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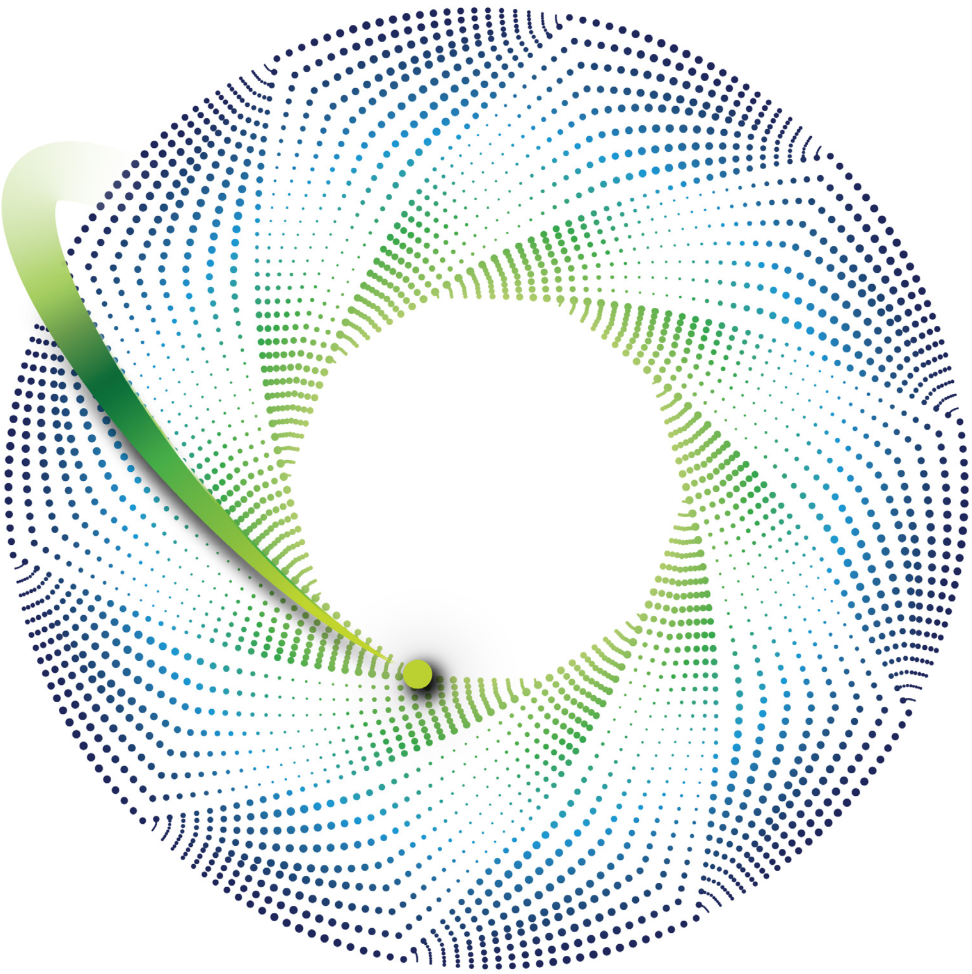

Papua New Guinea

Tax Alert

Income Tax Act Rewrite Series – Taxation of Individuals

Taxation of Individuals

This is the series of Alerts summarising the proposed major changes arising from the Income Tax Act rewrite. This is based on the 9th redraft of the legislation. We understand that the legislation will be introduced to Parliament in late November 2022 and have a commencement date of 1 January 2024.

In this article we summarise the implication for individuals. The changes for Salaries and Wages Tax and Trusts are the subject of previous alerts and therefore not repeated here.

Tax Residence

The definition of tax residence for an individual has been changed. The proposed definition is an individual who:

A. resides in PNG at any time during the year; or

B. has his or her domicile in PNG during the year unless the individual has a permanent home outside PNG for the year; or

C. is physically present in PNG for a period of, or periods amounting in aggregate to, 183 days in any 12-month period that commences or ends during the year; or

D. is citizen of PNG who is an employee of the Government posted abroad.

The definition in the present Income Tax Act provides an exclusion to item (c) where the Commissioner is satisfied that the persons usual place of abode is outside PNG and that they do not intend to take up residence here. Presently the 183 day test is also in refence to an income tax year.

Further, an individual is treated as physically present in PNG during any period that he/she is temporarily absent from PNG for business, employment, recreation etc.

The combination of these items is likely to make it harder for many individuals coming to PNG to argue that they are non-resident.

The important implication of this is that residents are taxable on their worldwide income, whereas non-residents are only taxable on PNG sourced income. Worldwide income (including income from foreign trusts) would need to be declared through lodgement of an annual income tax return. Foreign income of a tax resident that has incurred tax in the country of source, would usually still be taxable in PNG though a foreign tax credit may still be allowed. One exception may be for foreign capital gains not assessable in PNG.

