REPORT OF
THE ENTREPRENEURSHIP
AND INTERNATIONALISATION
SUBCOMMITTEE
ECONOMIC REVIEW COMMITTEE

13 SEPTEMBER 2002

MINISTER OF STATE
MINISTRY OF TRADE AND INDUSTRY
SINGAPORE

7 September 2002

Mr Lee Hsien Loong
Deputy Prime Minister and Minister of Finance
Chairman
Economic Review Committee

Dear Deputy Prime Minister,

In December 2001, you asked me to chair a sub-committee of the Economic Review Committee (EISC) whose terms of reference are to recommend ways to strengthen the spirit of entrepreneurship and innovation in Singapore, and to foster the growth and internationalisation of Singapore-based companies, including Government-linked companies.

I submit herewith the report of the EISC. We have had numerous meetings – subcommittee, focus groups and public forums – as well as cyber brainstorming sessions with participants at home and abroad. These participants came from a broad spectrum of our economy including business, professions, academia, labour, students and Government. This report is a considered outcome of these deliberations to build a more entrepreneurial economy with a significant external wing.

The biggest challenge here is to change the mindset of Singaporeans. This means that Singaporeans must have the instincts to sense business opportunities and take calculated risk, and have the desire to build something out of nothing. To mould a nation's culture is a tremendous and long-term effort, because these are societal behaviours that are embedded in its history.

The EISC recommendations are aimed at creating an environment that will encourage, facilitate and foster a vibrant enterprise sector in Singapore.

On behalf of the EISC members, I want to thank you for the opportunity and privilege given to us to participate in this national effort to help secure Singapore's future.

MR RAYMOND LIM
CHAIRMAN

MR TONY CHEW	MR GOH YEW LIN
MR VIKRAM KHANNA	MR NEAL KURZEJESKI
MR KWEK LENG BENG	MRS LIM HWEE HUA
MR ONG PENG TSIN	DR RON SIM CHYE HOCK
MR INDERJIT SINGH	MR TAY SIEW CHOON
MR WONG NGIT LIONG	DR WONG TAI

DEPUTY PRIME MINISTER AND
MINISTER FOR FINANCE
SINGAPORE

12 September 2002

Mr Raymond Lim
Chairman
Entrepreneurship and Internationalisation SubCommittee

Dear Raymond

Thank you for your letter of 7 Sep 2002 submitting the report from the Entrepreneurship and Internationalisation Sub Committee (EISC).

Your Sub Committee covers a critical and difficult issue. As Singapore faces fiercer global competition, we need more entrepreneurs, both to start new businesses and to take existing businesses beyond the domestic market. This is the only way to exploit emerging opportunities in the region, adapt to rapid changes in the environment, and create growth and wealth for our economy.

The EISC is right to call for a co-ordinated effort to develop entrepreneurship and internationalisation. These are complex issues involving many agencies, requiring close oversight and consistent follow through. You have developed a practical framework and proposed a comprehensive set of measures to strengthen the entrepreneurial spirit in Singapore and expand our economic space internationally. As the EISC correctly pointed out, the key challenge is to change the mindsets of Singaporeans.

The Government has already announced that it would accept several of your proposals, namely those which had been published earlier by your Government in Business Focus Group. For the rest, we will incorporate the key points of the EISC report in the ERC main report, which will be released in Jan 2003. Thereafter we intend to debate the ERC report in Parliament, where the Government will respond to its recommendations.

Finally, let me record my thanks to you, the members of the EISC and its three Focus Groups, for the effort you have put in. Implementing your recommendations will be a long term effort, but one that is vital for the next phase of Singapore's economic development.

Lee Hsien Loong
Chairman ERC

RECOMMENDATIONS REPORT OF ENTREPRENEURSHIP AND INTERNATIONALISATION SUB-COMMITTEE

Executive Summary

<u>Introduction</u>

The terms of reference for the Entrepreneurship and Internationalisation Sub-Committee (EISC) are to recommend ways to strengthen the spirit of entrepreneurship and innovation in Singapore, and to foster the growth and internationalisation of Singapore based companies, including Government-Linked Companies (GLCs).

2. Our desired outcome is to create a vibrant self-renewing and self-sustaining enterprise ecosystem that is connected to the larger global ecosystem. We cannot manufacture entrepreneurs but we can create the environment and conditions that allow, encourage and facilitate entrepreneurship. For example, our social climate should better tolerate failures, and uphold successful entrepreneurs as role models. The EISC also highlights that given the constraints of a small domestic economy, internationalisation and entrepreneurship are closely intertwined.

3. The EISC's recommendations do not constitute a blue print cast in stone. Instead, they kick off the start of an iterative process. Not all of the recommendations will work out as intended, but the EISC hopes that the Government will be entrepreneurial in trying out new approaches. A self-renewing and self-sustaining enterprise ecosystem in Singapore will not be generated overnight, and the EISC hopes that Government will continue the debate and discussion so that new ideas can continually surface.

<u>Framework of Recommendations - 6 Cs: Culture, Capabilities, Conditions, Connections, Capital and Catalysts</u>

4. The EISC believes there are 6 essential elements that need to be developed and sustained in a vibrant enterprise ecosystem.

(i) Culture

It is often debated whether entrepreneurs are born or made. The EISC does not have the answer but is of the view that there should be no lack of effort to prepare our young to be entrepreneurs. Entrepreneurship is not a textbook course and is best learnt from real world, hands on experience. EISC recommends creating the opportunities for our young to develop strong entrepreneurial instincts and understanding. The suggested approach is to provide all students at different levels, as well as working executives the opportunity to learn about enterprise and gain early exposure to business concepts.

(ii) Capabilities

Enterprise capabilities can be developed at both the individual and industry level. At the individual level, greater flexibility should be injected to allow freer movement of talent between the private and public sector. We should undertake a serious effort to attract global entrepreneurial talent to Singapore, as well as to tap local talent. At the industry level, there is scope to foster greater collaboration between enterprises to leverage each others' strengths to venture abroad.

(iii) Conditions

A. Regulatory Landscape

Collectively, regulations can impose a significant burden on businesses and create barriers to new businesses entering the market. The EISC recommends that Government adopt a structured, institutionalised and coordinated programme to cut public sector red tape. Also, the Government should take enterprise-friendly approaches to economic management, industry regulation, and procurement.

B. Government's Role in Business

Singapore has entered into a phase of development where the market functions well in allocating most resources and it is private enterprise and not Government that is best able to exploit evolving market trends and technologies. The EISC suggests some principles and approaches for Government's involvement in the private sector to help develop conditions for a more entrepreneurial economy, and the strategies ahead for GLCs, with a strong emphasis on growing our external wing. The Government's participation in the economy has certain strengths and these should be harnessed to help Singapore-based enterprises globalise.

(iv) Connections

Singapore has done well to develop the hard infrastructure to establish Singapore's global connectivity. It is important that companies whether local or foreign continue to treat Singapore as an integral part of their larger global operation. The EISC feels that much can be improved in terms of soft infrastructure to connect people and markets and recommends outward oriented policies to forge strong linkages between foreign markets and our home base.

(v) Capital

There are currently several gaps in enterprise financing. Most are found in equity financing for start-up enterprises and debt financing for emerging enterprises, that are mainly due to the financial institutions' traditional reliance on asset-based financing and lack of domain knowledge of various industries. The EISC therefore recommends that mechanisms be put in place to encourage more private sector financing of enterprises at start-up, growth and internationalisation phases, and for Government to implement broad-based measures to free up capital tied in the Central Provident Fund (CPF) and Housing Development Board (HDB) properties.

(vi) Catalysts

Government has been using incentives to attract Multinational Companies (MNCs) to invest in Singapore and drive our economic growth. To develop another key driver for Singapore's growth, it is necessary to encourage enterprise and wealth creation. The EISC therefore recommends a package of incentives and changes to tax regulations to channel more capital towards enterprise.

Single Agency to Co-ordinate Efforts

5. The EISC recommends that the Government designates a single agency to co-ordinate and drive efforts to develop entrepreneurship and internationalisation. It should be headed by an individual who has the authority to effect the necessary changes to achieving a vibrant, entrepreneurial economy.

Encourage giving back

6. Greater entrepreneurship and internationalisation will likely lead to a wider income gap. To sustain this drive, we need to give greater visibility to philanthropy, and encourage successful entrepreneurs to give back to society.

Summary of Recommendations

Culture
1. Develop Entrepreneurship education as a non-examinable, co-curricular enrichment activity in schools
2. Source for a broad range of programmes at student and adult level
3. Incorporate business projects in school curriculum
4. Include entrepreneurship education in the assessment of school rankings
5. Improve outreach by delivering such programmes through grassroots organisations such as the National Youth Council and Community Development Councils
6. Set up a non-profit Centre to promote programmes
7. Develop a world class Entrepreneurship programme at the tertiary level
8. Adopt management policies in our universities to encourage commercialisation of Intellectual Property (IP)
9. Increase Capability of Executives and Professionals to Manage International Operations
Capabilities
Individual level
1. Allow private public sector co-sponsorship so that scholars can discharge their bond in Singapore-based companies
2. Expose scholars to risk taking and enterprise by allowing first two years of bond to be served in start-up or SME
3. Check against rapid increase of government scholarships and encourage government agencies to source for talent in the market place
4. Attract Global Entrepreneurial Executives to Singapore
Industry level
1. Foster the development of industry clusters when venturing overseas
2. Raise the profile of Local Industry Upgrading Programme and expand it to promote globalisation
Conditions
Regulatory Landscape
1. Conduct a comprehensive licence-by-licence review
2. Impose a sunset rule on all licences
3. Set up a high-level private-public sector panel to review the licences
4. Reset all fees and charges to reflect cost recovery
5. Ensure adequate budget for self-financing agencies which volunteer to reduce their fees
6. Outsource licensing functions to the private sector through competitive tender
7. Institutionalise the Pro-Enterprise Panel
Government in Business:
1. Enact a generic competition law
2. GLCs established and maintained only for strategic purposes such as to manage critical resources, achieve public policy objectives, or develop new growth engines
3. Ensure that GLCs are commercially run and eschew national service by GLCs
4. Review constantly the stable of GLCs and divest non-strategic ones
5. Encourage a culture of partnership between GLCs, MNCs, SMEs and other companies in the private sector
6. Temasek Holdings (TH) to focus their GLCs to internationalising their core businesses
7. TH to explore various ways of divestment such as management and leveraged buyouts

