one of the factors influencing investment decisions. Of great importance were other factors such as well developed infrastructure, size of market, availability of trained labour force, existence of a capital market, and political stability. In view of this, it was rather difficult to determine explicitly the weight attached to the incentive factor - particularly tax incentives - by investors. However, since articulations in fiscal policy did influence levels of costs and profits at the enterprise level, it was generally agreed that incentives played a positive role in promoting industrial development in developing countries. This was also borne out by the experience of the CARIFTA countries and the Workshop observed that incentives were further needed to accelerate the pace of industrial development in the region. In future attempts at industrialization, the incentive policy, the Workshop stressed, should however be closely linked to the objectives and strategy of industrial development which needed to be stated explicitly.

8. The Workshop distinguished several types of fiscal and non-fiscal incentives. Among fiscal incentives, it further made a distinction between revenue (tax) incentives and expenditures (subsidies) incentives. Generally, fiscal incentives influenced level of costs, encouraged early recovery of capital and contributed to maximum retention of profit at the enterprise level. Tax incentives were generally preferred to direct subsidies although both measures implied sacrifices. Subsidies in the form of direct assistance such as for in-factory labour training, feasibility studies etc. might be more effective in certain situations. Among non-

fiscal incentives, granting of protection was considered to be most important. It was stated that in the minds of investors, a high degree of protection probably ranked higher than some of the fiscal incentives. It was, however, pointed out that the Caribbean countries did not use a single incentive but a combination of fiscal and non-fiscal incentives, in which protection played a major role in many countries. It was generally recognized that where other complementary factors affecting investment were present, the role of incentives would be more effective.

9. Some participants pointed out that within the framework of the CARIFTA Agreement the role of incentives had to be reassessed. CARIFTA had produced a larger integrated market and hence the extent and intensity of incentives had to be re-examined. It was pointed out that the size of market could be considered a distinct advantage since import coefficients for industry were generally at a much higher level and were comparable to some of the larger integrated markets outside the region. However, some of the relatively less developed member countries of the CARIFTA region were not immediately in a position to exploit the increased size of the market owing to infrastructural deficiencies of their economies.

10. It was the general consensus of the Workshop that harmonization of incentives was essential among member countries of CARIFTA. Harmonization of tax incentives within the CARIFTA region would permit a reduction in the 'auction of capital' or 'leap-frogging' that had arisen because of competition for foreign investment in the region. A well-planned scheme might also serve to correct imbalances within the region between the more developed and less developed territories. Further a properly defined scheme of incentives could create greater linkages within the Area and thus assist regional development by maximizing regional incomes. Harmonization also would facilitate a rational approach to the formulation of regional industrial policy and avoid revenue losses arising through competition in the granting of incentives.

CHAPTER III: EVALUATION OF EXISTING INCENTIVES

11. The principal objective of the existing tax incentive policy in the CARIFTA countries was to promote industrial development. However, existing incentive legislation did not fully reflect industrial priorities in a strategy of development. The criteria prescribed for the granting of incentives were in most cases couched in general terms. They did not distinguish various types of industries nor did they identify any favoured areas of manufacturing activity. The incentives were therefore not tailored to any specific objective but a pre-determined package was extended to industries regardless of their actual priorities. Some incentive laws embodied the concept of a "pioneer industry" approach and a few referred to beneficial effects on employment and output.

12. Formulation of general criteria did not, however, imply the non-existence of priorities. The translation of general criteria into specific objectives had inevitably to be left to the administration which, owing to inadequate specificity in incentive laws, had to use largely suasion and various ad hoc measures with investors in order to attain certain objectives such as utilization of local raw materials. Some countries have introduced separate and formal measures for the promotion of certain types of activities. For example, Barbados and Jamaica have enacted special legislation for the promotion of export industries. Similarly Trinidad and Tobago has introduced special legislation for cement, fertilizers and petrochemical industries.

13. The experience of some countries indicated that the granting of duty free importation of raw materials did not encourage a search for local inputs. Investors often rejected local raw materials on various grounds such as quality, price and inadequate volume. This incentive was found to be particularly suitable for largely export industries and "enclave" industries. Some participants

pointed out that investors considered protection and duty free imports more important than income tax concessions. Generally, it was considered essential to have built-in performance requirements leading to the substitution of imports.

