
CHAPTER 6. TAXATION MEASURES

6.1 OVERVIEW

The 2011 Budget introduces a number of taxation policy measures. The Government will undertake a further but modest Tariff Reduction Program (TRP), with the aim of promoting an internationally competitive and efficient private sector, and update housing tax concessions which have been substantially eroded over time by house price inflation.

The Government will also seek to improve environmental and social outcomes by allowing tax deductions for environmental protection and clean-up costs, and reduce the alcohol content of beverages which receive concessional excise treatment.

Other taxation measures will enhance Retirement Savings Accounts and seek to improve compliance in the remittance of salary and wages taxes.

There are also a number of minor policy and technical amendments to clarify the law and administrative procedures, strengthen enforcement activities, increase administrative efficiency and correct technical errors.

There are no new taxes introduced in this budget.

6.2 TARIFF REDUCTION PROGRAM

The 2011 Budget introduces a modest TRP that will be implemented over seven years starting in 2012. The TRP is consistent with the 2007 Tariff Review, which found that tariff reduction from 1999-2006 had delivered significant benefits to PNG, and recommended further tariff reductions.

Items in the prohibitive and protective tariff rates will be gradually lowered in three year intervals until they are more closely aligned with the intermediate rate of 15.0 per cent. The intermediate rate on goods produced in PNG will remain unchanged. Overall, this will achieve lower and more uniform effective rates of protection.

However, tariffs on selected agricultural goods produced extensively in rural PNG such as fresh produce, fruits and vegetables will remain at their current rate. In addition, the non-ad valorem tariffs on alcoholic beverages and tobacco will not be reduced in order to help support better health outcomes.

A key objective of the TRP is to encourage the development of more efficient and internationally competitive industries that maximise PNG's comparative advantages. The TRP will reduce input costs for many businesses, reduce the costs of development activities in PNG, and reduce the price of consumer goods. The TRP will make PNG's exports more competitive on world markets and boost growth in export industries.

Table 26: Tariff Reduction Program: 2012 - 2018

| Category | Old and Existing Rates | | | | New Rates | | |
|------------------------------------|------------------------|-----------|-----------|------|-----------|-----------|------|
| | 1999-2000 | 2001-2002 | 2003-2005 | 2006 | 2012-2014 | 2015-2017 | 2018 |
| Intermediate Rate | 30% | 25% | 20% | 15% | 15% | 15% | 15% |
| Protective Rate | 40% | 35% | 30% | 25% | 20% | 15% | 15% |
| Prohibitive Rate | 55% | 50% | 45% | 40% | 35% | 30% | 25% |
| Selected Agricultural Items | | | | | | | |
| Protective Rates ¹ | 40% | 35% | 30% | 25% | 25% | 25% | 25% |
| Prohibitive Rates ² | 55% | 50% | 45% | 40% | 40% | 40% | 40% |

Source: Department of Treasury and PNG Customs

1. Includes coffee and tea, vanilla, cardamom, ground nuts and copra, coconut and honey.

2. Includes a range of fresh fruits and vegetables (including but not limited to tomatoes, onions, lettuce, carrots, potatoes, taros and yams, eggplant, bananas, watermelon, pineapples, citrus fruits and avodados) and cashew nuts.

At the same time as reducing tariffs, the Government is investing substantially in key infrastructure projects, education and law and order, to address some of the business impediments and skill shortages that confront business over the medium term.

The TRP is estimated to reduce revenue in 2012 by K10.0 million.

6.3 HOUSING TAX CONCESSIONS

The Government will update a number of thresholds relating to housing tax concessions to better reflect housing market conditions. The net effect of these amendments is an estimated increase in revenue of K8.0 million in 2011.

6.3.1 Employer Assistance to Purchase a First Home

The limit on the cost of housing will be increased from K75,000 to K400,000 for repayable amounts provided by an employer to an employee to purchase their first home. This threshold better reflects current market conditions.

Furthermore, the “low cost housing scheme” for a subsidy provided by an employer to an employee to purchase a first home will be renamed “employee first home buyer scheme” to better reflect the current operation of the scheme.