8.	TH to constantly review its GLCs to rationalise, consolidate or divest
9.	Attract world class talent into GLCs
10.	TH to limit investment in new businesses to those with potential to internationalise
11.	Ministries and Statutory Boards must not set up enterprises to provide services that the private sector can provide
12.	M&SBs must not corporatise or privatise regulatory functions
13.	Statutory Boards(SBs) to consciously divest enterprises with proactive plans for private sector to take over
14.	Conduct mandatory periodic housekeeping of enterprises set up by Ministries and Statutory Boards
15.	Avoid allegations of conflict of interest by ensuring the enterprises do not utilise the name of SBs and that their board of directors is independent
16.	No best-of-both-worlds deals where the enterprises divested by Ministries and Statutory Boards enjoy a moratorium whilst competing in the market
17.	Outsource more Government functions to the private sector
18.	Allow suppliers to retain IP arising from Government projects
19.	Government to provide test beds for SMEs' products and services whilst maintaining principles of openness, non-discrimination and value for money
Connections	
1.	Position IE Singapore as the champion of our internationalisation effort
2.	Focus IE Singapore's efforts on certain industry clusters and pioneer enterprises
3.	Grant pioneer status to most promising enterprises, which will be selected by a private sector panel
4.	Devise simple and effective performance indicators for IE Singapore
5.	Institutionalise the Singapore Overseas Network initiated by the ERC
6.	Relax criteria for valued employees of Singapore-based enterprises to obtain Permanent Resident status
7.	Take a holistic approach in developing a global brand name for Singapore
8.	Establish a network of Double Taxation Agreements
9.	Continue to push ahead with Free Trade Agreements and establish a robust industry consultation process
Capital	
1.	Support and facilitate the formation of a private equity exchange
2.	Allow losses from investments in qualified start-ups to be tax-deductible
3.	Implement an equity financing scheme equivalent to the Start-ups Enterprise Development Scheme to support broad based enterprises
4.	Encourage cash-flow financing
5.	Encourage financing using intellectual property as collateral by waiving for 5 years taxes on profits arising from such financing
6.	Study feasibility of a Technology Credit Guarantee Fund to facilitate access to bank loans
7.	Review lending rates and criteria for the Regionalisation Finance Scheme to ensure it is relevant
8.	Implement hybrid debt-equity financing scheme to support emerging enterprises to grow, expand or internationalise, either organically or through acquisition
9.	Open up government financing options through other financial instruments
10.	Free up CPF that is above a pre-determined threshold sufficient to meet the basic retirement needs of members
11.	Allow HDB flats to be re-mortgaged or sub-let under certain conditions
12.	Waive taxation on income remitted from abroad

Catalysts
1. Incentivize private equity funds which help Singapore-based companies grow, expand or internationalise
2. Waive taxation for qualifying start-ups for 5 years
3. Waive all estate duties
4. Defer taxation for 2 years on income arising from Singapore operations if foreign subsidiaries are making losses in their initial years of operations
5. Expand the list of expenditure items eligible for double tax deduction
6. Encourage Singapore-based enterprises to invest in branding and support their efforts to profile their brands internationally
7. For start-ups, impute tax liability on stock options only when gains are realisable, or seven years from time of exercise whichever is earlier
8. For start-ups, tax gains on stock options at a rate lower than the personal income tax rate if the underlying shares are sold more than 1 year after date of exercise
9. Streamline incentives for enterprises
Rounding up
1. Appoint a single dedicated agency to co-ordinate efforts to develop entrepreneurship and internationalisation headed by an individual responsible to co-ordinate and drive entrepreneurship development and internationalisation in Singapore
2. Monitor results constantly and have clear outcome indicators
3. Encourage enterprise philanthropy

Overview
- An Enterprise Ecosystem

Introduction

1 The Terms of Reference of the EISC are to recommend ways to strengthen the spirit of entrepreneurship and innovation in Singapore, and to foster the growth and internationalisation of Singapore-based companies, including the GLCs.

2 In the World Competitiveness Yearbook 2002 released on 30 April 2002, the report highlighted that although Singapore has made great progress in economic development in the last 40 years, largely due to our success in attracting MNCs, this strategy alone may not be adequate to ensure Singapore's future prosperity. Countries in the region are improving their business environment to compete for foreign direct investment, and Singapore will have to differentiate itself by developing an environment conducive for entrepreneurial activity and enterprise development. Further, Singapore's rate of entrepreneurial activity, measured by the percentage of adult individuals who are trying to start or are already running an enterprise, is low - 5.2% compared to 11.7% for the US.

3 The Government has recognised the need for Singapore to progress from a capital-driven economy to an innovation-driven economy. Hence, while we actively promote the manufacturing and services sectors, we need to recognise the growing importance of the Intellectual Property (IP) sub-sector that cuts across the twin engines of economic growth.

4 There are two important starting points to our recommendations. First, we cannot manufacture entrepreneurs, but we can create the environment and conditions that allow, encourage and facilitate entrepreneurship.

5 Second, we have to work within the constraints of our small domestic market. For our enterprises to grow, they need to expand internationally. In the context of Singapore, internationalisation and entrepreneurship are closely intertwined.

6 Our past efforts have laid a good foundation for us to build on. We are already a business and commercial centre and a hub for communications; we have a strong reputation for reliability and efficiency; we have developed sizeable clusters of high value-added industries in electronics, chemicals, pharmaceuticals and the life sciences; and we protect Intellectual Property rights robustly.

An Enterprise Ecosystem

7 Our desired outcome is a vibrant enterprise ecosystem. This will not be a closed habitat, but intimately connected to the larger global ecosystem. Singapore will be a competitive location for global companies to locate the high value-added segments of their value chains. From Singapore, they will plan, execute, and manage their growth into global operations.

8 The enterprise ecosystem will be self-renewing and self-sustaining, with new businesses being created, constantly moving into Singapore and venturing out of Singapore. Budding ideas can develop into viable enterprises, existing businesses can grow and internationalise, and obsolete ones will fall by the wayside. Within this system, a multitude of local and foreign, big and small enterprises co-exist, some of which will compete, whilst others will form clusters to complement and support each other. Workers constantly renew their skills and can move from company to company.

9 The ability to sustain a vibrant enterprise ecosystem should be a key strength for us to withstand lower-cost competition from the region.

10 The Government cannot plan, implement or manage such an ecosystem. It should be organic and natural. Many of Singapore's first generation successful entrepreneurs were born naturally, out of hardship and a strong will to survive. But we do not wish hardship upon ourselves. Moving forward, the challenge for Singapore is to create the desire in enough Singaporeans to want to make it on their own rather than work for someone. This breeding ground for the new generation of entrepreneurs will be based on a combination of positive and essential elements to help them develop and grow. There has to be the right social climate, where successful entrepreneurs are admired and regarded as role models, rather than resented for their affluence. The society must also be forgiving towards those who tried and failed, and not to humiliate or dampen their ability to start afresh. We must also strike a right balance between providing social safety nets for Singaporeans, and extending the nets so wide that Singaporeans become dependent and reliant on Government.

Framework of recommendations

11 We think there are several essential elements that is within the Government's ability to develop, which we have termed as the 6 'C's. They are **C**ulture, **C**apabilities, **C**onditions, **C**onnections, **C**apital and **C**atalysts.

12 Within this framework, the EISC undertook an extensive review of many Government policies, and proposed several new initiatives. Our recommendations are described in the following parts:

Part 1: Entrepreneurial Culture – recommends fostering a new generation of Singaporeans with strong entrepreneurial instincts and understanding.

Part 2: Enterprise Capabilities – recommends ways to develop and harness a critical mass of talent in the private sector to inject vibrancy into the enterprise ecosystem.

Part 3: Conditions: Regulatory landscape - recommends enterprise-friendly approaches to economic management, industry regulation and procurement by the Government

Part 4: Conditions: Government in business – recommends the principles and approaches for Government's involvement in the private sector to help develop conditions for a more enterprising economy.

Part 5: Global Connections – recommends outward oriented policies to foster strong linkages between foreign markets and our home base.

Part 6: Availability of Capital – recommends ways to address current structural inadequacies so that more capital is available to fund promising enterprises at all stages of their development.

Part 7: Pro-enterprise Catalysts – recommends a package of incentives and changes to tax regulations to channel more capital towards enterprise financing.

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Part 1 – Entrepreneurial Culture

Introduction

1 The biggest challenge for Singapore to develop a vibrant enterprise sector is to change the mindset of Singaporeans. This means that Singaporeans must have the instincts to sense opportunities and take calculated risk, and have the desire to build something out of nothing.

2 To mould a nation's culture is a tremendous and long-term effort, because these are societal behaviours which are embedded in its history. In fact, it is often debated whether entrepreneurs are born or made. The EISC does not have the answer to this question, but there should be no lack of effort to prepare our young for the future. We can only do this through our education system.

3 The 2000 Global Entrepreneurship Monitor report for Singapore posted a poor score in terms of the extent to which training or creating businesses was incorporated into our education and training systems at all levels. Singapore's primary and secondary school systems were singled out for insufficient encouragement of creativity, self-sufficiency and personal initiative. Our school curricula and teaching systems should be reviewed and adjusted to encourage these qualities.

Recommendations

Develop Entrepreneurship education as a non-examinable, co-curricular enrichment activity in schools

Source for a broad range of programmes at student and adult level

Incorporate business projects into the school curriculum

Include entrepreneurship education in the assessment of school rankings

Improve outreach by delivering through schools and grassroots organisations

Set up a non-profit Centre to promote these programmes

Develop a world class Entrepreneurship programme at the tertiary level

4 The EISC supports the inclusion of an entrepreneurial and enterprising spirit in the Ministry of Education's (MOE) Intermediate Outcomes of Education for secondary and pre-university education. The Thinking School Learning Nation Program launched in 1998 has also infused creativity skills into the school syllabi. However, only a small number of young people – less than 10% - in Singapore have benefited from programmes specially designed

to teach entrepreneurial skills. We should extend entrepreneurship programmes to all education levels, including the adult workforce.

5 Entrepreneurship education is not a textbook course. It is best learnt from real world, hands-on experience. Mentoring by experienced businessmen is essential. Hence, within the formal education system, we do not recommend that Entrepreneurship be offered as an examinable topic. It should instead be a co-curricular and enrichment activity with schools required to set aside at least 5 days per annum for entrepreneurship activities. The approach is to provide all students the opportunity to learn about enterprise and gain early exposure to business concepts such as cash flow, return on assets, and market positioning.

6 In offering such courses, we should source for a range of innovative programmes. One example is Bizworld, which was developed by the Founder of Draper, Fisher and Juvertson and has been introduced in some of our schools. Others include involving students in running mini-enterprises during their vacation, or forming a Young Entrepreneurs Club in schools.

7 As part of the Thinking School Learning Nation Program, project work has been incorporated into the school curriculum. School students are required to do projects in subjects such as Science and Social Studies. Since entrepreneurship can be best learnt through hands-on experience, it is recommended that our schools should also consider introducing business projects as part of school curriculum.

8 Entrepreneurship education should be included in MOE's assessment of a school's value-add or success, and be included as a measure in the annual school ranking exercise. Through such measures, Singapore parents will more likely change their attitude towards entrepreneurship.

9 Beyond schools, we should try to deliver such programmes to young people through the National Youth Council (NYC) and Community Development Councils (CDCs). This will improve the outreach of such programmes. To train the adult workforce, commercial programmes can be supplemented by public organizations such as Ministry of Manpower, the Singapore National Employers' Federation (SNEF) and the National Library Board (NLB). In this regard, the EISC supports the Self-Employment Training (SET) programme launched by the Ministry of Manpower (MOM) recently. In the case of NLB, it can leverage on its existing network of libraries and public spaces to (a) build a Resource Centre for entrepreneurship, (b) provide designated spaces for groups to network, interact and exchange ideas on the subject, and (c) organize talks by successful entrepreneurs and businessmen.

10 To support this effort, it is proposed that Entrepreneurship programmes be driven through a Singapore Entrepreneurship Education Development

Centre. The centre should be run as a non-profit organisation and facilitated by the economic agencies. Its purpose is to (a) promote Entrepreneurship education and monitor the effectiveness of existing programmes; (b) develop trainers for such programmes; (c) raise awareness of the importance of Entrepreneurship by organising conferences, or giving out recognition awards to successful programmes or enterprise projects.

