Export Taxes on Rubber in Malaya—A Survey of Post-War Development

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EXPORT TAXES ON RUBBER IN MALAYA — A SURVEY OF POST-WAR DEVELOPMENT

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The post-War development of export taxes on rubber in Malaya can be divided into two distinct periods, namely the pre-Korean War period and the post-Korean War period. Since the Korean War boom, the rates of taxation on rubber exports in Malaya have been much higher. At the same time, the export tax structure has become wider in scope and more complicated.

DEVELOPMENT BEFORE THE KOREAN WAR

The pre-Korean War period can again be conveniently divided into three distinct phases. The first phase dated from the time when export duties were reintroduced in Malaya in December, 1945, soon after the re-occupation to March, 1946. During this period, the Federated Malay States pre-War export tax rates, including the tax on rubber, were made applicable throughout Malaya. But the War Tax on rubber exports at 5% ad valorem was not re-imposed since the War was over. The Federated Malay States rubber export duties were the lowest in pre-War Malaya compared to other states that had export taxes on rubber, and are given below: 3

<table>
<thead>
<tr>
<th>Price per pound (in cents)</th>
<th>Duty</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under 20</td>
<td>1%</td>
</tr>
<tr>
<td>20 to under 22</td>
<td>1 1/2%</td>
</tr>
<tr>
<td>22 to 24</td>
<td>1 1/2%</td>
</tr>
<tr>
<td>24 to 26</td>
<td>2%</td>
</tr>
<tr>
<td>26 to 28</td>
<td>2 1/2%</td>
</tr>
<tr>
<td>28 to 30</td>
<td>3%</td>
</tr>
<tr>
<td>30 and above</td>
<td>3 1/2%</td>
</tr>
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The second phase was between March 1946 and February 1947. During this period specific taxes took the place of the former sliding scale duties. The specific

1. Malaya refers to the territories comprising the present Federation of Malaya. Singapore is not included, as there has been no taxation on exports in Singapore, a 'free' port.

2. The duty was imposed under The Customs Duties Order made under the B.M.A. Customs Proclamation, (Proclamation No. 30) and published in B.M.A. Gazette Notification (G.N.) No. 100 of 1945.

3. The Straits Settlements had no taxation on exports. Each of the five Unfederated Malay States had a separate customs tariff structure. For the various export duties in force in all the states, see Malayan Statistics (I & E 3), July, 1941, (Singapore, Government Printer), Appendix XX, pp. 478-482. For the 1936 F.M.S. export tax on rubber, see F.M.S.G.N. No. 4005 of 1936. There was no change in the export duty on rubber in the F.M.S. since 1936.

4. For further information on these specific taxes, see The Customs Duties (No. 3) Order published in B.M.A.G.N. No. 340 of 1946 and The Customs Duties (No. 4) Order, published in Malayan Union (M.N.) G.N. 3088 of 1946.
duty was 4 cents per pound which in fact amounted to a great increase in the export tax compared with the previous graduated rates. At 20 cents per pound, for example, the old rate would be 0.3 cents, whereas the new rate was 4 cents. At the other end of the scale when the price was 35 cents per pound, the old duty would be 1.5167 cents and the new rate of 4 cents per pound was about 166% higher. This high rate of duty was reduced to 2.75 cents per pound with effect from November, 1946. Of the 2.75 cents, 0.25 cent was "credited as cess to the Rubber Fund" for research purpose. The actual duty was therefore only 2.5 cents per pound. It remained at this rate for only about 4 months.

Between February, 1947 and 31st December, 1950 a flat ad valorem rate of 5% was imposed, distinct from the sliding scale duty in the first phase and the specific rates in the second phase. The research cess of 0.25 cents per pound remained unaffected. This 5% flat rate existed for nearly four years up to the end of 1950. Comparing with the old specific rate of 2.5 cents per pound the new tax of 5% ad valorem would be lower if the price of rubber were below 50 cents per pound. For nearly three years between February, 1947 to the end of 1959, the gazetted price of rubber for the purpose of calculating the export duty was under 50 cents per pound. Thus, for nearly three years the rate of duty payable was less than it would have been under the former specific rate of 2.5 cents per pound.

