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Mr. Whitaker and Industry: Setting the Record Straight*

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I INTRODUCTION

After 16 years of unbroken Fianna Fáil rule, the first four of the five general elections of the period 1948-1963 saw sitting governments unseated. Economic policy pivoted: protectionism was abandoned; foreign direct investment welcomed and an application for membership was made to the EEC. Whitaker's *Economic Development* appeared in 1958. Lemass took over from de Valera as Taoiseach in 1959. The 'long 1950s' remains of enduring fascination to Irish historians.

Conventional wisdom accords the bulk of the credit for the turnaround in policy to Seán Lemass, Minister for Industry and Commerce in most Fianna Fáil governments since 1932 and Taoiseach from 1959 to 1966, and T. K. Whitaker, Secretary of the Department of Finance from 1956 to 1969. This arguably downplays the importance of the intensified electoral competition of the time, and undervalues the achievements of the second inter-party government, which introduced export profits tax relief – the genesis of Ireland's low corporation tax regime – in 1956. Fine Gael and Labour had long advocated liberalising the restrictions on foreign ownership of industry before

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Fianna Fáil finally yielded (Bew and Patterson, 1982, McCarthy, 1990). Whitaker's particular role in the reform process is – to our minds – seriously misrepresented by Walsh and Whelan (2010) in a recent paper in this journal. The present note assesses their main assertions in this regard in the light of information available from the archival records.

II THE WALSH AND WHELAN THESIS

Walsh and Whelan (2010) refer throughout to "Whitaker's export-oriented industrial policy", which was based, they argue, on the development of linkages with new and largely foreign-owned industry attracted by "export tax relief and capital grants". His thinking on linkages was supposedly based on the advice of Louden Ryan, a TCD economist whom "Whitaker appointed (to) a Capital Investment Advisory Committee" established by the government in 1956. They assert, furthermore, that Whitaker "… manages the drive towards free trade in a controlled and phased manner… The phased diminution of tariffs and the gradual introduction of exporting incentives were implemented to minimise the political instability of implementing free trade".

Barry (2009a, 2010) has written previously of the process of 'juggernaut' reforms to which the introduction of export profits tax relief (EPTR) by the second inter-party government gave rise: "While EPTR did not directly threaten established (protectionist) interests, it led to a considerable strengthening of the export lobby. This increased the pressure for further liberalisation". Walsh and Whelan suggest that this was planned by Whitaker: "Politically, Whitaker realised that in order to navigate the move to free trade, the introduction of export tax incentives (yielding positive gains) should be embedded first. Then, once the benefits from these reforms have taken hold in the economy, the more painful reforms of tariff reductions should be implemented, but in a phased way". As past of this strategy, they claim, "Whitaker backed green field exporting companies based outside Dublin to deliver prosperity for Ireland, even though the jobs and power were on the side of the traditional, heavily unionised and highly protected industries in the greater Dublin area".

III THE HISTORICAL RECORD

Tariff Reductions as an Element of Broader Industrial Strategy?

Whitaker's 1956 paper to the Statistical and Social Inquiry Society is generally seen as the seminal document setting out his economic philosophy on the eve of his appointment as Secretary of the Department of Finance. "While the opportunity for industrial expansion afforded even by our limited home market has not yet been fully availed of", the paper argues, "… it would be unduly restrictive to concentrate attention on the home market alone. It is much more important that industrialists, whether native or foreign, should be induced to establish industries here capable of competing in export markets". This is the only reference to foreign investment in the document, and Whitaker appears to count himself among the many for whom "… an industrial expansion based mainly on agricultural raw materials (has) seemed the most sensible form of development in our circumstances, as being more natural, more secure and of greater assistance to our balance of payments". The broader strategy on which he focuses here consists of supply-side measures to supplement liberalisation: education and technical training, reduced taxation, tackling of restrictive work practices, provision of utilities including power supplies and transport services, and a closer alignment of pay to productivity.

The later civil service debates on trade liberalisation to which Walsh and Whelan refer took place between October 1959 and January 1960 and largely pitched the Department of Finance (in the person of T.K. Whitaker) against the Department of Industry and Commerce (in the person of its secretary, J.C.B. MacCarthy), with occasional interventions from Agriculture, Foreign Affairs, the Department of the Taoiseach and others. The memos were drawn together and published by T.K. Whitaker in 2006 under the title *Protection or Free Trade – The Final Battle*. As Whitaker explains, this "semi-official" correspondence was intended especially for the eyes of Seán Lemass, who had assumed office as Taoiseach only a few months previously.

