

The much awaited IRC Taxation Circular TC 2013/4 - Administration of the Foreign Contractor Withholding Tax (FCWT) Regime was issued on 16 December 2013. This newsletter briefly discusses the salient features of the above circular.

Objective

- To clarify the order in which the various withholding taxes will apply when they are applicable alongside FCWT;
- To reiterate the IRC view on the taxation of personal services income;
- To announce changes to the application of withholding taxes to foreign contractors;

Who is liable to FCWT?

Any person who is party to a prescribed contract and not specifically excluded is liable to FCWT. The following activities are prescribed under the act-

- the installation, maintenance or use in PNG of substantial equipment or substantial machinery; or
- the construction in PNG of structural improvements or other works, including -
 - the construction of roads, including bridges, culverts or similar works forming part of a road;
 - the erection of buildings, fences or similar improvements;
 - the clearing or draining of land;
 - the construction of ports or port facilities;
 - the construction of facilities for the provision of water, light, power or communication; and
 - the provision or improvement of transport facilities of any kind; or
- the use of, or right to use, in PNG, any industrial, commercial or scientific equipment including any machinery or apparatus or appliance, whether fixed or not, and any vehicle, shipping vessel or aircraft,
- the provision in PNG of professional services or services as an adviser, consultant or manager.

Excluded persons

The following persons are not liable to FCWT though they may be party to prescribed contract -

- Resident company

- A resident person, who is ordinarily resident of PNG.
- A person who derived a salary or wages income
- A person who derives a management fee

If any person who is party to prescribed contract, derives a salary or wages income or management fee income, he will not be liable to FCWT. However he will be liable to Salary or Wages Tax or Management Fee Withholding tax, as the case may be.

Where several withholding taxes regime apply to same payment then the IRC will apply the taxes in following order –

1. Salary and Wages Tax (SWT)
2. Management Fee Withholding Tax (MFWT)
3. Foreign Contractor Withholding Tax

Excluded income

Generally under the common law rules, any offshore income derived by a non-resident is not liable to tax in PNG however the Act deems all income derived from a prescribed contract to have a source in PNG. This means that where a non-resident derives both offshore and onshore income from a prescribed contract, the gross contract income will be liable to FCWT. However where the entire income under a contract is derived offshore, no FCWT shall apply.

Personal services income

As detailed in Taxation Circular TC2013/1 where individuals are providing personal services on a routine basis over a period of time, they are likely to be most likely subject to Salary or Wages tax.

Where the services are wholly or substantially provided from outside PNG and the individual's services are ancillary to a contract (prescribed or not), then MFWT or FCWT may apply instead of SWT.

IRC's new approach to application of Tax treaties

The circular spells out IRC's new approach to application of certain provisions of tax treaty to foreign contractors-

- In order to determine if an activity carried out by a foreign contractor constitute a permanent establishment (PE), IRC will consider all the activities carried out by him in PNG and not only on an individual contract basis. The nature and duration of all contracts will be considered before arriving at a conclusion;
- Where IRC concludes that a foreign contractor does not have a PE they will consider the application of other articles of the tax treaty such as Royalties and technical fees, Dependent personal services and Independent personal services;
- As mentioned above where several withholding taxes applies they will be applied in the order of SWT, MFWT and FCWT.

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Notable changes to FCWT assessment

The circular suggests various administrative changes to the FCWT assessment. Major ones are indicated below-

- Taxpayer who wish to be taxed on their actual taxable income will need to seek permission from the Commissioner in writing within 12 months from the end of income year in which they have derived the income failing which the law deems an assessment to have been made. The lodgement and extension requirements applicable to normal tax returns will apply;
- In order to ensure that the foreign contractor seeking annual assessment option do not default on the withholding tax the Commissioner General may impose certain conditions. The taxpayer may be required to still pay FCWT or Provisional Tax or Advance Payments Tax which will be allowed as a credit in their income tax return;
- The Commissioner will consider various factors before allowing an approval to adopt actual basis of assessment. These may include degree of connection to PNG, parties to contract, prior contracts in PNG, length or duration of contract, future business plans, reputation of foreign contractors and associated parties, financial resources, compliance history, etc.;
- In determining the compliance profile of the foreign contractor, one of the important consideration would be the arm's length nature of the transactions and any other transfer pricing risks associated. IRC has growing concern about certain foreign contractors who continue to report losses year after year;
- The Commissioner General believes that subjecting a non-resident taxpayer to precisely the same tax requirements as a resident taxpayer effectively satisfies the non-discrimination clauses contained in certain tax treaties, and this objective is not achieved by merely adjusting the tax rates of non-resident in line with the resident tax rates. Hence all the prescribed payments subject to FCWT will be liable to 12% tax rate.

Obligations of resident entity

IRC deems the PNG resident entity as an agent of the foreign contractor and requires it to fulfil the following obligations –

1. Lodge a signed copy of contract or invoices with the IRC within 14 days;
2. Request the IRC for a formal determination on the application of FCWT to the above contract;

3. Apply for an Income Tax File number in relation to the Foreign Contractor;
4. Defer from making payments to the foreign contractor till a formal determination is obtained;
5. Deduct the prescribed FCWT from the payments made to foreign contractor;
6. Remit the FCWT deducted using the tax file number allotted within 21 days from end of month in which such payment was made.

Date of Application

The FCWT circular will apply retrospectively in relation to all payments made under a prescribed contract on or after 16 September 2013.

CONTACT US

If you want to know how the above changes affects your entity or want to get more information on this newsletter please email Hari at

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Disclaimer

This newsletter is prepared to provide a general overview of the recent FCWT circular and is not meant to be an expert document. The author does not accept any responsibility to any person for any statement, opinion, omission or error.