UNITED NATIONS
ECONOMIC AND SOCIAL COUNCIL

REPORT ON

HARMONIZATION OF FISCAL INCENTIVES TO INDUSTRIES

IN THE CARIFTA TERRITORIES

UNITED NATIONS
ECONOMIC COMMISSION FOR LATIN AMERICA
OFFICE FOR THE CARIBBEAN, 1969
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PREFACE

This report is the outcome of the study on Harmonization of Fiscal Incentives to Industry in the CARIFTA territories conducted by the United Nations Economic Commission for Latin America. This study was undertaken at the request of the Commonwealth Caribbean Heads of Governments made at their fourth meeting (Resolution 10) and covers the territories forming the Caribbean Free Trade Association and Belize, whose inclusion in the study was subsequently requested.

A team of experts was assembled by ECLA to undertake the study. The team comprised:

(i) Mr. Iqbal Gulati, Regional Economic Adviser attached to the ECLA Office for the Caribbean;

(ii) Mr. D.M. Bhouraskar, Chief of Public Finance Section, Division of Public Finance and Financial Institutions, Department of Economic and Social Affairs, United Nations, New York; and

(iii) Mr. Gustavo Wiese, Regional Adviser on Fiscal Policy attached to the Permanent Secretariat of Central American Common Market.

Mr. Iqbal Gulati was appointed as the leader of this team.

The team visited all the territories except Dominica and Grenada. It held discussions with senior officials from all the territories, and was formally invited to attend the Third Meeting of the East Caribbean Common Market Council of Ministers in St. Lucia. It thus had the privilege of meeting with the Council and discussing matters connected with the harmonization of incentives. The leader of the team also visited Belize.

A draft of this report was submitted to the Commonwealth Caribbean Regional Workshop on the Harmonization of Fiscal Incentives to Industry held at Port-of-Spain from 8 to 12 September 1969. The summary and conclusions from the Report of the Workshop (E/CN.12/844) are reproduced here in Annex I. The expert team has offered its comments on some of the views expressed at the Workshop. These comments are included in Annex II.
On behalf of ECLA, and on behalf of the members of the team, I should like to express our thanks to the Governments, their Ministers and Officials, for extending to the team their maximum cooperation, courtesies and consideration.

Carlos Quintana
Chapter I

INTRODUCTION

1. When the Governments of the Commonwealth Caribbean agreed upon the formation of the Caribbean Free Trade Area (hereafter referred to as CARIFTA), they were, it appears, fully aware that effective progress towards trade liberalisation within the free trade area would depend in large measure on common action in other areas, especially those of industrial policy, external tariff, and incentive policy. The rationale of a common incentive policy is simple and should be quite obvious. Firstly, with respect to commodities in which member countries agree upon free mutual trade, it is essential that disparities in tax incentives should not ordinarily be allowed to distort the inter-member cost structure of their production. Secondly, but no less importantly, member-territories should avoid making sizeable sacrifices in terms of revenue (in addition to what the consumers directly undergo under the impact of protective policies of Governments) in competitive bidding among themselves by the offer of more and more generous tax concessions. Instead, they can offer the attractions of a unified market of a size much larger than any of the national markets, taken separately.

2. Article 23 of the Agreement provides for the approximation of legislation with respect to tax concessions granted for the purpose of encouraging the establishment or development of manufacturing industry.

3. Paragraph 1 of Article 23 provides that no member territory may introduce more generous tax concessions than the most generous already obtaining in any of the member territories. Paragraphs 2 and 3 lay down procedures for notification of changes in incentive provisions made by member territories and for dealing with representations. In paragraph 4 of the same Article, the CARIFTA Council is authorised to recommend, on its own initiative, proposals for the approximation of concessions within the Area. These proposals may include schemes for the increase or reduction of concessions consistently with the provisions of the Agreement and may be implemented notwithstanding the provisions made in paragraph 1 of the said Article.
4. On a careful reading of Article 23, it becomes clear that the provisions of paragraph 1 are intended to be transitory in nature. Until the CARIFTA Council has had time to formulate its recommendations for the approximation of tax incentives being offered to manufacturing industries, individual member territories are allowed under paragraph 1 to introduce changes in their existing tax incentives, as long as they do not thereby offer more generous incentives than the most generous already obtaining in any of the member territories.

5. The long-term objective, however, appears to have been for harmonizing industrial incentives in the region on a rational basis, and the Agreement clearly foresees the possibility that this exercise in harmonization might entail not only increases but also reductions in concessions already being offered. That is why the Agreement clearly states that the proposals of the CARIFTA Council for the approximation of industrial incentives do not have to conform to the rule laid down in paragraph 1, i.e. of approximation at the most generous level of concessions already obtaining.

6. It is in the above context that a Resolution of the Fourth Heads of Government's Conference on Regional Integration called upon the United Nations Economic Commission for Latin America (ECLA) to undertake a study on the harmonizing of incentives. This Resolution was included in Annex A of the CARIFTA Agreement.

7. This report is the outcome of the study undertaken on behalf of ECLA in pursuance of the above Resolution of the CARIFTA Heads of Governments. It is hoped that it will help the CARIFTA Council in formulating its proposals for the approximation of industrial tax incentives and lead ultimately to the adoption of a regional policy on industrial incentives. Also, it is hoped that in due course the Council will, on the basis of the experience gained in harmonizing industrial tax incentives, want to go further and seek to harmonize tax incentives being offered in various member territories in other fields such as tourism, housing, mining and even agriculture so as to ensure balanced development of the territories in the Area. In that sense, this exercise will only mark the beginning of a number of exercises in harmonization of incentives.
8. While the present study derives its authority from the Resolution cited above (followed by formal requests by three of the member Governments in the Area), it covers not only the present eleven member territories of CARIFTA but also Belize (British Honduras) which expects to join the grouping and whose inclusion in the study was specifically requested by the Government.

9. This report is divided into five chapters including this introductory chapter. Chapter II gives the general economic background of the Area, in so far as it is immediately relevant to the subject under study. In Chapter III is attempted a review of the existing situation in the Area with regard to tax incentives offered to industries. This is followed in Chapter IV by an evaluation, principally in terms of economic criteria, of not only the existing incentives but also the machinery and procedures set up for their administration. Chapter V presents recommendations for a regional incentive policy for the Area and outlines a scheme for the harmonization of tax incentives offered to industries.

10. A draft of this Report was submitted to the Caribbean Regional Workshop on the Harmonization of Fiscal Incentives to Industries held at Port-of-Spain from 8 to 12 September 1969. The participants at the Workshop were senior officials drawn from all the member territories of CARIFTA and Belize. The summary and conclusions of this Workshop are reproduced here as Annex I and the team's comments on principal points of divergence with the Report are included in Annex II.
Chapter II

ECONOMIC BACKGROUND

11. A regional incentive policy for the promotion of industrial development must, of necessity, be formulated in the context of the prevailing economic circumstances of the area it covers. The economic picture of the area comprising of the eleven member territories of CARIFTA and Belize is dominated by a few predominant characteristics, some of which are quite peculiar to this Area. The regional policy for harmonization of incentives must, therefore, take due note of these. 1/

12. The first of these characteristics is the smallness of the size of not only each territory by itself but also of the Area as a whole. The total population of the Area comprising of the twelve territories is estimated at 4.5 million in 1967. Although the per capita income of Area as a whole is, relatively speaking, not as low as of most underdeveloped countries in the world, the combined national income of the territories is still small. It is roughly half the combined national income of the five member-countries of the Central American Common Market. As an index, however imperfect, of the size of the market, it shows how small even an integrated Caribbean market would be.

13. The second main characteristic of the Caribbean economic picture is the serious disproportion between the supply of labour force and of the other factors of production. Current unemployment levels in the Area range from 12% to 18% and the average rate of growth of population is estimated at 3% for the Area as a whole. With population growing at such a high rate and the existing levels of unemployment already high by any standard, not only has the problem of providing full productive employment become a serious economic issue but also it has acquired a great measure of urgency in view of its social implications.

1/ In this very short review of the economic background of the Area, the authors of this report have relied principally on the Chapter on "Characteristics of the Caribbean Economies" by William Demas in his book, The Economics of Development in Small Countries (1965).
14. Thirdly, the economies of almost all the territories are structurally highly dependent. They derive a substantial part of their current national income from a small number of primary exports, namely, sugar, banana, mineral oil and bauxite, sold to a few developed countries. Primary exports of the Area are estimated to have contributed nearly 30% to the Area's combined gross product in 1963. Their role in providing employment is even more significant, accounting as they do for over 40% of the Area's working force. But while in the past, including the decade of 1950's, primary exports were the prime-mover of the Area's economic growth, there is increasing evidence that they may not be able to play that role in the future. In fact, agricultural exports of the Area are vitally dependent on special arrangements granted principally by the U.K., and to some extent by Canada, and there is serious danger of earnings from this source not only not increasing but actually declining in the near future. This danger has arisen because of the distinct improvement in the chances of British entry into the European Common Market which may oblige Britain to forsake its old Caribbean sources of its agricultural imports. Constraint on the growth of the Area's mineral exports may emanate more from the supply side than from the demand side. But, on current reckoning, there is no immediate danger of any significant slackening with respect to these exports.

15. While primary production and its export dominate the economic picture of the Area, manufacturing plays a rather minor role in this picture. The contribution of the manufacturing sector to the Area's gross domestic product was estimated at 14% in 1967, and its contribution to the Area's employment was even lower.

16. The Caribbean economies are dependent structurally not only in the sense that a few primary exports going to even fewer countries contribute significantly to their national incomes, but also in that they rely greatly on foreign capital inflows for the financing (of their relatively high rates) of gross capital formation. The average rate of gross capital formation for the Area as a whole is currently estimated at 26% a year. Of this the portion financed by foreign sources, including reinvestment of profits by foreign firms operating in the Area but excluding depreciation allocations, was as high as 36%. If depreciation allocations were included, as they should be, the dependence on foreign
capital would rise very much higher. For Trinidad and Tobago, for instance, the corresponding ratios for 1968 are estimated to be 23% and 62% respectively. This relatively high dependence on foreign funds is due largely to the structural characteristics of the economies, especially of those territories dependent on mineral extraction and refining. Partly, however, it is also a reflection of the low level of domestic savings (i.e. excluding savings of foreign enterprises).

17. The growth of tourism in the Area has been quite rapid in recent years and can be said to have helped diversify the economies to the extent it has reduced, relatively, their dependence on primary exports. But it cannot be ignored that the tourist trade, particularly as it has developed in this Area, has some of the same characteristics as the primary exports. Tourist trade of the Area is highly dependent on the North American continent for both demand as well as source of finance for investment. Also tourist trade has contributed to the growth of local skills at almost the same comparable level of technology as have the Area's primary exports. However, the growth of tourism, if sustained, should provide an additional stimulus for local manufacturing.

18. The fourth significant characteristic of the Area's economic picture is that the extent of economic cooperation among the territories, at the eve of the formation of CARIFTA, was not only very limited but also somewhat lopsided. Trade within the Area accounted for a very small proportion of the total foreign trade of the territories comprising the Area. The share of intra-regional trade in the total foreign trade had remained, more or less, unchanged at around 6% in recent years. At the same time, however, the share of manufactured products, excluding minerals and mineral products, in intra-regional trade, though rather small at present, had been on the increase. The share of manufactures, covered by SITC sections 5 to 8, in intra-regional trade rose from 27% in 1957 to 34% in 1963.

19. But the gain of the increasing share in intra-regional trade in manufacturing had gone to the territories which dominated the manufacturing sector of the Area. Jamaica and Trinidad & Tobago together accounted for 85% of the Area's combined gross manufactured product in 1967. Guyana and Barbados together accounted for another 11%. But
while Jamaica and Trinidad & Tobago together dominated the manufacturing sector, in so far as the trade in manufactured products within the Area was concerned, it was Trinidad and Tobago which dominated the scene, with its share at 59% of the trade as against Jamaica's share of only 18%.

20. To sum up this short review of the economic background, the Area offers, relatively speaking, a rather small-sized market which is in need of basic structural transformation with a view to meeting its serious problem of high (and even rising) level of unemployment, and to reducing its excessively dependent character. While the relative smallness of its present contribution can be taken as a measure of the scope that should exist for the expansion of the manufacturing sector in the Area, future expansion of the manufacturing sector would have consciously to seek a better inter-territorial balance than exists at present.
Chapter III

REVIEW OF EXISTING TAX INCENTIVES

21. The practice of offering tax concessions to new and developing manufacturing enterprises is quite widespread. It is especially so among the developing countries of the world, with the objective of accelerating industrial development. The twelve Caribbean territories covered by this study are no exception. With the help of these tax concessions, the Governments hope not only to encourage the investment of domestic savings but also attract foreign capital into the manufacturing sector. It is broadly true that the development of the manufacturing sector helps developing countries diversify their respective economies and also create, both directly and indirectly, new and more rewarding opportunities for the use of local resources, physical and manpower, whereby the rate of growth of domestic output and incomes can be accelerated.

I. CHOICE OF INDUSTRIES AND ENTERPRISES

Eligible Industries:

22. Each of the twelve Caribbean territories, which the present study covers, offers some tax concessions to manufacturing enterprises. While the principal tax laws of these territories governing the grant of tax concessions do not identify any favoured areas of manufacturing activities, they do lay down some broad, and rather vague, conditions of eligibility.

23. With respect to these broad conditions of eligibility, the twelve Caribbean territories could be divided into three broad groups:

(a) The territories in this group set themselves virtually no formal limitation on the choice of industries. They lay down a very broad requirement such as that "the industry is not being conducted on a commercial scale or at all and for which there are insufficient conditions to enable such industry to be conducted on a commercial scale;" or an industry where there is
favourable prospect of further development. 1/
In this group fall Antigua, Dominica, St. Kitts-
Nevis-Anguilla, St. Vincent and Trinidad & Tobago. 
Belize too can be said to belong to this group.

(b) The territories in this group require that in order 
to qualify for tax concessions the growth of the 
manufacturing industry concerned should not only 
be generally of benefit to the territory but also 
"have a beneficial effect on employment both in 
numbers and in gross wages". 2/ In this group of 
territories fall Barbados, Grenada, Jamaica, 
Montserrat and St. Lucia.

(c) In this last group falls only one territory, 
namely Guyana, whose law requires not only that 
the trade in question should be "wholly of a 
developmental and risk-bearing nature" but also 
"is likely to be instrumental to the development 
of the resources of, and beneficial to the Colony". 3/

When Guyana's law speaks of the development of indigenous resources,
it possibly refers to both physical and manpower resources of the 
territory.

24. In a sense, Barbados and Jamaica can also be said to belong to 
group (c). Their legislations require that before approving an industry 
consideration should also be given to "whether manufacture of the 
product would utilize raw materials or skill available to the Island".

25. While the formal position is vague, in actual practice the 
territories seem to have evolved some system of priorities in the choice 
of industries for concessional treatment. In Barbados and Jamaica, for 
instance, manufacturing exclusively for export is accorded a special 
treatment through formal legislation specially enacted for the purpose. 
But in other territories, as for example Trinidad and Tobago, while no 
special legislation has been enacted for the purpose, manufacturing for

1/ See Section 3 of Trinidad and Tobago's Aid to Pioneer Industries 
Ordinance, 1950.

2/ See Section 3 of Jamaica's Industrial Incentives Law, 1958.

3/ See Section 2 of Guyana's Income Tax (In Aid of Industry) 
Ordinance, 1951.
export has been accorded a somewhat higher priority within the framework of the general incentive legislations. Also, resort has been made sometimes to special legislation for according a higher priority to certain types of industries. In Trinidad and Tobago, for instance, separate incentive legislations were enacted for cement, fertilizer, tyre, lubricating oil and petrochemical industries. Also, Barbados and Jamaica enacted special measures for the promotion of factory construction by itself.

Pioneer Approach:

26. In view of the particular approach followed in these territories in granting concessions, the task of exercising choice as between industries effectively arises at the time of the approval of enterprise. All of them subscribe, formally or informally, to what is referred to as the 'pioneer enterprise' approach. The approach is conceived principally in relation to import-substitute industries, although, formally speaking, approval has to be obtained even by enterprises manufacturing entirely for exports. Basically, the idea is to give the benefit of tax concessions not to all enterprises in an industry but only to a few early starters. These early starters are supposed to face greater risks than those who enter the same industry later. Accordingly, while more than one enterprise in an industry might be granted the benefit, this concession would not be extended once it is felt that establishment of additional capacity in that particular industry does not call for special encouragement. In some cases, it is quite likely that given the size of the domestic (i.e. national) market, establishment of additional capacity may not be justified unless there is reasonable prospect for export.

Financial and Technical Viability:

27. Whether an enterprise manufactures a product for the domestic market or for export, all the territorial laws on the subject of incentives insist upon the approval of the enterprise itself. This, as indicated above, springs partly from the 'pioneer enterprise' approach to which all the territories seem to subscribe. Underlying almost all incentive legislations in the Area is also a certain concept of viability, principally financial, to which an approved enterprise must conform.
28. In Barbados, Belize, Grenada, Jamaica, Montserrat and St. Lucia, to qualify for approval an enterprise should first be a company and, at the same time:

(a) be adequately financed,

(b) have adequate trained personnel or be able to obtain their services,

(c) have access to necessary technical information,

(d) be able to obtain adequate raw materials, and

(e) possess (or will possess) the necessary factory.

Guyana too insists on the enterprise being a company to qualify for tax concessions but does not set any viability conditions. On the other hand, the formal position of Trinidad and Tobago along with Antigua, Dominica and St. Kitts is that to qualify for approval an enterprise does not have to be a company, nor do these territories lay down any conditions which an enterprise should satisfy. But in actual practice they too require an applicant to submit all the information necessary to enable the authorities not only to examine its financial and technical viability, but also evaluate its project in the broader context of the economy.

Level of Investment:

29. In St. Kitts-Nevis-Anguilla, the new incentive legislation dealing with Special Development Areas prescribes a minimum level of investment (EC $250,000) to qualify for tax concessions and also the period within which the construction of the factory in the area declared as a special development area should commence. No other territory imposes, formally or informally, such a condition. Though, in actual practice, the proposed level of investment may influence the decision to approve or reject an application, no rigid rules seem to have evolved in any of the territories on this matter.