The debates were triggered by the need to decide whether or not to apply for membership of EFTA, the seven-country free trade area established in 1960 in response to the formation of the EEC, and in which the UK was the dominant economy. Membership would have entailed reducing industrial protection and exposing the domestic market to further competition. Whitaker believed that this would be beneficial and would improve Irish industrial export prospects. Industry and Commerce argued to the contrary that the effects of membership would be catastrophic.

Whitaker is ultimately swayed not by Industry and Commerce but by a memo from the Department of Agriculture which argues that EFTA membership would probably require Britain to extend equivalent agricultural access to other EFTA member states and that Irish interests would therefore be best served by seeking a Free Trade Area arrangement with Britain alone (Barry, 2009b).

Whitaker continues to emphasise the 'pure' case for trade liberalisation however. The Department of Finance memo of December 14, 1959 entitled

Reasons for Reducing Protection argues, inter alia, that:

- The inadequacy of protectionism as a remedy for the problems of unemployment and emigration had become obvious.
- Action was becoming more urgent as competition in export markets would grow as other European countries achieved greater specialisation, higher output and lower costs through tariff reductions and freer trade.
- As long as protection was maintained, there would be no compulsion to increase quality and efficiency.
- High costs in protected industries were being transmitted to other sectors. This reduced competitiveness more generally, and the consequent lowering of living standards vis-à-vis Britain encouraged emigration.

There is no evidence here of the strategising suggested by Walsh and Whelan. The argument is for immediate across-the-board tariff cuts.[1]

Export Profits Tax Relief

Export Profits Tax Relief was announced by Taoiseach John A. Costello, leader of the second inter-party government, in a speech to an inter-party meeting on 5 October 1956 and included in the Finance (Miscellaneous Provisions) Bill which was passed by the Oireachtas shortly thereafter.[2]

The proposal for export profits tax relief had first surfaced in a 1945 Foreign Trade (Development) Bill prepared by the Department of Industry and Commerce. This was ultimately withdrawn in the face of opposition from the Department of Finance, which deemed the proposals to be "objectionable in principle". Were public funds to be allocated to stimulate the export trade, Finance agued, "… this assistance should take the form either of a direct subsidy which can be effectively measured, or of loans and grants analogous to those in operation in Northern Ireland".[3]

The Department of Finance and the Revenue Commissioners repeated these objections each time the proposal resurfaced, as it did on various

[1] The fact that the first Irish tariff cuts were implemented only in 1963 raises the question as to why they were delayed. Daly (1992) has characterised the 1938 Anglo-Irish Trade Agreement which ended the economic war with Britain as having established a new equilibrium that balanced the forces of export-oriented agriculture and protected industry. This equilibrium was shattered by the changes in the external environment that the formation of EFTA and the EEC represented. Barry (2009b) argues that the tariff cuts were implemented only once it had become clear to dominant agriculture interests that this was required if full rather than associate membership of the EEC was to be achieved. Full membership was required if access was to be had to the vast subsidy programmes of the emerging Common Agricultural Policy.

[2] National Archives of Ireland (NAI), Department of the Taoiseach: Taois/S/14818A,B,C.

[3] NAI, Taois/S13765A.

occasions over the following years (Barry, 2011). In March 1955, the Minister for Industry and Commerce requested Finance to revisit the matter. The request was passed to the Revenue Commissioners who replied, in a memo to Finance of July 31, 1956, that "… the fair distribution of the income tax charge is an essential element of the tax system" and that "… there are activities other than exports that are just as important even from the point of view of the balance of payments". On September 20, Whitaker wrote to his minister that such relief would be contrary to Irish obligations to the OEEC. Furthermore, "I have always felt that it is production which should be aided rather than exports" and the proposal, if implemented, would further postpone the day "… when we can bring farming profits within the income tax net". The Minister of Finance endorsed these points in his memo to government advocating that the proposal be rejected.[4] On this occasion however, Whitaker and his Department were overruled by the Taoiseach and Export Profits Tax Relief was introduced.[5]

The 50 per cent tax remission introduced by the inter-party government was expanded to 100 per cent by Fianna Fáil shortly after the latter's return to power in 1957. In the face of this, Whitaker argued continuously that double taxation relief was to be preferred from Ireland's point of view. On the opening of a Danish-run fish farm in Ireland in 1958, he wrote to the Minister for Lands that "… nothing we can do will relieve the Danes of *all* tax on their income from the trout farm. A double taxation agreement would secure that they paid only *one* tax – and that tax to the *Irish* Exchequer. The exports tax concession will secure that they pay one tax – but to the *Danish* Exchequer."[6] He asserted later that "Department of Finance concerns regarding the policy remain, and remain the same."[7]

Decentralisation

Walsh and Whelan write that "Whitaker backed green field exporting companies based outside Dublin to deliver prosperity for Ireland even though the jobs and power were on the side of the traditional, heavily unionised and highly protected industries in the greater Dublin area."