14. The participants also stressed the relationship between specific incentives offered by various countries and their basic tax structures. It was pointed out that basic tax structures were different and contained varying degrees of built-in incentive effects whose influence became more obvious after the enjoyment of specific incentives by enterprises was exhausted. In order to remove these disparities, it was considered highly desirable, as a next step, to work towards harmonization of basic tax structures of CARIFTA countries.

15. With regard to the form of protection, the Workshop discussed the relative merits of quota restrictions and tariffs. It was stated that protection essentially implied certain amount of sacrifice or acceptable degree of inefficiency. It was admitted that the use of tariffs would introduce some element of competition which was largely precluded by the use of quota restrictions. It was therefore necessary to move towards the use of tariffs whenever appropriate. A number of participants, however, defended the current practice of quota restrictions. It was pointed out that consumers in the region had not only a high propensity to consume imported goods but such behaviour was also marked by considerations of quality or prestige associated, in the public mind, with imported goods. At least in the short-run, quota restrictions were more effective in checking these consumer preferences. Secondly, different countries accorded different degrees of protection to industries and degrees of competition also varied for the same industries in different countries. Under these circumstances, quota restrictions were administratively more effective and they also had the merit of preventing dumping which might otherwise take place under a tariff system. It was, however, agreed by all participants that it was essential to evolve a regional

policy towards protection taking into account particularly the interests of relatively less developed member countries of CARIFTA. It was envisaged that in keeping with the spirit of balanced regional development, the latter group of countries might have to offer partial protection for certain industries against competitive imports from the more developed member countries. The question of protection in all its forms was therefore very relevant to the scheme of incentive harmonization.

16. The participants noted that non-tax incentives were given in very few countries. For example, in a few countries factory facilities were given to only export industries and to highly labour intensive industries as well as financial assistance provided to investors. Several participants stressed the need to extend relevant and effective technical assistance to small investors.

17. The Workshop observed that in most of the countries the follow-up procedures and an ex-post appraisal of the impact of incentives was still far from satisfactory. This was explained largely by the non-availability of relevant, complete and accurate data. The incentive legislations did not generally enjoin on investors the obligation to provide relevant data for appraisal nor were the efforts of different administrative agencies within the individual territories systematically coordinated. As a result of this, there was hardly any adequate information in a majority of countries to evaluate net benefits accruing from the granting of incentives.

CHAPTER IV: REGIONAL HARMONIZATION OF INCENTIVES

18. After evaluating existing incentives, the Workshop directed its attention to the formulation of a regional incentive policy. It discussed various aspects of such a policy such as objectives of regional incentive policy, classification of industries, concept and definition of contribution made by industries and the scale of income-tax benefits to be accorded to them, depreciation provision, treatment of imported raw materials, transitional arrangements, etc.

19. In the discussions on regional incentive policy the Workshop recalled certain guidelines included in the CARIFTA Agreement in particular to the effect that certain industries may need regional protection and also that the less developed member countries would require preferential incentive treatment so as to accelerate their pace of development.

Objectives

20. It was stated by some participants that incentives were essentially intended for private investors who sought to optimize their rates of return. It was argued that certain objectives such as optimal location of industry and equitable distribution of developmental gains could be pursued outside the framework of incentive harmonization though they were important within the framework of integration. Although profit maximization was a legitimate objective of private enterprise, a regional incentive policy, it was argued by a majority of participants, should seek to reconcile maximization of private profits with maximization of local contribution to the region. The formulation of regional incentive policy within the framework of CARIFTA Agreement therefore assumed several dimensions. It was stressed by all participants that a regional incentive policy must form an integral part of the overall development strategy in the Area and ought to provide discriminating tools of

implementing priorities underlying that strategy. It was, therefore, considered essential to spell out principal objectives of regional incentive policy. The Workshop attached great importance to the achievement of full employment, utilization of regional resources, diversification of the present economic structures obtaining in the Area, and a balanced regional development. It was, therefore, considered essential to ensure optimality in the location of industries and an equitable distribution of gains arising from development, and also to avoid as far as practicable any tendency towards polarization. It was also pointed out that the relatively small size of the CARIFTA market imposed certain constraints on industrial development in the Area and these could be mitigated if markets could be found abroad for industrial products of the Area. In such cases, production for the domestic market alone was unable to realise economies of scale and would take place at sub-optimal levels. The Workshop, therefore, placed an added emphasis on production for the markets outside the Area and stressed the need for according special incentives to exports, the encouragement of which would be crucial in industrial development strategy; at the same time a regional programme of incentives should have due regard for the fiscal position of the countries in the region.