4/ Jamaica's Industrial Incentive Law defines 'company' as any company incorporated or registered in the island or a company incorporated outside but carrying on business in the island. The corresponding legislation in Barbados appears to be more restrictive in that it insists on the company's registration in the island. Belize requires the company to be "formed and registered under the Companies Ordinance" of the territory.
Follow up on Performance:

30. By and large, it is true of all the territories in the Area that when an enterprise gets the necessary approval entitling it to tax concessions it is obliged to start construction and then production within the stipulated time. Any failure on either score has to be explained to the satisfaction of the competent authorities. Failure to do so may attract penalties, including revocation of the approval itself. Once an enterprise is duly established there is little, if any, follow up on its performance. As indicated earlier, in some territories, the legislation enjoins the selection of industries on the basis of their beneficial impact on resource-use and employment but no later evaluation.

31. In addition, rules exist in all the territorial legislations to restrict the employment of non-nationals and also to prevent abuse of machinery, plant and materials imported free of duty, and there is possibly some amount of follow-up in this respect. But when it comes to following up on such matters as investment, employment and training of local personnel, and use of local inputs the existing administrative and legal position, on all accounts, is highly unsatisfactory.

II. TAX CONCESSIONS CURRENTLY OFFERED

32. Tax concessions being offered to manufacturing enterprises in the Area fall into two broad groups: (a) income tax relief, and (b) duty free importation. The objective underlying the first group of concessions is to increase after-tax profits. The objective underlying the second group of concessions is to reduce the cost of inputs. Even in the latter case, the ultimate impact should ordinarily be to increase the after-tax profits of the beneficiary. Still the two sets of concessions are so distinctly different, including in their impact on investment decisions, that they have to be considered separately.

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5/ Although Trinidad and Tobago's legislation is rather broadly worded, its new Plan singles out this aspect as one of the important deficiencies in the administration of the territory's tax incentives and proposes that as a matter of policy industries receiving incentives should be followed up to ensure that they fulfill the obligations undertaken on application. See Draft Third Five Year Plan, p. 115.
(a) Income Tax Reliefs

33. As will be observed from Appendix I to this Report, concessions falling in this group are being offered in the form of –

i) holiday from income tax,

ii) relief from income tax on dividends paid out of tax-exempt profits,

iii) relief from income tax on interest on borrowings,

iv) deferral of depreciation deductions,

v) accelerated depreciation deductions, and

vi) carry-forward of losses.

i) Income Tax Holiday:

34. All the territories offer exemption from income tax for a period of years beginning, generally, with the date of production. Jamaica and Barbados offer the approved enterprise a choice between two options. One option is of a straightforward exemption of 7 and 10 years respectively as from the date of production. Under the second option a slightly shorter tax holiday period is combined with deferral of depreciation deductions during the tax holiday period within 3 years of the date of production. By a recent amendment of the Jamaican law, enterprises wanting to manufacture new products – defined as products with respect to which 20% of the Jamaican market is supplied by existing manufacturers in the Island – get a 10-year tax holiday from the date of production or within 3 years thereafter and also deferral of depreciation deductions. In Jamaica, exemption from income tax during the tax holiday period may be either full or 50%. But no criteria are laid down, nor have any evolved over time, on which to rest the decision to grant 100% or 50% of the benefits.

35. Trinidad and Tobago, Guyana and St. Kitts offer a full tax holiday of 5 years which can be extended to 10 years, together with deferral of depreciation deductions until after the tax holiday period. Belize and St. Vincent offer a full 10-year tax holiday but without deferral of depreciation deductions. Of the remaining six territories, Grenada, Montserrat and St. Lucia offer a 7-year tax holiday and Antigua
and Dominica offer a 5-year tax holiday, without deferral of depreciation deductions. The tax holiday offered by St. Lucia may be full or partial but no criteria have been set for determining the extent of holiday to be granted.

36. Lately, for factories located in parts designated as special development areas, St. Kitts has decided to offer a 15-year tax holiday and Dominica a 30-year holiday. Jamaica too, offers an extension of between 1 to 5 years in tax holiday for an enterprise manufacturing a new product and located in designated special development areas.

37. In all the territories, the tax holiday period is related to the date of production which is set for the enterprise in the order approving it for the grant of tax holiday. The enterprise is expected to start turning out its produce in marketable quantities by this date.

ii) Relief from Income Tax on Dividends:

38. All the territories, except Antigua, extend exemption from income tax to dividends paid out of profits accruing to an approved enterprise during its tax holiday period. With the exception of Jamaica and Trinidad & Tobago, all other territories require that to qualify for this exemption dividends should be paid out within a specified period. Belize, Grenada, Montserrat and St. Lucia insist on distribution within the tax holiday period. Barbados, Dominica, Guyana, St. Kitts and St. Vincent allow a further two years, after the expiry of the tax holiday period, for tax exempt distributions to be made. Jamaica and Trinidad & Tobago formerly imposed a similar limitation but have removed it recently. They have possibly recognized that such a limitation only forces enterprises to distribute their profits rather than plough them back. It appears that St. Vincent too has recently removed this limitation on distribution.

39. Several of the territories impose a few additional conditions for dividends paid out of tax holiday profits to qualify for exemption in the hands of recipients. One such condition is that non-resident recipients will qualify for tax exemption, provided they are not liable to income tax on such dividends in the country of their residence; Guyana and Trinidad & Tobago do not impose any such condition and
St. Vincent and St. Kitts seem to have recently abolished this condition. Jamaica belongs to the group which imposes this condition but unlike the rest Jamaica qualifies its condition further. Where a non-resident shareholder is liable to tax on such dividends in his country of residence, his exemption from income tax in Jamaica would be restricted to the excess, if any, of tax payable in Jamaica over that payable in his country of residence. Thus what the Jamaican provision seeks to do is to relieve the non-resident shareholder of tax to the extent that Jamaica is foregoing its revenue in his favour and not in favour of the foreign treasury. The corresponding provision in other territories disqualifies a non-resident shareholder altogether regardless of what amount of tax is payable by him in his country of residence.

40. Another condition which is imposed by Belize, Grenada, Montserrat and St. Lucia is that the total amount paid to shareholders, residents and non-residents, as tax exempt dividends should not exceed the amount invested by these shareholders in the enterprise. One possible justification for this type of restriction could be that these distributions are considered to be in the nature of repayment of capital and as such are exempted only to the extent of the capital subscribed by the shareholders. But the assumption underlying this argument cannot be valid if the shareholders continue to retain, as they do, their shareholdings. Another possible justification could be that this restriction would prevent unduly large amounts to be distributed as tax exempt profits. Where the tax holiday is granted for 7 years, the above restriction would amount to limiting annual tax exempt distributions to 14% of equity capital — a liberal rate of return but limited none-the-less.

iii) Relief from Income Tax on Interest Payments:

41. Barbados offers exemption with respect to interest paid on its debenture stock by an approved enterprise. This exemption holds with respect to the first seven years of the tax holiday period under either of the two tax holiday options that Barbados offers. Where, however, the interest recipient is a non-resident, he will be exempt only if he is not liable to tax on such receipts in the country of his residence. Along with Jamaica, Barbados also offers a 15-year exemption on interest paid by an approved factory builder on its debenture stock.

6/ Their respective Income Tax Ordinances, as updated, do not impose this restriction on tax exempt dividends paid to non-resident shareholders.
42. Trinidad and Tobago does not offer a general exemption on interest payments. But in the case of a few special industries, viz; petrochemicals, lubricating oils and greases, and fertilizers, tax exemption has been offered for the duration of the tax holiday period - which in all the three cases is for 10 years - with respect to interest on loans raised by approved enterprises. St. Kitts too has offered, through its very recent legislation, exemption on interest received by persons making loans to an approved manufacturer locating a factory in the designated special development areas.

43. In none of the territories offering tax exemption on interest paid by approved manufacturers, is any special rule laid down for the treatment of such tax-exempt interest in calculating profits or losses during the tax holiday period. But the permission to deduct tax exempt interest in the calculation of its profit or loss enables an enterprise to extend his effective tax exemption beyond that formally allowed. Barbados does, however, stipulate for an approved builder of factory that tax exempt interest is not to be taken as a deduction in the calculation of profits. Jamaica does not lay down this stipulation for its approved builder.

iv) Deferment of Depreciation Deductions:

44. Most territories require that with respect to investment made during the tax holiday period, normal annual depreciation deductions should be made during the tax holiday period. But some territories allow these deductions to be deferred until after the tax holiday period has expired. Barbados and Jamaica allow this under one of the two tax holiday options. (Jamaica now allows it for all new products). Guyana, St. Kitts and Trinidad & Tobago permit this to all manufacturing enterprises approved for tax holiday. Guyana and Trinidad & Tobago go even further and allow such enterprises to claim these deferred depreciation deductions at accelerated rates allowed under ordinary Income Tax rules. On the other hand, Barbados, Jamaica and St. Kitts expressly forbid this.  

1/ As will be observed from Appendix III to this report, with the exception of Dominica and Belize, all the territories allow faster recovery of capital by allowing a higher deduction than is normally allowed. This concession is widely available to any enterprise incurring expenditure on plant, machinery, and, in most cases, industrial building.
45. Deferment of normal depreciation deductions means that an enterprise can claim these deductions against profits accruing to it on expiry of the period. The result naturally is to reduce the taxable profits of the enterprise during this subsequent period. It can be taken to mean either an extension of the tax holiday period or, even more appropriately, the grant of a substantial investment allowance. It is more in the nature of investment allowance because the extent of relief from income tax is tied up to the amount of investment in depreciable assets — which is precisely what a straightforward investment allowance is supposed to do.

46. But the really disturbing aspect of the concession to compute tax holiday profits without making depreciation deductions arises because dividends are payable tax free in these territories to the full extent of profits thus calculated. It is quite conceivable that on the expiry of the tax holiday period (or within a short while thereafter) an enterprise enjoying this concession may not only have no reserves for further expansion but also have no funds left with itself even to replace its old assets so as to maintain its existing level of production. The likelihood of such a situation arising is particularly strong when tax exemption of dividends paid out of tax holiday profits is made conditional to distributions being within the tax holiday period and a short period thereafter, as is the case in Barbados, Guyana, and St. Kitts.

v) Carry-forward of Losses:

47. Some territories make no special rules for carry-forward of losses, if any, incurred by an enterprise during the period for which it enjoys tax holiday. In the absence of any special provision, the rules applying

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8/ Deferment for a period of 10 years would be equivalent to an investment allowance of 61% assuming that the normal deductions are allowed at the rate of 10% of capital cost, on the declining balance method.

9/ Barbados and Jamaica offer outside of the incentive laws, a straightforward investment allowance of 20% on expenditure incurred on plant and machinery by any enterprise engaged in designated basic industries. The allowance can be claimed against profit chargeable to tax.
to ordinary business losses are possibly being applied in these territories to losses incurred in the tax holiday period. Normally, trade losses not set off against income from other sources in the same year can be carried forward to subsequent years. Antigua, Belize and Dominica fall in this group.

48. Barbados, Grenada, Jamaica, Montserrat and St. Vincent belong to the group which allows losses not written off during the tax holiday period i.e. net losses, to be carried forward to the year or years immediately following and set off against the income of the same enterprise. Barbados allows carry-forward of such losses for 5 years, and Grenada, Jamaica and Montserrat for 6 years. St. Vincent allows an indefinite carry-forward provided the set-off does not reduce the income tax payable in any one year by more than 50%. In Barbados, under the tax holiday option which does not allow deferment of depreciation deductions, the law specifically allows such deductions to be included in the computation of loss in the tax holiday period. But in Jamaica, under a similar option such deductions are specifically excluded in the computation of tax-holiday period loss to be carried forward. Thus, the Jamaican provision is more restrictive than the Barbados provision. Grenada and Montserrat prescribe the same rule as Jamaica, and St. Vincent’s rule appears to be in line with Barbados in this respect. But while Barbados, Jamaica and St. Vincent allow losses carried forward to be set off against the subsequent income of the same enterprise, Grenada and Montserrat do not seem to impose such a restriction.

49. Guyana, St. Kitts and Trinidad & Tobago allow any loss incurred in the tax holiday period to be carried forward and set off against the income in subsequent years. They do not require that only losses not written off during the same period can be carried forward. Thus there need be no netting of losses for the tax holiday period as a whole. Interestingly enough, all these three territories also allow deferment of depreciation deductions until after the expiry of the tax holiday period. Guyana and Trinidad & Tobago impose no limitation on the period for which such losses can be carried forward. Nor does St. Kitts. But St. Kitts requires that the set-off of such losses should not reduce the tax payable in any one year by more than 50%.
50. Barbados and Jamaica too offer a tax holiday option with deferment of depreciation deductions but both allow only net losses i.e. losses not written off, of the tax holiday period to be carried forward and that too for a specified number of years.

(b) Duty-Free Importation

51. As can be seen from Appendix II to this Report, concessions offered under this heading are principally of two types:

i) exemption of machinery, plant and construction materials from import duties, and

ii) exemption of materials and fuels from import duties.

i) Duty-free importation of machinery, plant and construction materials:

52. All the territories provide for duty-free importation of machinery, plant and construction materials by approved enterprises for a specified period. This period usually terminates with the end of the tax holiday period. Generally speaking, the territories do not, however, extend this concession to the importation of items as might be required for effecting repairs or replacements to the existing machinery or plant. Barbados is an exception in that it specifically provides for the duty-free importation of machine parts to be used for effecting repairs, so long as they are imported within the period of 10 years laid down for duty-free importation. Guyana withholds this concession not only from items imported as replacements of existing plant and machinery but also from all machinery and plant not of "British Empire origin".

53. Jamaican law authorizes the Government to withdraw this concession with respect to any article that is produced locally and is both available in adequate quantity and also comparable in price and quality with similar imported articles. Other territories do not specifically make similar provision. But some of them seem to keep this consideration in mind while granting licence for duty-free importation to individual applicants.

54. Belize offers duty-free importation of not only plant, machinery and building materials but also vehicles. Most other territories do not allow duty-free importation of ordinary commercial vehicles.
Duty-free importation of materials and fuels?

Materials going into the manufacture of exports are generally relieved of import duty, either through in-bond importation or through drawback of duty already paid. As is the practice almost all over the world, the customs legislations in the territories covered by this study contain appropriate provisions to this effect. Barbados and Jamaica are the two territories which have enacted separate incentive legislation for enclave enterprises i.e., those engaged exclusively in the manufacture of exports. These legislations provide for duty-free importation of not only plant, machinery and construction materials, but also of materials, fuels, containers and labels. Other territories take recourse to the appropriate provisions in their customs legislations to grant duty-free importation of materials to enclave enterprises. All territories, including Barbados and Jamaica allow duty-free importation of materials to home based enterprises also, with respect to their exports.

As regards enterprises manufacturing for the domestic markets, none of the territories, except Belize and St. Lucia, authorize through their respective incentive legislation duty-free importation of raw materials. But various territories do take recourse, in varying degrees though, to their respective customs legislations to permit duty-free importation of materials to certain enterprises manufacturing for the domestic market. For instance, Guyana's list of exemptions from import duty specifies 18 industries with respect to which certain imported raw materials can be imported duty free. It

The Development Incentives Ordinance of Belize authorizes the Minister to "exempt any raw materials imported for use in a development enterprise from payment of customs duty and entry tax on such terms and conditions as may be stated in the Order." The Ordinance does not require that this concession be given to export enterprises or to enterprises manufacturing any special products. It is believed that in practice the Government tries not to allow duty-free importation of raw materials produced locally. St. Lucia's Development Incentive Ordinance does not specifically provide for duty-free importation of raw materials but a Resolution of the Legislative Council, deriving its authority from the Ordinance, passed on 10 December 1968, grants this exemption specifically.
appears, however, that the territory which has made most extensive use, in recent years, of its customs legislation to allow duty-free importation of industrial raw materials and components is Trinidad and Tobago.

57. As in other territories, in Trinidad and Tobago, the principal incentive legislation dealing with pioneer industrial enterprises does not offer duty-free importation of raw materials. The territory's special incentive legislations concerning cement, nitrogenous fertilizers, and petrochemicals \(^{11}\) industries offer duty-free importation of not only raw materials but also fuel and containers. In actual practice, however, enterprises engaged in other industries and granted the pioneer status have also been granted duty-free importation of raw materials. Even enterprises not approved for pioneer status may be, and in fact are, granted duty-free importation of raw materials. \(^{12}\)

58. Since the formation of CARIFTA, the member-territories other than Trinidad and Tobago are believed to have become more liberal, in varying degrees though, in granting duty-free importation of industrial materials. They are believed to have been under strong pressure for the grant of this concession from enterprises manufacturing for the CARIFTA (including national) market. This pressure derives its main strength from the argument that duty-free importation of raw materials allowed to Trinidad and Tobago manufacturers places the competing manufacturers in the other member territories in an unfavourable competitive position within not only the CARIFTA market but also their respective national markets.

III. RELATED QUESTIONS

59. No comparative study of tax concessions offered by different countries can presume to offer a satisfactory picture without giving

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\(^{11}\) In the case of petrochemicals, a restriction was introduced whereby the approved manufacturer has to satisfy the Comptroller of Customs that such articles are not produced in the territory at reasonable prices.

\(^{12}\) On 30 June 1968, the number of pioneer enterprises enjoying duty-free importation was 102; the number of other assisted industrial enterprises enjoying this concession was 184.
some idea of the position in each of the countries concerned with respect to such intimately related matters as the general level of income taxation, government policy on protection of domestic producers against foreign competition, and other non-tax incentives offered by the government for promotion of industrial development. An attempt is made in the paragraphs that follow to give some idea of the position of the territories covered by this study with respect to these related matters.