11 Together with Government agencies such as Economic Development Board (EDB) and SPRING, the Centre can help source for programmes, and identify mentors that could provide guidance to students.

12 Formal courses on Entrepreneurship can be introduced at the tertiary level. The EISC supports the National University of Singapore's (NUS) efforts in setting up the Centre for Entrepreneurship in October 2001 to promote entrepreneurship among students, professors, researchers and alumni, and Nanyang Technological University's (NTU) effort to form the Nanyang Technopreneur Centre in January 2001. We recommend that our universities consider creating a world class Entrepreneurship programme, and consider collaborating with reputable foreign institutions such as Babson College and the Kauffman Center for Entrepreneurial Leadership.

<u>Adopt management policies in our universities to encourage commercialisation of IP</u>

13 World-class universities usually strike a good balance between teaching, basic research and commercial application of inventions. For example, the 7 national universities of Israel are key pillars of its economy. These universities adopt management policies that encourage IP commercialisation and inspire teachers and students to form ventures. To illustrate, the R&D system is highly independent and fiercely competitive due to limited government funding, and researchers are forced to compete for funds.

14 While our local universities are strong in teaching and basic research, there could be better collaboration with industry to commercialise the economic benefits from research and development. The EISC recommends that at least one of our universities align their management policies with this objective. This should include:

- Adopting a guiding principle that applied research projects must secure industrial sponsors before receiving matched research grants from the university.

- Encouraging faculty members to collaborate with industry and commercialise their research. The university can consider allowing their faculty members to run businesses for up to a limited amount of time a week; or offering part-time contracts or a leave of absence to faculty members interested in spinning off ventures. Remuneration packages and policies on IP may need to be adjusted accordingly to provide recognition of individual inventors.

Increase Capability of Executives and Professionals to Manage International Operations

15 There is also scope for educating the adult workforce in entrepreneurship and internationalisation. Many of our businessmen have indicated that in their internationalisation effort, a major problem is the lack of expertise in areas such as international management, product marketing, design engineering, mergers and acquisition, post acquisition integration, and IT infrastructure.

16 Government can take the lead in organising such programmes for its officers. The programmes can include 1-2 years attachment to foreign MNCs for graduates or mid career executives, or Executive programmes run by reputable business schools or management consultants. These programmes should then be opened to full paying, private sector participants.

Part 2: Enterprise Capabilities

Introduction

1 Enterprise capability is needed at both the individual as well as the industry level. When venturing overseas, 'individual field craft' is important in establishing personal relations and making deals. But individual skills can be put to good use only if there is an industry formation effective in making headway into foreign markets.

2 For the individual, certain entrepreneurial capabilities can perhaps be developed through early exposure to business concepts. This has been addressed in Part 1 on Entrepreneurial Culture. But one immediate way to strengthen our enterprise capability is to encourage freer flow of top talent between the public and private sectors.

3 At the industry level, there is scope to foster greater collaboration among our enterprises to leverage on each other's strengths when venturing abroad. Our enterprises will be more effective if they collaborate when venturing overseas.

Recommendations

4 Our recommendations in developing enterprise capabilities are as follows:

Allow private public sector co-sponsorship so that scholars can discharge their bond in Singapore-based companies

Start a scheme for scholars to be allowed to serve two years of their bond working in start-ups and Small and Medium sized Enterprises (SMEs)

Check against rapid increase of scholarships given out by Government agencies

5 A significant strength in our system to groom our young talent is the Government scholarship system administered by the Public Service Commission (PSC). It has been successful in ensuring that the civil service recruits some of Singapore's best and brightest of each cohort, and maintains effective governance in the public sector. Of the top 3% of each age cohort (about 1,300) in terms of academic results, the government employs 30% of them through scholarships – much higher than Government's share of Gross Domestic Product (GDP) (19%) and the labour force. This demonstrates the importance the Government puts on top talent. Significantly, these scholars are given an early opportunity to be exposed to foreign culture and to establish overseas friendships and networks. This is an important aspect of

enterprise capability, and should be fully leveraged upon to promote entrepreneurship and internationalisation.

6 We should however encourage a healthy circulation of talent between the public and the private sector. The EISC feels that the inter-employability of private and public sector talent is still restricted. The civil service only needs about 10% of its scholars to take on top posts and spend their careers in the civil service. For the rest, they may contribute more to Singapore by working in the private sector. While not necessarily entrepreneurial, most scholars possess intellectual, analytical and planning abilities that are assets to any organisation. Many studied in foreign universities, are exposed to foreign cultures, and can contribute to international expansion of businesses.

7 However, except for a minority who work in the few government agencies that are close to the industries, the difference in required skill sets creates an inertia for the private sector to employ public sector officers, especially after they have settled in the public service for a few years. Others are held back financially because of liquidated damages they need to pay to discharge their outstanding bonds.

8 The EISC therefore supports the recently announced "Gap-year" programme for Government scholars. It further proposes some adjustments to the scholarship system to ensure a better flow through of public sector talent into the private sector.

9 First, we should allow the public and private sectors to pool funding for certain pre-selected scholars. This is what EDB has been doing with private enterprises, as part of its developmental initiatives for the private sector. For these scholars, they can discharge their scholarship obligation by serving in a Singapore-based enterprise immediately after graduation. This arrangement can be extended to government scholars that are so funded. The detailed mechanics for deployment of these scholars would have to be worked out.

10 Second, we propose a specific scheme for scholars to be allowed to serve two years of their bond working in start-ups and SMEs. This should be separate from schemes to attach scholars to MNCs and larger companies because the proposal is to expose scholars to risk taking and entrepreneurship. Preferably scholars should be allowed to do the two years in business at the early and formative part of their working careers. Such a measure will institutionalise a "revolving door" concept in talent management, where officers who have left for the private sector return to serve after a few years.

11 Third, with greater devolution of personnel functions in the civil service, we should monitor the number of scholarships given out by various ministries to ensure that the civil service does not end up taking a lion's share of top talent. While the number of scholarships given out now is arguably not excessive, it is increasing over the years. Government should consider very carefully any further increase in the number of scholarships issued, and should try to rely more on recruiting talent directly from market.

Attract Global Entrepreneurial Executives (GEEs) to Singapore

12 In building up enterprise capabilities, we should continue to bring global talent into Singapore, including GEEs to start and grow enterprises here. We should identify entrepreneurial executives with international experiences and good track records. Other countries have embarked on similar efforts. In the late 1980s, Taiwan embarked on an aggressive programme to attract talented Taiwanese Americans to start new enterprises in Taiwan. It managed to attract about 5,000 Taiwanese to return to Taiwan every year. China has also recently started to attract its overseas scholars to return to China.

13 To help attract GEEs to Singapore, we need to tailor incentive programmes that appeal to the individual. As a start, we recommend the following:

14 First, there must be sufficient flexibility in our employment pass system. GEEs are resourceful people who do not lack ideas or funds. But many will come to Singapore without a well paid job or a specific opportunity, and our foreign talent policy, which issues employment passes based on income and educational level, must reflect this reality. Further, we should consider extending our facilitation to the close family members of GEEs. For example, school-going children accompanying an entrepreneur should be granted student passes, and spouses allowed work. GEEs tend to operate in a team of people of diverse backgrounds and qualifications, with each member qualifying for different types of employment passes. We should inject flexibility in our system to allow these less qualified team members to work on specific projects in Singapore, subject to some qualifying criteria.

15 Second, we should engage various associations to help GEEs settle in Singapore. For example, the Business Group of Hua Yuan Association, and the Singapore chapter of The IndUS Entrepreneur (TiE) Network can help handhold, counsel and lend emotional support to GEEs of the respective nationalities.

Tap on local talent

16 We should however not underestimate the capabilities of local talent that could also play a crucial role in jump-starting entrepreneurial activities in Singapore. Often, these local talent have good business ideas and capability

to execute their plans, but are constrained by the availability of capital and the lack of mentorship. The EISC has made recommendations to address some of the current financing gaps in Part 6 of this report.

Foster the development of industry clusters when venturing overseas

17 There are certain industry clusters in Singapore where no one enterprise has all the necessary competencies to compete abroad. However, individual enterprises choose to make their own foray into the same foreign markets. The larger GLCs may be able to clinch good deals, but if they were to partner other Singapore enterprises with complementary skill sets and compete abroad, the impact could certainly be greater.

18 Ideally, GLCs or larger enterprises can provide management expertise and risk capital, and outsource supporting functions to SMEs instead of trying to duplicate their competencies. SMEs can contribute in terms of ground knowledge, new business ideas and entrepreneurial expertise. Competition and partnership between GLCs and SMEs will therefore exist in parallel. Competition hones their skills, while partnerships help them leverage on each other's strengths.

19 This is not a new concept. EDB has adopted a cluster approach in attracting MNCs to Singapore and this has served us well over the years. A similar approach for international expansion should be just as workable.

20 But left on their own, the private sector is unlikely to forge such industry clusters. There is also feedback that this is further exacerbated by GLCs and SMEs generally viewing each other with suspicion and distrust. There is therefore a role for agencies such as IE Singapore and SPRING to identify and catalyse the development of specific industry clusters. We can start with those where we may have an advantage and competencies which are scalable, such as aviation, maritime, telecommunications and media, land transport, infrastructure and engineering, technology and electronics, finance, real estate, food and resources.

21 Government agencies could bring together complementary players to work together. In particular, IE Singapore will need to build up cluster enabling capabilities, provide an information platform to help companies access foreign markets, and navigate foreign bureaucracy. It should identify key enterprises that are capable of leading the pack in overseas ventures. To do so, IE Singapore should partner Temasek closely to facilitate the outward expansion of Singapore-based industries.

22 In line with this, trade missions should be organised along cluster lines. There should also be post-mission follow up to capitalise on the bonding fostered among the participants.

23 Permanent intra-cluster associations should be formed to promote industry development, conduct research, interact and network. These should be privately run associations, but they can qualify for Government funding if certain targets are achieved. Government Research Institutes could be roped in as members of these associations. An excellent example is SEMATECH, the semiconductor cluster which was formed this way.

<u>Raise the profile of Local Industry Upgrading Programme (LIUP) and expand it to promote globalisation</u>

24 A good scheme to help foster a mindset of partnership is the LIUP, which encourages MNCs to help upgrade SME vendors. The SMEs will benefit from the transfer of technical, operational and management skills, while the LIUP partners benefit from a reliable and dependable pool of local suppliers. Central to this partnership is the LIUP Manager, typically an employee of the LIUP Partner, who will plan and execute the upgrading programme for the vendors.

25 While the LIUP has over the years evolved to cover the statutory boards and GLCs, this is not well known by the public. Out of the existing 115 LIUP partners, 20 of them are statutory boards and GLCs. There are only a small number of LIUP partnerships fostered between SMEs and the large established local enterprises.

26 We recommend taking steps to raise the profile of the LIUP, and highlight the possibility of larger Singapore enterprises helping to upgrade SMEs. We should expand the LIUP to cover instances where GLCs and larger local enterprises lead a cluster of enterprises, including SMEs, to venture overseas.

27 This will encourage GLCs and larger local enterprises to provide a 'beachhead' in penetrating foreign markets and bringing other SMEs in their tailcoats. The bigger enterprises can provide support to the SMEs and save them time and resources in conducting market research, due diligence, and corresponding with foreign government agencies. Given the overall cost savings, the Government should implement an incentive scheme to encourage larger enterprises to play this role.