During 1950, except for three isolated instances at the beginning of the year the price rose steadily and rapidly to $2.15 1/2 per pound in the second week of October, and fell slightly to $1.89 in the last week of the year. This sudden rise in price was due to the outbreak of the Korean War which resulted in an exceptionally vigorous demand for rubber, particularly by the United States for stockpiling purposes. Throughout 1950, the export tax remained at 5% ad valorem, despite the large price increases particularly in the second half of the year.

On 12th September, 1950 when the rubber price reached a high mark of about $1.40 per pound, the Government of the Federation of Malaya through its Acting Financial Secretary wrote to the various Malayan rubber associations inviting their views on a Government's proposal to increase the rates of export taxation on rubber. The proposal leaked out to a local newspaper which published the Government's letter "almost in extenso". The Government proposed that at a price of $1.50 per pound, the tax would be 43.5 cents, which was 29% of the price, whereas the existing tax rate was only 5%. The proposed change was so revolutionary that it was made to the rubber associations with the specific assurance that their views would not be treated lightly, and would be submitted

7. For the purpose of computing export duty, prices of rubber are published weekly in the Government Gazette. All rubber prices unless otherwise stated refer to gazetted prices.
9. Ibid, speech by Mr. Tan Siew Sin, p. 424. $1.50 per pound was the approximate price prevailing at the time of the Legislative Council debate on 28th February, 1950.
to the Secretary of State for his consideration. Obviously any major change was to be taken only with the blessing of Whitehall. In fact there are reasons to believe that the move to increase the export duty had originated from Whitehall, and not from the Federal Government.10

Rumours ran wild in the Federation and in Singapore over the tax proposal. The rubber market came almost to a standstill. Buyers in the Federation were reported to pay 20 cents per pound below the current market price in anticipation of the tax increase. The Government came out immediately with the following press statement: "It is intended to make no change in the export duty of rubber until all sections of the industry have been consulted and have had an opportunity to state their views."11

This assurance did not quieten the market. In the adjournment speeches of the Legislative Council on 28th September, 1950, members having vested interests in the rubber industry rose up one after another to attack the Government on the manner in which the tax proposal was handled, giving rise to confusion in the rubber market, the exceedingly high rates of taxation proposed, and the lack of powers of the Federal legislature to debate and decide on the issue.

The Acting Financial Secretary then promised that no new rate of export duty would be imposed before 1st December, 1950, and that at least two weeks' notice would be given before the changes in export duty would become effective. These assurances were greeted with applause by the legislature.

In fact the tax changes became effective only from 1st January, 1951, though the price of rubber had already taken a speedy upward turn in the second quarter of 1950. The export tax machinery, for various reasons, could not be put quickly enough into action. This resulted in a considerable loss in windfall tax revenue. It also resulted in a delay in mopping up the excessive money supply generated at that time. This delay made the fight against inflationary pressures in Malaya at a later date more difficult.12

Another important point is that the proposed taxes had the effect of making the unofficial members of the Legislative Council realise unequivocally their "impotence" over such an important matter as the revision of import and export taxes. Under the British Military Administration wide powers on customs matters including the imposition of tariffs were placed in the hands of the Deputy Chief Civil Affairs Officer.13 These powers were transferred to the Chief Secretary when the Malayan Union was set up,14 and when the Federation was set up later,

10. Ibid, speech by Mr. Khoo Teik Ee, p. 423. It is to be noted that under the Constitution of the Federation of Malaya, only the Federal Government could impose import or export duties. This is also the position at present.