Income Tax Levels

60. As can be seen from Appendix III to this Report, the range of tax rates applying to both companies and individuals is quite wide. The rate of tax on company incomes ranges in the Area from 20% in Montserrat to 51.7% in Barbados. At the same time, however, it cannot be ignored that in ten of the twelve territories, the spread is much narrower, namely between 37½% and 45%. With respect to individual incomes, again the range is wide, extending from the maximum marginal rate of 20% in Montserrat to 75% in Barbados, Jamaica and St. Kitts. Here too, nine territories have maximum marginal rates between 65% and 75%. But in Trinidad & Tobago and Jamaica, falling into this group of nine, the maximum rates of 65% and 75% respectively apply to a much higher slab of income than in the remaining seven. In Jamaica, the maximum rate of 75% is payable on the portion of individual income exceeding $35,520 whereas the same rate starts applying in St. Kitts on income exceeding $18,500, and in Barbados on income exceeding $24,000. In Trinidad and Tobago, the maximum rate of 65% is payable on the portion of individual income exceeding $60,000 whereas the same rate starts applying in Antigua on income exceeding $14,400, in St. Vincent on income exceeding $15,000, in Grenada on income exceeding $20,000 and in St. Lucia on income exceeding $24,000. In Guyana, the maximum rate of 70% is payable at the portion of income exceeding $14,500 whereas in Belize it starts applying when income exceeds $35,000.

61. On the whole, the existing position with respect to the level of income taxation in the Area is that the rates applying to company income are somewhat lower in less developed member territories of CARIFTA than those applying in the rest of the territories, but this is not so with regard to individual incomes. Montserrat apart, the burden of tax on
individual incomes should work out to be higher in less developed territories (and also Barbados and Guyana) than in Jamaica and Trinidad & Tobago. Belize, which is not yet a member of CARIFTA, is in the same position as the less developed member territories of CARIFTA.

62. In this connection it is important to note also that, unlike the rest of the territories, Trinidad and Tobago now subscribes to a system of company taxation under which a company pays tax on its profits on its own behalf, and not on behalf of its shareholder. Therefore, the distributions are separately taxable. Thus a company in Trinidad pays 45% tax on its profits and a withholding tax on its distributions made abroad. (The statutory rates laid down for various types of distributions are subject, however, to bilateral tax agreements with different governments.) Jamaica too has recently announced its intention to adopt a similar system as from 1970 when the rate of tax payable by companies on their own behalf will be set at 35% and the withholding tax on distributions, made both locally and abroad, will be payable at the rate of 37½%. In the rest of the territories, the whole tax paid by the Company with respect to the distributed part of its profits is a withholding tax. Therefore, there is no further withholding to be made on distribution.

Protection from Foreign Competition

63. It is estimated that in Jamaica nearly two-thirds of the enterprises manufacturing for the home market and enjoying income tax holiday and other concessions are, at the same time, enjoying some degree of protection from foreign competition. In most cases, protection has been given through quantitative restrictions imposed under a system of import licensing.

13/ In the Tax Agreements negotiated so far, substantial reductions have been agreed upon between Trinidad and Tobago and the countries concerned. The effective burden of the withholding tax on distributions going to these countries is naturally much lower than what it would be if the full statutory rates were applicable.
64. In Trinidad and Tobago too, protection of the home market for domestic manufacturers has taken the form mostly of quantitative restrictions on imports. The list of items subject to quantitative restrictions, called the Negative List, has grown to great proportions in recent years. As in Jamaica, in Trinidad and Tobago too in most cases enterprises receiving benefits of tax holiday and duty-free importation of plant, machinery and, even, raw materials have, at the same time, been extended protection from foreign competition. Again, in Trinidad also protection has been given largely by imposing quantitative restrictions on imports of similar foreign goods. 14/

65. Jamaica and Trinidad & Tobago together account for 85% of the total gross manufactured product of the Area. Both the territories appear to be making liberal use of the system of import licensing in imposing quantitative restrictions on imports of foreign substitutes and thereby protecting their enterprises manufacturing for the home market. Not much use seems to have been made of the higher tariffs to protect the home products. In both the territories, import licensing which now covers a fairly wide range of items has been offered largely in addition to, and not in lieu of, tax concessions that the manufacturers have been granted under their respective incentive programmes.

66. While in the rest of the territories also, the Governments have armed themselves with power to impose quantitative restrictions on imports, this power is not being exercised as freely as in Jamaica and Trinidad & Tobago. The explanation for this restraint in the other territories is not necessarily that they are sceptical of the advantages of this form of protection, but possibly because they have far fewer import substitute industries to protect.

67. It is believed that as a pre-condition to granting protection through quantitative restrictions, the manufacturer is usually asked to

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14/ Between January 1967 and June 1968, as many as 80 additional tariff items were placed on the Negative List. During the same period, 85 factories enjoying income tax holiday and/or duty-free importation are believed to have started production.
assure (and even demonstrate with facts and figures, his ability in this respect) not to raise prices for the consumers of his products by more than a reasonable margin above the similar imported products. At the same time, the Governments retain to themselves the right to issue licences for imports, as and when it has reason to believe either that the local manufacturer is unable to meet the entire local demand, or that the prices the consumer is being called upon to pay for the local product are unjustifiably high. It appears, however, that in actual practice the overall impact of quantitative restrictions on imports has generally been to raise consumer prices.

Other Non-tax Incentives

68. Several territories offer not only tax concessions and protection but also several other facilities to industrial enterprises. For instance, in Barbados four sites have been earmarked for industrial development. The Barbados Development Board offers factory space at these sites at concessional rental and is even prepared in certain circumstances to construct a factory at the client’s request. In Jamaica, the Industrial Development Corporation constructed 24 factories at a cost of $8.2 million between 1956 and 1963 and rented them out to manufacturers. In the 1963-68 Development Plan, a little over $1 million a year was projected for factory construction by the Corporation. The rentals charged by the Corporation are said to contain an element of small subsidy. In Trinidad and Tobago too, the Industrial Development Corporation had, by the end of 1966, 114 factory sites to offer in various industrial estates developed by it. But of these only 20 has been occupied so far. In other territories, this type of assistance, if any, is in its infancy.

69. Provision of finance on favourable terms as an incentive for industrial development, is not being used on any great scale. But institutions have been, or are being, set up in some of the territories to provide finance for industrial development on favourable terms. Jamaica has already established a development bank of its own and Trinidad is in the process of establishing one in the very near future. The principal objective of these institutions is to offer financial help on reasonable terms to local entrepreneurs.
70. On the whole, it appears that of the incentives offered in the Area to supplement tax concessions, protection from foreign competition is by far the most important. Other non-tax incentives do not seem to have played any significant role, at least not so far, in the whole package of incentives available to manufacturing enterprises coming up within the Area.
Chapter IV

EVALUATION OF EXISTING TAX INCENTIVES

71. Evaluation can only be made in terms of a set of certain objectives. The principal objective of the tax incentives offered to manufacturing industries in the territories covered by this study was, no doubt, to promote industrial development. But industrial development is promoted not for its own sake but with a view to helping attain certain economic goals. In the Caribbean context, accelerated industrial development is aimed at with a view to both diversifying the economies and at the same time accelerating the rate of growth of domestic incomes, through a fuller and better use of local resources.

72. Diversification of the economy would call for a shift in emphasis from traditional areas of production and investment and re-channelling of available savings, domestic as well as foreign, in the development of non-traditional areas of production. 1/ At the same time, it may as well be an objective of economic policy to rely as little as possible on foreign funds for the country's development. 2/ In that case mobilization of local savings and their redirection to industrial development will become objectives in themselves.

73. Accelerating the rate of growth of domestic incomes presumes fuller and better use of available local resources. While most of the territories would want to accord a rather high priority to the use of local manpower, 3/ the fullest development of local physical resources

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1/ Guyana's 1966/72 Development Programme accords diversification of output "our first priority". See P. II.1.


3/ Jamaica's 1963-1968 Plan, for instance, referred to the territory's employment problem as one "which stands in the centre of its policies and programmes" and went on to say that "the measures designed to stimulate activity in the private sector are aimed at the provision of an increasing number of jobs from year to year". See Pages 55-56 of the Plan.
with maximum possible benefit accruing to the country, is also accorded a high priority. 4/

74. It is in the light of the above objectives that the system of industrial tax incentives, which now obtains in the territories covered by this study, has been appraised in the following paragraphs. An attempt has been made in this chapter both to make an overall evaluation of the impact of existing industrial tax incentives offered in the Area and also to evaluate major concession offered under the present system separately. But it goes without saying that it is in their totality that these concessions, in combination with non-tax concessions offered by the territories, would exercise their beneficial impact.

I. OVERALL EVALUATION

75. Relevant and complete information, necessary for an evaluation of tax incentives in terms of their impact on investment, employment and value added in the manufacturing sector, is difficult to come by for all the territories. However, even if sufficient information were available, evaluation in these terms is not easy to make. Any exercise in such evaluation encounters a principal conceptual difficulty, namely the difficulty of separating gains in value added, employment or investment attributable to tax incentives from gains that would have accrued otherwise. Would a given investment have taken place in the normal course, if no tax incentives were offered? Assuming that the answer is no, how much investment would have taken place in the absence of tax incentives? Only then would one know, what gains in investment to attribute to tax incentives. The same goes for gains in employment and value added. Thus it is in only very broad terms that an evaluation can be made and that too with respect to the territories for which some information is forthcoming.

76. In Jamaica, between 1950 and 1966, a total of 134 factories had been established under its various incentive laws. The investment involved in these factories is estimated at $170 million. By the end

of 1967, the number of these factories had risen to 168 and employment in these factories stood at 10,000 which comprised about 15% of total industrial employment. In Trinidad and Tobago, the number of pioneer factories (i.e. those enjoying both tax holiday and duty-free importation), established till the end of 1966, was 136 and the investment in these factories was estimated at $210 million; employment was estimated at 6,650. By the end of 1967, the number of these factories had risen to 147 and employment to 7,550. Employment in pioneer factories comprised nearly 16% of the employment in the manufacturing sector. In addition, a good number of factories were established in Trinidad with Government assistance limited mainly to duty-free importation of plant and machinery and also raw materials. These provided employment to an estimated 6,500 workers. Thus the total employment provided by both pioneer and other assisted factories accounted for about 30% of the total industrial employment.

77. It is significant that in Trinidad and Tobago, between 1964 and 1968, investment in factories accorded pioneer status was nearly five times as high as that in factories approved for other assistance. But the estimated additional employment in the two categories of factories was very nearly the same, i.e. 4,000 each. This could possibly be taken as an indication that capital intensive enterprises could be attracted when duty-free importation was combined with income tax exemption which, in Trinidad, includes a sizeable investment allowance.

78. Equally significant is the fact that in Jamaica, of the total employment in factories set up under incentive laws, nearly half was accounted for by factories manufacturing exclusively for exports. Over the period 1960 to 1967, the increase in employment in export factories accounted for about 65% of the total increase in employment in factories established under incentive laws. The only additional tax benefit offered to export factories (i.e. over and above those offered to approved factories manufacturing for the home market) was duty-free importation of raw materials and fuels – a benefit they were legitimately entitled to even if there was no incentive programme in operation. In Jamaica, unlike in Trinidad and Tobago, duty-free importation of raw materials to factories producing for the home market was more an
exception than the rule. And even an active policy of protection from foreign competition was not adopted until 1965. Since then, progress in the establishment of home based enterprises has been more rapid than in the past. Jamaican experience could possibly be taken to indicate that, for home based enterprises, exemption from income tax was perhaps less important than protection or duty-free importation of raw materials combined with that of plant and equipment.

II. SEPARATE EVALUATION OF CONCESSIONS

Income Tax Exemption

79. Exemption from income tax reflects itself in a higher net return for any enterprise. Therefore, the fuller this exemption and the longer the span of this exemption, the greater is the gain to the enterprise. Of course, the assumption is that (a) the enterprise makes profits during the period of the tax holiday, and (b) the benefits of tax exemption extended to the enterprise cannot be, or is not actually, pre-empted by some other governments. 5/

80. While, therefore, there is no doubt about the attractiveness of income tax exemption, it is important to note that this attraction is being offered with virtually no strings attached. Generally speaking, exemption from income tax extends to the whole of profits during the period of tax holiday regardless of what return they represent on capital invested. Also, it is available to all approved enterprises. In a few of the territories, there do exist provisions for differentiating between enterprises. But even in these territories differentiation is not tied up to any objective criteria. Lately, however, an attempt has been made in a few territories to tie up some amount of differentiation with the development of backward regions.

5/ In their tax agreements with other countries, the territories of the Areas have not had much success so far in securing tax sparing arrangements so as to prevent formal pre-emption of exemptions extended by these territories. In actual practice, the enterprises enjoying exemptions have several ways open to them to avoid
31. The existing position with respect to income tax exemption therefore, is that, barring a few exceptional cases, it is available to approved enterprises without any qualifying requirement or restriction. There is no requirement that ties up the extent or length of the exemption to any performance beneficial to the economy. Nor is there any restriction imposed with respect to the use of the profits thus exempted, or even the portion thereof which represents saving in tax.

**Tax Exemption of Dividends**

82. If all the territories were subscribing to the same system of company taxation as obtains in Trinidad and Tobago since 1966, and as is being introduced in Jamaica from 1970, the question of exempting dividends could be considered independently of the exemption of company income. Under the system of company taxation that obtains in the other territories, the company pays tax on behalf of its shareholders. The exemption of dividends in the hands of shareholders was, therefore, only a logical extension of the exemption of the company's profits from income tax.

83. But the exemption of dividends on the condition that tax holiday profits are distributed within a given period is impossible to justify because it defeats one of the principal objectives of the whole system of tax incentives, namely, encouraging investment in industries. When an enterprise is allowed to defer depreciation deductions until the tax holiday period has expired, the existing rule requiring distribution of the tax holiday profits within a given period becomes doubly offensive because it almost forces the enterprise to fold up within that period.

84. As regards the rule that exemption of dividends is available only if the non-resident recipient is not taxable on such receipts in his home country, it appears that the underlying intention is conveyed only by the Jamaican provision whereby the shareholder is relieved of tax to the extent that the territory does not forego its revenue to the foreign treasury.

**Tax Exemption of Interest Payments**

85. Exemption of interest in the hands of recipients may be justified in certain special circumstances, for instance where the capital
structure of a company is unavoidably debenture- or loan-oriented. But its implications in terms of revenue foregone for the territory granting the exemption ought to be clearly understood.

86. Interest payments are ordinarily allowed as a deductible expense in the computation of chargeable profits or losses. If the deduction of tax exempt interest is allowed in the computation of losses to be carried forward, interest payments become a device for extending one's tax holiday beyond the formal period. As things stand, only one territory, namely Barbados, provides a safeguard against such abuse.

87. Even granting that safeguards can be taken to prevent use of interest payments as a device for extending the tax holiday period, it may still not be to the advantage of the territory concerned to give exemption on interest payments, if interest is payable abroad. When tax becomes payable on interest payments, i.e. on expiry of the tax holiday period, the rate at which non-resident recipients become liable is much lower than the rate at which tax is payable on company profits. This is largely so regardless of the system of company taxation but it is more so under the system obtaining in Trinidad and Tobago. From the point of revenue, debenture or loan financing of capital, particularly when it comes from abroad, is to the disadvantage of the recipient country. But exemption of interest payment encourages precisely this type of capital financing from abroad.

Depreciation Deductions

88. Accelerated depreciation deductions allow early recovery of amounts invested in depreciable assets and can, therefore, be said to reduce risk. Investment allowances permit recovery of capital larger than that actually invested. Deferment of depreciation deductions is also a device permitting recovery of amounts larger than those actually invested and is, in effect, an investment allowance, though specially devised for enterprises enjoying tax holiday. Investment allowances (including deferment of depreciation deductions) permit a higher net return. So does a straightforward exemption from income tax. But the difference is that the earning of a higher net return is tied up with the level of investment in one case whereas in the other case it is tied up to nothing, except, of course, the establishment of the enterprise itself.
89. It could be argued that in economies confronted with the problem of large unemployment, investment allowances are inappropriate since they would create a bias in favour of capital as against labour. To the extent that these two factors are mutually substitutable, the objection is quite valid. But, by and large, the scope for substitution is extremely limited in most areas of manufacturing. In fact, given the technology, which cannot undergo any major readjustment in the short run at least, investment in plant and machinery should help create additional jobs. Where an enterprise is manufacturing for export, any readjustment in technology may be undesirable even when it is feasible. In such a context, to tie up a given addition to the rate of net return with the level of investment might serve the economy better than to leave it altogether untied.

30. What is objectionable, however, about the investment allowance given in the form of deferment of depreciation deductions until beyond the tax holiday period is to allow these accumulations to be distributed as tax exempt dividends. Even more objectionable is the rule requiring early distribution.

Carry-forward of Losses

91. The permission to carry forward losses, if any, of the tax holiday period is evidently intended to take care of genuine cases of hardship. Ordinarily, most enterprises would expect to make little profit in the first one or two years of production. Tax exemption during this early phase means little to them. It is only the exemption beyond this phase that holds promise of tangible gain to them. Any enterprise, therefore, weighing gains of tax holiday would consider the period as a whole and only if these are attractive enough will it decide to undertake the venture. It is, therefore, only appropriate that in permitting the carry forward of losses, the entire tax holiday period is treated as one accounting period and only net losses are allowed to be carried forward.

92. It could certainly be argued that for the tax exemption incentive to be effective, it should be available to an enterprise during the period when it is actually making reasonable profits. Some territories offer the option whereby an approved enterprise could choose any date
within 3 years of the date of production for the tax holiday to commence. This is evidently intended to achieve the above purpose. But in these territories only the net loss of the tax holiday period can be carried forward.

**Duty-free Importation of Plant and Machinery**

93. The general case for granting this concession rests on the promise that high tariffs on plant and machinery raise capital costs and, therefore, deter investment. But in this Area this concession serves principally to eliminate the tariff differential against non-Commonwealth sources with respect to imports of plant and machinery. Preference tariff on most items of plant and equipment is, by and large, very low in this Area and, therefore, unlikely to be a major consideration influencing investment decisions. But the differential against non-Commonwealth sources is large enough to influence the decision regarding the source of import. Once an item of plant or machinery is imported, it would ordinarily be an objective of economic policy to use it as intensively as possible. Thereby, a developing economy not only saves, usually scarce, foreign exchange but also possibly raises the value added for every dollar of capital cost already incurred. Following this line of reasoning, it should also be in the interest of a developing economy to encourage the repair of existing machines and discourage their premature replacement.