Part 3 – Conditions: A Pro-Enterprise Regulatory Landscape

Introduction

1 Our emphasis on clear rules has been instrumental in building up a clean and transparent bureaucracy. This is a considerable strength that we already have which should continue into the future. But in the fast changing world, we risk having government rules falling behind the curve of change. Over the last few years, many agencies have been active in removing and reviewing obsolete licences, but this is not enough.

2 Although each licence is not onerous, collectively licences can impose a significant burden on businesses and pose a barrier to new businesses entering the market. Entrepreneurs would be subject to legislative drag, instead of being free to innovate. Too much regulation also breeds a culture of apathy and dullness.

3 But regulations were put in place for good reasons, usually to help protect the public. But if we want to cultivate a more entrepreneurial environment, over time, we should minimise regulations and let the public make its own informed choices. This means adopting a more structured, institutionalised and co-ordinated programme to cut red tape. We should also approach the regulation of business activities from a negative list perspective such that whatever is not prohibited is permitted. This is also to recognise that business activities often run ahead of regulations and that the latter should not be an impediment to innovation and enterprise.

Conduct a comprehensive licence-by-licence review

Impose a sunset rule on all licences

Set up a high-level private-public sector panel to review the licences

4 We recommend a transparent and rapid bureaucratic process, which should begin with a comprehensive license-by-license review, to be completed by, end 2004. During the review, agencies should be guided by the following questions:

a) Is the licence already obsolete and can be done away with?

b) Is the licence too prescriptive and can be turned into guidelines instead, and let the consumers decide for themselves?

c) Is the licence conditioned on other licences being obtained first, hence making the public run sequentially from counter to counter? Can we have better inter-governmental co-ordination?

d) Can we change the licensing system into a simple registration system, and rely on post market surveillance to ensure that various conditions and standards are met?

e) Can we change it into a class licence, so that so long as certain conditions are met, the licence is granted automatically?

5 Introducing changes to licensing requirements can be a complex process, especially if it involves multiple agencies. To facilitate this process, we recommend imposing a "Sunset Rule" that takes an across-the-board approach to state that all licenses shall become automatically obsolete within three years of its introduction. All licences in the future would thus need to be rejustified periodically including the existing licences that survive the comprehensive review we suggest in paragraph 4.

6 We must not inadvertently compromise on safety and quality standards that are vital to Singapore. There must be balanced considerations on whether a licence should be retained, eliminated or refined. We recommend that in this comprehensive review of existing licences and future periodic review of licences, the Government set up a high-level Rules Review Panel comprising senior civil servants, private sector representatives and regulators to deliberate the need for each licence seriously.

<u>Reset all fees and charges to reflect cost recovery</u>

<u>Ensure adequate budget for self-financing agencies which volunteer to reduce their fees</u>

<u>Outsource licensing functions to the private sector through competitive tender</u>

7 The Government's current fees charging framework is based on cost recovery. This concept is sound in cases where the licenses can be justified, as it instils discipline and avoids cross-subsidies between different services. However, the impression of some businessmen is that many of our existing Government fees seem to be aimed at maximising revenue. Whether this impression is correct or not, the EISC felt that there are two shortfalls with our current system which should be addressed.

8 First, agencies that are self-financing have no incentive to reduce their fees, as this results in smaller operating budgets. Second, fees that are based on cost recovery will still be higher than necessary if they are not subject to market competition and price pressures.

9 We recommend a thorough resetting of all Government fees, in conjunction with the licence review. For agencies that reduce their fees and hence revenue, we propose that the Ministry of Finance take steps to ensure that their budgets are adequately provided.

10 Agencies should also explore outsourcing their licensing functions to the private sector enterprise that can charge the lowest fees. A possible area to do this is the various safety inspections before obtaining a licence. For services that can practically only be performed by one provider, we should consider giving the selected service provider a limited tenure to introduce some competitive pressure.

Institutionalise the Pro-Enterprise Panel

11 The Pro-Enterprise Panel (PEP) was set up in 2000 to provide a major push to the pro-enterprise movement. It is chaired by the Head of Civil Service, and comprises both private and public sector members. The PEP conducts regular meetings with the private sector to hear its complaints, and helps mediate between regulators and the private sector. It has been effective in addressing the complaints raised. There is however concern that the PEP might lose its effectiveness with the change in representation over time.

12 We recommend that the Government institutionalises the PEP and ensure that the Head of Civil Service will always occupy the Chairman's post. We recommend appointing a supervising Minister to the PEP. The PEP should also have appropriate representation from the Singapore Business Federation (SBF).

Part 4 – Conditions: Government in Business

Introduction

1 When Singapore first gained independence, the private sector was too weak to provide much-needed jobs and to support economic growth. Government therefore stepped in as a state entrepreneur, creating GLCs and Government agencies to provide services critical for the growth of the economy, such as development banking, aviation, telecommunications, ports, and power. Singapore Airlines was created through the de-merger of Malaysia-Singapore Airlines shortly after Singapore's separation from Malaysia. SembCorp Marine was set up using naval facilities left behind by the British. GLCs are now an important part of the Singapore economy, contributing about 13% of Singapore's Gross Domestic Product.

2 This model was necessary in the initial stages of our economic development, and has worked well. Our GLCs are not like the State-Owned-Enterprises found in some countries that are a drain on the nation's resources. They are professionally run. Many of them are listed on the stock exchange, have reputable brand names, and are profitable.

3 Singapore has entered a different phase of development and the challenges are different today. Unlike in the past where GLCs were created to boost economic growth and to fill market gaps, the private sector is now much more sophisticated. The market functions well in allocating most resources and responding to demand conditions. Business environment now is fast changing and competition is driven by continuous innovation. It is private enterprise, and not the Government, that is the most knowledgeable about and best able to exploit evolving market trends and technologies.

4 Our current priority must be to grow our external wing by encouraging Singapore-based enterprises to globalise their operations. We need to harness the entrepreneurial spirit in the economy to succeed. The Government's participation in the economy had certain strengths, which can be retained and leveraged upon to tackle these new challenges.

5 In line with this, the EISC recommends the following for the Government, Temasek Holdings, individual ministries and statutory boards.

Recommendations

Government

6 The Government no longer needs to take a hands-on approach by involving itself in business. It should encourage the private sector to be at the frontier of developing new business ideas. Its primary role is to ensure a level playing field and provide opportunities for all enterprises to have a fair chance

to succeed. It should intervene only under exceptional circumstances, such as market failure. We recommend that the Government adopt the following:

<u>Enact a generic competition law</u>

7 The EISC welcomes the Government's recent announcement to enact a generic competition law and set up an independent competition authority in 2 to 3 years.

8 Singapore does not have a generic competition law to prohibit cartel activities like price fixing and market division, and abuse of dominance by significant market players. We have enacted such rules only for specific sectors, like energy and telecommunications, which are more prone to anti-competitive behaviour. A generic competition law that covers all sectors will institutionalise and give teeth to Government's longstanding pro-competition policy. It will form part of our enabling infrastructure for entrepreneurship and ensure fair play between all enterprises, including MNCs, GLCs and SMEs.

9 However, competition law should not impose a new layer of regulation and burdensome compliance costs to businesses. In many countries, overlapping jurisdiction between competition authorities and regulators can lead to confusion and uncertainty for businesses.

10 To prevent this, we must make clear distinctions between competition law and regulation. First, the action of a competition authority is often a one-time structural rectification of the market, such as breaking up a monopoly, or dismantling a cartel, while sectoral regulators will referee the conduct of market players continuously at the micro level. Second, regulation is often *ex ante* – meaning that regulators will require market players to seek approval before they can act. Competition law is primarily *ex post* – it allows market players to operate freely in the market, taking action only when they overstep the line. Competition law is therefore regulation with a much lighter touch, and more pro-enterprise in nature. Where there is overlapping jurisdiction between competition authority and sectoral regulators, there must be a clear process to resolve them expeditiously and not burden businesses with uncertainty.

11 The EISC proposes the following key elements of the generic competition law:

a) <u>Comprehensiveness</u>. All sectors of the economy and all enterprises, MNCs, GLCs, SMEs, should be subject to competition law.

b) <u>Continuous review</u>. All laws that restrict competition should be continuously reviewed.

c) Equality of access. All companies should have equal access to critical national infrastructure, such as roads, telecommunications and power distribution network.

d) Anti-collusion. Collusion, bid rigging, price fixing, which involve co-ordinated actions by different market players, should be criminalised.

e) Abuse of dominance. Competition law should not be against dominance – as this is a legitimate motivation of all businesses – but should prohibit abuse of dominance, such as using predatory pricing to exclude new entrants.

f) Mergers and Acquisitions. Transactions of certain thresholds either in value or resulting market share should be pre-notified to the Competition Authority. The Authority will assess the competitive implications of the merger. However, we should keep this process as simple as possible so as not to discourage industrial consolidation and restructuring.

g) Penalties. There should be a schedule of penalties for violations of competition law, including stipulations on which offences will be considered criminal offences.

h) Exemptions. Certain activities done in national interest should be exempted from the law. These could include collective wage bargaining, setting of essential charges such as public transport fare, activities to promote cluster-based development and international competitiveness.

12 Generic competition law will institutionalise a regime where GLCs do not enjoy unfair privileges, and must compete on equal footing in the market, just like any other commercial entity. The Government's approach to govern GLCs should be in line with this policy. We propose that the Government abide by the following principles in setting up and maintaining GLCs.

Establish and maintain GLCs to manage critical resources, achieve public policy objectives, or develop new growth engines

13 Businessmen have expressed concern that over the years, the number of GLCs has grown to cover many industries, encroaching into private sector space. The government should be involved in business only where it achieves its strategic objectives. These include the following:

a) Management of critical resources. Where ownership is critical to Singapore's economic prosperity, such as the airport or seaport; or where provision of a good or service is a natural monopoly, such as the distribution of power, and desired outcomes may not be assured through market regulation;

b) Public policy objectives. Where ownership enables the Government to provide services that achieve public policy objectives for the public good, such as ensuring affordable health care, education and housing; and

c) Development of new growth engines. Where private enterprises are unable or unwilling to participate because the risks are high or the gestation period is too long, but the growth potential can be enormous. One example is the life sciences.

14 Notwithstanding the above, the Government's participation in the new growth sectors should end when the private sector is ready to assume its proper role. When developing new growth engines, the Government should at the outset consider other ways of involving the private sector instead of resorting to setting up and owning GLCs. This could be done through incentives to attract private sector participation, or co-investing with private sector parties. Even when the Government has to set up a GLC, there should be some form of private sector participation. Such an approach will ensure better commercial discipline.

Ensure that GLCs are commercially run and eschew national service by GLCs

15 Government should not interfere with the operations of GLCs, and should ensure that they are commercially run. In exercising its rights as a shareholder to appoint members to the board of directors, it should choose those who contribute optimally to the businesses of the GLCs. The Government should not accord GLCs subsidies and special privileges. Conversely, GLCs should not be asked to perform 'national service', which is defined broadly as any project or activity that they would not have done if it was evaluated purely on a commercial basis.

