



September 2021 - Special Edition

Income Tax Act rewrite

Following a number of rounds of discussion, drafting and engagement between IRC and Treasury representatives, this week saw the release to a limited audience of the seventh draft of the new Income Tax Act.

We understand the intent is to engage through limited invitation with those who provided written submissions during the public engagement phase in early 2020. The form of engagement is expected to be a “consultative meeting” being planned at the end of month.

There is currently no indication that the timeline for legislation has altered, meaning that a bill containing the rewritten provisions may enter Parliament in November 2021. However, the effective date of any new legislation remains uncertain. It appears possible that it may be implemented from 1 January 2022, although it is also possible that it could be deferred to provide additional time for the tax administration processes and systems to be adequately and appropriately developed before the legislation takes effect.

The initial impression of the seventh draft of the legislation is that it is largely unchanged from the earlier version that was made available. The form of the document is a significant departure in style and structure from the current version and arguably does go some way towards the original stated intention of simplification.

However, as previously noted, the rewrite took on a number of new policy areas, and eliminated a number of existing elements of the tax system. Given that these changes have survived into this subsequent version, it would appear that these were not errors of omissions, but deliberate policy developments.

The list of issues that taxpayers will need to consider will be sizable, and these will contain items that could be considered as beneficial as well as those that will potentially increase tax burdens. These considerations include:

- **Capital Gains Tax (CGT):** The most recent draft continues to contain a limited capital gains tax regime. Taxable assets are PNG real property and interests in companies whereby more than 50% of their assets are PNG real property. Real property includes a tenement granted under the Mining Act or Oil and Gas Act. Holders of taxable assets will choose a cost base of original cost or fair market value at the date of effect of the legislation.
- **Primary production:** Removal of virtually all tax concessions currently offered to encourage investment in the primary production and agricultural sector.
- **Payments to non residents:** Some “foreign contractors” may move from a withholding tax to lodging a tax return in PNG, and deduction of withholding tax from payments to them will no longer be required. In some cases payments not previously subject to withholding tax will become taxable, and tax deductions may be denied for payments on which correct withholding is not made.

- **Management fees:** The discretion for the IRC to allow management fee deductions in excess of the current 2% deduction limit is proposed to be removed, so a hard deductibility cap will apply to management fees paid to non-residents.
- **Tax depreciation:** There is significant simplification of tax depreciation rates, by use of pooling of assets into classes. But this is offset by the removal of nearly all the current accelerated depreciation concessions.
- **International tax:** Significant changes are proposed to the rules for foreign losses and foreign tax credits. Foreign exchange losses will be quarantined and cannot be offset against other income. Dividends received from foreign companies will be fully taxable in PNG. In some cases the passive (investment) income of a foreign subsidiary company may be subject to tax in PNG.
- **Employment taxes:** There are expected to be significant unfavourable impacts for employees - the stated intention is to move to market value taxation of benefits, including housing and motor vehicles, although the rules for housing are not yet included in the rewrite. The dependent rebate is removed, and there is no reduction in marginal tax rates.

In addition to the potential changes in the technical treatment of certain taxes and taxpayers, the draft legislation also highlights some other principles and observations that will shape the tax environment into the future, for example:

- The role of regulations appears expanded as these are able to be implemented for a wide range of uses (none of the proposed regulations are currently available in the draft). It is feasible that significant tax policy changes may be implemented through regulations in the future, rather than through a revision of the law.
- The draft Act would appear to signify an increase in the level of compliance process that taxpayers will be required to conduct, with a greater use of notifications required to be made to the IRC - often contemporaneously with transactions, rather than as part of the annual return process.
- The rewritten Act refers to the Tax Administration Act (TAA) that was passed by Parliament in 2017, but has not yet come into operation. The TAA may require some rewrite to reflect different terms and terminology between the Acts.

While the timing of commencement remains uncertain, all PNG taxpayers will need to address the impact at some stage, and being prepared early is always the best strategy. If you want to know how this will affect your business, get in touch with your PwC tax adviser.

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