6.3.2 Increase Housing Thresholds and Benefits

The *Income Tax Act 1959* provides highly concessional taxation treatment for employer provided housing. Employees are not taxed on the value of the housing provided, but are instead taxed on the prescribed benefits contained in the Income Tax Regulations. The prescribed benefits were last updated in 2003, and since that time, the cost of housing has appreciated substantially.

Over the past 7 years, the substantial appreciation of housing costs has had two key effects on this concession.

- It has provided a large and growing tax subsidy to employees who receive free housing from their employer, but particularly to high income employees. For example, the implicit tax subsidy for a high income earner in employer-provided housing that rents for K5,000 per week is over K100,000 per annum.

- Modest accommodation previously assessed to be “low cost” or “medium cost” is now assessed as “high cost” in many cases. Hence low and middle income earners are taxed on the same housing benefits as high income individuals living in expensive housing.

To address these issues, the Government will update the prescribed thresholds and benefits to better reflect current market conditions. The amendment seeks to strike a better balance between encouraging and supporting employers who provide accommodation to employees, and ensuring fairness for all taxpayers, including those who do not benefit from employer provided housing. It also restores equity between employees living in high cost, medium cost and low cost housing.

While the increase in taxable benefits is highest for individuals living in employer-provided housing with a market value in excess of K800,000, these individuals will still pay an effective rate of tax of less than 5 per cent of the underlying value of housing benefits, which compares favourably with marginal income tax rates. The measure will apply from 1 January 2011 and is estimated to increase tax revenue by K10.0 million in 2011.

Table 27: Prescribed Housing Thresholds

| | Current thresholds 2003-2010 | New thresholds from 2011 |
|---------------------|--|---|
| Low cost housing | Market value of up to K95,000 (or rent up to K300 per week) | Market value of up to K400,000 (or rent up to K1,000 per week) |
| Medium cost housing | Market value of between K95,000 and K220,000 (or rent between K300 and K950 per week) | Market value of between K400,000 and K800,000 (or rent between K1,000 and K3,000 per week) |
| High cost housing | Market value of over K220,000 (or rent of K950 per week or above) | Market value of over K800,000 (or rent of K3,000 per week or above) |

Source: Income Tax Act 1959 and Department of Treasury

6.3.3 Increase Stamp Duty Exemption Threshold for First Home Buyers

The stamp duty exemption threshold for first home buyers will be increased from K210,000 to K500,000 from 1 January 2011. The current threshold was last updated in 2003 and has fallen behind the substantial increase in the cost of housing. The stamp duty calculation will also be simplified for a first home purchase by applying a uniform rate of stamp duty of 5% on the amount of the purchase price in excess of K500,000.

This measure will assist many people to buy their first home. Changes to this tax exemption are estimated to reduce revenue by K2.0 million in 2011.

6.4 ENVIRONMENTAL AND SOCIAL TAX MEASURES

The Government will introduce two tax measures that seek to improve environmental and social outcomes in PNG.

6.4.1 Environmental Expense Tax Deductions

The Government will clarify the *Income Tax Act 1959* to allow environmental protection and cleanup costs as a specific tax deduction from 1 January 2011. This measure will support

and encourage companies to safeguard the environment in their pursuit of income earning activities. The amendment will remove uncertainty about the tax deductibility of environmental expenditure which occurs “before” or “after” the income producing activity.

6.4.2 Reduction in Alcohol Content of Concessional Excise

The Government provides a concessional rate of excise for alcoholic beverages made from fruit grown in PNG. The concession is being used to produce high alcohol beverages that are inexpensive, which is contributing to anti-social behaviour and adverse health effects. The concession is also eroding the Government’s excise revenue base.

To address these concerns, the Government will limit the alcohol content of beverages that benefit from the concessional rate of excise to 10 per cent by volume, from 1 January 2011. Currently, there is no limit of the alcohol content of this excise item.

The Government will also clarify that the concession only applies to fruit grown and fermented in PNG, and not to beverages made from imported alcohol. This is consistent with the original policy intent of the concession.

6.5 ENHANCEMENT OF TAX COMPLIANCE FOR SALARY AND WAGES TAX

A penalty will be introduced from 1 January 2011 on directors of private companies who fail to act on notices from the Internal Revenue Commission (IRC) on the company’s non-remittance of salary and wages tax. This measure will not apply to directors by virtue of a Government position, directors appointed by NEC, or directors not in a position to direct the company.