16 If the Government needs to achieve certain national policy objectives through GLCs, it should do so without undermining the commercial discipline of the GLCs. The restructured hospitals are a good example of this. They are run commercially and have to break even. This ensures that they have the incentive to be efficient and productive, but at the same time, their patients benefit from well-defined Government subsidies.

Review constantly the stable of GLCs and divest non-strategic ones

17 The Government should constantly review the stable of GLCs and keep only those that serve strategic purposes.

18 As for the non-strategic GLCs, the Government should divest them in an orderly fashion, taking into account capital market conditions and seeking appropriate returns for its investments. We must allow foreign companies to buy stakes in these divested companies if we want to maximise shareholders' value. But Temasek should not divest for divestment's sake if this means accepting fire-sale prices for good assets.

Encourage a culture of partnership

19 While the Government should not interfere with the commercial decisions of GLCs, it can actively help encourage and foster a culture of partnership between GLCs, MNCs and SMEs. As a policy, Government agencies like IE Singapore and SPRING should encourage collaboration amongst Singapore-based companies to better compete globally. This will be further elaborated in Part 5 of this report.

Temasek Holdings

20 Temasek Holdings was formed in 1974 to hold Government investments. Although it is not involved in the daily operations of GLCs, it has oversight over key appointments, the strategic outlook and governance of GLCs. In so doing, Temasek Holdings should seek to maximise shareholder's return in the long term. It should benchmark the performance of its GLCs against industry peers – domestically, regionally and globally.

21 Temasek Holdings recently released a new charter, which the EISC welcomes as it is coincides with many recommendations made in this report. To reinforce the Charter, the EISC recommends the following for Temasek Holdings:

Focus GLCs to internationalise their core businesses

22 GLCs are natural candidates for internationalisation given their size, depth of management and the competencies that they have built up over the years. Temasek Holding's key mission should be to grow GLCs into globally competitive enterprises that are anchored in Singapore. Temasek Holdings should compel GLCs to scale up relevant core competencies to build global businesses, as oppose to concentrating on the local market to build a diverse range of unrelated businesses.

23 International expansion can be done through the acquisition of existing foreign companies that strengthen the core businesses. This is an important strategic complement to organic growth. Temasek, however, must ensure that its companies can effectively manage, digest and exploit what has been acquired. A good example is Neptune Orient Lines establishing a global presence through the acquisition of American President Line. There are also

success stories by the private sector, such as City Development's acquisition of foreign hotel chains.

24 In cases where a dilution of its stake in GLCs is necessary for the GLCs to grow their businesses out of Singapore, Temasek should be prepared to do so. The international expansion of Singapore Telecoms and the Development Bank of Singapore are cases in point. Temasek should be prepared to cede control in GLCs where it makes commercial sense. This way, GLCs can also benefit from a broader shareholding base when trying to access capital markets for future acquisitions.

Explore various ways of divestment

25 Besides initial public offering and trade sale, other methods of divestment should be given due consideration. For example, management and leveraged buyouts would give the people who are already familiar with the business the opportunity to grow the company. This helps ensure that expertise in that industry is not lost but further developed.

Review constantly its stable of GLCs

26 Temasek Holdings should review its stable of GLCs constantly, and be prepared to rationalise, consolidate or divest them where it makes commercial sense and benefits shareholders.

Attract world class talent into GLCs

27 Temasek should make a conscious effort to cast a wide net to attract world class managerial talent into GLCs. This should not be confined to the appointment of Chief Executive Officers and board members but also upper management – so that best practices in management can percolate down the ranks. Conversely, under-performing board members and management staff should be removed. Temasek should carry out rigorous succession planning and leadership development across all GLCs.

Limit investment in new businesses to those with the potential to internationalise

28 Temasek should not be disallowed from investing in new businesses. However it should be selective and limit such investments to businesses with the potential to internationalise. These are to be in new growth sectors where the private sector in Singapore is unable or unwilling to undertake the risks, such as large investments with long gestation periods.

Ministries and statutory boards

29 The primary role of many Government agencies is to regulate and promote certain industries in an impartial manner, and ensure a level playing field to all market players. In carrying out their missions, many statutory boards have also set up enterprises. These are technically not GLCs, but are nonetheless fully or majority owned by statutory boards to either address certain market failures, or instil commercial discipline in some of the statutory board's functions.

30 There must however be rules governing the setting up of enterprises under statutory boards. If not done correctly, this can give rise to a conflict of interest and economic distortions. Statutory boards can also encroach into the space of the private sector and detract from Government's enabling role in providing development opportunities for the private sector. The EISC therefore proposes that statutory boards abide by the following disciplines when setting up enterprises:

<u>Do not set up enterprises to provide services that the private sector can provide</u>

31 We recommend that the Government institute a 'Yellow Pages' rule. Statutory boards should not set up enterprises when there are private sector players that are providing or able to provide the service. In fact, statutory boards should seize such opportunities to provide business opportunities to the private sector.

<u>Do not corporatise or privatise regulatory functions</u>

32 Statutory boards should as far as possible not corporatise regulatory functions because these are often monopoly functions and could lead to rent seeking by the enterprise. Further, it will not be in the enterprise's financial interest to review and trim down regulations, as this will mean loss of revenue in fees and charges. This goes against our effort towards liberalisation and deregulation. If indeed the corporate form is deemed as the best structure to carry out its regulatory functions, then it must run on a non-profit basis.

33 In a similar vein, it will be better to keep activities of statutory boards that are strategic to their missions as a public function, even if the activity can be structured to attract a commercial return.

<u>Make a conscious effort to divest enterprises owned by statutory boards</u>

34 Even if setting up an enterprise under a statutory board is necessary, there should be proactive plans to encourage private sector to take over the function eventually. Criteria should be set to monitor the emergence of private

sector equivalents, so as to divest the enterprise when the private sector is ready, including to foreign players.

Conduct mandatory periodic housekeeping

35 There should be a mandatory periodic housekeeping, say every 3 to 5 years, of all enterprises set up by ministries and statutory boards to decide which to divest and which to keep.

Avoid allegations of conflict of interest

36 Statutory boards should avoid subjecting themselves to allegations of conflict of interest. They should ensure that the enterprise does not utilise the name of the statutory board in the domestic market, and that the board of directors is independent of the management of the statutory board.

Do not grant best-of-both-worlds deal

37 Further, the enterprise should not enjoy a moratorium on its domestic business from the government while at the same time being allowed to compete with the private sector in that market segment.

Outsource more Government functions to the private sector

38 A viable alternative to setting up enterprises is to outsource functions to the private sector. Where agencies are not willing to outsource, there should be proper justifications, such as national security or confidentiality concerns. We recommend a systematic reduction of activities by each agency, and setting targets to achieve this. This way, all agencies will think of ways to develop the outsourcing industry.

Allow suppliers to retain IP arising from Government projects

39 Valuable IP can arise from Government tender projects. However, the Government may not have the capability, resources or incentive to commercialise this IP. For this reason, in the US, the Bayh-Dole Act enables SMEs, nonprofit organisations and universities to retain IP that they invented with federal funding. This has spurred the transfer of technology from laboratories to the marketplace. The EISC recommends that the Government allows its suppliers to retain IP arising from Government projects, and consider enacting a similar Act if appropriate.

Provide test beds for SMEs' products and services

40 Government can play an important role not just as an investor, but also as a customer. To support the outsourcing effort, Government should have a more open mind when procuring goods and services. Nokia was a beneficiary

of such a policy adopted by the Finnish government. The success of Nokia has in turn fed 300 first-tier suppliers.

41 There are some good examples in Singapore too. The Public Utilities Board, for example, contracted an SME to use 'bioscrubbers' which can better filter and treat sewage air at sewage facilities. This resulted in a safer working environment and lower operating cost. The company is currently conducting research to upgrade its product. The Government has also adopted the Diagnostic Tutorial and Assessment system developed by an SME. This is a web-based system, self-learning and self-assessment system which can improve the learning process and help reduce teachers' marking time.

42 These few success stories notwithstanding, the feedback is that many SMEs often fail to qualify for Government tenders because agencies are not prepared to try them out due to their lack of track record. As a result, there have been cases of SMEs being awarded contracts by MNCs, but are unable to secure contracts from Government agencies.

43 We should maintain the current principles of Government procurement, which are openness, non-discrimination and value-for-money. Nevertheless, we believe there is scope for all government agencies to review their procurement practices so that products and services offered by SMEs are not automatically ruled out simply because they do not have the necessary track record. To illustrate, Government should specify requirements, and not solutions. Its tender specifications should not be skewed in favour of standardised products and services such that innovative solutions from SMEs would never qualify. SMEs may well give us better value-for-money solutions.

Part 5: Global Connections

1 Entrepreneurship and internationalisation can bear fruit for Singapore only if the wheels of international commerce continue to turn. Historically, Singapore survives economically by being of service to the world, with our base firmly entrenched in Southeast Asia. It is important that global companies, whether local or foreign owned, continue to treat Singapore as an integral part of their larger global operations and use us as a gateway to the region.

2 There are various factors that contribute to our international relevance. Political and social stability, fiscal prudence, low inflation, and a clean and efficient bureaucracy are internal systems and institutions that bolster investors' confidence.

3 There also needs to be a set of infrastructure that establishes our global connectivity. We have done very well in terms of hard infrastructure, such as airport, seaport and telecommunications. The EISC feels that much can be improved in terms of soft infrastructure, in terms of connecting people and markets. We suggest the following areas of improvement:

<u>Position IE Singapore as the champion of our internationalisation effort</u>

<u>Focus IE Singapore's efforts on certain industry clusters and pioneer enterprises</u>

<u>Grant pioneer status to most promising enterprises, which will be selected by a private sector panel</u>

<u>Devise simple and effective performance indicators for IE Singapore</u>

4 Just as EDB has successfully brought MNCs to Singapore, we need an agency that focuses on bringing Singapore-based enterprises overseas – like a 'reverse EDB'. The EISC therefore welcomes the reorientation of the Trade Development Board into IE Singapore.

5 IE Singapore should be the champion for internationalisation of Singapore enterprises. It should co-ordinate and leverage on various international network of offices such as those run by EDB and Contact Singapore. This will enable IE Singapore to better provide enterprises with timely knowledge and intelligence, help navigate foreign bureaucracies and connect enterprises with resourceful institutions and individuals. It can even provide physical facilities, through a 'plug-and-play' concept, for Singapore-based enterprises when they go overseas.

6 IE Singapore needs to be able to focus its efforts and not try to be everything to everybody. Although there will be broad-based programs, such

as market awareness education, tax incentives and grants, IE Singapore should be given the flexibility to provide customised services to selected enterprises and industry clusters where there is a higher chance of success. This should include high value-added intelligence gathering, consultancy work and expert advice. This is the only practical way forward given its limited resources.

7 To help IE Singapore focus its effort, emerging International Singapore Companies (ISCs) should be accorded 'pioneer status'. Pioneer ISCs can be accorded customised facilitation to grow overseas in return for their commitment to retain and expand their operations in Singapore. The Government could co-invest with these ISCs in their overseas ventures. Since each ISC has unique priorities and needs– the package of assistance to each ISC could be identified on a case by case basis.

8 A private sector panel could be formed to assist IE Singapore in identifying pioneer ISCs, taking into account their track record, IP ownership, level of commitment of their management team and growth potential. Qualifying conditions can vary depending on the industry. We could adopt such an approach to grooming ISCs for 50 enterprises as a start, and over time, grow the number to 300-600.