**Duty-free Importation of Raw Materials**

94. As regards duty-free importation of raw materials, fuel and packing materials, the present situation, especially as it has evolved since the formation of CARIFTA, is somewhat confused. Generally speaking, duty-free importation of raw materials regardless of the processing undergone abroad creates a bias not only against local substitutes but also

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6/ The differential now ranges between 2½% to 15%.

7/ The present policy for excluding machine parts from duty-free importation does not, therefore, serve the best interests of the territories. In a developed economy, of course, where the problem principally is of slackening total demand, economic policy might seek exactly the opposite.
against local inputs, labour and material. Therefore, this concession would generally militate against local processing.

95. Where imported raw materials etc. go into the manufacture of exports, duty-free importation may have to be allowed far more liberally than when they go into the manufacture of import substitutes. Even with respect to exports, however, the objective of incentive policy must always be the encouragement of maximum processing at home.

III. EVALUATION OF NON-TAX CONCESSIONS

96. Of the non-tax concessions, the concession that is most used is the protection from foreign competition. Other concessions, namely, provision of factory sites at favourable rentals and provision of finance, have by comparison remained in the background and it is quite unlikely that they would have contributed significantly to industrial development in the Area. On the other hand, protection seems to have helped significantly in the development of home based industries.

Protection from Foreign Competition

97. Formally speaking, protection from foreign competition is not part of the scheme of tax incentives offered to industries; still, protection is currently being offered in the Area mostly in combination with tax concessions. At the same time, whatever protection is offered, it is given through quantitative restrictions much more than through high tariffs.

98. To some extent at least protection and tax concessions offered under incentive programmes overlap. If duty-free importation of plant and machinery and raw materials reduces the input costs, protection allows output prices to be raised. Thus protection and duty-free importation fall in a different category than income tax exemption because the latter presupposes the earning of profits whereas duty-free importation and protection, both, help in the very earning of these profits. It is in this light that the experience in Jamaica with respect
to home based industries is to be viewed. Duty-free importation and protection are close substitutes, depending of course upon the extent of import content of an industry's output. On the other hand, income tax exemption would largely complement but not replace duty-free importation or protection.

99. As regards the choice between high tariffs and quantitative restrictions, it appears that the balance of advantage generally lies with the former as a method of protection. Firstly, reliance on the latter places a considerably greater burden on the administrative machinery. It becomes the function of administration constantly to keep reconciling the demands of the local industries for protection against foreign imports with the obligation to the consumers of supplying the goods affected at reasonable prices - a none too easy task as experience in the Area seems to indicate. On the other hand, while protection through higher tariffs is no doubt premised on a certain increase in the prices to the consumers, it imposes no responsibility on the administration to prevent the prices from rising - a responsibility which, in any case, may be difficult to fulfil. Secondly, protection through higher tariffs has an advantage over that through quantitative restriction that it retains some element of competition, or at least of the threat of competition. Thirdly, within the framework of the former, to the extent that imports still meet part of the local demand, the treasury, and not the import trade, appropriates the gain from the higher prices of imports. And this gain in revenue would naturally reduce the need for the Government to raise revenue through other

9/ Evaluation of tax incentives in other parts of the world confirms that businessmen tend to consider protection more important to them than income tax exemption. In Mexico's case, for instance, its high tariff is considered possibly the biggest factor in promoting new industries. In Central America, too, tariff protection is considered more important than incentives. (George E. Lent, Tax Incentives for Investment in Developing Countries, in IMF Staff Papers, July 1967, P.281.)
taxes for whatever purpose such revenue may be spent; one of such purposes may be to subsidize certain commodities to keep their prices from rising. 9/

IV. ADMINISTRATIVE ARRANGEMENTS

100. In the grant of various tax concessions discussed above, all the territories subscribe to the principle of selectivity with respect to both industries and enterprises. There can be no doubt that the selectivity approach reflecting the priorities that inform a territory's economic policy should secure optimal returns for the sacrifice involved in the grant of incentives. Unfortunately, however, the guidelines laid down in the respective statutes for selection are so very wide and vague that too much responsibility is placed on those administering the incentives arrangements. When administration is called upon to apply criteria of selection which are not spelt out precisely, it leaves considerable room for arbitrariness in their application not only between one industry and another but also between one enterprise and another within the same industry. It is doubtful if in actual practice the selectivity approach, as has been applied in the territories, secured optimum results. Also, in the regional context, the existing arrangement has led to disparities in the dispensation of tax incentives between member territories, particularly with respect to enterprises within the same industry.

101. As has been observed earlier in this chapter, once an enterprise manufacturing a specific product is approved, tax concessions are offered, by and large, on a non-discriminatory basis. Regardless of whether

9/ Lately, there has been some amount of rethinking in the Area on both the role of protection and the choice between quantitative protection and high tariffs. For instance, Trinidad and Tobago's Third Plan not only calls for a review of the list of items subject to quantitative import restriction but also enjoins that, in future, generally speaking an industry should not expect to receive both pioneer status and protection at the same time and, as far as possible, quantitative restrictions should be replaced by higher tariffs.
they contribute more or less to the domestic economy in general terms, or in specific terms such as in regard to employment, use of local physical resources, or balance of payments, the approved enterprises are, generally, eligible for the same set of concessions. Even in territories where there exist provisions authorising the Governments to offer partial concessions i.e. a percentage rather than complete exemption from income tax, little exists by way of guidance as to the basis of differentiation between enterprises. Nor have any criteria and procedures been developed in actual practice for the evaluation of enterprises with a view to making use of this power to differentiate between enterprises.

102. Further, while the selection procedures which have evolved over a period seem to require a fairly detailed examination of applications before they are granted or rejected, little time or resource is being devoted in any of the territories on the evaluation of the actual performance of the selected enterprises. Once an enterprise is selected, the tasks of administration are limited to making sure that—

(i) the factory is established or starts production on time,

(ii) the factory does not employ any unauthorized foreigner, and

(iii) the factory does not abuse the duty-free importation concessions.

103. As things stand, in most territories the approved enterprises are under no obligation to furnish at regular intervals full information on their operations during their tax holiday period. The result is that even if the administration wanted to evaluate their performance, it may find itself severely handicapped in the absence of adequate information. One of the first steps towards a performance-oriented administration of tax incentives would be to require, by law, the submission by enterprises granted tax concessions of detailed information on their operations at regular intervals.
Chapter V

RECOMMENDATIONS FOR REGIONAL HARMONIZATION

I. REGIONAL INCENTIVE POLICY

104. The express objectives of the free trade association established by the CARIFTA Agreement are not only to promote the expansion and diversification of trade within the Area, but also to encourage balanced and progressive development of the economies and to ensure that the benefits of free trade are equitably shared by the member territories. In the formulation of the regional incentive policy for industrial development, these very objectives of the Agreement can be said to provide some broad guidelines.

Specific CARIFTA Guidelines

105. At the same time, the Agreement sets certain specific guidelines for the regional policy for tax incentives offered for the promotion of industrial development. It recognizes that "certain industries may require for their economic operation the whole or large part of the entire regional market protected by a common external tariff or other suitable tariff". Also accepting "the principle of seeking to establish more industries in the less developed countries", the Agreement requires that "subject to existing commitment", the regional policy of incentives should bear in mind "the special needs of the less developed countries for preferential treatment, such as soft loans".1/

106. Thus the Agreement clearly recognizes the need for —

(a) having to protect certain industries on a regional basis to provide them the whole or a large part of the regional market, and

(b) for offering special incentives with a view to accelerating industrial development in the less developed member territories.

For industries in the first group the Agreement envisages the use principally of the instrument of regional protection. For industries

1/ See Resolutions 4, 5 and 7 as reproduced in Annex A to the CARIFTA Agreement.
falling in the second group, the Agreement speaks of according special incentive treatment. It is not clear, however, whether or not the special incentives which the Agreement envisages included tax concessions over and above those offered in the better developed member territories. This doubt has been raised because the Agreement exemplifies the special needs of the less developed member territories in terms of their need for soft loans only.

107. That the Agreement completely over-ruled any disparities between member territories with respect to tax concessions would, however, be a very narrow interpretation of the relevant resolution. Surely, the authors of the Agreement could not have ignored that already at least one major member territory, namely Jamaica, was just beginning to offer additional tax concessions with a view to encouraging the location of new industries in the less developed parts within the territory. If the regional incentive policy were to concede to differentials in tax concessions a role in alleviating the imbalances in development within a territory, such policy could not be specifically precluded from using the same instrument for correcting imbalances between territories.

108. Perhaps the reference to tax-concession-differential was deliberately avoided, with a view not to restricting the scope of regional policy for balanced industrial development. At the same time, the reference to soft loans was possibly meant to broaden the sphere of action towards correcting inter-territorial imbalances; for, after all, the role which various non-tax factors play in stimulating or deterring development cannot be easily overlooked. For instance, serious infra-structural deficiencies in certain territories would be virtually impossible to compensate with tax incentives. Instead, positive action is called for in correcting such deficiencies to enable such territories to attract industries.

109. It is, therefore, assumed that the offer of tax-concession-differentials by less developed member territories within the framework of a regional incentive policy is not ruled out by the Agreement. It would, however, be over-optimistic to rely entirely on the differentials in tax concessions to secure balanced industrial development in the region.
Regional Strategy for Development

110. Within the broad framework of the CARIFTA Agreement, the question of harmonizing tax incentives can be said to assume several dimensions. The objective of freeing and promoting trade among the territories in commodities produced within the Area constitutes only one, albeit essential, dimension. Tax incentive policy must, at the same time, form an integral part of the overall development strategy in the Area and should reflect the priorities of such a strategy. Development strategy within the area will, no doubt, have to take account of the relative supply of factors of production within the Area. For instance, current thinking in the Area on development planning not only accords the highest priority to the achievement of full employment but also lays great store by mobilization of domestic savings which are currently too low to meet the Area's capital needs.

111. The relative abundance of working force and scarcity of domestic savings are phenomena that the CARIFTA Area shares with most developing countries all the world over. But, the Area is particularly well endowed with respect to certain natural resources, as for example bauxite, mineral oil, natural gas and also forest products. This is apart from the particular advantage that much of the Area enjoys with respect to its location and climate, thereby making it particularly attractive to tourist industry. And these it must fully exploit.

Factory Scarcities

112. A rational incentive policy should not be content, however, with reflecting factor supply situation indirectly through its articulation of development priorities. The incentive policy must directly articulate the relative supply position of various factors. In doing so, it should seek to secure maximum employment of the relatively abundant factors in the area because only thereby would increased industrial activity generate optimum additional income for the territories.

Export Orientation

113. The relatively small size of the CARIFTA market imposes certain constraints on industrial development in the Area. But these can be mitigated if markets were found abroad for the industrial products of
the Area. Otherwise, industrial development predicated on the market of this size might, in the case of several products, mean substituting high-cost local products for low-priced mass-produced imported products. In such cases, production for the domestic market alone is unable to realise economies of scale, and therefore takes place at sub-optimal levels. Incentive policy for the region might, therefore, justifiably wish to place an added emphasis on production for the markets outside of the Area. But production for the export market might be considered essential, and therefore worthwhile promoting, not only because it helps achieving optimal scale but also because this may enable the economies to increase the employment of local resources, particularly labour, and thereby secure an increase in local incomes. It is probably for this reason that in several developing countries special incentives are offered not only to encourage home based industries to venture into the export market but also for the establishment of enclave enterprises, which manufacture exclusively for export.

114. Within the Area, some of the territories have already provided in their incentive programmes specially for firms producing exclusively for the export market. Some other territories accord special treatment, at the time of selection, to such enclave enterprises, within the framework of their general incentive legislation. In the CARIFTA context, naturally such firms will be producing only for export outside of the Area.

115. A view was expressed that it was not necessary to harmonize incentives offered for such enterprises since their products will not compete for the Area market. This view, however, overlooks that in the absence of agreement on tax incentives for enclave enterprises, scope will remain for competitive bidding among the territories for foreign capital to come to enclave enterprises within their respective jurisdictions. On the other hand, agreement reached on incentives to enclave enterprises, will go one step further towards the goal of

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2/ This is already the case in both Barbados and Jamaica. But it is not clear if other territories, such as Trinidad and Tobago, do likewise.
balanced development of the economies of the Area expressed in the CARIFTA Agreement. 3/

Related Questions

116. Whatever regional policy is agreed upon on tax incentives, such agreement must take place within the framework of some understanding among the territories on such closely related subjects as the level of income taxation (including level agreed upon in tax agreements with third countries), the level of protection and also the level of non-tax incentives. Any scheme of incentives adopted without agreement on these intimately related questions would only amount to transferring the burden of mutual competitive outbidding among the territories from tax incentives on to these areas. Further, in this competition the larger and better developed territories will have a distinct advantage over the smaller and less developed member territories in the Area in always being able to offer more attractive terms. This will only defeat the whole purpose of the exercise on incentive harmonization.

117. Thus it would appear that in seeking to harmonize tax incentives offered to manufacturing enterprises, agreement will have to be sufficiently broad-based as to cover the above questions, which, we feel, are closely linked to incentive policy. The territories should, in particular, agree broadly on the level of income taxation, particularly the level applying to companies, on the level of protection, whether through the use of tariff or through quantitative restrictions, and on the level of other non-tax incentives to be offered to manufacturing enterprises. Agreement on these matters should help considerably in the realization of a common incentive policy.

118. As regards tax incentives, the regional policy should bear in mind the need for less developed territories to offer special incentives, conform to the broad strategy of development for the Area and also articulate directly the relative factor supply position in the Area.

3/ Although this study is concerned with the manufacturing industry only, the line of reasoning taken here would apply as much to tourist trade as it does to enclave type of manufacturing because in tourist trade also the "product" is very largely exported.
Such an incentive policy would, it appears, have to emphasize the use of local resources, particularly labour, to encourage reinvestment of business profits, and also to place accent on manufacturing for export outside the Area. Even for enterprises manufacturing exclusively for export, it would be desirable for the territories to agree on a common set of tax incentives.

II. PROPOSED SCHEME OF INCENTIVES

119. Once agreement is reached on the broad contours of a regional incentive policy, it should be possible to proceed to the discussion of the scheme for incentive harmonization for the Area. Such a scheme must set down clearly the following:

(a) scope of harmonization;
(b) classification of industries;
(c) selection of enterprises;
(d) level of tax concessions;
(e) income tax reliefs;
(f) duty-free importation;
(g) property taxes and other local taxes;
(h) transitional arrangements.

(a) Scope of Harmonization

120. Article 23 of CARIFTA Agreement calls for the harmonization of tax incentives offered to manufacturing industries. It might still be useful to indicate clearly the type of tax incentives which it is proposed that the scheme of incentive harmonization should cover. There need not be any argument that such a scheme should include all incentives offered in the form of various types of income tax relief or duty-free importation.

121. As regards taxes (such as property taxes) imposed by or on behalf of the local bodies (municipalities, corporations, etc.), the present practice in almost all the territories is to grant exemption thereto from to enterprises approved for income tax reliefs. But it appears that in all the territories granting this exemption, except Barbados, the relief given thereby usually works out to be quite small relative to other reliefs. It is generally agreed that this relief could not have played any significant role in the industrial development of the territories.
On the other hand, in view of the limited financial resources of local bodies, the grant of this exemption (or its withdrawal) could make quite a difference to their finances. Ordinarily, local rates of taxation would be expected to be related to their revenue requirements. It is therefore proposed that under the regional scheme of incentive for industries exemption from property and other local taxes should not be given.

(b) Classification of Industries

122. Selectivity should, as before, continue to be the principal basis for the grant of tax incentives to industries, to obtain optimal results for the sacrifice made in the area in terms of Government revenue that is thereby foregone. As noted earlier, the difficulty however with the existing territorial legislations on the subject of incentives is that the qualifying criteria, particularly for the selection of industries, are couched in very broad, and therefore necessarily vague terms. But criteria for selection of industries can be worked out only if the major elements of the basic strategy for industrial development were clearly known. In the absence of a clearly articulated strategy for the Area, it might be difficult to build an industry-wise preference into the scheme of tax incentives.

123. At the same time, it might be considered desirable to exclude certain industries in the Area completely from the purview of tax incentives. 4/ For instance, it might quite justifiably be felt that taking into account the existing position in the Area with respect to the availability of raw materials and the manufacturing capacity, it might not be necessary to give tax incentives for their expansion. In that case, an agreed list of such industries as can be excluded from the purview of tax incentives altogether may be drawn up. This could be a first step in exercising selection between industries in the grant of tax concessions.

4/ This approach, namely of listing the industries not eligible for a tax concession, has already been adopted by Trinidad and Tobago in the grant of rebate in income tax for increased exports.
124. Also, as indicated above, it might be perfectly justified, on purely economic considerations, to encourage industries engaged exclusively in the manufacture of export goods. Such enterprises will fall in a special category.

125. Another group of industries which might call for a different, though not necessarily overall preferential incentive treatment, is that of capital-intensive industries. These would be such industries in which -

(i) the initial investment involved is quite substantial;
(ii) capital-out ratio is rather high, and also
(iii) on the basis of known technology, there is little room for substituting labour for capital.

These criteria would have to be quantified in the light of the requirements of the Area.

126. Thus it appears that for the purpose of an incentive harmonization scheme, industries may be grouped as under:

(i) Industries not eligible for tax incentives.
(ii) Enclave Industries
(iii) Capital-intensive Industries
(iv) All other industries.

Agreed lists will have to be drawn up for industries falling in groups (i) and (iii). Industries manufacturing entirely or partly for the local market will fall in either group (iii) or group (iv). These will include not only regional industries, i.e. those for which, in terms of the Resolution adopted by Fourth Heads of Government Conference on Regional Integration, the need is recognized of offering protection from foreign competition on a regional basis, but also small scale industries. A small scale industry could be defined in a number of ways. But from the point of view of this Area, a definition in terms of a certain maximum level of investment should be preferable to a definition in terms of the level of employment. A small scale industry could be defined in a number of ways. But from the point of view of this Area, a definition in terms of a certain maximum level of investment should be preferable to a definition in terms of the level of employment.
industries, though a certain distribution might usefully be made in the matter of non-tax incentives.