Classification of Industries

21. The Workshop considered alternative classifications of industries so as to relate benefits to their contribution. The Expert Team's Report on harmonization had suggested a classification into: (a) industries not eligible for tax incentives, (b) enclave industries,^{1/} (c) capital-intensive industries, and (d) all other industries. Some participants suggested a classification into terms of: (i) insular import substitution, (ii) regional import substitution, (iii) enclave,

^{1/} i.e. industries which sell all their output abroad.

and (iv) resource based export industries. A reference was also made to the classification of industries included in the Central American Agreement on the Harmonization of Fiscal Incentives.

22. On the question of establishing a regional list of industries to be excluded from incentives, the participants expressed different views. Those who favoured such a list argued that although no industries may be excluded now, it was essential to accept the principle of exclusion and provide a device which might be needed later. Others pointed out that no industries, including the existing ones, should be denied the benefits of incentives now or later. They envisaged a possibility where what may be considered as a traditional industry in the country may need incentives for its development in another country. There was general agreement that provision should be made at some stage for the compilation of a list of industries which would not qualify for fiscal incentives. Some participants envisaged difficulty in the early preparation of such a list.

23. Because of the special nature of enclave industries it was stated by several participants that these industries should be excluded from any classification that aimed at linking benefits to performance. Such industries, they argued, were attracted essentially by the lower labour costs prevailing in the region, but offered little scope for generating any backward linkage effects. The application of any performance criteria e.g. local value added^{2/} was therefore not relevant to these industries. Some participants questioned the view that the local value added consideration was not significant in the case of such industries and

^{2/} For a definition of this concept, please see paragraph 138 of the Expert Team's Report and for a modified version see paragraph 25 (a) of this Report.

pointed out that in a dynamic situation local value added by them may increase owing to the use of local raw materials and participation of local equity capital. A majority of participants, however, favoured their exclusion and preferred a flat period of tax holiday irrespective of their contribution to local value added. It was agreed by all participants that incentives for such industries needed to be harmonized and that less developed member countries of the Area should offer more attractive incentives to such industries than relatively developed countries.

24. The Workshop expressed concern over the "leap-frogging" tendency of enclave industries. The participants envisaged two situations where an enclave enterprise may move from one territory to another. It may simply extend the scale of its operations and establish an additional plant in a member territory offering higher incentives. Alternatively, it may close its plant in a territory, after the expiration of tax holiday period, and reopen in another territory. In the latter case, it was suggested that an enclave enterprise should be allowed to enjoy tax holiday only for the period equivalent to the difference between the longer period available in a less developed territory and the period of tax holiday which the enterprise had already enjoyed. The Workshop did not reach any conclusion on measures to prevent their "leap-frogging", but it was recognized that any territory may offer the full benefits to a new enterprise coming to that territory. The Workshop noted the practice whereby tax holiday could be extended indefinitely and expressed concern about it.

Performance Criteria and Specific Incentives

25. The Workshop appointed a small Committee to review performance criteria and the regional scheme of specific

incentives included in the Expert Team's Report ^{3/}.
The views of the Committee were subsequently submitted to the Workshop. The Committee had made the following recommendations:

(a) Performance Criteria, Concept and Measurement

The local value added should be the criterion for measuring contribution made by all industries other than enclave industries. The local value added was defined as follows:-

The sum of

- (i) wages and salaries paid during the year;
 - (ii) raw materials (including fuels) and components of regional origin and those certified for area treatment under CARIFTA Agreement;
 - (iii) interest and management charges paid;
 - (iv) profits before tax (after making all the deductions including depreciation deduction)
- LESS the sum of
- (v) wages and salaries paid to non-citizens;
 - (vi) interest and management charges accruing to non-citizens; and
 - (vii) profits distributed and remitted abroad (including all branch profits of foreign companies not reinvested locally).

With respect to item (ii), it was envisaged that certain raw materials produced in a given member territory may not qualify for area treatment,^{4/} but may make a substantial contribution to local value added at the national level. It was agreed to draw up a list of such raw materials at the regional level with a view to accord them preferential treatment in the calculations of local value added in other territories.

^{3/} See paragraphs 119 to 155 of the Report.

^{4/} Under CARIFTA Agreement.