Garret FitzGerald, in a 1959 paper to which the title of the present note pays homage, directly contradicts this. He writes that "… the policy of encouraging decentralisation of industry by means of special grants finds little support in *Economic Development*. Mr Whitaker remarks that with virtually

[4] NAI, Department of Finance, Fin F200/10/56.
[5] Ibid.
[6] NAI, Fin/F049/012/58.
[7] NAI, Fin/F049/005/58-F049/013/58.

the whole country undeveloped it seems wasteful to subsidise remote areas especially, by providing more extensive grants for industrial development in these areas than in other better favoured parts of the country".

Chapter 24, paragraph 31 (c) of *Economic Development* states explicitly that "… a realistic appraisal of development prospects indicates that, apart from exceptional cases, industries must be at or near the larger centres of population. Special subsidisation of remote areas by more extensive grants for industrial development is wasteful and retards progress in areas better situated". Whitaker's recommendation was not incorporated in the government's *First Programme for Economic Development* (1958). McCarthy (1990, p. 62) suggests that "… the impetus for this decision doubtless was Fianna Fáil's desire not to alienate its traditional support in rural areas".

Decentralisation was supported by the Department of Industry and Commerce, of which Lemass was minister at the time. The Department argued that the Whitaker proposal "… would nullify the objective of the Undeveloped Areas Act", though it was prepared to "… envisage the possibility of larger grants outside the undeveloped areas than at present, particularly where a new industry might otherwise be lost to the country".[8]

Linkages and "Whitaker's Industrial Policy"

Walsh and Whelan assert that Whitaker appointed academic economic advisors, including Louden Ryan, to the Capital Investment Advisory Committee established by government in 1956. Lee (1989, p. 343), drawing on Fanning (1979, p. 507), provides a very different account, writing that "… the Capital Investment Advisory Committee, established in late 1956, came, it would appear, as a nasty surprise to Finance. This seems to have been established by the cabinet, and to have had the bulk of its membership nominated without reference to Finance. Neither the chairman, John Leydon, who had resigned as Secretary of Industry and Commerce in 1956, nor the two young economists on the committee, Patrick Lynch and Louden Ryan, were likely to display an excessive reverence for the traditional Finance approach".

Walsh and Whelan extrapolate from the fact that Whitaker and Ryan interacted across various committees and societies to suggest that "Whitaker shaped policy on the advice of the economist Louden Ryan, who in turn based his concept of the importance of industry linkages in Ireland's development on the theoretical framework put forth by (Albert) Hirschman".

Industrial policy was not however under Whitaker's remit, but under that of the Department of Industry and Commerce with which Finance had a

[8] NAI, Fin/06/10/57; Memo for Government, *Economic Development* 4 July 1958.

fraught relationship. The two camps remained at loggerheads on many issues, including the Control of Manufactures Acts of 1932 and 1934 which placed restrictions on foreign ownership of industry (Daly, 1984). As early as 1955, Finance had favoured repeal rather than amendment of the acts.[9] In the face of Industry and Commerce objections however, the acts were not amended even when export profits tax relief was introduced (Barry, 2011). They were partly amended in 1958, though the OEEC report on Ireland of that year remarks that "… despite the recent relaxation of restrictions, the conditions governing foreign investment in Ireland are still more restrictive than would seem appropriate in the light of Ireland's overriding need for new investment and enterprise".[10] They were completely repealed only by an act of 1964.

The Department of Industry and Commerce was among the least enthusiastic supporters of the Whitaker initiative that led ultimately to *Economic Development*. McCarthy (1990, p. 47) notes that "Whitaker's task-force consulted the Department of Industry and Commerce only sporadically". Although the National Archives contain a list of queries submitted to Industry and Commerce over the course of the preparation of *Economic Developme*nt, none relate to matters that remained contentious between the two departments, including the merger of the industrial promotion agencies, the ending of preferential regional grants for new industries, and planned capital investments in steel, ship-building and a nitrogenous fertiliser plant.[11]

The sections on industry in the government *First Programme* involved significant compromises between the views expressed in *Economic Development* and those held by Industry and Commerce. The original draft of the section headed Foreign Participation opened with a statement that "… the Government welcome foreign participation in the drive for expansion in industry where it is likely to result in new industrial activity or an increase in our industrial exports". When these words appear in the *Programme for Economic Expansion*, they are preceded by a statement reiterating the government's commitment to fostering Irish-owned industry: "… there are substantial advantages in the development of industry under Irish ownership and control. While this development will be fostered in every way, the Government welcome foreign participation …"[12]