127. In the application of this scheme, the Governments should be given the freedom to be more restrictive, if they wish but not more liberal. It is assumed also that a list will be drawn up for the Area as a whole of industries which are specifically excluded from the purview of these concessions. This list would have to be reviewed at regular intervals and brought up-to-date. Each territory may be given the freedom to add any other industry to this list but not to remove any industry from the list. Similarly, a list will have to be drawn up of capital intensive industries for the Area as a whole. But in this case each territory may have the freedom to remove any particular industry from the list but not to add any additional industry to such list. The over-riding objective in suggesting this restriction on the freedom of territories to modify the lists would be to ensure that this freedom is not exercised to offer benefits over and above what is agreed upon in a regional scheme.

(c) Selection of Enterprises

128. The existing position in all the territories is that selection effectively occurs at the enterprise level rather than at the industry level. But in the context of the Area market, the application of the present approach raises a number of problems. Firstly, the pioneer enterprise approach which now informs the selection of enterprises is rather narrowly conceived in terms of the national situation. If the same approach is to continue hereinafter, it will have to be applied in the context of a much wider market. If, as is most likely, the selection of enterprise is entrusted to the national administrations, it is not unlikely that there would arise wide disparities in the application of this approach. On the other hand, if the suggestion made above is accepted for drawing up a list of industries which would be entirely excluded from eligibility to tax incentives, it will have already achieved the principal objective underlying the pioneer enterprise approach.

129. It would be a fair assumption to make that as long as an industry is not placed on the list of excluded industries, then not only is there
room for expansion in such industry but also such expansion deserves to be encouraged. The pioneer enterprise approach also implies some assumption regarding the level of output which an industry, especially when it is an import-substitute industry, should reach before it can be depended upon to expand on its own. Once, therefore, the suggestion to draw up the list of excluded industries for the region as a whole is adopted, the major objective of pioneer enterprise approach will have been achieved, namely of not giving concessions to enterprises which do not deserve them. Of course, it is assumed that this list of excluded industries will be brought up-to-date at regular intervals and necessary procedures will be established in this regard.

There are other important considerations which Governments in the Area keep in mind before approving an enterprise. Under the existing incentive regime in most territories, it is not only obligatory that the approved enterprise should be a company but also that the authority should be satisfied with regard to its financial viability. The applications have, therefore, to be fully supported by necessary information and evidence in this regard. Some territories require local incorporation; others are thinking in terms of incorporation as a local public company, as distinct from a private company; one territory plans to impose a certain minimum proportion of local participation in the capital of such a company as an additional qualifying condition. There is no gainsaying that each of these requirements has considerable merit. There is, however, a strong feeling among the territories that not all of them are yet in a position to impose these conditions, at least not to the same extent. In the circumstances, it appears the selection of enterprises should be entirely a matter for each territory to decide on whatever criteria each wishes to impose. For the purposes of the regional scheme it should be enough if (a) the enterprise approved by a national administration is not engaged in an excluded industry, and (b) its industrial classification conforms to the regional scheme.

Thinking on these lines is clearly reflected in the Trinidad and Tobago Plan for 1969-73, especially in the modifications to the draft made by the Cabinet before its submission to Parliament.
(d) **Level of Tax Concessions**

131. There exists a wide disparity in the level of tax concessions now being offered to industries by various territories. In any attempt at harmonizing these concessions, the first and very important question to answer would be: should the regional scheme of incentives seek to offer a higher or lower total of tax concessions than those being offered today? The answer to this question will determine whether in the process of harmonizing tax concessions the bias should be towards raising or reducing the present level of tax concessions.

132. One of the most important contributions of the establishment of a free trade area should have been the widening of the unified local market. Previously, enterprises had to predicate their calculations and projections on the basis of smaller national markets. Now that the market for locally produced goods would be much wider than before, it should make a significantly favourable impact on these calculations and projections. It should thereby reduce the need for offering the attractions of tax concessions, particularly income tax concessions offered to those manufacturing for the local market, at least not at the same level as before. In fact, recent reviews of tax incentives offered in developing countries have raised serious questions about the very effectiveness of tax concessions in attracting capital, especially from abroad. This is how the IMF study sums up its review of tax incentives offered in developing countries:

"The available evidence suggests that, in general, developing countries need not be concerned about matching the tax benefits of other countries in order to attract foreign capital for new industries. Tax considerations typically play a role subordinate to more basic economic factors in the location of industry. Competitive bidding among countries by the offer of more and more generous tax concessions tends to reduce revenues from foreign investment without increasing the total flow of capital, especially for import substitute industries serving a domestic market."[1]

In any case, it will be generally agreed that, at best, tax concessions are one of the several important factors which influence investment decisions.

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In the circumstances, the regional scheme of tax incentives proposed in this Report seeks an overall reduction in the level of concessions now being offered in the Area.

133. Another aspect of the present position is that, by and large, once an enterprise crosses the barrier of approval, it is eligible for tax concessions, with little variation between one approved enterprise and another on the basis of either promise or performance. This, as has been pointed out earlier, is not satisfactory from the point of view of getting the optimal returns. Since the foremost objective of accelerating industrial development is to secure the generation of additional incomes within the Area, the appropriate thing to do would be to tie up tax concessions as far as possible to the performance in this respect, namely to the contribution of the enterprise to the value added locally. This would certainly imply a major departure from the existing practice obtaining in the Area, but is one that should have occurred long back. 8/

134. Alongside this, it would be advisable to encourage reinvestment of profits. This would achieve two purposes:

(a) it would mobilize savings for industrial development, and

(b) it would reduce the outflow of funds abroad.

At the same time, distribution of profits might be actively discouraged for precisely the same reasons. On the whole, it should be easier to attract the investors already operating within the Area to opportunities for diversification and expansion, than new investors not quite familiar with the Area. However, this might possibly come into conflict with the broader objective of diversifying ownership of business and industry. To the extent this conflict does arise, appropriate safeguards will have to be provided for at the national level. The broad scheme of tax concessions is outlined in the following paragraphs in the light of the criteria set out above.

8/ Already, Trinidad's new Development Plan calls for a reformulation of incentives in a manner that places accord on the maximisation of the percentage of local value added in the value of gross output of industries.
(e) Income Tax Reliefs

135. The scheme of income tax exemption proposed here seeks a combination of complete exemption for a relatively short initial period and a longer partial exemption thereafter. The extent of the proposed partial exemption is tied to the contribution of a firm to the economy in terms of value added locally. The calculation of value added locally suggested herein seeks to introduce a bias not only for the use of local labour and materials but also for local processing, including local fabrication of tools and plant, and ploughing back of profits within the Area.

Complete Exemption from Income Tax

136. It is proposed that all approved enterprises should be entitled to complete exemption from income tax (i.e. full tax holiday) from the date of production for a period of:

- 3 years in Barbados, Guyana, Jamaica and Trinidad & Tobago
- 6 years in less developed territories.

For enterprises established in designated (according to criteria agreed upon at the regional level) less developed parts of Barbados, Guyana, Jamaica and Trinidad & Tobago, the period of tax holiday may be fixed as 4 years.

Partial Exemption from Income Tax

137. On expiry of the tax holiday period, the enterprises should be accorded partial relief from income tax for a further period of 10 years according to the following schedule, depending upon the percentage value added locally by an enterprise every year.

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9/ In Puerto Rico, this designation of less developed zones for purposes of industrial incentives is based on the necessity of establishing factories in that particular zone, taking into account its population, and the nature and opportunities of employment existing there, and with due regard also to difficulties such zone confronts in attracting factories. The designation of zones is made upon the recommendation of a Committee comprising of the Planning Board Chairman, the Secretaries of Treasury, Labour and Commerce, and the Economic Development Administrator. The same Committee may recommend deletion or re-designation of zones.
### Percentage Value Added Locally

<table>
<thead>
<tr>
<th>Percentage Value Added Locally</th>
<th>For enterprises manufacturing exclusively for exports</th>
<th>For other Enterprises</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 10%</td>
<td>NIL</td>
<td>NIL</td>
</tr>
<tr>
<td>Between 10-25%</td>
<td>30</td>
<td>20</td>
</tr>
<tr>
<td>25-50%</td>
<td>50</td>
<td>35</td>
</tr>
<tr>
<td>Above 50%</td>
<td>75</td>
<td>50</td>
</tr>
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For purposes of paragraphs 136 and 137 above, the following definitions are suggested:

**Approved Enterprises:** All new enterprises and extensions of existing enterprises manufacturing products, not specifically excluded, established and/or approved after the coming into force of the regional scheme may be considered as approved enterprises for the purpose of the scheme.

**Date of Production** should be the date on which the approved enterprise starts manufacturing its product in marketable physical terms, or the date not later than 18 months from the date of approval, whichever is earlier. In the case, however, of an enterprise engaged in capital intensive industries, as specified, the date of production will be the date by which the enterprise has exhausted its claim of investment allowance against its income chargeable to tax.

Percentage value added locally during a year shall be calculated according to the formula: \( \frac{T \times L}{100} \), where

- \( T \) stands for the total value of output sold by the enterprise during the year and
- \( L \) stands for total value added locally. The total value added locally by an enterprise will be arrived at by (a) **adding items (i), (ii), (iii) (iv)** and (v):

  1. **wages and salaries paid during the year;**
  2. **raw materials (including fuels) and components purchased locally;**
  3. **interest and management charges paid;**

\[10/\] The inclusion of this item (as netted) in a firm’s value added is deliberate; it is designed to introduce a bias in favour of local materials and components.
iv) depreciation deductions as allowed under income tax rules;  
v) profit before tax (after making all the deductions including depreciation deduction);  

and (b) deducting from the sum thus arrived at the sum of items (vi), (vii), (viii), (ix), (x) and, where appropriate, (xi):  

vi) wages and salaries paid to non-citizens;  
vii) interest and management charges accruing to non-citizens;  
viii) profits distributed and remitted abroad (including all branch profits of foreign companies not reinvested locally);  
ix) import content of raw materials (including fuels) and components purchased locally;  
x) depreciation deductions pro rata, with respect to import-content of depreciable assets;  
xii) element of protection enjoyed with respect to local sales.  

Items (ix) and (x) will be determined by an authority so designated by each Government and the enterprise shall be obliged to furnish all the necessary information as would help the authority concerned to determine the import content of raw materials (including fuels) and components purchased locally and also of the depreciable assets of the enterprise.  

Item (xi) will also have to be determined by an authority so designated by each Government, and the enterprise shall be obliged to furnish the said authority with all the necessary information. Where the enterprise is enjoying tariff protection, a further item of deduction would be the amount arrived at by the value of output of the enterprise sold locally multiplied by the rate of protection duty. Where protection is given through quantitative restriction, the corresponding amount would be the difference between the value of 

10/ The inclusion of this item (as netted) in a firm's value added is deliberate; it is designed to introduce a bias in favour of local materials and components.  

11/ The inclusion of this item, as netted, in a firm's value added is deliberate again, designed as it is to encourage locally fabricated plant, machinery and tools.
output at prices charged locally and the value of output at international prices.\textsuperscript{12}

Percentage relief from income tax during a year is the proportion by which the enterprise will be relieved of the income tax liability as calculated under normal income tax rules.

139. Investment Allowance: For enterprises engaged in listed capital intensive industries only, an investment allowance is proposed of \(30\%\) on the original cost of machinery and plant. This allowance should not be treated as a normal depreciation deduction. It will be a deduction over and above the normal depreciation deductions with respect to capital expenditure incurred on machinery and plant. As already indicated, such an enterprise should be entitled to claim this allowance before the commencement of its tax holiday period.

140. Depreciation Deductions: It is proposed that all approved enterprises should be required to make normal depreciation deductions in accordance with income tax legislation during the period of complete tax-exemption and the period of partial tax exemption following that. In the case of enterprises engaged in capital intensive industries, normal depreciation deductions will also be made during the period before the tax holiday period when investment allowance is being claimed against the chargeable income of the enterprise. Accelerated depreciation deduction may be allowed in the form of an initial allowance of \(20\%\) with respect to new expenditure incurred on depreciable assets after the expiry of the period of complete tax exemption.

\textsuperscript{12}Where an industry enjoys protection from foreign competition, the inclusion of all profits made by a firm is, in most cases, bound to overstate its contribution to value added. In the Central American Common Market, where it still remains undecided whether or not to include profits in the calculation of a firm’s value added, when a firm’s net benefit to Balance of Payments is to be calculated, the c.i.f. value of imports for which the firm manufactures local substitutes, and not the ex-factory price of local substitutes, is used as the basis. The objective clearly is not to allow the firm to claim credit for value added through higher prices charged under the cover of protection.

\textsuperscript{13}The existing situation in this regard is far more liberal in territories which allow deferral of depreciation deductions. For a five-year tax holiday, deferral of depreciation deductions at the rate of \(10\%\) a year, under the declining balance method, would be equivalent to an investment allowance of \(41\%\).
141. **Carry-forward of Losses:** For all approved enterprises, the period of complete tax exemption should be considered as one accounting period for the computation of net loss. Net loss thus calculated may be carried forward against the income of the same enterprise only, but for as long as it is not written off completely.

142. **Treatment of Dividends:** Dividends paid out of profits of the initial period of complete exemption should, it is proposed, be exempt from income tax in the hands of shareholders provided (a) the authorities concerned are fully satisfied that these profits were so exempt and (b) the distribution of the enterprise in the year for which exemption is claimed in the hands of shareholders does not exceed 10% of equity capital. Where the shareholder is a non-resident, he would be exempted from only so much of income tax as exceeds his liability on such dividends in his country of residence. As regards profits made by the approved enterprise during the subsequent period of partial exemption, they should not be given any exemption in the hands of shareholders. This, it is hoped, will discourage enterprises from distributing such profits. In no case should there be any provision, directly or indirectly, forcing distribution of profits by such enterprises.

15/ The objective of this second qualification is to deter large distributions in any year and not to withhold exemption in the hands of the shareholders.

15/ It might well be argued that under the system of company taxation obtaining in territories other than Trinidad and Tobago (and, as from 1970, Jamaica too), denying the benefit of partial exemption to shareholders on their dividend income is tantamount to withdrawing the partial exemption from the company itself. This is valid provided it is assumed that profits enjoying partial exemption must necessarily be distributed as dividends. If they are ploughed back, the partial exemption is not surrendered. Nor does the shareholder lose in the process because accumulation of reserves by the company reflects itself in the appreciation of the market value of his equity, which, at least so far, is not taxable in the Area.
143. Treatment of Interest: Exemption from income tax of interest payments in the hands of recipients should not be granted. Such an exemption could be much costlier in terms of revenue loss to Government than exemption of dividends. As a matter of strict regional policy, interest payments made by any enterprise, approved or not, should, it is strongly urged, be subject to tax in the hands of recipients like any other receipt. 16/

144. Enterprises Manufacturing partly for Export: Where an approved enterprise is exporting only a part, and not whole, of its output outside of the Area, partial relief from income tax proposed in paragraph 137 above should be given with respect to profits attributable to exports at the rates set out in the schedule for enterprises manufacturing exclusively for exports. With respect to the balance of its profits, i.e. those attributable to sales within the Area, relief would be available to such an enterprise at the lower rate applicable to other enterprises in the schedule referred to above.

16/ Where the territories have, in their tax agreements with capital exporting countries, agreed to impose on ordinary interest payments made abroad a rate lower than the company rate of tax (and this holds true for most of the territories covered by this study), foreign companies might still find it to their advantage to rely more on loan than equity finance. But this would naturally work out to the disadvantage of the concerned territory's treasury. Since tax agreements take time to modify, it might be worthwhile introducing some sort of ceiling on the ratio of loan to equity finance for foreign private capital. This recommendation should not be construed as an argument against a government policy restraining the extent of foreign participation in the equity capital of an enterprise with a view to encouraging local participation. In fact, the local value added formula proposed in this Report seeks also to achieve the same objective.

Also, under the system of company taxation where the company pays tax on its own behalf and even the resident shareholder gets no credit for that (in Trinidad, the resident shareholder gets credit for almost 85% of the tax paid by the company) there is a natural bias in favour of loan financing even for local capital. Therefore, there would be a case for a similar restriction on local capital as well under such a system.
145. For purposes of paragraph 144 above, it is proposed that profits attributable to exports should be taken to be the amount produced by the formula:

\[ \frac{P \times E}{S} \]

where \( P \) is chargeable profit of the enterprise for the year;
\( E \) is sales proceeds (ex-factory) of the output of the enterprise exported during the same year outside of the Area; and
\( S \) is the sales proceeds (ex-factory) of the total output of the enterprise sold during the same year (excluding any excise duty, if paid).

Although ordinarily the rate of profit per unit of output should be lower for export than for local sale, under the proposed formula it is assumed to be the same. This is deliberate. The intention is to create thereby a bias in favour of export-oriented import-substitute enterprises as compared to both purely import-substitute enterprises and also enclave enterprises.

146. Increased Export Allowance: This additional relief from income tax is proposed to be offered to all manufacturers, including approved enterprises after they have exhausted their period of partial exemption, on the basis of the increase they show in their export sales. It is proposed that the allowance should be given at the rate of 1% of the profits attributable to exports for every 1% increase in the proceeds from the sale of exports during the year over the sale proceeds from exports in the year immediately preceding. The profits attributable to exports will be calculated in the manner proposed in paragraph 145 above. The allowance should not, however, exceed the tax that would have been payable on the profits attributable to exports in that year at the company rate of tax. This allowance should, it is believed, promote expansion in exports even after the other tax concessions have exhausted themselves.