(b)	<u>Structure of Contributions and Groups of Industries</u>	<u>Percentage Value Added Locally</u>
	Group I:	50 and above
	Group II:	20 and over
	Group III:	Less than 20
	Group IV:	Enclave industries

As an additional precondition it was suggested that the more developed countries should offer the prescribed tax holiday in Group I only to those industries which manufactured capital goods, intermediate goods and industrial raw materials. This qualification would be non-applicable to less developed territories. Importation of plant, equipment and spare parts should be exempt from duty for all enterprises falling under Groups I, II and IV for the duration of the tax holiday period. For Group III, such exemption should be given for five years.

(c) Pioneer and Existing Industry

A distinction was made between a pioneer industry and an established industry. If an enterprise or enterprises in a territory in an industry met at least twenty percent of domestic (national) demand then that industry would be considered as an "established" industry and any subsequent enterprise in the same industry in the same territory should receive tax holiday for the residual period.

(d) Income-Tax Holiday

Benefits should be proportional to contribution measured in terms of local value added; except for enclave industries. The following scale of incentives was suggested:

<u>TYPE OF INDUSTRY</u>	<u>NUMBER OF YEARS TAX HOLIDAY</u>		
	<u>Developed Countries^{5/}</u>		<u>Less developed countries</u>
	<u>Developed Areas</u>	<u>Depressed Areas</u>	
Group I	10	up to 15	10
Group II	5	up to 7	8
Group III	NIL	NIL	5
Enclave Industries ^{6/}	10	up to 15	15

It was recognized that less developed territories might wish to accord protection to some of the industries falling under Group I even against competitive imports from more developed member countries. It was therefore, recommended that they should invoke Article 39 of the CARIFTA Agreement for this purpose. If such an industry did not receive protection, then it would be entitled to 15 years tax holiday in a less developed territory.

(e) Performance Appraisal

Since tax holidays were to be given ex-ante, it was considered essential to prescribe certain procedures for appraising performance. First appraisal should be undertaken after three years from the date of production. If the expected performance is not satisfactory in terms of local value added, then benefits should be made proportional to the contribution. Subsequent evaluations should be undertaken every two years and adjustments should be made to the benefits on a pro-rata basis. In the case of

^{5/} i.e. Barbados, Guyana, Jamaica and Trinidad and Tobago as per CARIFTA Agreement.

^{6/} As agreed already at the Plenary Session of the Workshop.

industries falling in Group II, if the performance is found to be unsatisfactory after the first three years, then tax benefits should be revoked. They may be continued only if it is proved satisfactorily that adverse performance was the result of special circumstances affecting the enterprise or industry in question.

(f) Duty Free Importation of Raw Materials

Importation of raw materials may be exempted from duties provided such raw materials are not available in the region in adequate quantity. When raw materials are available in adequate quantities and comparable price and quality suitable tariffs should be levied on their importation.

(g) Depreciation

Normal depreciation, in accordance with income tax legislation, should be deducted during the period of tax holiday and deferment of depreciation deduction until after the end of tax holiday period should not be permitted.

(h) Investment Allowance

Since capital intensive industries were not separately identified, the Committee did not recommend investment allowance.

(i) Export Allowance

The Committee endorsed the proposal included in paragraph 145 of the Expert Team's Report.

26. The Workshop discussed these recommendations of the Committee and made several observations. In the first place, it accepted the principle of the use of local value as the criterion of measuring contribution made by all enterprises

other than those engaged in enclave industries. It also agreed with the definition of this concept as given by the Committee and, further, agreed that a list of raw materials as proposed in paragraph 25 (a) should be drawn up.

27. Some participants questioned the concept of depressed area in a more developed country and its use for according a preferential treatment to such areas. It was pointed out that such a concept was vague and not relevant to regional harmonization. Such distinctions could be made only among countries and not within a country. It was noted that this concept was used for granting special concessions only in one territory where considerations such as level of unemployment, opportunities for employment, infrastructure facilities, social amenities, and proximity to main towns were considerations in designating a depressed area. It was pointed out by some participants that such conditions existed even in some of the main towns of member territories which could not however be considered as depressed areas. The Workshop did not reach any conclusion on a clear and precise definition of the concept of depressed areas and underlined the need to study this concept further.

28. A view was expressed that the recommendations of the Committee contained in paragraphs 25 (d) and (g) were too restrictive and less liberal than the existing criteria prevailing in some territories and would adversely affect their competitive position vis-a-vis third countries. In particular, it was suggested that the industry qualification for Group I as proposed in paragraph 25 (b) above - viz., that they engage in the manufacture of capital goods, intermediate goods, and industrial raw materials - should be deleted and the less developed countries may be allowed to give a tax holiday of 15 years to industries in Group I. It was further suggested that enterprises should be allowed to defer depreciation deductions until after the end of the tax holiday period.

