



Papua New Guinea

Tax Alert

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Important Changes to the Application of Management Fee Withholding Tax

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Important Changes to the Application of Management Fee Withholding Tax

The IRC has issued a new Public Notice relating to management fees (see [Management-Fee-Withholding-Tax-Tax-Public-Notice-5th-October-2021.pdf \(irc.gov.pg\)](#)). It addresses two key areas and has important ramifications for taxpayers resident in four treaty countries:

1. The first part of the Notice discusses the limitation on the deduction of management fees by the payer, as contained sections 68AD and 155M of the Income Tax Act. Broadly, section 68AD limits the deduction of management fees to 2% of PNG sourced assessable income, or 2% of allowable deductions (excluding management fees) whichever is the greater. The IRC reaffirms that where management fees are paid to a tax resident of a treaty country, provided that the management fee meets the tax treaty's transfer pricing / arm's length requirements, and are supportable as such, then the allowable deduction can increase to the arm's length amount (even where that amount exceeds the 2% rule).
2. The second part of the Notice focuses on management fee withholding tax (MFWT), which is levied at 17% on management fees that are an allowable deduction to the payer. Under section 68AD deductible management fees are deemed to have a source in PNG. However, the application of the 17% MFWT on payments to non-residents is subject to the operation of a relevant tax treaty. A tax treaty is relevant where the non-resident recipient is a tax resident of that treaty country. The IRC Notice outlines a significant change in their approach as to previously accepted outcomes for tax residents of a number of treaties, being: Canada, Australia, Singapore and New Zealand. In short, the IRC now views that MFWT applies to all management fee payments to tax residents of these four countries, effective from 1 October 2021. The tax treaty outcomes stated by the IRC are summarised in the table below. With respect to the 4 countries for which 17% is stated, there are some important considerations for affected taxpayers:
 - A. The IRC approach states that the Business Profits Article (Article 7) of the relevant tax treaties has been misapplied, and that taxpayers cannot rely on this provision to conclude PNG has no taxing rights under the treaty and that MFWT does not apply. Article 7 states that the business profits of a tax resident of the other treaty country may only be taxed in that other treaty country unless that enterprise has a permanent establishment in PNG. If there is a permanent establishment of that enterprise in PNG, then the profits attributable to the permanent establishment of that enterprise may be taxed in PNG. While not expressly stated by the IRC, the IRC approach infers that:
 - i. Management fees are not considered as business profits. If management fees are not business profits then the source of income under the DTA would retain a PNG source (as conveyed under the domestic law); or
 - ii. If management fees are business profits, they are not business profits to the extent there is no permanent establishment in PNG; or
 - iii. The Other Income Article of the treaty provides a residual right to tax the management fees despite the operation and outcome of Article 7.
 - B. Of relevance, some countries do take the approach of insisting the withholding tax is deducted from payments, but then allow for a refund of that tax where the treaty operates. The IRC's Public Notice has not suggested that this would be the IRC's approach, but rather than no refund would be available. To object the taxpayer would need to file a tax return and claim a refund. This could be a long and difficult path.

Tax Treaties – Management Fees

Name of the Country, where the recipient is Resident	Whether Management fee Withholding tax is applicable	If yes, at what rate it is to be deducted	DTA Article #
Non-Treaty	Yes	17%	
Treaty			
Canada	Yes	17%	Other Income (Article 21, para 3)
Australia	Yes	17%	Income Not Expressly Mentioned (Article 21, para 2)
Singapore	Yes	17%	Income Not Expressly Mentioned (Article 23)
New Zealand	Yes	17%	Other Income (Article 21, para 3)
China	No	-	Other Income (Article 22, para 1)
South Korea	No	-	Other Income (Article 22, para 1)
UK	Yes	10%	Technical Fees (Article 14)
Malaysia	Yes	10%	Technical Fees (Article 13)
Indonesia	Yes	10%	Technical Fees (Article 13)
Fiji	Yes	15%	Technical Fees (Article 13)

We will be seeking clarification from the IRC on their approach. If you would like to discuss the Public Notice with us please contact one of the below.

For more details please contact your key Deloitte contacts or any of the following:

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