17/ Except possibly those on the list of excluded industries.
(f) Duty-free Importation

147. Machinery and Plants: If uniformly low rates of duty were applicable to imports of machinery and plant from non-Commonwealth as well as Commonwealth sources, there might be no necessity to provide for this duty-free importation. If, however, the existing margins of preference for imports from Commonwealth sources must be retained, the incentive scheme for the region would, it is felt, have to provide for duty-free importation by approved enterprises of machinery and plant. This concession should be available for the period covering the whole period beginning with the approval of an enterprise and ending with the ten years of partial exemption from income tax. At the same time, it is proposed that the concession should extend to machine parts imported by the enterprise for repair and/or replacement during the same period.

148. Construction Materials: Duty-free importation of construction materials should be allowed only if they or their near-substitutes are not available locally in sufficient quantity and at competitive prices.

149. Raw Materials: As a matter of policy, duty-free importation of raw materials and components should not be allowed as part of the scheme of tax concessions except where imports go into the manufacture of exports. At the same time, it cannot be over-emphasised that whatever duties are imposed on imported raw materials (including fuels) and components would have to be uniform throughout the Area in all cases where the end-products would be eligible for Area Treatment.

150. Assuming that harmonization of tax incentives is accorded the high priority it deserves in the overall scheme of economic integration, it will be difficult to disassociate it from a complementary exercise in the fixation of common external tariff with respect to industrial raw materials, components and fuels. In fact, in the larger exercise on common external tariff if the unification of tariffs is to be phased over a period, as is likely to be the case, the tariffs on these items would deserve to be accorded a high priority, almost at par with the protective tariffs on items competing with local manufacturers. When these tariffs are being restructured, as a broad
principle the rates of duties should be fixed in a manner that
they rise sufficiently progressively with the degree of processing
imports undergo outside of the Area so as to build into the system
of tariff a strong bias in favour of processing within the Area.

(g) Property Taxes and other Local Taxes:
151. Under the regional scheme, it is proposed that no exemption
should be offered with respect to taxes levied, by or on behalf
of, local bodies.

(h) Transitional Arrangements:
152. The Governments in the Area seem to feel committed strongly
to the arrangements already entered into under their respective
incentive legislations. The existing enterprises enjoying tax
benefits under these dispensations would, therefore, have to be
allowed to continue enjoying them until these benefits expire in
due course. At the same time, it cannot be overlooked that until
such time as all the enterprises in the Area operate on the basis
of uniform set of concessions, there will remain problems of
granting full and free access, to the products of enterprises
enjoying distinctly better terms than others, within the Area.
It is, therefore, necessary to persuade these enterprises to have
themselves reclassified under the regional scheme, once it is
introduced.

153. For enterprises approved under the old legislations and
choosing to be governed by them, it would have to be made
absolutely clear that none of the benefits under the new
scheme would be made available to them. Nor should such enter-
prises be entitled to claim the protection of Article 23(1)
whereby no member territory can introduce more generous con-
cessions than the most generous already obtaining in any of
the member territories. In fact, it might be worthwhile going
as far as to deny area treatment to the products of enter-
prises choosing to remain under the old dispensation.
154. Among existing enterprises applying for approval under the regional scheme, there would possibly be two types. The first type of enterprise would be one in whose case the period between its date of production and the date of the coming into force of the regional scheme is less than the period of complete tax exemption allowed under the regional scheme. Such an enterprise should, it is proposed, be entitled to complete tax holiday for the difference, and partial income tax relief in the period thereafter. Also, it should be eligible for other benefits under the regional scheme in the whole of this period including the period of complete tax exemption. The second type of enterprise would be one in whose case the period between the date of production and the date of coming into force of the regional scheme exceeds the period of complete tax holiday allowed under the regional scheme. Such an enterprise should, it is proposed, be deemed for every year (or part of the year) of this excess, during which the enterprise enjoyed tax holiday under the old incentive legislation, to have enjoyed already partial tax relief for twice the period. Therefore, under the regional scheme, the enterprise should be entitled to partial tax relief and other benefits under the regional scheme for only the remaining period.

155. In the event it is decided not to go as far as to deny area treatment to enterprises choosing to enjoy tax concessions under the old dispensations, it will be necessary to safeguard new enterprises. The problem arises where such an existing enterprise is entitled under the old dispensation to import raw materials, fuels and/or components free-of-duty, and is now accorded area treatment with respect to its products. Under the regional scheme, the enterprises producing a similar product for the local market and approved under the regional scheme anywhere in the Area would not be eligible for duty-free importation of raw materials etc. But in this particular circumstance, the enterprises approved under the regional scheme would have to be granted the same duty-free concession. This concession should be given for the period for which the Government, of the territory in which the existing enterprise is located, is obliged under its old legislation to continue extending this facility to the existing enterprise.
III. EVALUATION, ENFORCEMENT AND CO-ORDINATION

156. Since the incentive legislations now extant in the Area subscribe to the selective approach, the eligibility of each enterprise must be separately determined before benefits are awarded. Some of the territories, namely, Barbados, Guyana, Jamaica and Trinidad & Tobago, have established special institutions with the principal objective of appraising the applications. In the rest of the territories, the appraisal of applications is undertaken generally by the departments entrusted with the promotion of industrial activity. In all the territories, the final approval of application lies in the hands of the appropriate Ministers.

157. The approach proposed in this Report for the formulation of the regional scheme is also selective. To start with, it calls for a list of industries which may be excluded altogether from the purview of the scheme. Then, also with respect to industries not thus excluded, the eligibility of each enterprise to tax concessions under the regional scheme will be conditional upon the grant of prior approval by the respective national administration. And to gain this approval, an enterprise must pass any test that the national administration might wish to prescribe. Finally, and here the proposed regional scheme goes much further than anything attempted so far, the extent of benefits is tailored to the contribution each enterprise actually makes to the local economy. This calls for a continuing evaluation of every enterprise covered by the scheme until it exhausts its entitlement to tax concessions. Thus evaluation will, in fact, be the principal sheaf-anchor of the proposed regional scheme. It is, therefore, extremely important that the agencies entrusted with this task at the national levels should have competent technical staff to undertake objective evaluation.

158. The agencies entrusted with evaluation work will have to work very closely with other agencies within each national administration charged with the administration and/or enforcement of different aspects of incentive scheme. The income
tax administration, for instance, will be responsible for the dispensation of income tax relief. But it will have to go entirely by the appraisal of the evaluation agency with respect to the contribution of an enterprise to the local value added. Some aspects of the evaluation are such as would call for a type of technical expertise which the income tax administration is ordinarily unlikely to possess. Likewise, while the customs administration in each territory would take care of administering the concessions for duty-free importation, verification of valuations placed on imports, especially of capital goods, could not be left entirely to customs administration. The evaluation agency should try to develop expertise whereby such valuations can be adequately checked.

159. The question naturally arises: to whom could these different administering agencies turn for assistance in such aspects of evaluation in which they themselves lack the necessary technical expertise? In territories such as Jamaica and Trinidad & Tobago, the technical wings of the respective Industrial Development Corporation could possibly be entrusted with such a job. Perhaps Barbados and Guyana would also be in a position to strengthen their technical wings to undertake this job for themselves. As for the less developed territories, they would perhaps find it much more economical to set up a joint agency to undertake such technical work for all of them. Assuming that the broad machinery of evaluation in the Area is organised along the lines indicated, it will become essential that there should be a continuing exchange of information and experience between the evaluation agencies in the Area, so as to ensure not only uniformity of procedures and standards but also their continuing improvement.

160. With respect to enforcement, while some aspects of it will continue to be as important as they are at present, others will become even more important. For instance, each order granting approval to an enterprise sets down the dates by which factory construction must start and by which the factory must start production. The enforcement of these dates will remain important,
in order not only to prevent abuse but also to ensure speedy
development. As for the maintenance of accounts in prescribed
forms and the supply of appropriate information within prescribed
time limits, their enforcement will assume even greater importance
under the regional scheme. The implementation of the regional
scheme is predicated on a continuing evaluation of the actual
performance of approved enterprises which can only be undertaken
on the basis of a regular inflow of adequate information from
these enterprises.

161. Again, although the responsibility for enforcement would
rest on the concerned department or departments in each
territory, the need for a continuing exchange of full information
between the territories cannot be overstated. Also, frequent
exchanges of experience among persons engaged in each territory
in different aspects of enforcement could lead to not only
uniformity of administrative standards but also to their con-
tinuing improvements.

162. It would be important, therefore, to centralise work for
the Area (perhaps by setting up a sort of industrial incentives
clearing house within the Regional Secretariat) for the collation
and analysis of all the necessary information on enterprises
approved under the regional scheme of industrial incentives, and
for its circulation at regular intervals, say quarterly, to all
the member territories. Towards this end, the national
administrating authorities entrusted with the approval and
subsequent evaluation of enterprises would have to undertake
to feed such a central agency, at frequent intervals, with all
the necessary information, beginning with information
collected at the time of approval of enterprises and, followed
up by information on the evaluation of their actual contri-
bution to the economy year after year in terms of employment,
use of local materials, investment and local value added. The
importance of this work in achieving an effective harmonization
of industrial incentives cannot be easily minimized.
Annex 1

Summary of Conclusions
of the
Commonwealth Caribbean Workshop on Harmonization
of Incentives to Industries in the CARIFTA Territories
(E/CN.12/844)

1. 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.

2. 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.

3. 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.

4. 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.

5. 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.

6. 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.

7. 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.

8. The Workshop agreed on a classification of industries into enclave industries and other industries.

9. The participants accepted the principle of establishing a list of industries, at the regional level, that would be excluded from any incentives.

10. The Workshop agreed that in any regional incentive policy, preferential treatment should be accorded to the less developed territories.
11. 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.

12. The Workshop accepted the principle of local value added as the criterion 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.

13. 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 1 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 1 in more developed territories.

14. Agreement was reached on making a distinction between a pioneer industry and an existing industry and on the scale of benefits to be extended to them.

15. 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.

17. 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.

18. 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.

19. With regard to the transitional arrangements, it was agreed that the enterprise 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.
Expert Team's
Comments on the Report of the Workshop

1. Our Report on Harmonization of Fiscal Incentives to Industries in the CARIFTA Territories, in its draft form, constituted the principal working paper at the Workshop. The Workshop discussed all the aspects of a regional incentive policy and examined our recommendations on all issues. It was heartening to note that the area of agreement was substantially large. The participants agreed with our basic approach to the problem and accepted the majority of the recommendations made in the Report.

2. In particular, the Workshop agreed to the principal objectives underlying a regional incentive policy and accepted the principle of employing local value added as the criterion for measuring contributions made by all enterprises - except enclave industries - and relating income tax benefits to such contribution. The Workshop did make some modifications, on grounds principally, of administration, to the definition of local value added given in our Report. We fully appreciate that administrative difficulties would be encountered in the use of a conceptually comprehensive definition of local value added and our Report does not seek to understate them. It must, however, be pointed out that the modified definition adopted by the Workshop is more liberal by virtue of what it excludes, particularly the element of protection. This would naturally dilute, to some extent, the local value added condition of eligibility for the granting of benefits. This fact would, therefore, have to be borne in mind in formulating the scale of benefits, should the modified definition of local value added be ultimately adopted.

3. Departure from the use of local value added as a criterion for measuring contribution was made by the Workshop only in the case of enclave industries. It was pointed out that these were foot-loose industries and offered only a temporary solution to the economic problems of the region. However true this may be (and this

* E/CH.12/844
itself is arguable), there is no reason for not tying up the tax benefits given to enclave enterprises to their performance. Their contribution to local value added, however significant, is bound to vary from industry to industry and from enterprise to enterprise. Naturally, those making a relatively higher contribution deserve to receive more encouragement. It is therefore essential, in our view, to relate tax benefits to the contribution the enclave enterprises make to the region.

4. Other issues, where the views of the participants differed from those of ours, relate largely to the nature and extent of income tax benefits to be offered. In the first place, the Workshop preferred a fixed period of complete tax holiday to be offered ex-ante to a combination, as proposed by us, of complete tax holiday for a limited duration and appropriate partial tax holiday of a prolonged period, the latter based on an evaluation of performance. These two approaches have obvious implications for the evaluation of performance. The Workshop agreed that even though a complete holiday only be offered for a fixed period, the length of this period should be tied up to performance in terms of local value added. It would be, therefore, reasonable to expect that the member territories would insist on the submission of income tax and performance returns even during the period of tax holiday. It should be then not only easy but also appropriate for the administration to undertake evaluation on a continuing basis. In fact, in our scheme,

1/ Incidentally, this proposal for combining a complete tax holiday in the beginning with a partial tax holiday in the period to follow is not new to the Area. One of the two options offered in Barbados and Jamaica to approved manufacturing enterprises combines an initial full tax holiday with a subsequent partial tax holiday. Trinidad and Tobago's Fiscal Review Tripartite Committee (1967) recommended substituting the existing system of full tax holiday only by a combination of a short initial tax holiday with a longer subsequent period of partial tax holiday. What our proposal seeks to do, in addition, is to tie up the partial tax holiday to performance in terms of local value added and exports.
the evaluation exercise would start only at the end of the initial limited period of complete tax holiday. Also, the seemingly psychological advantage of granting a long full tax holiday ex-ante, as claimed by the participants, may be, on the contrary, outweighed by the frustration likely to be caused by the periodic adjustments to an offer made ex-ante, which might become necessary in the light of the subsequent evaluation of the actual performance of an enterprise.

5. The scheme of income tax exemptions considered by the Workshop, including reservations made in Group I by some participants, suffers, in our opinion, from two major weaknesses. In the first place, it does not take into account, and mitigate, special problems faced by capital-intensive industries. It is true that a majority of participants had wished to restrict, for more developed territories, the maximum benefit of 10-year tax holiday proposed for Group I only to certain categories, namely those manufacturing capital goods, intermediate goods and industrial raw materials. Unfortunately, the Workshop did not reach any agreement on the application of this additional condition in more developed territories. It should be obvious however that under our scheme, provided they contributed more than 50 percent in local value added, capital intensive industries would enjoy more liberal benefits than under the scheme for which the Workshop indicated its preference. We have proposed an investment allowance of 30% for such enterprise in addition to the full tax holiday of 3 years and half of the full benefits for ten succeeding years. If these benefits are translated in terms of full tax holiday, the period of full tax holiday available to such enterprises should generally exceed ten years.

6. The failure of the Workshop to appreciate fully the problems of capital intensive industries arises, in our opinion, principally from the classification of industries it considered and which differs somewhat from our scheme of classification. In our classification, we have separated, and highlighted, capital intensive industries and have argued out for them a case for investment allowance. Since the classification adopted by the Workshop did not explicitly
recognise the importance of identifying such industries separately, their problems and the relevance of an investment allowance in their context got lost in the general scheme of income tax exemption.

7. Secondly, the Workshop scheme of income tax benefits does not provide for any preferential treatment to enterprises which sell only a part of their output in the export market. This omission is serious, particularly in view of the fact that the participants themselves attached great significance to production by import substitution enterprises for the markets outside of the Area and stressed the need for granting special incentives to exports. We strongly believe that in order to overcome the constraint of the relatively small size of the CARIFTA market and to ensure economies of scale, it would be essential to give export relief to export oriented enterprises.

8. Another point of disagreement with our Report centered around the concept and definition of depressed areas in more developed countries and the incentive treatment to be accorded to them. It is obviously extremely difficult to give any objective credence to this concept or to suggest acceptable quantifiable characteristics for its measurement. Nevertheless, we are willing to accept it as a "working concept" which can be understood only in relation to issues of regional development within a more developed territory. It is, however, difficult to accept the premise, implied in the Workshop Report, that for purposes of incentives such "depressed areas" should be treated on par with less developed territories. "Depressed areas" would have still the advantage of benefiting from the centrally provided services such as marketing and research. Moreover, the cost of extending infrastructure facilities to such areas is likely to be much less than of rectifying major infrastructural deficiencies of less developed territories. For these reasons, while it may be necessary to accord some preferential treatment to depressed areas in more developed territories, between these depressed areas and less developed territories, it would be desirable to give a more preferred treatment to less developed territories as is suggested in our Report.
9. In conclusion, we submit, with all modesty, that the scheme of income tax benefits proposed by us has more merits than the one considered by the workshop. It has the advantage of distinguishing various primary objectives and of giving weights to them in accordance with their importance. It must be recognized that performance has several dimensions and although local value added is a primary objective, other significant aspects of performance cannot be ignored. It is only a system of partial tax holidays which can be linked to various aspects of performance. Once it is decided to give, ex-ante, a fixed period of full tax holiday, flexibility for a conscious use of a scheme is naturally frozen and it is difficult to tailor benefits in proportion to contribution made to different objectives.

10. We should also like to express our serious reservations on the views expressed by some participants in favour of deferring deduction of depreciation allowances until after the end of the tax holiday period. Such deferment permits recovery of capital in excess of the amount actually invested and is tantamount to an investment allowance. They are also similar, in some respects, to a tax holiday in that they allow a higher net return. What is most objectionable about the deferment of depreciation deductions, until beyond the tax holiday period, is to allow these accumulations to be distributed as tax exempt dividends. This the participants concerned were fully prepared to concede. They felt however, and quite strongly, that to withdraw this particular concession, alongside, what they believed to be, a general scaling down of tax concessions even in the scheme considered by the Workshop, might affect adversely the competitive position of the CARIFTA territories as against third countries in attracting industrial enterprises. We do not share this fear, however, for we believe that the additional attraction offered by a unified market much larger in size than that of any individual member territory of CARIFTA should compensate largely for the suggested scaling down in concessions under the regional scheme.
Appendix I

INCOME TAX RELIEFS OFFERED IN CARIFTA TERRITORIES AND BELIZE TO SPECIALLY APPROVED MANUFACTURING ENTERPRISES UNDER THEIR RESPECTIVE INCENTIVE LEGISLATIONS

**Type of Relief - A. Holiday from Income Tax**

**ANTIGUA** - A person declared a **Pioneer Enterprise** is exempt from income tax on profits from pioneer operations for five years from the production day.

**BARBADOS** - A company declared an **Approved Enterprise** can choose one of the two options below:

Option (1) comprises of exemption of profits of the enterprise from income tax for ten years from the date of production.

Option (2) comprises of complete exemption from income tax in the first seven years and 2/3rd exemption in the eighth year and 1/3rd in the ninth year, as from the date chosen by the approved enterprise within 3 years from the production day.