29. Several participants objected to the deletion of the industry qualification as proposed in paragraph 25 (b) above and argued that such a deletion would widen the range of industries that would be eligible for incentives under Group I, since it would be easy for many industries to satisfy the criterion of local value added of more than 50%. It was suggested that if the industry qualification were to be eliminated, it would be necessary either to reduce the length of the tax holiday period or to raise the required percentage of value added to over 50% for more developed countries. It was also suggested that the relevant value added criterion for Group I should be relatively lower for less developed territories in order to raise effective advantage in their favour. Several participants also argued strongly against deferment of depreciation deductions. Some participants expressed strong agreement with the strategy implied by the recommendations in the Expert Team's Report, namely that there should be a short period of full tax exemption to be followed by a longer period of partial tax exemption, such exemption being related to performance in exports and value added.

30. In its discussions on the nature and extent of income tax benefits, the Workshop reached an agreement on several points as well as expressed reservations on a few questions. It accepted the principle of the use of local value added as the criterion of measuring contributions made by all enterprises - except enclave enterprises - and of appraising their performance during the period of benefits. It also accepted the principle of establishing a list of industries to be excluded from the granting of any concessions under the regional incentive scheme. The Workshop agreed on establishing two groups of industries, viz. enclave industries and "other industries". An agreement was also reached on the nature and extent of income tax benefits to be extended to enclave industries.

All the participants consented to the idea of establishing groups of industries in terms of contribution made by them to the local value added to the region. It was envisaged and agreed that in more developed countries benefits would be extended only to those industries which made a contribution in excess of a certain minimum contribution in terms of local value added. The Workshop also agreed that in formulating a scheme on regional incentive policy, preferential treatment should be accorded to the less developed countries. However, consensus could not be reached on retention or otherwise of the additional condition of the application of Group I benefits in more developed countries to only certain types of industries. Some participants felt that without this additional condition, the exemption recommended for a fixed tax holiday period to specific industries in Group I, for more developed countries in particular, would be unduly liberal. Some participants also felt that for more developed territories it was essential not only to retain the industry condition but also to raise the local value added percentage while keeping at a lower level the value added percentage for less developed territories. A view was also expressed that the fixing of appropriate scales of value added for determining rates of benefits should have regard for conditions in the region.

Investment Allowance

31. The participants considered that the concept of investment allowances, supplemented if necessary by accelerated depreciation allowances, for capital goods industries, intermediate goods industries and industries producing industrial raw materials would be appropriate for the region. However such concessions should be allowed in lieu of income tax exemptions and not be additional to it. Income tax exemption of a fixed duration to such industries could be allowed only as an alternative to such capital allowances.

Carry-forward of Losses

32. The Workshop agreed that the net losses incurred by an approved enterprise during the tax holiday period taken as a whole should be allowed to be carried forward indefinitely until they are set off against subsequent profits of the same enterprise from the same source.

Treatment of Dividends

33. It was agreed that (i) dividends paid out of profits of the period of tax exemption should be exempt in the hands of shareholders provided the authorities were satisfied fully that these profits were so exempt; (ii) where a shareholder was a non-resident he shall be exempted from so much of income tax as exceeds his liability on such dividends in his country of residence; and (iii) there should be no provision, directly or indirectly, forcing distribution of tax exempt profits by imposing any time limitations on their distribution.

Interest Payments

34. The participants generally agreed that interest payments should not be exempt from income taxation. Apart from the revenue loss incurred and the possibility of an involuntary extension of tax holiday period - if such payments are allowed in the computation of losses to be carried forward - tax exemption of interest payments encouraged, under the present circumstances, loan financing of investment and thereby discriminated permanently between those enterprises that did and those that did not enjoy tax holidays.

Raw Materials

35. The Workshop accepted the Committee's recommendations on the duty-free importation of raw materials and agreed with the principle of establishing a list of raw materials available within the region. This could be done at the regional level e.g. by the CARIFTA Secretariat if each

government informed the CARIFTA Secretariat of raw materials produced within its territory.

Transitional Arrangements

36. With regard to the transitional arrangements, the Workshop agreed that these should be devised in such a manner so that they are not particularly harmful to the new enterprises established after coming into force of the regional agreement on incentive harmonization. It was stated that in principle that enterprises operating under the old incentive legislation should be given a free choice either to continue to enjoy these benefits, previously accorded, or to opt for reclassification under the regional incentive scheme. Where an industry has been "established" ^{7/}, a new enterprise(s) which meets the criteria proposed under the new scheme would receive the benefits applicable.