11. Ibid, speech by Mr. Khoo Teik Ee, p. 424.

12. For the development of inflationary pressures in Malaya and the measures taken by the Government to control the situation see, for example, Proceedings of the Federal Legislative Council (Fourth Session), February, 1951 to February, 1952 (Kuala Lumpur, Government Printer), speeches made by various speakers on 25th April 1951, 26th April 1951, 11th July 1951, 12th July 1951, 21st November 1951 and 30th January 1952, pp. 7-442.


14. For the transfer of powers to the Chief Secretary, see Section 4 of the Interpretation and Transfer of Powers (Proclamation) Ordinance, 1948.

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these same powers were delegated by the Chief Secretary to the Financial Secretary. He, like his predecessors, was under no legal obligation to report to the legislature on any customs order made.

Mr. Tan Siew Sin, the present Minister of Finance, then an unofficial member of the Legislative Council, was most outspoken on the necessity for the Federal legislative to be consulted on the revision of import and export duties, and he was supported by other unofficial members.

Five months later, in April, 1951, the Government introduced a bill making it obligatory for the Financial Secretary when making a customs order to lay that order for the confirmation of the Legislative Council. Unless the Council "by an affirmative resolution within ten days of its being so laid, approves that order, then the order will cease to have effect and not only would it not operate any further, but any money paid under it will be refunded."

DEVELOPMENT SINCE THE KOREAN WAR BOOM

There have been many important changes made in the system of taxation on rubber export since the Korean War boom in Malaya. These changes can be conveniently grouped under two headings: changes made before the publication of the Mudie Mission Report, and changes made after Government had considered the Report of the Mission.

(a) The pre-Mudie Mission Period

The first major change in the export duty on rubber after the Korean War was made by the Customs Duties (No. 41) Order which came into force on 1st January, 1951. Under this new Order, the export tax for the price of rubber at or below 60 cents per pound remained at 5% ad valorem. Above 60 cents per pound the tax was on a graduated scale rising progressively according to the formula \( (1.55P - 63)/10 \), \( P \) being the price of rubber in cents per pound. Thus under the old rate, if the price of rubber was $1.00 per pound, the export duty was 5 cents. Under the new rate, it was 9.2 cents. The new export tax was referred to in the Order as Schedule I duty.

The order also contained another major change in the levy on rubber export. This was the imposition of a cess, for the first time in the history of the rubber industry in Malaya, intended to assist the replanting of rubber trees. The cess was called Schedule II cess. At or below 60 cents per pound, there was no tax under Schedule II. Above 60 cents per pound, the tax was on a sliding scale,

18. The Mission consisted of the Chairman, Sir Francis Mudie, formerly Home Member of the Viceroy's Executive Council in India and latterly Head of the British Economic Mission to Yugoslavia, and two other members. Their main terms of reference were the examination of the taxation of the rubber industry and the maintenance of existing capital in the industry. They arrived in Malaya in June, 1954 and presented their Report in August, 1954. This was laid before the Legislative Council on 6th October as Legislative Council Paper No. 58 of 1954.
but the rates were much lower than those under Schedule I. The formula for calculating the Schedule II cess, applicable when the price was above 60 cents per pound was \((0.45P - 27)/10\), where \(P\) was the price of rubber in cents per pound.

There was also a research cess imposed under the order known as the Schedule III cess. Under this a flat rate of 0.50 cent per pound was payable to the Malayan Rubber Fund. This research cess was not new and was a continuation of past practice. The order also made provisions for forward purchase, which need not engage our attention here. At Appendix A is a table showing the rates of duties payable under the various Schedules at different price levels under the No. 41 Customs Order.

It must be pointed out that the revolutionary changes in the tax structure embodied in the No. 41 Customs Order had never been referred to the Federal Legislature for approval or discussion. The order was made before the Customs Orders (Approval by Resolution) Bill was introduced in the Legislative Council requiring a customs order to be referred to the legislature for approval. There has, however, been full consultation between the Government and the rubber growers’ associations.