**BELIZE** - Any company declared a **Development Enterprise** is exempt from income tax for a period commencing from the date of the Order and terminating ten years after the production day.

**DOMINICA** - A person declared a **Pioneer Enterprise** is entitled to exemption from income tax on its profits for five years from the production day. However, under a special Agreement with a company, Sunday Island Port Authority Ltd., within the area marked out for special development in and around the CABRITS, exemption from income tax, as from several other taxes, is given for a period of 30 years as from 16.2.1968, the date of the Agreement, to all licensees including manufacturing enterprises.

**GRENADA** - A company declared a **Development Enterprise** is entitled to exemption from income tax on its profits for seven years from the production day.

**GUYANA** - A manufacturing company, other than a gold or diamond mining company is, on authorization, entitled to an exemption from income tax for five years from the date of such authorization.

It has recently been announced that this period of tax holiday could be extended to ten years and that a two-year tax holiday could be considered for smaller investments in secondary industries.

**JAMAICA** - A company manufacturing a 'new product' or for exports only is entitled to exemption from income tax for a period of ten years from the date of production or from a date chosen within three
years thereafter. The period may be extended up to fifteen years with respect to designated special development areas in the country. A product may be designated a new product if less than 20% of the national market is being supplied by existing approved manufacturers. While a manufacturer of exports only is entitled to 100% exemption, other manufacturers may be granted 100% or 50% exemption, depending upon the approved products.

For approved products other than 'new products', an approved company may choose benefits under either of the two options:

Under Option (1) income tax exemption is given for seven years from the production day,

Under Option (2) complete exemptions from income tax for four years from the date chosen by the enterprise within three years from the date of production is combined with partial exemption in the following two years as under:

(a) if the product is entitled to 100% relief, it will enjoy the exemption with respect to 33-1/3% of income in the fifth year and to 66-2/3% of income in the sixth year before deduction of annual allowances; or

(b) if the product is entitled to 50% relief, it will enjoy the exemption with respect to 66-2/3% of income in the fifth year and 83-1/3% of income in the sixth year before deduction of annual allowances.

Montserrat — A company declared as Development Enterprise, is entitled to exemption from income tax on its profits for a period of seven years from the production day.

St. Kitts — A person declared as Pioneer Enterprise, is entitled to exemption from income tax initially for a period of five years from the production day. This may be extended on application, for a further period of five years.

A Pioneer Enterprise which is established within a designated Special Development Area and during the Special Development Period (i.e. ending on 31.12.1973) will be entitled to exemption from income tax for a period of fifteen years from the production day.

St. Lucia — A company declared a Development Enterprise is entitled to such proportionate relief from income tax as is specified in the Development Order for a period of seven years from the production day.
ST. VINCENT - Any person declared as Pioneer Enterprise is entitled to exemption from income tax for a period of ten years from the production day.

TRINIDAD & TOBAGO - Any person declared as Pioneer Manufacturer is entitled to exemption from income tax for a period initially of five years from the production day. This period may be extended from five years to a period not exceeding ten years where circumstances warrant it.

In specific cases, as in the case of Cement, Fertilizer, Lubricating Oil, Tyre and Petrochemical manufacturing, exemption from income tax has been given straightaway for a period of ten years from the production day.

Type of Relief - B. Treatment of Dividends

ANTIGUA - There is no provision specifically exempting distributions made by a company out of tax holiday profits in the hands of the recipients. Nor is it clear if in any specific case, e.g. West India Oil Company, such exemption was agreed upon.

BARBADOS - Where profits of a company in the first seven years of the ten-year tax holiday period under Option (1) and of the nine-year period of tax holiday under Option (2), are kept in a separate account, dividends paid therefrom are exempt in the hands of the shareholder: i) if he is a resident of the island; or ii) if not a resident, he is not liable to pay income tax on the dividend in his country of residence; and iii) the dividend is paid within two years after the expiration of the 10-year or 9-year holiday period, whichever is applicable; provided further that the exemption from income tax shall not exceed the amount of tax which would have been payable by the approved enterprise in the absence of the exemption.

BELIZE - Dividends paid out of profits of tax holiday period and distributed during the said period are not taxable in the hands of shareholders; provided (a) the amount thus paid does not exceed the amount invested by the shareholder in the enterprise and (b) the shareholder is not liable in his home country to income tax on such dividends.
DOMINICA - A sum equal to the income arising to the company during the tax holiday period and distributed within the tax holiday period and two years thereafter to its members is exempt from income tax in the hands of such members:

provided where a member is a non-resident, he is not liable to income tax on the dividend in the country of his residence.

It appears that this restriction on non-resident members was removed when the Income Tax Ordinance (1966), sub-section (4) of Section 11, was updated.

GRENAADA - A sum equal to profits accruing to a development company during the tax holiday period and distributed during that period, shall not be chargeable in the hands of shareholders:

provided the total amount paid as dividends does not exceed the amount invested by the shareholder in the development company during the tax holiday period;

provided also where the shareholder is a non-resident, he is not liable to income tax on the dividend in his country of residence.

GUYANA - A sum equal to the income arising to the company during the tax holiday period and distributed within the tax holiday period and two years thereafter to its members is exempt from income tax in the hands of such members.

Where dividends are paid out of profits of the tax holiday period, viz., 7 years under Option (1), 6 years under Option (2) and 10 to 15 years for New Products and exports only, and they are kept in separate accounts, a shareholder is exempt from income tax 1) if he is resident or 2) if not so resident, is not liable to income tax in his country of residence. Provided this exemption shall not extend to surtax and shall not exceed the tax which the company would have paid on the profits in question.

Where a non-resident shareholder is liable to tax on the dividend in question in the country of his residence, he shall be exempt from so much income tax as exceeds his liability in his country of residence.

MONTSERRAT - Where profits accruing to a development company during the tax holiday period and paid to shareholders during that period, they shall not be chargeable in the hands of shareholders:
MONTSERRAT (cont'd.)

provided the total amount paid as dividends does not exceed the amount invested by the shareholders in the development company during the tax holiday period; provided also where the shareholder is a non-resident he is not liable to tax on the dividend in the country of his residence.

ST. KITTS

A sum equal to the income arising to the company during the tax holiday period and distributed within the tax holiday period and two years thereafter to its members is exempt from income tax in the hands of such members;

provided where a member is a non-resident, he is not liable to income tax in the country of his residence. It appears that this restriction on non-resident members was removed when the Income Tax Ordinance (1966), sub-section (6) of Section 8, was updated.

ST. LUCIA

A sum equal to profits accruing to a development company during the tax holiday period and distributed during that period shall not be chargeable in the hands of shareholders;

provided the total amount paid as dividends does not exceed the amount invested by the shareholders in the development company during the tax holiday period; provided where the shareholder is a non-resident, he is not liable to income tax on the dividend in the country of his residence.

ST. VINCENT

A sum equal to the income arising to the company during the tax holiday period and distributed within the tax holiday period and two years thereafter to its members is exempt from income tax in the hands of such members. It appears that the restriction on distribution within the tax holiday period and two years thereafter was withdrawn recently. Sub-section (5) of Section (7) of the Income Tax Ordinance 1967, does not impose this restriction on tax holiday profits to qualify for exemption in the hands of members.

TRINIDAD & TOBAGO

Where a pioneer manufacturer is a company, it is entitled to distribute a sum equal to the income arising during the tax holiday period to members of the company during the tax holiday period and within two years thereafter and every such sum is exempt from income tax in the hands of the members. Under Finance Act,
1966, distributions of such tax exempt profits are relieved of tax in the hands of members regardless of timelimit provided the company maintains a special account to the satisfaction of the Inland Revenue Board.

**Type of Relief - C. Tax Treatment of Interest Payments**

**ANTIGUA**
- No exemption seems to exist for interest payments by a pioneer manufacturer in the hands of recipients.

**BARBADOS**
- Interest payments made by an approved enterprise on its debentures with respect to the first seven years of its tax holiday period under either of the options are exempt in the hands of recipients. Also interest payments made by an approved builder of factory on its debentures are exempt in the hands of the recipients for fifteen years from the date of the completion of the Factory construction;

Provided where the recipient is a non-resident he is not liable to income tax thereon in his country of his residence.

But while such tax exempt interest is not allowed as a deduction in the calculation of the tax holiday profits of the approved builder, there is no such stipulation with respect to tax exempt interest paid by an approved (manufacturing) enterprise.

**BELIZE**
- No exemption seems to exist for interest payments by a development enterprise in the hands of recipients.

**DOMINICA**
- No exemption seems to exist for interest payments by a pioneer company in the hands of recipients.

It is not clear if in the case of industries set up in the specially earmarked part of the CABRITS, such exemption has been granted. Sub-section (8) of Section 2 of the Agreement refers to non-taxation of rentals or licence fees paid "by a licensee to the holders of evidence of indebtedness and/or shares or other securities of the Authority or of the Company".

**GRENADA**
- No exemption seems to exist for interest payments by a development company in the hands of recipients.
GUYANA - No exemption seems to exist for interest payments by a company enjoying tax holiday in the hands of recipients.

JAMAICA - No exemption seems to exist for interest payments made by an approved enterprise in the hands of recipients. Where, however, interest payments are made by an approved builder of factory on its debentures they are exempt in the hands of recipients for a period of fifteen years. There is no express provision stipulating whether such tax exempt interest will, or will not, be deductible as an expense in the computation of tax holiday profits or loss of the approved builder.

MONTserrat - No exemption seems to exist for interest payment by a development company in the hands of recipients.

ST. KITTS - No exemption seems to exist for interest payments by pioneer manufacturers in the hands of recipients.

But interest payments made by such pioneer manufacturers as qualify as special developers are exempt in the hands of the recipients for a period of fifteen years. There is no stipulation whether that interest so exempt will, or will not, be treated as a deductible expense in the calculation of tax-holiday period profit or loss.

ST. LUCIA - No exemption seems to exist for interest payments by a development company in the hands of recipients.

ST. VINCENT - No exemption seems to exist for interest payments by pioneer manufacturer in the hands of recipients.

TRINIDAD & TOBAGO - There is no general exemption for interest payments made by pioneer enterprises. In certain special industries, viz., fertilizers, lubricating oils and petro-chemicals, exemption has been granted for ten years with respect to interest payments by approved manufacturers in the hands of recipients provided either the loans were raised abroad and/or were of at least five years' duration. There is no provision requiring that such tax exempt interest payments should, or should not, be deducted as an
expense in the computation of tax-holiday period profits or losses. The general presumption, however, is that they are deductible.

**Type of Relief**

- **D. Depreciation Deductions**

**ANTIGUA**
- Assets will, it appears, be written down during the tax holiday period in the normal manner laid down in the Income Tax Ordinance. Ordinarily, initial allowance at the rate of 20% of expenditure incurred on machinery, plant and industrial building is allowed but this is not allowed to a pioneer enterprise.

**BARBADOS**
- Under Option (1), notional depreciation of plant and machinery will be made during the tax holiday period and annual deductions can be claimed after the tax holiday period on the basis of the written down value. Under Option (2), no depreciation deductions shall be made during the first seven years. Thereafter, depreciation deductions shall be computed as if the capital expenditure on plant and machinery less the amount of deductions made before the commencement of the tax holiday period had been incurred on the last day of the seven-year period.

No initial allowance or investment allowance can be claimed with respect to the cost of plant and machinery acquired during the tax holiday period under Option (1) and till the end of the tax holiday period under Option (2).

Industrial enterprises not operating under the incentive laws are entitled to an investment allowance of 20% of capital expenditure on plant and machinery, if engaged in a Basic Industry, otherwise to an initial allowance of 20%, in the year in which the expenditure is incurred.

**BELIZE**
- During the tax holiday period, the assets are to be depreciated in the manner normally allowed under Income Tax Ordinance for wear and tear. No provision exists for initial or investment allowance with respect to capital expenditure incurred by an industrial enterprise.

**DOMINICA**
- Assets will, it appears, be written down during the tax holiday period in the normal manner laid down in the Income Tax Ordinance which provides for annual depreciation deductions but not for any initial allowance or investment allowance.
GRENADA - Assets will, it appears, be written down during the tax holiday period in the normal manner laid down in the Income Tax Ordinance which provides not only for annual depreciation deductions but also for initial deduction of 20% for plant and machinery and 10% for commercial building in the year in which such expenditure is incurred. It is not clear, however, if and when a pioneer enterprise is obliged to make the initial deduction.

GUYANA - No depreciation deduction shall be made in computing the income of the tax holiday period. In computing the income of the enterprise after the tax holiday has expired, depreciation deductions shall be made as if capital expenditure incurred up to the end of tax holiday period were incurred on the first day following thereafter. The enterprise can claim also initial allowance at the rate of 40% of capital expenditure on plant and machinery and 10% of capital expenditure on industrial building, as is allowed to other industrial enterprises.

JAMAICA - For an enterprise manufacturing a New Product or exports only, depreciation deductions shall not be made during the tax holiday period but after that period upon the original cost less any allowances claimed before the tax holiday period. As for other approved enterprises, the position will be as below:

Under Option (1), notional depreciation of assets will be made during the tax holiday period and depreciation deduction shall be claimed after the tax holiday period on the written down value.

Under Option (2), prior to the commencement of the tax holiday period, depreciation deduction shall be made but they will cease during the first four years of holiday period; again deductions will be made starting with the fifth year of the tax holiday period on the original cost less the deductions made before the commencement of the tax holiday period.

Industrial enterprises not operating under incentive laws are entitled to an investment allowance of 20% of capital expenditure, if engaged in a Basic Industry, otherwise to an initial allowance of 20%, in the year in which expenditure is incurred.

MONTSERRAT - Assets of the enterprise will, it appears, be written down during the tax holiday period in the normal manner laid down in the Income Tax Ordinance which provides not only for annual depreciation deductions but also for initial deduction of 20%
MONTSERAT (cont'd) — for plant and machinery and 10% for commercial building in the year in which such expenditure is incurred. It is not clear, however, if and when a pioneer enterprise is obliged to make the initial deduction.

ST. LUCIA — No depreciation deduction shall be made in computing the income of the tax holiday period. Depreciation deductions after the tax holiday period shall be computed as if the capital expenditure incurred up to the end of the tax holiday period were incurred on the first day following the end of the said period. Such computation, however, will not include initial allowance which is allowed at the rate of 20% of capital expenditure incurred on plant, machinery and industrial building.

ST. VINCENT — Assets of the enterprise will, it appears, continue to be written down during the tax holiday period. After the tax holiday period, allowances for depreciation and initial allowance can be claimed on the written down value of the assets at the end of the last year of the tax holiday period. Initial allowance can be claimed at the rate of 10% for industrial building and 20% for plant and machinery.

TRINIDAD & TOBAGO — No depreciation deductions shall be made in computing the income of the tax holiday period. Depreciation deductions shall be computed after the tax holiday period as if the capital expenditure incurred up to the end of that period were incurred on the first day following thereafter. The enterprise can also claim initial allowance at the rate of 20% on capital expenditure incurred on plant and machinery and 10% on industrial building which is allowed to all industrial enterprises.
Type of Relief - B. Carry-over of Losses of Tax Holiday Period

ANTIGUA - No special provisions exist with this respect. It is not clear whether such losses can be set off against income from other sources during the same year or whether they can only be carried forward and set off against income from the same source. Ordinary losses not set off against income from other sources can be carried forward for the next six years in succession under the Income Tax Rules of the territory.

BARBADOS - Under Option (1), all losses incurred during the tax holiday period in excess of the profits of the same period of the same enterprise may be carried forward over the five succeeding years. Such losses shall include notional depreciation.

Under Option (2), all losses incurred during the first seven years in excess of any profits during the same period together with any loss incurred and not set off before the commencement of the seven-year period may be carried forward and set off over the five years following the nine-year period of tax holiday.

Under either option, losses carried forward could be set off against the income of the enterprise only from the same source.

BELIZE - No special provisions exist with this respect. It can be assumed, therefore, that regular provisions of Income Tax Ordinance would apply, whereby trade losses not set off can be carried forward to subsequent years without any limitation on time.

DOMINICA - No special provisions exist with this respect. It can be assumed, therefore, that regular provisions of the Income Tax Ordinance will apply whereby losses not set off can be carried forward over the next five years provided the set-off in any of these years will not reduce the tax payable by more than 50%.

GRENADA - Losses which have not been written off during the tax holiday period less any allowance made during the period with respect to depreciation of assets can be carried forward over six succeeding years. It is not clearly indicated if the losses thus carried forward can be set off against the income of the same enterprise only.
GUYANA - Any loss incurred during the tax holiday period shall be set off without limitation against the income arising to such a company during the period immediately following. It is not clear if losses incurred during the tax holiday period have to be first set off against income of the enterprise during the same period. Nor is it clear if losses carried forward can be set off against the income of the company from a source other than this enterprise.

JAMAICA - For manufacturers of New Products and exports only, losses not written off during the tax holiday period can be carried forward for the following six years. For other approved manufacturers, under Option (1), losses incurred and not written off during the tax holiday period without taking into account any depreciation of assets can be carried forward over the next six years.

Under Option (2), losses incurred and not written off during the six years of tax holiday period after taking into account allowances made before the tax holiday period and during the last two years of the tax holiday period, can be carried forward for six years following the tax holiday period. In any event, losses carried forward could be set off against the income of the approved enterprise only.

MONTSERRAT - Losses which have not been written off during the tax holiday period less any allowance made during the tax holiday period with respect to depreciation of assets may be carried forward in the six succeeding years. It is not clearly indicated if the losses thus carried forward can be set off against the income of the same enterprise only.

ST. KITTS - Any loss incurred during the tax holiday period can be set off against the income of the pioneer enterprise during the years immediately following the tax holiday period provided the set-off does not reduce the income tax payable in any of these years to less than 50%. It appears that no netting of losses is required against income of the pioneer enterprise during tax holiday period.