Impact of Tax Treaties

A Double Tax Agreement (DTA) can in certain instances override the domestic law. For example, in the case of the Australian DTA the primary test is based on the location of the individual's "permanent home". Where the taxpayer has a permanent home in both locations alternative tests are available for determining the residence for the purpose of the DTA. In the Australian case, for example, where the taxpayer can argue that they are non-resident in PNG the corollary is that they are resident in Australia. This means they are taxable in Australia on their worldwide income and only taxable in PNG on PNG sourced income.

Unfortunately, PNG does not have an extensive DTA network. Currently PNG has 10 operational DTA's.

Tax Return not Required

An individual is not required to file a tax return in the following circumstances:

- Their only income is employment income from which salaries or wages tax has been deducted.
- Where the person's income falls below the tax-free threshold (currently K12,500 per annum for resident individuals).
- A non-resident whose only PNG source income is subject to "non-resident withholding tax".
- A person specified in the Regulations (not yet issued).

In addition, it should be noted that the first K200 of interest income from each financial institution will be exempt from income tax. Withholding tax on dividends paid by a resident company is a final tax and therefore not subject to further tax in the hands of the individual. It is not clarified how this will work in the case of dividends paid to a resident trust where the individual becomes entitled to that income. Please see our separate Alert on the taxation of Trusts for further details.

Small Business Tax

The small business tax (SBT) regime applies in the following circumstances:

5. An individual conducts the business solely in PNG.
6. The individual is not registered for GST and their turnover did not exceed the GST threshold (K250,000).
7. Their business does not include professional services, which is defined to mean medical, dental, legal, accounting, financial, managerial, engineering, architectural, consulting, or other similar services.

The individual can elect out of the regime or back into the regime after a three-year period.

Where the individual's turnover is less than K60,000 the annual tax liability is K250. Where it is greater than K60,000, the tax is payable quarterly and equates to K62.5 plus 2% of the turnover above K15,000 for the quarter.

To protect the integrity of the SBT provisions there are anti-avoidance provisions to avoid splitting income between associates as well as seeking to convert employment contracts into contracts for services (business income). Sole traders will find they are employees of their clients under these rules even where not previously employees.

Taxable Income

A taxpayer is required to return the following income:

H. Employment Income;

I. Business Income; and

J. Property income (including dividends, interest, royalties, rent, annuities, and pensions unless already included in business or employment income).

As noted above, if the individual has only employment income and / or dividends they will not need to file a return. The new Act quarantines losses between business and property income.

Income derived by the individual from a partnership or from a trust will be included within the appropriate category above.

Individuals may obtain deductions for donations only to IRC approved non-profit bodies, including religious organisations, but this cannot exceed 10% of that person's assessable income.

Capital Gains Tax (CGT)

A new CGT regime is included within the new Act.

The assets within the charge for CGT has also been restricted to the following:

A. PNG real property;

B. a membership interest in an entity where more than 50% of the value of the interest is derived, directly or indirectly, from PNG real property; and

C. an option or right to acquire an asset referred to in the preceding paragraphs.

Exempted assets include the following:

A. the principal place of residence of an individual;

B. an asset that is used by a person solely to derive exempt income; and

C. a gain derived or loss incurred on the first commercialisation of customary land.

The cost of a taxable asset held on the date of introduction of CGT will, at the election of the taxpayer, be the actual cost or the fair market value on that date. CGT will be payable at the rate of 15% of the capital gain. The legislation also provides for special rules for part disposals, splitting of assets, creation of new assets and replacement assets (roll -over relief).

Tax Returns and Payment

Income Tax returns are due for lodgement 3 months after the end of the tax year (31 March). Tax is payable by provisional tax payments due in 3 instalments on 31 March, 30 June and 30 September of the tax year. Any balance of tax is due on the same date the return is due for filing (3 months after year end).

Each of the provisional tax payments are based on 1/3rd of the prior year's tax liability increased by an uplift factor (to be determined by Regulations).

There are also rules allowing an application for a variation (reduction of provisional tax) and covering the situation where the individual did not have a tax liability in the prior year.

CGT returns and the payment of tax are due:

A. where the transfer document is required to be stamped under the Stamp Duties Act, by the earlier of –

   i. the due date for stamping (60 days after the issue of a stamp duty assessment); or

   ii. 21 days after the date of disposal of the asset; or

B. in any other case, within 21 days after the date of disposal of the asset.

A small business taxpayer with income less than K60,000 does not need to file a tax return. The K250 tax liability must be paid on 30 June of the tax year.

When turnover exceeds K60,000 the individual must furnish a SBT return for a quarter within 15 days after the end of the quarter. The tax payable by a small business taxpayer for the quarter is due on the same date.

Outlook

The above-mentioned changes to the taxation of Individuals are significant and taxpayers should take time to ensure they understand the implications. There are situations were individuals, for example, may become tax resident or become taxable in PNG on trust income. Planning in advance of any changes is therefore prudent. If you would like to discuss the changes, or their impact, please let us know.

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