The changes have been described as revolutionary because for the first time in Malaya, the Government had considered that it was its vital responsibility to utilise its tax machinery to finance the all important replanting programme. Some doubts were expressed at the time both in respect of the wisdom of replanting and as to whether the Government should step in actively to promote replanting, though at present few would question the wisdom of Government’s help in ensuring that replanting is carried on urgently and on a large scale. It meant also the introduction for the first time of high progressive rates of taxation at price levels above 60 cents per pound. They made the tax burden of the industry doubly heavy since corporate taxes had also been introduced in Malaya after the War.

These changes also signified a radical change in the Government’s policy. It meant a deliberate pursuit of an income stabilization policy through the export tax machinery. The setting up of a stabilization fund was one of the three reasons Government gave for increasing export taxes on rubber. The other two reasons were the financing of replanting, and the collection of more revenue to meet the mounting Emergency expenditure.

One further point should be mentioned. The idea of financing a replanting programme through the imposition of a cess on rubber export did not originate from the Government as is often believed; it in fact emanated from the rubber

20. See, for example, Proceedings of the Federal Legislative Council (Fourth Session), op. cit., speech by Mr. H.H. Facer, p. 137.


22. This stabilization policy was later hotly debated in the Legislative Council. See, for example, Proceedings of the Federal Legislative Council (Fourth Session), pp. 137-134.
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industry, though in later years it was the Government that tried to push the scheme through with vigour and enthusiasm.

The Customs Duties (No. 45) Order which came into force on 1st March, 1952 contained a new Schedule IV tax of 4½ cents per pound which was levied on rubber exports when the price was more than 75 cents per pound. This tax was superimposed on the tax structure created under the previous orders.

The money collected under Schedule IV was paid into two Funds — Fund A for estates and Fund B for smallholdings. The proportion payable into each of the two Funds was based on the respective annual production of estates and smallholdings.

The two Funds are under the charge of the Replanting Board set up under the Rubber Industry (Replanting) Fund Ordinance, which came into force on 1st May, 1952. Money collected for Fund A under Schedule IV was returned unconditionally to individual estates against actual production figures submitted. Money collected for Fund B was not returned directly to individual smallholders, but grants were made to smallholders who replanted rubber trees. The grant to smallholders was then $400 per acre.

The money collected under Schedule II was paid to the same two Funds in the same proportion for estates and smallholdings as in the case of Schedule IV cess. It was however returned to individual estates against figures of actual replanting or new planting undertaken. For smallholdings proof of replanting was difficult to obtain and in their case the money was kept in Fund B together with the Schedule IV cess.

The Schedule IV cess had the full support of the smallholders' representatives on the Rubber Producers' Council. The estate owners did not voice any opposition since the money collected under the cess would be refunded to them unconditionally.

The Schedule IV cess was later revised to make it operative irrespective of the rubber price. It was feared that if the price fell below 75 cents per pound the commitments of the Replanting Board could not be adequately met. It was realized that for a replanting programme of an extensive nature, the source of finance should not be stopped abruptly unless there already existed a sufficiently large surplus fund from which the annual grants under the replanting programme could be made. Such a surplus fund did not exist. Thus, the amendment was a wise move, though it is doubtful whether at very low prices, smallholders could afford to pay this duty.

23. Ibid, p. 144, speech by Mr. Khoo Teik Ee.

24. For information on the progress of replanting rubber in Malaya before the arrival of the Mudie Mission, see The Rubber Industry (Replanting) Board, Scheme No. 2 for the Administration of Fund B, Report on Operations for the Period 1st November 1952 to 31st December 1953, Kuala Lumpur, Caxton Press Ltd.


26. The Rubber Producers' Council consists of representatives of the Rubber Growers Association, the United Planting Association of Malaya, the Malayan Estate Owners' Association, and representatives of smallholders. The Council was set up in March, 1951.