9 It is important that the list of pioneer ISCs is not static, but constantly reviewed to identify new promising enterprises. This way, we cast our net wide for maximum effectiveness.

10 The success of IE Singapore should be measured at both the broad based and the customised levels. In this aspect, it is useful to study the experience of EDB. EDB has distilled its complex task into a simple performance metric, which is the amount of Fixed Asset Investment it brings into Singapore every year. This has guided EDB's effort over the years. The task for IE Singapore is equally complex, but we should also devise clear targets to gauge its achievement in the next 5 years. Some possibilities are the number of enterprises that have grown overseas, the value creation in Singapore attributed to these enterprises, or the number of Singapore-based enterprises that have a turnover above a certain threshold, say S$20mn. IE Singapore's budget and the performance bonus of its staff should be pegged to the achievement of these targets.

<u>Establish a Singapore Overseas Network</u>

11 People networks are important in internationalisation efforts. These networks have played a decisive role in the success of Jewish and Indian enterprises. They are organic institutions that evolved over time. However, as a multi-racial, young nation, there are no similar international networks for Singapore. We can leverage on the overseas Chinese and Indian networks but

only up to point, as our people will ultimately identify themselves with Singapore.

12 Notwithstanding, we should take early opportunity to establish an overseas network for Singapore. More and more young Singaporeans are working and studying overseas, and are keen to maintain their linkages to Singapore. A sample survey of Singaporeans who graduated from Massachusetts Institute of Technology, Harvard and Stanford from 1999-2000 showed that 50% of them are working in the US. The enthusiastic involvement of overseas Singaporeans in contributing suggestions to the Economic Review Committee is a case in point. The challenge is to provide a permanent platform for communication, sharing of ideas, information and resources.

13 The EISC proposes to institutionalise the Singapore Overseas Network (SON) which was initiated by the ERC. The SON could be extended to include non-Singaporeans who have a special interest in and affinity to Singapore, and who are willing to serve as connectors. Examples would be expatriates who have lived in Singapore and have returned to their homelands. Government could help SON set up a live directory of such individuals, which will describe their work experiences and business interests. In the longer term, the SON should consist of chapters located in major cities around the world.

14 Rather than task a government agency to do this, it is perhaps better to identify a group of interested Singaporeans living in various parts of the world to kick-start this. The advantage is that they could harness a sizeable network very quickly through their personal contacts. The Government can provide grants and manpower support through its overseas offices.

<u>Relax criteria for valued employees of Singapore-based enterprises to obtain Permanent Resident status</u>

15 One way to broaden our overseas network is through our policy on granting Permanent Resident status. Foreign talents who have worked for Singapore-based enterprises and granted Singapore Permanent Resident status, are likely to be positively disposed to Singapore and willing to contribute their expertise and contacts to our economic progress. The EISC proposes that Government relax the criteria of certain valued foreign employees of Singapore-based enterprises to obtain Permanent Resident status. We can deem, say, 50% of the time when they work overseas for an ISC as being residence in Singapore and contributing to their eligibility for Permanent Resident status. This will also better enable ISCs in attracting talent.

Take a holistic approach in developing a global brand name for Singapore

16 Singapore has a clear and consistent economic identity that is based on its strong leadership and the successful implementation of its economic plans and strategies. This should be built upon to portray a rounder image for Singapore as a global city of the 21st century where arts, sports and culture also feature prominently. A strong brand name for Singapore will help our enterprises internationalise and attract foreign talent.

17 The EISC recommends that the Government co-ordinate the effort of various agencies to develop a global brand image for Singapore. If necessary, we should appoint an agency to align the efforts of various promotional agencies to ensure consistency in the tone, manner and messaging of their various marketing efforts for Singapore. We should better communicate Singapore's new attractiveness in art, culture, nightlife and sports.

Establish a network of Double Taxation Agreements (DTA)

18 Singapore has established a network of DTAs with many countries. DTAs can help enhance Singapore's attractiveness as an investment location for enterprises owning IP and as a springboard for these enterprises to reach out to our region. As Singapore progressively becomes a net exporter of IP products, the benefits of DTAs would increase.

19 The EISC recommends that Singapore establish a network of DTAs with our key economic partners, provided that the terms of agreement serve our larger national interest.

Continue to push ahead with Free Trade Agreements (FTAs) and establish a robust industry consultation process

20 The EISC proposes that the Government continues to push ahead with its FTA strategy. Our priority should be to push ahead with timely implementation of ASEAN free trade agreements, conclude our bilateral FTAs with US and the ASEAN-China FTA, and launch FTA negotiations with the EU and India. We should also pursue FTAs with Latin American countries.

21 The EISC notes that 84% of our domestic exports take the form of intra-firm trade, i.e. transfer of manufacturing components and intermediate products between subsidiaries of MNCs. MNCs are therefore the biggest beneficiaries of Singapore's FTAs. Although Singapore has practically no applied tariffs, they would benefit from tariff elimination from their home country. This would anchor manufacturing activities in Singapore and enhance our global connectivity.

22 We should also take the opportunity to use FTAs to help local enterprises internationalise. To illustrate, many processed food exporters in Singapore still face substantial tariff and non-tariff barriers when exporting their products into key markets.

23 The EISC proposes that Government establish a rigorous and robust consultation process to obtain feedback from our industries on their areas of interest for our FTAs. The Singapore Business Federation can facilitate this process. IE Singapore should build up expertise to help local enterprises commercialise the benefits of FTAs.

Part 6: Availability of Capital

Introduction

1 A key condition for the growth of enterprises is the availability of capital at various stages of their growth. There are typically three stages in the life cycle of a successful enterprise. At the start-up stage, an enterprise develops its business model and product prototype, acquires its first customers, and gains some financial support. It then becomes an emerging enterprise, where it enhances its product line and gains market share. Finally, it grows into a globally competitive enterprise, with a strong brand name and operations worldwide.

2 At the start-up stage, financing would typically be in the form of equity investment by the founding members, their family and friends, and business angels. It is usually difficult for start-up enterprises to obtain access to venture funds or banks loans as they lack track records and have no tangible assets.

3 Enterprises at the emerging stage are at a trajectory point of their business, and need additional financing to see through its expansion. It is usually difficult for enterprises to secure debt financing at this stage because our financial institutions may not be conversant with overseas markets, or lack domain industry knowledge to undertake the necessary credit risk analysis. It is easier to raise funds from new and existing shareholders.

4 Globally competitive enterprises are well established and are unlikely to face problems with financing.

Current market gaps in financing

5 Although Singapore has a vibrant financial sector, the EISC felt that there are several gaps in enterprise financing which should be plugged.

6 Equity financing for start-up enterprises. Following the bursting of the dotcom bubble in 2000, venture capitalists and business angels have been shying away from start-ups. Instead, they have capitalised on depressed valuations to shift funding to lower-risk, later-stage enterprises, particularly in the technology sector. The loss of risk appetite by venture capitalists and business angels in the start-up stage is likely to be temporary, but it will take time for the pendulum to swing back. In the interim, this has negative ramifications for the entire enterprise ecosystem, as the lack of funding can kill off many promising start-up enterprises, especially those outside the technology sector.

7 Debt financing for emerging enterprises. Financial institutions in Singapore tend to be cautious and extend credit facilities based on the amount of tangible assets collateralised. This heightens the personal

consequences of business failure, and can dampen the entrepreneurial spirit. When venturing overseas, enterprises are also unable to secure financing in the overseas capital markets as they are new entrants with no track record.

8 The main reason for the gap in our market is that financial institutions have traditionally relied on collateral in the form of physical assets. Lending against cash flow is not considered prudent in the case of SMEs, and this is compounded by a lack of domain knowledge in various industries. Many Government financing schemes, such as the Regionalisation Financing Scheme (RFS) and the Local Enterprise Financing Scheme (LEFS), are not working as well as they could because financial institutions still insist on 100% collateral, notwithstanding that the Government is sharing the default risk.

9 With greater banking consolidation and cost consciousness, banks are likely to continue to shy away from more complex and expensive cash flow lending because of the perceived higher risks involved. In the past, investment in growth companies also came from successful listed companies, which recycle profits from core businesses into new ventures. However, the markets now reward companies for their focus on their core businesses.

10 We deem this situation to be a market failure because SMEs are finding it unnecessarily hard to access funds for growth. In Hong Kong, SMELoan Hong Kong Limited[1] was set up in August 1999 to lend money to SMEs based on cash flow evaluation. SMELoan does not take deposits, and obtains its funds from equity investments. As at December 2001, it has loaned out US$50 million to 345 customers. Its bad-debts ratio is 1.2% of net funds employed. SMELoan's key success factor is the ability to use Internet technology to underwrite loans, interact with customers and manage risk continuously, instead of conducting upfront and lengthy credit checks.

11 Banks are currently not subject to any restrictions on the amount of unsecured credit facilities they can extend to a particular corporate account. However, finance companies are constrained in their ability to grant unsecured facilities by the Finance Companies Act, and their SME lending is therefore largely collateral driven.

Recommendations

12 To address the current market gaps in financing of enterprises, the Government can encourage and incentivise a market response. In addition, the Government can also fill the gaps where it makes commercial sense to do so. The EISC recommends the following:

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[1] SMELoan Hong Kong Limited is backed by venture capital firm Whitney & Co. and International Finance Corporation, a private sector investment institution of the World Bank Group. More information can be obtained at *www.smeloan.com*.

Private sector financing for start up enterprises

Support and facilitate the establishment of a private equity exchange

13 Enterprise financing should be as private sector driven as possible. Government can facilitate this by setting up a private equity exchange that allows enterprises to raise funds through the issuance of shares to selected investors, and providing a forum for investors to trade their shares. An additional advantage is that such an exchange provides market valuations for start-up or emerging enterprises, hence allowing owners to use their shares as collateral to secure bank loans. Listing criteria and disclosure standards need not be as high as that for the mainboard Singapore Exchange.

14 A private equity exchange can adopt several trading mechanisms, such as an over-the-counter Bulletin Board, bid-ask spread for the more liquid counters, or periodic auction for less liquid counters. The High Technology Property Exchange in Shenzhen, which has about 2000 listings, even allows intellectual property rights to be transacted.

15 At the inception stage, the exchange will need the support of the Government. In the case of the London OFEX, the British government allows tax exemption on capital gains, and tax deductions on capital losses. We propose that either the Singapore Exchange or a private sector company drive this project with the support of the EDB and adequate incentives from the Government.

Introduce an Entrepreneur Investment Incentive (EII) to allow losses from investments in qualified start-ups to be deducted from taxable personal or corporate income

16 To give a further boost to the availability of private funding, we propose an EII to encourage more 'business angels' to emerge. In the US, business angels form the backbone of start-up financing. The EII is modelled after the existing Technopreneurship Investment Incentive (TII), where the business angel can deduct from his taxable income losses from investments in qualifying high technology start-ups. The proposed EII expands the scope of this scheme to the non-high technology start-ups.

Government financing for start up enterprises

Implement an equity financing scheme equivalent to the Start-ups Enterprise Development Scheme (SEEDS) to support broad based enterprises

17 Government can also provide incentives to attract a range of equity investment in start-ups. SEEDS has been a successful scheme providing funding to start-up enterprises with innovative or intellectual content. However, by limiting the scheme to these start-ups, we could miss

opportunities to groom a broader base of promising enterprises, such as the likes of Starbucks and MacDonalds.