^{7/} See paragraph 25(c) of this Report.

CHAPTER V: SUMMARY AND CONCLUSIONS

37. Although it was rather difficult to determine explicitly the weight attached to the incentive factor - particularly tax incentives - by private investors, the Workshop agreed that incentives played a positive role in promoting industrial development in developing countries. (Paragraph 7).

38. There was a general consensus that harmonization of incentives was essential among member countries of CARIFTA. Harmonization would aid in balanced regional development, permit a reduction in "leap-frogging" of capital, facilitate a rational approach to the formulation of a regional industrial policy and avoid revenue losses arising through competition in the granting of incentives. (Paragraph 10).

39. The existing incentive legislation, although intended to promote industrial development, did not fully reflect industrial priorities in a strategy of development. The criterion prescribed for the granting of incentives was in most cases couched in general terms. (Paragraph 11).

40. There was an important relationship between specific incentives and disparities in basic tax structures of CARIFTA countries. This relationship became more obvious after the enjoyment of specific incentives by enterprises was exhausted. The Workshop, therefore, considered it highly desirable for CARIFTA countries to work towards harmonization of their basic tax structures. (Paragraph 14).

41. Protection played a very significant role in a scheme of incentives and could not, therefore, be considered independently of a regional incentive policy. The participants generally recognized that the use of tariffs was preferable to quota restrictions as instruments of protection. At the same time they pointed out certain advantages - in the short run - of the quota system which is now widely used in the region. They stressed the need to evolve a regional policy towards protection

taking into account particularly interests of relatively less developed member territories of CARIFTA. (Paragraph 15).

42. The Workshop observed that in a majority of CARIFTA countries, the follow-up procedures and an ex-post appraisal of the impact of incentives was still far from satisfactory owing to the non-availability of relevant, complete and accurate data. (Paragraph 17).

43. The Workshop stressed that a regional incentive policy must form an integral part of the overall development strategy in the Area and ought to provide discriminating tools of implementing priorities underlying that strategy. It described principal objectives of a regional incentive policy as the achievement of full employment, diversification of the present economic structure, and a balanced regional development. In view of the relatively small size of the CARIFTA market and the limitations it placed on industrial development in the Area, the Workshop attached great significance to production for the markets outside the Area and stressed the need for according special incentives to exports. (Paragraph 20).

44. The Workshop agreed on a classification of industries into enclave industries and other industries. (Paragraph 21).

45. The participants accepted the principle of establishing a list of industries, at the regional level, that would be excluded from any incentives. (Paragraph 22).

46. The Workshop agreed that in any regional incentive policy, preferential treatment should be accorded to the less developed territories. (Paragraphs 19 and 30).

47. The Workshop agreed on the need for harmonizing income tax benefits for enclave industries among CARIFTA countries. The Workshop did not appreciate the necessity of relating benefits extended to enclave industries to their performance in terms of local value added but recommended a

fixed period of income tax holiday. (Paragraph 23).

48. The Workshop accepted the principle of local value added as the criteria for measuring contribution made by all enterprises - except enclave - and relating income tax benefits to such contribution. For ease of administration, it modified the definition of local value added given in the Report of the Expert Team. (Paragraph 25(a)).

49. The Workshop established three groups of contributions for industries in terms of local value added and recommended, on an ex ante basis, fixed periods of income tax holiday for the three different groups; both for developed and less developed territories. The benefits available under Group I in more developed territories were to be restricted only to certain types of industries. There was, however, no consensus on the duration of benefits as well as the scope of their application for Group I in more developed territories. (Paragraphs 25(b) and (d)).

50. Agreement was reached on making a distinction between a pioneer industry and an established industry and on the scale of benefits to be extended to them. (Paragraph 25 (c)).

51. Since tax holidays were to be given ex ante, it was agreed to evaluate the performance of tax exempt enterprises periodically and to ensure that the intended benefits were proportional to the promised performance. (Paragraph 25 (e)).

52. In matters of carry-forward of losses, and interest payments the Workshop agreed with the recommendations contained in the Report of the Expert Team. (Paragraphs 32 and 34).