This amendment is intended to address a large and growing pool of unpaid salary or wages tax by some companies. The amendment is also intended to promote competitive neutrality by ensuring companies do not gain an unfair advantage over other companies by not complying with their salary and wage tax obligations.

6.6 ENHANCEMENT OF RETIREMENT SAVINGS ACCOUNTS

The maximum balance for Retirement Savings Accounts (RSAs) will be increased from K100,000 to K250,000 from 1 January 2011. The amendment better reflects retirement lump sum payouts, which have increased substantially in recent years owing to high superannuation fund returns, higher wages and higher employment.

In addition, withdrawals from RSAs in excess of the prescribed limit will no longer result in the loss of the tax exemption on investment earnings. The current treatment can result in disproportionately large penalties for small breaches of the limits. Excess withdrawals will continue to be taxed at a uniform rate of 30.0 per cent.

6.7 MINOR POLICY AND TECHNICAL AMENDMENTS

A number of minor policy and technical amendments will be introduced from 1 January 2011 to clarify the law and administrative procedures, strengthen enforcement activities, increase administrative efficiency and correct technical errors.

The *Income Tax Act 1959* will be amended to:

- enable service of court proceedings on corporate taxpayers without the need to conduct company searches at the Investment Promotion Authority;
- expressly provide for the Commissioner General of the Internal Revenue Commission to have general administrative power of the Income Tax Act;
- allow the sharing of tax information amongst certain law enforcement agencies;
- clarify the procedure for resource operations to make an election to pool allowable exploration expenses under section 155N; and
- correct a minor technical error to Section 159A(4) by replacing 'gas' with 'resource' and update section 241 by replacing the reference to 'High Commissioner' with 'Minister'.

The Goods and Services Tax Act 2003 will be amended to include in the definition of 'Resource Company' companies who hold a mining lease, to provide access to GST zero-rating.

The *Customs Tariff Act 1990* will be amended to clarify the import duty exemption provided to the PNG LNG project during the construction phase, to ensure the law works as intended.

6.8 AREAS OF POLICY DEVELOPMENT IN 2011

The following represent areas of policy development that will be considered in 2011, for which the Government wishes to provide notice to industry or seek industry comment. Industry and other interested groups are invited to lodge submissions on these issues by 30 April 2011, as part of the regular process for making Pre-Budget submissions.

Export Subsidy Program

PNG's Export Subsidy Program is scheduled to be abolished as of 31 December 2015, regardless of the date of first export sales, to be consistent with PNG's obligations under the World Trade Organisation.

Taxation of unit property trusts

The Government will consider amendments to the taxation of unit trusts to remove barriers to participation by superannuation entities.

This may assist to create new property unit trusts, thereby deepening investment markets in PNG, providing greater scope for property investors to diversify risk and improving access to property investment for smaller investors. This may also contribute to larger developments on existing parcels of land.

The Government will consult on the feasibility and potential design of a proposal and the attractiveness for local entities. This includes the mechanism to ensure that superannuation entities are subject to similar rates of tax when investing in property directly and when investing through unit trusts.

Taxation refunds

The Government will move to discontinue the current practice of limiting income tax refunds by annual appropriation. This practice can result in delays in the payment of tax refunds, which is inconsistent with the Government's objective of encouraging voluntary compliance with the tax laws and ensuring fairness for taxpayers. This will involve changes to the administrative practices of the Internal Revenue Commission.

Payment of mining and petroleum tax instalments

The Government will investigate the extent of underpayment of mining and petroleum tax instalments by mining and petroleum companies through the year. The Government will consider introducing a penalty regime to discourage the significant underestimation of mining and petroleum taxation instalments.

Highlands Highway Special Tax Credit

The Government will consider reinstating a Special Tax Credit rate for repairs to the Highlands Highway for a period of time, while seeking to avoid any abuse of the concession.

Nil assessments

In considering a technical amendment to recognize nil assessments in the definition of assessment, the Government will look to introduce a longer period of time for IRC to review returns with a nil assessment (compared to returns with a positive assessment).