18 We recommend implementing an equity financing scheme equivalent to SEEDS to cover a broader base of enterprises. We will retain the current funding principle, which is that the Government will match on a dollar-for-dollar basis, funding from an independent 3rd party that has performed due diligence on the enterprise. The independent 3rd party can be a GLC, Temasek Holdings or any other private sector company. This will also encourage greater partnership between GLCs and other private sector enterprises. Government's investment will be subject to a cap of S$250,000, and can be in the form of redeemable preference shares to facilitate exit.

Private sector financing for emerging enterprises

<u>Encourage cash-flow financing</u>

19 We need to encourage new and creative forms of debt financing to evolve in the private sector. It is recommended that the Government should encourage financial institutions to develop cash flow financing by allowing double tax deduction on related costs for a period of 5 years.

20 Under current regulations, banks are free to provide unsecured credit facilities, including using cash flow financing. Notwithstanding this, cash flow financing is not common in Singapore because of the banks' lack of domain knowledge of the SME industries. However, under the Finance Companies Act, finance companies are not allowed to extend more than $5,000 of unsecured credit facility to any particular account.

21 With greater consolidation in the banking sector, SMEs now have fewer choices. Finance companies would play an increasing role in plugging the gaps in enterprise financing. We recommend that MAS permit licensing of new specialised SME loan institutions that focus on cash-flow financing. These companies would not be allowed to take deposits and would have to fund their operations through equity or through debt markets. It is further recommended that MAS consider liberalisation of the finance company sector to allow competent finance companies to broaden their SME lending; new entrants with specialised skill sets should also be allowed. This may require an amendment to the Finance Companies Act.

<u>Waive for 5 years taxes on profits arising from financing using intellectual property as collateral, and study the feasibility of a Technology Credit Guarantee Fund to facilitate access to bank loans</u>

22 In the UK and US, enterprises can obtain financing by pledging their trademarks and patents directly to the financial institutions. In Korea, the Government plays an intermediary role between financial institutions and

enterprises through a Korean Technology Credit Guarantee Fund, which provides a guarantee for enterprises with intellectual property to secure private sector financing.

23 We recommend that a Technology Credit Guarantee Fund be set up to help promising enterprises owning intellectual property to gain access to financing. Government can use tax incentives to further promote the securitisation of intellectual property as a means of raising funds. It could consider waiving for 5 years taxes on profits arising from financing using intellectual capital as property.

Government financing for emerging enterprises

<u>Review Government lending rates for the RFS periodically to reflect market lending rates</u>

<u>Allow 15% of the loan for working capital financing</u>

<u>Reduce local ownership requirement from 51% to 30%</u>

24 The RFS is a debt financing scheme that helps local enterprises to set up operations overseas. While funding comes from the Government, banks act as conduits to conduct the necessary due diligence. To ensure that banks carry out their assessment properly, they must share 30% of the default risk. The RFS has however not quite taken off for various reasons. The EISC proposes the following changes to the scheme:

25 RFS lending rates of 6.25-6.75% were fixed a few years back and have become unattractive. This is because Government fixed its interest at 4% per annum, and the banks in turn requested for a 2-3% spread in managing the scheme. It is proposed that Government periodically review its lending rates to reflect market interest rates.

26 Currently, RFS loans can be used for acquiring physical assets such as plants and machinery, but not working capital, which is a major difficulty for enterprises venturing into new markets. This partly reflects the lack of competency in performing credit assessments based on cash flow, as mentioned earlier. It is recommended that RFS loans can include a working capital portion not exceeding 15% of the total loan amount. For a start, relevant qualifiers such as trust receipts or confirmed sales orders can be used to assess the application for working capital loan.

27 Currently, the RFS is granted to enterprises that are majority Singaporean-owned. Given that our objective is to create a vibrant enterprise ecosystem where both local and foreign owned enterprises use Singapore as a springboard to the region, we recommend to reduce the local ownership qualifying condition from 51% to 30%.

Implement a hybrid debt-equity financing scheme to support emerging enterprises in their growth and internationalisation, either organically or through acquisitions

28 The EISC recommends that the Government be prepared to support promising emerging enterprises seeking funding to finance their growth, organically or through acquisitions. The approach is similar to that of EDB dedicating resources to co-invest with MNCs to bring strategic activities to Singapore. We must set aside the requisite resources, and muster the right know-how to co-invest with promising enterprises to acquire and develop technology, intellectual property and other competencies, and to gain international market share. We can impose other qualifying criteria to ensure that enterprises that utilise such funds for internationalisation maintain strong linkages with Singapore.

29 This can be done by implementing a hybrid debt-equity financing scheme whereby the debt financing part can be in the form of a convertible loan jointly extended by the Government and an independent 3rd party who would conduct the due diligence. The equity financing portion can be structured like the SEEDS where EDB co-invests with independent 3rd party investor. One way to implement this is to extend the SEEDS scheme to support emerging enterprises by adjusting Government's co-investment limit beyond the current $300,000 cap for such enterprises.

Open up Government financing options through other financial instruments

30 Within the framework of Government financing schemes like RFS and SEEDS, the Government can also calibrate the risk and reward trade-offs in its investments through various financial instruments. This would broaden the scope of Government financing assistance to commercially viable enterprises of various risk profiles. To illustrate, there should be flexibility in the RFS to also allow Government to issue convertible, as opposed to plain vanilla, debt to more risky enterprises. The option to convert debt to equity in order to partake in the enterprise's success will compensate for the higher risk of failure. A comprehensive review of all other financing options should be conducted to bridge the gaps that currently exist between debt financing and equity financing.

Broad based measures

31 As far as possible, we should free up capital in the economy. To this end, the EISC proposes the following:

Free up CPF that is above a pre-determined threshold sufficient to meet the basic retirement needs of members

32 As highlighted by the ERC CPF Working Group, CPF is fundamentally a sound system and has served its purpose well. The EISC supports the recommendations of the CPF Working Group to strengthen our financial resilience and inject more flexibility into our labour market for all segments of workers.

33 In our next phase of economic development, we need as much nimble money as possible to be in the hands of wealth creators and entrepreneurs. Recognising this, the CPF system has been progressively liberalised for investment and other uses. Currently, about 40% of CPF funds are used for property purchases, 17% are used for other investment purposes, whilst the remaining funds are kept in Ordinary, Special or Medisave accounts. The EISC felt that there is scope to unlock more CPF to further enhance capital mobility.

34 In line with the refocusing of CPF to provide for the basic retirement needs for members in the 10^{th}-80^{th} percentile income spectrum, we should grant higher income CPF members the option to take out their excess funds to manage on their own.

35 We recommend establishing a threshold balance above which this flexibility will be granted. The threshold need not be in line with the Minimum Sum. As a start, we should set the threshold sufficiently high, so that only, say, 10% of members who have sufficient balance in their accounts can be granted the option. We can review the scheme after 5 years.

Allow HDB flats to be re-mortgaged and sub-let

36 Our high home ownership rate has been good for Singapore in helping to root Singaporeans. But as a result, a large part of national savings, in the form of cash and CPF, are tied up in property, especially HDB flats.

37 The EISC welcomes the Government's recent announcement to allow HDB market interest rate applicants to source their financing from commercial banks. It notes that they are individuals who are either (a) private property owners; (b) permanent residents; (c) households who earn $8,000 or more a month; or (d) persons who already have enjoyed two concessionary housing loans. The EISC recommends that for this group of individuals who will effectively be buying the HDB flats as though these are private properties, that they be allowed to refinance their flats beyond the outstanding loan amount and to let out their flats if they so choose.

Waive taxation on income remitted from abroad

38 Currently, our taxation environment tilts individual and corporate decisions against remitting income earned abroad back to Singapore as it would be taxed once the money is remitted back. Compared to Hong Kong that has a full territorial basis of taxation and simply does not tax income from abroad, it is more complicated and thus more costly to pool foreign income back to Singapore.

39 The ability and ease of pooling income from all sources to Singapore enables more efficient financial management. Enterprises are able to gain better negotiating position for more attractive financing terms and centre their funding and risk management activities here. Income remitted from all sources can also be used to service loans and other financial liabilities. Further, it would encourage enterprises to internally fund their expansion in Singapore. Alternatively the savings will also enable companies to pay out more dividends, thus enhancing value to their shareholders.

40 As companies become more and more international, the costs of remitting offshore funds will be an important factor in their decision on where to locate their financial management function to support further growth. Waiving taxation of foreign income will therefore stimulate our financial services sector to provide wider ranging and more sophisticated investment and wealth management services. It will also start a virtuous cycle of companies locating more and more activities such as international human resource management and procurement in Singapore where their funds are being managed. All these new activities in Singapore will translate into new tax revenue.

Part 7: Pro-Enterprise Catalysts

Introduction

1 The Government has been using tax incentives to encourage economic activities with high value-added or significant spin-off benefits. This has contributed to our success as a capital-driven economy, where MNCs invest in Singapore to drive economic growth.

2 While this approach will continue to be relevant, it will become more challenging to carry out as emerging lower-cost competitors in the region also offer similar tax incentives. Beyond attracting MNCs to Singapore, another key driver for our future economic growth will be to encourage Singapore enterprises to internationalise and penetrate the markets of the region. As with attracting MNCs, this effort would require Government's support through various tax incentives and regulations to catalyse the process.

3 In this regard, the EISC strongly supports the Government's recent move to reduce corporate and income taxes, and to raise the Goods and Services Tax (GST). We recommend additional tax incentives and regulations to encourage enterprise and wealth creation. The proposals in this chapter should help shift us decisively from being a capital-driven economy to a knowledge-driven economy.

Recommendations

Incentivise private equity funds which help Singapore-based enterprises grow, expand or internationalise

4 We recommend that the Government encourage more private equity funds and fund managers to help Singapore enterprises grow, expand or internationalise. For example, the incentive currently administered by EDB to promote the venture capital funds industry could expand to cover private equity funds if they can add value by helping enterprises grow or restructure through acquisitions, turnarounds or buyouts. For funds that are dedicated to helping Singapore-based enterprises internationalise, a tax waiver on profits up to 5 years should be considered. 'Approved' funds must dedicate at least 50% of their portfolio for investment to help Singapore-based enterprises with their internationalisation efforts.

Waive taxation for qualifying start-ups for 5 years

5 We recommend that certain start-ups can commence paying taxes on their profits after 5 years from the time of incorporation. This scheme will not help the majority of start-ups, which tend to be loss-making in their initial years. But it can help those which are profitable, and where availability of working capital is critical to their survival and growth in the initial years of

operations. We can set certain qualifying criteria like the start-up has to own intellectual property, must secure independent financing, and so on.

Waive all estate duties

6 Estate duties are generally unpopular amongst entrepreneurs. Avoidance of estate duty through trusts and other legal structures is commonplace and unproductive. Several countries have already eliminated estate duties. We recommend to waive all estate duties.

Defer taxation on income arising from Singapore operations if foreign subsidiaries are making losses in their initial years of operations

7 In any internationalisation effort, it is common for foreign ventures to incur losses in their initial years of operation. Many foreign operations therefore depend on their flagship operations in their home country to provide financial backing to tide over this difficult phase. Countries that have many MNCs tend to adopt a world-wide taxation system. However, such a system would have significant structural impact on our industries and should be studied further.