53. On the treatment of dividends, the Workshop agreed with the recommendations of the Expert Team except to the provision that the distribution of the enterprise in the year for which exemption is claimed in the hands of the shareholders should not exceed 10% of equity capital. (Paragraph 33).

54. Importation of plant, equipment and spare parts are to be exempted from duty during the period of income tax holiday. It was agreed that importation of raw materials should be exempt from duties provided such raw materials were not available in the region in adequate quantity. The Workshop also agreed to the principle of establishing a list of raw materials available within the region. (Paragraphs 25 (b), (f) and 35).

55. With regard to the transitional arrangements, it was agreed that the enterprises operating under the old incentive legislation should be given a free choice either to continue to enjoy those benefits or to opt for reclassification under the regional incentive scheme. (Paragraph 36).

List of Participants

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7/ Members of the Expert Team

AGENDA

1. Opening Addresses
2. Adoption of the Agenda
3. Role of Incentives in Industrial Development and of Harmonization in Economic Integration
4. Evaluation of Existing Incentives and of Selection and Follow-up Criteria and Procedures
5. Formulation of Regional Incentive Policy:
 - i) Broad Requirements of a Regional Incentive Policy;
 - ii) Income Tax and Customs Duty Reliefs; and
 - iii) Selection and Evaluation Criteria and Procedures.
6. Adoption of the Workshop Report.

List of Documents submitted to the Workshop

A. WORKING PAPERS

1. EXPERT TEAM'S REPORT ON HARMONIZATION OF FISCAL INCENTIVES TO INDUSTRIES IN THE CARIFTA TERRITORIES - in draft form

E/CN.12/845

B. BACKGROUND PAPERS

1. AGREEMENT ESTABLISHING THE CARIBBEAN FREE TRADE ASSOCIATION
2. AGREEMENT ESTABLISHING THE EAST CARIBBEAN COMMON MARKET
3. CENTRAL AMERICAN AGREEMENT ON FISCAL INCENTIVES TO INDUSTRIAL DEVELOPMENT
4. PROTOCOL (ON PREFERENTIAL TREATMENT FOR HONDURAS) TO CACM AGREEMENT ON FISCAL INCENTIVES TO INDUSTRIAL DEVELOPMENT
5. DRAFT REGULATIONS TO THE CACM AGREEMENT ON FISCAL INCENTIVES TO INDUSTRIAL DEVELOPMENT

STATEMENT MADE ON BEHALF OF EXECUTIVE
SECRETARY
OF UNITED NATIONS ECONOMIC COMMISSION FOR LATIN AMERICA

Mr. Chairman, Rt. Hon. Prime Minister, Hon. Ministers, Your Excellencies, participants, ladies and gentlemen.

On behalf of the Executive Secretary of the U. N. Economic Commission for Latin America, I have the honour of making a brief statement at this inaugural session of the Workshop on Harmonization of Fiscal Incentives to Industry among CARIFTA countries. This is the second Workshop to be held by the Commission in this area since the establishment of its office in Port-of-Spain two and a half years ago.

The Governments of the Commonwealth Caribbean have, in recent months, taken some significant steps in the direction of closer economic co-operation. The ECLA has been closely associated with the deliberations and studies leading up to decisions in this connection, and it hopes to continue assisting actively in the future. An important aspect of this assistance is the organization of training programmes and workshops.

This Workshop was conceived as part of the study on the harmonization of incentives which the Heads of Governments requested the Commission to undertake. As a first step in fulfilling this request, the ECLA Office for the Caribbean assembled a team of United Nations experts headed by Mr. Iqbal Gulati, Regional Economic Adviser for the Caribbean. The team visited most of the member territories and has prepared a Draft Report which was circulated five weeks ago for study and comments by member Governments.

This Report is the principal document before the Workshop, which brings together high level Government officials who are engaged in policy formulation and implementation, and experts in the field of economic and fiscal policy from the United Nations, the Permanent Secretariat of the General Treaty on Central American Integration

and the University of the West Indies. It is hoped that as a result of the discussions and exchange of views between these officials and specialists, there would emerge some consensus regarding the measures to be taken towards harmonization of incentives, and to their phasing in the CARIFTA region.

This present exercise itself in harmonization of incentives may, as the authors of the Report put it, be just the beginning of a series of exercises on this subject. The ECLA would be very happy to assist further in this regard, as and when it is requested.

I would like to take this opportunity of mentioning two other closely related areas in which ECLA is actively involved. At the request of Governments, the ECLA has also been assisting in studies regarding industrial feasibilities in CARIFTA countries. In collaboration with the United Nations Industrial Development Organization, a team of specialists surveyed the area and their report has already been made available to Governments for study.