27. As a matter of interest, the original intention of the Government was that the Schedule IV cess was to operate as a replanting cess for both estates and smallholders. The strong opposition from the estate-owners caused the cess to be made applicable to smallholdings only.
EXPORT TAXES ON RUBBER IN MALAYA

When the Mudie Mission came to Malaya in 1954, the structure of export taxes in the rubber industry could be briefly summed up as follows:—

(a) There was the export duty proper or Schedule I tax of 5% *ad valorem*, if the price per pound was 60 cents and below, and above 60 cents the tax was on a progressively graduated scale.

(b) There was the Schedule II cess payable by both smallholders and estate-owners, returnable to estate-owners against actual replanting or new planting undertaken.

(c) There was the Schedule III research cess which at that time was 0.5 cent per pound.

(d) Finally there was the smallholders' replanting cess or Schedule IV cess of 4½ cents per pound payable irrespective of price.

(b) The post-Mudie Mission Period

With the tax structure at the time, the rubber industry naturally felt that it was overtaxed. This was the chief reason why the Mudie Mission was invited to Malaya. Its main terms of reference were to determine the burden of taxation shouldered by the industry, and to consider whether, with this burden, the industry could still put aside enough funds for replanting purposes.

The Mudie Mission recommended that the Schedule II cess be abolished on the grounds that the amount collected was negligible when the price was not high. In 1954 for example, the amount collected for Fund A and Fund B under Schedule II cess was only $4.30 million, whereas the amount obtained from Schedule IV cess was $57.40 million. However, it must be pointed out that when the price was high, the position would be different. In 1951, for example, when the price was exceptionally high, the amount collected under Schedule II was $49.93 million. In any case there is little doubt that the declining yield from Schedule II cess*28 must have greatly influenced the Mission to come to the conclusion that the funds from Schedule II cess "were too meagre to induce estates to replant on an adequate scale".29 This recommendation to abolish the Schedule II cess was accepted by the Federation Government.30

Another important recommendation of the Mission was the extension of the Schedule IV cess to cover estates as well.31 The representatives of estates on the Rubber Producers' Council were strongly against this on the grounds that it introduced an unnecessary and avoidable principle of compulsion on re-investment in the estate sector of the industry, and that at low price levels, the industry would not be able to put aside the 4½ cents per pound cess for replanting.32 Whatever the merits and demerits of the estate owners' arguments, in view of

28. $49.93 million in 1951, $20.94 million in 1952, $1.02 million in 1953, and $4.30 million in 1954. Figures of collections from Schedules II and IV cesses were obtained from Annual Estimates of Revenue and Expenditure of the Federation of Malaya (Kuala Lumpur, Government Printer), 1952 & 1955.


their persistent and strong opposition, the Government decided not to proceed along the lines recommended by the Mission since much importance was attached to cooperation, mutual confidence and understanding between the Government and the industry. It is interesting to recall that this recommendation of the Mission was in fact also a proposal put up by the Government in 1952 to estate-owners, but then withdrawn on their opposition.

The most important recommendation of the Mission was that at 60 cents and below 60 cents per pound, the Schedule I duty should be abolished, above 60 cents up to 78 cents, it should be reduced, and above 78 cents, the rates should be more steeply graduated. The Mission felt that at 60 cents per pound and below, the industry could not pay export duties, and at the same time put aside enough money for replanting. Above 78 cents per pound, higher rates of taxation were recommended partly as an anti-inflationary measure, and partly because there could be justification for the Government to participate in windfall gains, which should benefit the nation as well as the industry. After much discussion with the Rubber Producers' Council, which strongly opposed this recommendation, the Government in April 1955 adopted a compromise scheme, which remains almost unaltered to the present time.

The Government's scheme was as follows:—

(a) At 60 cents per pound and below 60 cents per pound, the ad valorem rate of duty was reduced from 5% to 4%, because while the Government agreed with the Mission that at such low prices, the rate of export duty, taking into account the other cesses, was high, it could not "contemplate the abolition of export duty as a regular source of revenue."