8 The EISC proposes that at the fiscal margins, we should encourage Singapore-based enterprises to internationalise. We can do this by allowing Singapore-based enterprises to defer for 2 years tax payments arising from their operations in Singapore. The deferred amount can be pegged to a proportion of the losses that are incurred by their foreign operations.

9 This should be a restricted scheme, with sufficient checks in place to prevent the concession from being exploited and eroding our domestic tax base.

10 To achieve this, approval for the proposed concession should be on a case-by-case basis, and evaluated against a set of criteria, which can include the following: (a) the company must be assessed by an independent panel to have a substantial home base and committed to add value to the Singapore economy; and (b) the amount to be offset is subject to an absolute amount cap, and commensurate with the equity investment in the overseas entity.

11 The scheme should be reviewed after 3 years, during which the Government can decide if it is effective and whether it should be continued.

Expand the list of expenditure items eligible for double tax deduction

12 The double tax deduction scheme incentivises enterprises to expand their overseas markets by allowing certain expenditure items related to market development to be deducted twice. However, the current list of expenditure items needs to be updated to reflect efforts to acquire core competencies and intellectual property, as these are now essential for any internationalisation effort.

13 The EISC proposes adding the following expenditure items:

a) Registration and enforcement of intellectual property rights;

b) Localisation of designs and labels;

c) Bidding for projects;

d) Conducting of due diligence on foreign markets; and

e) Sending of Singapore-based executives abroad for training or for posting.

Encourage Singapore-based enterprises to invest in branding and support their efforts to profile their brands internationally

14 An internationally recognisable brand is a valuable asset in any internationalisation effort. However, it takes years of effort and huge amount of investment to build up brand equity, and many enterprises will not have the patience or resources to do so. Currently, expenses relating to the marketing of brands overseas are already double tax deductible and of good help to enterprises. In addition, the EISC suggests the following measures to encourage brand building as an investment.

15 The Government should give more recognition to the branding efforts of Singapore-based enterprises. This can be in the form of a prestigious Brand Award, to be chosen by a panel of international brand experts. The winners could be given a significant monetary prize to invest in the worldwide registration of their trademarks.

16 The Government could also consciously profile Singapore brands to foreign investors and visitors, especially at exhibitions and events organised by Government agencies.

<u>For start-ups, impute tax liability on stock options only when gains are realisable, or seven years from time of exercise, whichever is earlier</u>

<u>For start-ups, tax gains on stock options at a rate lower than the personal income tax rate if the underlying shares are sold more than 1 year after date of exercise</u>

17 A knowledge enterprise at the start-up stage, faces a very different reality than an established enterprise. It is critical for such an enterprise to attract and retain talent, but it usually does not have sufficient cash to pay high salaries for talented staff. Hence, stock options become an attractive remuneration tool that also has the advantage of aligning the interest of individuals with that of the enterprise.

18 Our current approach is to tax stock options like salaries. Theoretically, we should then value the options using methods such as the Black Scholes model. But given the practical difficulties of doing such valuations, we impose a tax liability on gains at the point of exercising the options. As a concession, we allow a 5-year tax deferment, with interest charged at prime rate.

19 The EISC disagrees with the current principles for taxing the stock options of early stage companies for three reasons.

20 First, the current system fails to recognise that individuals remunerated on stock options are a hybrid of salaried employees and entrepreneurs. They forego fixed salaries in the hope of growing the enterprise, and in that sense are like entrepreneurs. If we treat them as entrepreneurs, we should not tax them when they fail to make a realisable profit from their stock options, just as we do not tax loss-making enterprises.

21 Second, we should therefore tax only realisable gains. In the Budget Speech this year, the Government announced a change in its rules to impute tax liability only after the moratorium on sale of shares has been lifted for the employee. But this does not fully address the concern that the current system still taxes hypothetical gains because at the point of imputing tax liability, the shares may be illiquid and the gains are not realisable. The Government currently calculates ‘gains’ from exercising options on illiquid stocks by computing the difference between the exercise price and the share price estimated from the net asset value of the enterprise.

22 This practice is unfair for the taxpayer. The valuation of a start-up for taxation purposes should be on a going-concern basis. Such a valuation will be driven by the growth potential and future cash flow of the enterprise, and not its current net asset value. An enterprise with a bad business model destroys value and can drive its market price to below net asset value. Short of a trade sale or a listing in the stock exchange, we cannot establish a fair realisable gain for an individual that has exercised an illiquid option.

23 Third, gains from stock options comprise both income and capital appreciation. As we have no capital gains tax in Singapore, it is unfair to compute tax liability based on the full gains of the stock options.

24 Because of the above shortcomings, we have created a situation where individuals involved in the early stage of a company are burdened with tax liability for unrealisable gains. To address this, the EISC recommends the following:

a) Impute tax liability only when stock option gains are realisable. The point of realisation should be at or after the point of exercise, when there is a valuation of the enterprise based on an going-concern either through listing or trade sale, and the moratorium on sale of shares for the individual expires.

b) Tax gains on stock options at a rate lower than the personal income tax rate if the underlying shares are sold more than 1 year after date of exercise. This is to recognise the capital appreciation is tax free in Singapore. It also encourages individuals to hold on to the options to drive the enterprise to a higher value. In the US, gains on Incentive Stock Options are taxed at the long-term capital gains rate of 20% instead of the ordinary income tax rate of up to 39.1% as long as the employees hold onto the underlying shares for a minimum of 1 year after the date of exercise.

25 As this scheme is meant for start-up enterprises, it should only be available to enterprises which gross asset values do not exceed S$100m.

26 In addition, we recommend that for mainboard listed enterprises, the maximum issued share capital that can be made available for stock options be increased from the current 15% to 25%. The limit of voting shares that can be held by a qualifying employee should also be increased from 25% to 30%. This will improve enterprises' ability to attract and retain talent. It is also in line with the revised Companies Act.

Streamline Incentives for Enterprises

27 The plethora of tax incentives, grants and loans can be confusing especially to smaller enterprises. We recommend that all agencies simplify and streamline all incentives for enterprises. SPRING should be a one-stop agency to help SMEs benefit from these incentives.

Part 8: Rounding Up

Appoint a single dedicated agency to co-ordinate efforts to develop entrepreneurship and internationalisation

1 In a recent survey conducted by the Ministry of Trade and Industry (MTI), it was observed that in terms of international competitiveness ranking, Singapore fares worst in areas where the Government has not assigned a dedicated agency to oversee them. Enterprise development is one such area. Businessmen often lament that there are too many incentive schemes, and that they need to interact with multiple agencies when starting a business.

2 The EISC recommends that Government appoints a single dedicated agency headed by an individual whose mandate is to co-ordinate and drive entrepreneurship and internationalisation in Singapore. He or she must be influential in the Government, yet able to garner support from the private sector.

Monitor results constantly

3 We should also monitor the success of our efforts in promoting entrepreneurship. Hence, beyond traditional macroeconomic indicators, MTI should track the following indicators:

a) Number of enterprises formed;

b) Number and growth rate of entrepreneurial growth enterprises, defined as those which have at least $1m in revenue and 15% growth a year;

c) Percentage of GDP attributed to entrepreneurial growth enterprises;

d) Number of Initial Public Offers of Singapore-based enterprises in major international stock exchanges;

e) Percentage of university students that want to own their own companies;

f) Number of GEEs attracted to Singapore;

g) Amount of royalties and licensing fees received by Singapore-based enterprises;

h) Number of spin-off enterprises from the universities and the public research institutes; and

i) Technology balance of payments. This refers to the international transfer of licenses, patents and royalties. A deficit indicates use of foreign technology while a surplus indicates the ability to sell the technology abroad.

Encourage giving back

4 Having more successful entrepreneurs will likely lead to a widening income gap. A sustainable drive for entrepreneurship and internationalisation should be accompanied by greater encouragement for philanthropy, and for the successful to give back to society. This could be in the form of public service, voluntary social work and providing mentorship for the next generation of entrepreneurs.

Conclusion

1 The EISC believes it is critical that we promote entrepreneurship and internationalisation, and develop a vibrant enterprise ecosystem for Singapore. We should not feel handicapped by our lack of landmass and natural resources. Countries like Japan and the Scandinavian states have turned their national constraints into enduring strengths. To illustrate, the lack of living and working space has driven Japan to the frontier of technology in miniaturisation. To overcome difficulties in communications and power transmission, Scandinavian states have built world class enterprises like ABB, Ericsson and Nokia. In the knowledge-based economy, it is sometimes not nature's endowment, but nature's deprivation that drives an economy's competencies and comparative advantages.

2 For Singapore, because of our small domestic market, we reach out to the world. We wooed MNCs to invest in Singapore when it was not politically correct to do so in the early days of our independence. Now, we host thousands of MNCs and even more global talent. Our trade to GDP ratio is 3 to 1 – unmatched by any other country. Our port and airport are intricately connected to the rest of the world.

3 It is the entrepreneurial spirit of our first generation of leaders and people that brought us to where we are. Entrepreneurship is therefore in the blood of Singaporeans. The issue now is how to uncover it, and channel that energy not just to nation building, but developing businesses and enterprises that can create wealth and raise the standard of living for Singaporeans.

4 Uncovering the entrepreneurial spirit of the Singapore society is not an overnight process. This report proposes putting in place some of the pre-conditions to allow an enterprise ecosystem to flourish. This is not a blueprint that is cast in stone, but represents the start of an iterative process. Not all the recommendations will work out as they are intended to, but to encourage entrepreneurship, Government should also be entrepreneurial in trying out new approaches. Debate and discussion will continue to be critical so that Singaporeans understand and take to heart the direction in which we need to proceed. The continued dialogue will ensure that new ideas are continually surfaced and that the best ideas win. This, in turn, will ensure our continued economic success.

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Mr Vikram Khanna
Regional Economics Editor, The Business Times

Mrs Lim Hwee Hua
Member of Parliament/Managing Director, Temasek Holdings

Mr Ng Kai Wa
CEO, InnoMedia

Mr Allen Patmarajah
Executive Chairman, AJP Advisors

Mr Kirpal Singh Sidhu
Chief Operating Officer, Silkroute Holdings

Dr Finian Tan
Managing Director, Credit Suisse First Boston

Mr Tay Siew Choon
Managing Director & Chief Operating Officer, Singapore Technologies

COMPOSITION OF SECRETARIAT

Mr Ong Ye Kung
Head, Secretariat

Kelvin Hong Kian Boon
Assistant Director and Head eBiz

Mr Henry Koh (till 2nd August 2002)
Assistant Director, Ministry of Trade & Industry

Ms Kathy Lai
Director, Corporate Planning Group, IE Singapore

Mr James Loong Fong Teck
Head, Technopreneurship & Venture Capital, Economic Development Board

Mr Donald Low How Tian
Deputy Director, Fiscal Planning, Ministry of Finance

Ms Low Yen Ling
Assistant Head, Enterprise Development, Economic Development Board

Ms Jacqueline Poh
Co-ordinator, Scenario Planning Office, Prime Minister's Office

Mr Steven Tan
Director, Enterprise Productivity Division, SPRING

Mr Yeo Kia Thye
Assistant Director, Investment, Ministry of Finance

Mr Yew Sung Pei
Director, Capability Development Group, IE Singapore

Mr Wong Peng Wai
Director, Enterprise Ecosystem Development, Economic Development Board