Industry and Commerce also succeeded in securing the removal of a draft paragraph which would have ended their involvement in industrial promotion

[9] NAI, Taois/S15735A.
[10] NAI, Taois/S16446.
[11] NAI, Fin 2001/3/1.
[12] NAI, Fin 2001/3/5 inter-departmental committee, *Programme for Economic Expansion*, para. 96.

or the awarding of grants. The recommendation made in *Economic Development* for the merger of the IDA and An Foras Tionscail was also rejected; the *Programme for Economic Expansion* made the IDA responsible for promotion, while grants awards would be the responsibility of An Foras Tionscail.[13]

Early drafts of *Economic Development* had also called for consultation with the World Bank before any decisions were taken to proceed with two projects supported by the Department of Industry and Commerce: a nitrogenous fertiliser plant and a major expansion of the state-owned Irish Steel plant in Cork harbour.[14] Industry and Commerce's response to these recommendations was uncompromisingly negative and the proposals for World Bank involvement did not make it into the government Programme.[15]

It is clearly ahistorical therefore to speak of "Whitaker's industrial policy". Industrial policy was clearly under the control of Industry and Commerce. It had successfully pushed through the export profits tax relief scheme to which Whitaker and Finance were opposed, and while it had, as early as 1950, recognised that granting the concession might induce export-oriented foreign industry to establish in Ireland, it had resisted complete repeal of the Control of Manufactures Acts, since this "… would permit of the unfettered investment of outside capital in unsuitable as well as suitable cases".[16]

And what, finally, of the question of linkages, which Walsh and Whelan claim to have been "… a key contributor to the success of Irish exporting"? Their claim is based on a 2007 paper which they co-authored and which examines the importance of linkages in Irish manufacturing over the period 1972 to 2003. This is substantially later than the historical epoch with which we – and their 2010 paper – are concerned. The nature of the FDI attracted to Ireland in the later period would, furthermore, have been influenced by EU accession.

The National Economic and Social Council in 1980 published a report by Eoin O'Malley entitled *Industrial Policy and Development: A Survey of Literature from the Early 1960s*. This examines, among other issues, the question of linkage development for the earlier period. The findings from

[13] NAI, Fin 2001/3/5; *Programme for Economic Expansion*, para. 107.

[14] *Economic Development*, unpublished version, 24.36 and 24.38 (a). Daly (2002) shows that Lemass continued to pursue a self-sufficiency policy on fertilisers.

[15] NAI, S16066A 4 July 1958, *Memorandum for Government*, App. I; Summary of observations on *Economic Development*.

[16] Costello papers, UCD Archives, 1954, P190/787/(2).

this earlier literature are almost universally negative (pp. 44-51). One representative study states that with the exception of food processing, "… the linkage effects of the new industries have been limited. They have not created many opportunities for secondary investments". Another concludes that "… substantial linkage effects emanate from the food industries but the rest of the foreign sector approximates to enclave growth. Consequently, the secondary stimulus to the domestic sector from the foreign firms is small".

These earlier studies do not necessarily invalidate the backward projection of the results from the later period, as the later study presumably uses more advanced techniques. Walsh and Whelan do not present any arguments that would justify such a backward projection, however. Indeed, Ruane (1981), in a review of the NESC report, suggests that the finding of "… the absence of backward linkages between foreign investment and the rest of the economy.. is hardly surprising." Kennedy, Giblin and McHugh (1988, p. 245) concur, arguing that "… where foreign firms were engaged in transfer pricing via imported inputs to maximise the tax advantage, this would tend to discourage purchases from domestic producers".

CONCLUSIONS

Historical accuracy is clearly desirable. We have presented archival evidence that Whitaker, as Secretary of the Department of Finance, opposed the introduction of export profits tax relief (for clearly defensible reasons), that he argued for immediate across the board tariff reductions rather than advising that they be delayed until new export-oriented industry had came on stream, and that he was overruled in arguing against decentralisation of industry.

Whitaker did not play a hands-on part in the formulation of industrial strategy and we have found no evidence that his thinking was influenced by the industrial linkages concepts of Hirschman. In fact we judge this unlikely. The only related discussion in *Economic Development* is in the context of industries based on primary raw materials. Projects generating a demand for indigenous materials and services were deemed to warrant special consideration in the *Second Programme for Economic Expansion* (FitzGerald, 1968, 100). This however refers to a later period than that with which we, and Walsh and Whelan, are concerned. This programme was scheduled to run from 1964 to 1970 but was jettisoned in 1967 (Lee, 1989, p. 353). There is no evidence that linkages played an important role in Irish industrial development in the pre-EU era.

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