ST. LUCIA - Losses which have not been written off during the tax holiday period less any allowance made during the tax holiday period with respect to depreciation of assets may be carried forward in the six succeeding years. It is not clearly indicated if the losses thus carried forward can be set off against the income of the same enterprise only.
ST. VINCENT

No loss incurred during the tax holiday period can be set off against the income from other sources but the net loss of the whole of the tax holiday period can be carried forward after the period provided, inter alia, the set off does not reduce the income tax payable in the year of set off by more than 50%. It is not clearly indicated if the losses thus carried forward can be set off against the income of the same enterprise only.

TRINIDAD & TOBAGO

Any loss incurred during the tax holiday period can be set off against the income of the same enterprise in the period immediately following without any limitation. No netting of losses is required against the income of the pioneer enterprise during the tax holiday period. Where a person carrying on two or more pioneer enterprises incurs a loss in one of such enterprises during the tax holiday period or part thereof which is coterminous with another pioneer enterprise of the same person, then he may be allowed to set off such loss without limitation against the income of the other enterprise after the tax holiday period.
CUSTOMS DUTY RELIEFS OFFERED IN CARIFTA TERRITORIES AND BELIZE TO SPECIALLY APPROVED MANUFACTURING ENTERPRISES UNDER THEIR RESPECTIVE INCENTIVE LEGISLATIONS

Type of Relief § A. Duty-free Importation of Machinery, Plant and Building Materials

ANTIGUA — Every pioneer manufacturer is entitled to import these items free of customs duty for a period of five years commencing from the date of his approval:

provided these items are required for the construction, alteration or extension of the pioneer factory but not for effecting repairs thereto.

BELIZE — Every approved enterprise is entitled to import free of customs duty and entry tax these items, including vehicles and tools, other than hand tools provided that the items thus imported are required for the establishment or expansion of the enterprise. This concession is available for a period beginning with the date of approval to the end of the tax holiday period.

BARBADOS — Every approved enterprise is entitled to import these items free of customs duty for the purpose of construction, extension or equipment of its factory and also for effecting repairs and replacements thereto. This concession is available for a period of ten years commencing from the date of approval.

The same concession is available to an approved factory builder without limitation of period but the Government may withdraw, by notification, exemption with respect to any article which is manufactured within the island and is available in adequate supply.

For approved enterprises which manufacture exclusively for exports, duty-free importation of these items is allowed without limitation of either time or local availability of substitutes.

DOMINICA — Every pioneer manufacturer is entitled to import free of customs duty these items for a period of five years commencing from the date of his approval. These items should be required for the construction, alteration, reconstruction or extension of the pioneer factory but not for effecting repairs thereto.

Under the Agreement entered into by the Government for the development of the CABRITS, this exemption is given with respect to all materials, supplies,
DOMINICA (cont'd) equipment, vehicles, spare parts required for construction, extension, repair or maintenance. This exemption is valid for the duration of the Agreement i.e. thirty years from the day it was signed.

GRENA DA Every approved enterprise is entitled to import these items free of customs duty from the date of the approval to the end of tax holiday period. These items should be required for construction, alteration, reconstruction or extension of the development premises or for their equipment but not for repairs or replacement.

The list of items specifically includes office equipment.

GUYANA Formally speaking, grant of duty-free importation of these items has to be applied for separately. These items should be required in direct connection with the establishment or development of industry, but not for replacement or renewal of existing factory. Where an application is granted, this concession may be given for a period not exceeding ten years for a mining enterprise and five years for any other industrial enterprise. Since it has now been decided to extend tax holiday up to ten years, it is assumed that duty-free importation of plant and machinery could also be extended.

JAMAICA Every approved manufacturer of an approved product, including a New Product, may be granted 100% or 50% exemption from customs duties (including tonnage tax) with respect to these items provided they are required for the construction, alteration, reconstruction or extension of the factory premises or for its equipment but not for repair or replacement.

The list specifically includes office equipment. But any item which is locally available in sufficient quantity and of reasonably comparable price and quality may be deleted from the list. This concession will be valid for the period ending with the tax holiday period i.e. of seven years under the first option, of six years under the second option and of ten to fifteen years for manufacturers of approved New Products. Approved export manufacturers will be entitled to duty-free importation for a period of ten to fifteen years not only of items required for construction, extension, or equipment of factory premises but also for repairs and replacement. An approved Factory builder is entitled to duty-free importation (100%) of articles required for factory construction subject to availability of corresponding articles of local manufacture.
MONTSERRAT — Every approved enterprise is entitled to import these items free of customs duty from the date of the approval to the end of tax holiday period. These items should be required for construction, alteration, reconstruction or extension of the development premises or for their equipment but not for repairs or replacement. The list of items specifically includes office equipment.

ST. KITTS — Every pioneer manufacturer is entitled to import free of customs duty these items for a period of five years commencing from the date of his approval. These items should be required for construction, alteration or extension of the pioneer factory but not for effecting repairs thereto.

It is assumed that with respect to approved enterprises set up in designated special development areas this concession will be available for a period of fifteen years from the date of approval.

ST. LUCIA — Every approved enterprise is entitled to import these items free of customs duty from the date of the approval to the end of tax holiday period. These items should be required for construction, alteration, reconstruction or extension of the development premises or for their equipment but not for repairs or replacement. The list of items specifically includes office equipment.

ST. VINCENT — Every pioneer manufacturer is entitled to import free of customs duty these items for a period of ten years commencing from the date of his approval. These items should be required for the construction, alteration or extension of the pioneer factory but not for effecting repairs thereto.

TRINIDAD & TOBAGO — Every pioneer manufacturer is entitled to import free of customs duty these items for a period of five years commencing on the date of approval. The period may be extended in suitable cases to a period not exceeding ten years. The items imported duty-free should be required for the construction, alteration or extension of the pioneer factory but not for effecting repairs. Even a manufacturer not approved as pioneer manufacturer is entitled to duty-free importation of these items for the purposes stated above.
This exemption was due to expire on December 31, 1969, but has been extended to December 31, 1971 or until a regional policy has been agreed upon on incentives under the CARIFTA Agreement.

Type of Relief – B. Duty-free Importation of Raw and Other Materials

ANTIGUA - Incentive legislation does not provide for this concession.

BELIZE - An approved enterprise may be granted duty exemption with respect to any raw materials imported for its use on such terms and conditions as the Government imposes.

BARBADOS - Duty-free importation of raw and semi-processed materials, food and packing materials is allowed for approved enterprises manufacturing exclusively for exports with no limitation with respect to time but subject to local availability of substitutes in adequate supply.

DOMINICA - The principal incentive legislation does not provide for this concession. But the Agreement on the CABRITS provides for duty-free importation of all raw and semi-processed materials required for manufacturing in the CABRITS. No distinction is made in the Agreement between manufacturing for export and that for sale within the territory.

GRENA - Incentive legislation does not provide for this concession.

JAMAICA - Under the incentive legislation of the territory, only approved export manufacturers are entitled to duty-free importation of raw and semi-manufactured materials, fuel and containers. Under the territory's Customs legislation, however, duty-free importation of raw materials and semi-manufactures, not available within the territory, required for the manufacture of specified products is allowed to approved manufacturers.
MONTSERRAT - Incentive legislation does not provide for this concession.

ST. KITTS - Incentive legislation does not provide for this concession.

ST. LUCIA - Incentive legislation provide for this concession to be granted by a Resolution of the Legislature. Under a Resolution adopted in December 1968, duty-free importation of raw materials, chemicals, other ingredients and supplies and semi-manufactured and manufactured goods to be used for by approved enterprises for manufacturing, assembling and blending processes was sanctioned till December 31, 1975.

ST. VINCENT - Incentive legislation does not provide for this concession.

TRINIDAD & TOBAGO - The territory's principal incentive legislation does not provide for duty-free importation of raw materials. But the Customs legislation does and the concession thereunder has to be separately applied for. Special legislations dealing with the manufacture of cement and fertilizers, provide for duty-free importation of raw materials, fuel and containers. The legislation concerning manufacture of lubricants makes a similar provision for duty-free importation subject, however, to the condition that if certain containers of local manufacture are available, this exemption will not be granted with respect to such types. Even non-pioneer manufacturers are eligible for duty-free importation of raw and semi-manufactured materials.

This concession was due to expire on December 31, 1969 but has been extended to December 31, 1971 or until the regional incentives policy under the CARIFTA Agreement has been agreed upon.
### Appendix III

**Comparative Tax Rates on Company and Individual Incomes in Caribbean Territories—and-Belize**

<table>
<thead>
<tr>
<th>Territory</th>
<th>Rate of Tax on Company Profits</th>
<th>Rate of Tax on Individual Incomes</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Highest marginal rate of tax</td>
<td>Income level at which the highest rate starts applying (E.C. Dollars)</td>
</tr>
<tr>
<td>Antigua</td>
<td>40%</td>
<td>65%</td>
</tr>
<tr>
<td>Barbados</td>
<td>51.7% (including 19.5% trade tax)</td>
<td>75%</td>
</tr>
<tr>
<td>Belize</td>
<td>40%</td>
<td>70%</td>
</tr>
<tr>
<td>Dominica</td>
<td>37½%</td>
<td>50%</td>
</tr>
<tr>
<td>Grenada</td>
<td>37½%</td>
<td>65%</td>
</tr>
<tr>
<td>Guyana</td>
<td>45% (plus 4.5% Development tax for 1968 only)</td>
<td>70%</td>
</tr>
<tr>
<td>Jamaica</td>
<td>42½% (to be reduced as from 1970 to 35% plus Withholding Tax at 37½% on all distributions)</td>
<td>75%</td>
</tr>
<tr>
<td>Montserrat</td>
<td>20%</td>
<td>20%</td>
</tr>
<tr>
<td>St. Kitts</td>
<td>40%</td>
<td>75%</td>
</tr>
<tr>
<td>St. Lucia</td>
<td>40%</td>
<td>65%</td>
</tr>
<tr>
<td>St. Vincent</td>
<td>40%</td>
<td>65%</td>
</tr>
<tr>
<td>Trinidad and Tobago</td>
<td>45% (plus Withholding tax on distributions abroad)</td>
<td>50%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>60%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>85%</td>
</tr>
</tbody>
</table>

*Subject to overall requirement that average rate will not exceed 50%.
### Comparative Income Tax Exemption Available to Selected Types of Approved Industrial Enterprises under the Existing Legislations and under the Proposed Harmonization Scheme in all CARIFTA Member Territories

<table>
<thead>
<tr>
<th>Type of Enterprise</th>
<th>Under the Existing Legislations in:</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Enclave enterprise with:</td>
<td></td>
</tr>
<tr>
<td>a) value added locally 5-year</td>
<td>5-year</td>
</tr>
<tr>
<td>between 25-50%</td>
<td>com-</td>
</tr>
<tr>
<td>b) value added locally over 50%</td>
<td>exempt</td>
</tr>
<tr>
<td>over</td>
<td>tion</td>
</tr>
<tr>
<td>25-50%</td>
<td>deprecia-</td>
</tr>
<tr>
<td>tion</td>
<td>tax holiday</td>
</tr>
<tr>
<td>Under the proposed harmonization scheme</td>
<td>Under the Existing Legislations in:</td>
</tr>
<tr>
<td>----------------------------------------</td>
<td>-------------------------------------</td>
</tr>
<tr>
<td><strong>Other Territories</strong></td>
<td><strong>B'dos.</strong></td>
</tr>
</tbody>
</table>

<p>| a) 6-year complete exemption + 10-year 50% exemption | 10-year complete 10-year complete exemption + 10-year complete 10-year complete 10-year complete 10-year complete | 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 5 to 10 |
| b) 6-year complete exemption + 10-year 75% exemption | 76% exemption | 76% exemption | 76% exemption | 76% exemption | 76% exemption |
| a) 3-year complete exemption | 3-year complete exemption | 3-year complete exemption | 3-year complete exemption | 3-year complete exemption | 3-year complete exemption |
| b) 3-year complete exemption + 10-year 75% exemption | 3-year complete exemption + 10-year 75% exemption | 3-year complete exemption + 10-year 75% exemption | 3-year complete exemption + 10-year 75% exemption | 3-year complete exemption + 10-year 75% exemption | 3-year complete exemption + 10-year 75% exemption |</p>
<table>
<thead>
<tr>
<th>Type of Enterprise</th>
<th>Under the Existing Legislations in:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital-intensive</td>
<td></td>
</tr>
<tr>
<td>enterprise</td>
<td></td>
</tr>
<tr>
<td>with value added</td>
<td></td>
</tr>
<tr>
<td>locally between</td>
<td></td>
</tr>
<tr>
<td>25-50% and:</td>
<td></td>
</tr>
<tr>
<td>a) exporting</td>
<td></td>
</tr>
<tr>
<td>50% of its total</td>
<td>5-year</td>
</tr>
<tr>
<td>output</td>
<td>complete</td>
</tr>
<tr>
<td>b) exporting</td>
<td></td>
</tr>
<tr>
<td>75% of its total</td>
<td>exemption</td>
</tr>
<tr>
<td>output</td>
<td>tion</td>
</tr>
</tbody>
</table>

2. Capital-intensive enterprise with value added locally between 25-50% and:

a) exporting
- 50% of its total output

b) exporting
- 75% of its total output
## Other Territories

<table>
<thead>
<tr>
<th>Under the proposed harmonization scheme</th>
<th>Other territories under the proposed harmonization scheme</th>
</tr>
</thead>
<tbody>
<tr>
<td>B'dos.</td>
<td>Guv.</td>
</tr>
<tr>
<td>a) 30% investment allowance + 6-year complete exemption from the date of production or 41.5% exemption b) 30% investment allowance + 6-year complete exemption within 3 years of the date of production + 66 2/3% exemption in the 6th year + 33/12% exemption in the 9th year + 1/3 deferment of depreciation deductions for 7-year period of complete exemption</td>
<td></td>
</tr>
<tr>
<td>Either 10-year complete exemption OR 7-year complete exemption beginning within 3 years of the date of production + 66 2/3% exemption in the 6th year + 33/12% exemption in the 9th year + 1/3 deferment of depreciation deductions for 7-year period of complete exemption</td>
<td></td>
</tr>
<tr>
<td>a) 30% investment allowance + 3-year complete exemption + 10-year 41.5% exemption</td>
<td></td>
</tr>
<tr>
<td>b) 30% investment allowance + 3-year complete exemption + 10-year 46.25% exemption</td>
<td></td>
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<tr>
<td>-------------------------------</td>
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</tr>
<tr>
<td>3. Import substitute enterprise manufacturing exclusively for CARIFMA market and with:</td>
<td></td>
</tr>
<tr>
<td>a) value added locally between 25-50%</td>
<td>5-year complete</td>
</tr>
<tr>
<td>b) value added locally over 50%</td>
<td>exempt-completion</td>
</tr>
</tbody>
</table>
### Other Territories

<table>
<thead>
<tr>
<th>Under the proposed harmonization scheme</th>
<th>Under the Existing Legislations in:</th>
<th>Under the proposed harmonization scheme</th>
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<table>
<thead>
<tr>
<th>Option</th>
<th>Duration</th>
<th>Tax Treatment</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) 6-year complete exemption</td>
<td>10-year complete exemption from the date of production OR</td>
<td>3-year complete exemption + tax deduction for tax in the 8th year + 33 1/3% exemption in the 9th year + deferment of depreciation deductions for 7-year period of complete exemption</td>
</tr>
<tr>
<td>b) 6-year complete exemption</td>
<td>7-year complete exemption beginning 3 years of the date of production + holiday for tax in the 9th year + holiday for tax in the 10th year + 50% exemption in the 11th year + 66 2/3% exemption in the 12th year +</td>
<td>3-year complete exemption + tax deduction for tax in the 8th year + 33 1/3% exemption in the 9th year + deferment of depreciation deductions for 7-year period of complete exemption</td>
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</table>
Type of Enterprise

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<tbody>
<tr>
<td>Under the Existing Legislations in:</td>
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<tr>
<td>4. Import substitute enterprise exporting 50% of its output outside CARIFTA and with:</td>
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<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>a) value added locally</td>
<td>5-year</td>
<td>5-year</td>
<td>7-year</td>
<td>7-year</td>
<td>5to10-</td>
<td>7-year</td>
<td>10-year</td>
</tr>
<tr>
<td>between 25-50%</td>
<td>complete</td>
<td>complete</td>
<td>complete</td>
<td>complete</td>
<td>complete</td>
<td>complete</td>
<td>complete</td>
</tr>
<tr>
<td>b) value added locally over 50%</td>
<td>exemption</td>
<td>exemption</td>
<td>exemption</td>
<td>exemption</td>
<td>exemption</td>
<td>exemption</td>
<td>exemption</td>
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<td></td>
<td>tax holiday period</td>
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### Other Territories

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<tr>
<th>Under the Existing Legislations in:</th>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>Jama</strong></td>
<td><strong>Guy.</strong></td>
</tr>
<tr>
<td>6-year</td>
<td>10-year</td>
</tr>
<tr>
<td>Either</td>
<td>complete exemption</td>
</tr>
<tr>
<td>tax within</td>
<td>3 years of production</td>
</tr>
<tr>
<td>60% exemption</td>
<td>60% exemption</td>
</tr>
<tr>
<td>8-year period</td>
<td>8-year period</td>
</tr>
</tbody>
</table>

**a) 6-year**
- Either 5-year complete exemption + 10-year partial exemption
- 10-year complete exemption from the date of production
- 41.5% exemption in the 6th year
- 33 1/3% exemption in the 7th year
- Deferment of depreciation deductions
- Tax holiday

**b) 6-year**
- Either 7-year complete exemption + 10-year partial exemption
- 7-year complete exemption beginning 6th year of production
- 62.5% exemption in the 8th year
- 66 2/3% exemption in the 9th year
- Deferment of depreciation deductions
- Tax holiday

**a) 3-year**
- Either 3-year complete exemption + 10-year partial exemption
- 10-year complete exemption from the date of production
- 41.5% exemption in the 6th year
- 33 1/3% exemption in the 7th year
- Deferment of depreciation deductions
- Tax holiday

**b) 3-year**
- Either 3-year complete exemption + 10-year partial exemption
- 10-year complete exemption from the date of production
- 41.5% exemption in the 6th year
- 33 1/3% exemption in the 7th year
- Deferment of depreciation deductions
- Tax holiday