(b) Above 60 cents per pound up to 80 cents the sliding scale rates would be lowered, but not to the extent as recommended by the Mudie Mission. Above 80 cents per pound, the sliding scale rates would be raised, but also not to the extent as recommended by the Mission. At Appendix B is a table showing the various schedule rates currently in force.

(c) The Government would over eleven years give a sum of $280 million to the rubber industry to help finance the rubber replanting and new planting programmes. Of the $280 million, 60 per cent would be given to the estate sector and the balance to the smallholdings.

An advantage of the Government's scheme was that the Rubber Producers' Council was prepared to give it its support. Perhaps it would be more correct to say that between the Government's scheme and that recommended by the Mission, the Council found the former the lesser of the two evils.

34. See Taxation and Replaiting in the Rubber Industry, op. cit. pp. 9-10.
36. For an alternative scheme recommended by the Rubber Producers' Council, see Taxation and Replaiting in the Rubber Industry, op. cit. pp. 8 to 9.
In view of the vital importance of replanting on a sufficiently large scale, the Government’s scheme had the advantage that it included a guarantee to finance the replanting and new planting programme. Over the following 11 years, $168 million would be allocated to the estates, while $122 million would be available for the smallholdings, in addition to funds from the Schedule IV cess. It may however be argued that under the Mission’s scheme, the funds obtainable from Schedule IV cess would be likely to bring in about $624 million in the 11 years on the basis of the 1953 production figures. This sum when allotted to Fund A at 60% would be $374 million, which would be more than the $280 million promised by the Government for both estates and smallholdings.

Further, under its scheme, should rubber price fall below 80 cents per pound, the Government would collect less revenue from the Schedule I duty than before while bearing the burden of the bill for the replanting programme. However, if the price stayed at, say, 90 cents per pound, the Government would be able to collect an additional $230 million under the new Schedule I duty. At $1.00 per pound, the additional collection would be $443 million. The Government would thus break even with the price of rubber slightly above 90 cents per pound, and gain about $163 million over the 11 years should the price be $1.00 per pound. At Appendix C is a table showing the different estimated annual yields from the old and new Schedule I duty, and also the yields under the Mudie scheme at different price levels.

In comparison with the Mission’s scheme, the Government’s scheme was weak as an anti-inflationary measure. At $1.50 per pound, the duty payable under Schedule I was only 22.5 cents, whereas under the Mission’s proposal, it would be 42 cents. The Korean War boom experience shows that at such high prices as $1.50 per pound, there would be serious inflationary pressures in Malaya, if the high prices persisted over a period of time. Whatever the merits and demerits of the present currency system, the burden of stabilizing the fluctuating Malayan economy has to be borne primarily by fiscal measures. A surplus budget based on a steeply graduated export tax structure which aims at mopping up the excessive demand appears to be the most practicable method available in Malaya.

The Government however was not unaware of this, and it therefore introduced an anti-inflationary cess operative only when the price exceeded $1.00 per pound. This cess would be returned to the estate sector of the industry by instalment when the price was “for eight successive weeks less than $1.00 per pound or such higher price as the Minister may determine.” In the case of the smallholders, as the returning of the cess was administratively impossible, it was therefore made payable to Fund B. Since this might unduly inflate Fund B, the Schedule IV cess could then be reduced to 2 cents per pound.

37. The funds collected from Schedule IV amounted to $56.7 million in 1953. This would add up to about $624 million in 11 years.

38. See Appendix C. Thus at 90 cents per pound for the price of rubber, the increase of the new duty over the old was about $20.9 million per year. Over 11 years the total increase would be $230 million.


40. The Schedule IV cess was in fact reduced to 2 cents per pound for more than three years between September 1956 and December 1959. See The Rubber Industry (Replanting) Fund (Cess) Order, 1956, Federation of Malaya L.N. 247/1956.