Another area in which the ECLA is participating actively is that of unification of external tariffs. The Commission has been assisting the East Caribbean Common Market in the preparation of its common external tariff, and hopes to be associated equally actively in the exercise about to be undertaken at the CARIFTA level. The Office for the Caribbean views these three aspects of the work as important ingredients in the formulation and implementation of a successful economic co-operation programme.

In organizing this Workshop, the ECLA Office in Port of Spain has continued to receive the generous assistance and support of the Government of Trinidad and Tobago. For this support we wish to record our appreciation. Within the next six weeks, the ECLA will be organizing another regional Workshop on integrated rural development, this time in Jamaica. In this regard, we have already been receiving the full assistance of that Government.

The Commission holds the view that through these workshops, and its participation at various other levels, it would be in a position to play a constructive role in the promotion of regional co-operation in the Caribbean.

OPENING ADDRESS BY THE PRIME MINISTER
OF
TRINIDAD AND TOBAGO

It is nearly two years ago - namely in October, 1967 - that, along with the other Heads of Governments of the Commonwealth Caribbean countries, I participated in an historic meeting in Bridgetown, Barbados, to set up the CARIFTA Agreement. At that Heads of Governments Conference, we passed a number of resolutions on economic integration. One of these resolutions reads as follows:

"Subject to existing commitments, a regional policy of incentives to industry should be adopted as early as possible on the basis of studies mentioned in Resolution 7 below, bearing in mind the special needs of the less-developed countries for preferential treatment, such as soft loans".

ECLA has now complied with this request from the Heads of Governments and has now submitted this initial Draft Report. It is now for you, the West Indian experts, to discuss this Report and so enable ECLA to complete its Final Report.

I know that you will do a good job. I have every confidence in your ability and your dedication to the great regional enterprise which we, the political leaders of the region, launched two years ago. I am certain, too, that the other Heads of Government repose the same confidence in you that I do. You cannot afford to disappoint us.

To a large extent, the fate of the Region will be shaped by you, the young technicians of the Region. You are, I am sure, all familiar with the history of the Region - with its melancholy pattern of division and antagonism between the islands. You will know from your studies in West Indian history of the "dog-eat-dog" attitude which in the past each individual island had towards the others. It was a question of either competing for favours from the metropolitan government, or influencing the

metropolitan government to discriminate against other islands in receiving preferences, or competing against each other for investments from metropolitan firms. You will know that this pattern has been in existence since the second half of the 17th century. You will also know that, with the achievement of political self-determination in the second half of the 20th century, it is up to us, the popularly elected leaders supported by our technicians, to seek to break this old traditional pattern of West Indian economy. Let us face the very bald truth. It is no use us West Indians complaining that outside Governments and outside investors manipulate us by playing off one territory against another; so long as we remain divided and so long as we pursue competitive rather than co-operative economic strategies, the dynamics of international relations - whether at the level of the outside Government or the outside firm - make this manipulation inevitable. In other words, we have to save ourselves from ourselves.

CARIFTA has survived for two years in spite of stresses and strains, tensions, anxieties and uncertainties. That it is surviving is indeed a matter of congratulation. But we must never rest, we must never consider our service to the West Indian peoples terminated until we, the politicians, and you, the technicians, have implemented all of the resolutions passed by the Heads of Governments in October, 1967. Already, the important study being done on Regional Industrial Development, with special reference to regional integrated industries and to the development of the less developed territories, is almost completed. The study being carried out by the University on Foreign Investment in the Region is nearing completion and we are about to embark upon a study of the Common External Tariff. And we are now showing our solidarity in economic matters, vis-a-vis the outside world, by agreeing to send a single CARIFTA Mission to the European Economic Community to put forward the consequences to our economy of Britain's entry into the Community.

We are, therefore, now in mid-stream in the perilous waters which we must cross in order to achieve West Indian economic integration. Let us not falter, now that we are encountering the tricky current of the harmonization of fiscal incentives. Let

us use our strength, our ingenuity and our determination to get past this current and so eventually find ourselves nearer to the beckoning shore of West Indian economic integration.

I wish you good luck and clear heads in your discussions and studies. From your Directors, Mr. Frank Rampersad and Mr. Iqbal Gulati, you will receive competent and sympathetic collaboration and guidance. They too need your competence and your sympathy for the regional cause.



