



25<sup>th</sup> August 2015

**Sir Nagora Bogan**

Chairman

Tax Review Committee

PO Box 1589

BOROKO, NCD

Dear Sir Bogan,

**RE: Submission of comments for the Review of the Taxation Laws**

The Consultative Implementation & Monitoring Council (CIMC) as one of the stakeholders would like to take this opportunity to thank your committee for seeking its input into the review of the Taxation Laws. This is no doubt a very important exercise as taxation affects both the taxpaying and non taxpaying citizens of this country and we are grateful for the opportunity provided to us to express our views on this matter.

CIMC through its Informal Economy Sectoral Committee has been actively facilitating discussion and dialogue on the issues affecting the informal economy since its inception in 2000. Through this process the committee has been able to develop the NATIONAL INFORMAL ECONOMY POLICY 2011-2015 and initiated the review of its accompanying legislation, the INFORMAL SECTOR DEVELOPMENT & CONTROL ACT 2004.

Constitutional Law Reform Commission (CLRC) is currently undertaking the review and it is expected to launch its report sometime in the month of October this year. Once launched, the report will be a vital source of information pertaining to the informal economy and should provide insights into issues relating to taxation within the informal economy. The Committee also has been actively engaging with other key stakeholders like the Bank of Papua New Guinea and the Department of Trade, Commerce & Industry looking into issues relating to financial inclusion and literacy and SME accordingly. These issues are intrinsically linked to the informal economy.

Therefore CIMC would like to encourage the taxation committee to closely dialogue with committees like the informal economy sectoral committee.

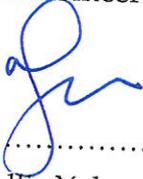
Accordingly, CIMC has hereby provided its views and thoughts on tax related issues in the form of a submission.

We hope that the information contained in this submission will adequately inform the committee in its deliberations and subsequent recommendations to the government concerning reforms relating to the taxation laws.

We look forward to your response and hope to continue on this partnership with the committee and IRC.

For enquiries please do not hesitate to contact myself on 321 1714 or email [Wallis.Yakam@cimcpng.org](mailto:Wallis.Yakam@cimcpng.org) or Busa Jeremiah Wenogo, Senior Project Officer, Informal Economy Sectoral Committee [BusaJ.Wenogo@cimcpng.org](mailto:BusaJ.Wenogo@cimcpng.org)

Yours Sincerely,



.....  
Wallis Yakam  
Executive Officer



## **CIMC FEEDBACK ON THE TAXATION REVIEW**

The following are comments from the CIMC concerning the taxation review

### **TAXATION IN THE SUPERANNUATION INDUSTRY**

#### ***1) Poor Saving Culture among most Papua New Guineans***

Most Papua New Guineans don't have the discipline to save money and subsequently lack knowledge in the area of budgeting, managing and making plans for the medium to long term. With this mind, any increase in tax threshold level will only encourage an increase in the inflation as people accelerate their spending and consumption which has an immediate impact on the level of inflation in PNG. An increase in the tax threshold level will not lead to any REAL increase in the purchasing power of working class Papua New Guineans given that the increase in the level of inflation will rapidly erode their purchasing power due to "poor savings culture"

#### **Recommendation:**

It is recommended that in addressing the issue of rising inflation, government should not only resort to increasing the tax threshold level rather it should channel these increases into superannuation funds. This is because most Papua New Guineans do not have a "savings culture" and have a very low financial literacy skills and knowledge. Therefore, by increasing members' contribution (in the form of diverting increase in tax threshold into super funds) it ensures that their contribution is saved/stored away in the long term and its access/availability is protected under very strict rules and guidelines. This it is hoped will ease/delay potential inflationary pressures that could have arisen in the short term. Members are then able to reap rewards in the form of interest being added to their contribution due to profitable outcomes. This outcome is a win-win situation for both the government and working class Papua New Guineans.

#### ***2) Income fluctuation is a major feature of informal economy***

Recent reforms within the Superannuation Industry have allowed informal economy participants to contribute to super funds through voluntary savings products like EDA

Super from NASFUND. However, not a lot of informal economy participants are aware of this product. Rules and guidelines for voluntary contribution products like EDA SUPER should take into consideration the nature of income for most of these voluntary contributors. Most of the informal economy participants' incomes are not steady and are susceptible to movement in commodity prices and other associated market related costs.

### **Recommendation**

To accelerate the market uptake of such voluntary products and maintain its existence the government should contribute a certain portion of the GST as interest towards voluntary savers' savings.

### ***3) Taxing retirement fund is unfair***

The current arrangement where retirement funds are taxed is a major disincentive for the retirees. It is also deemed unfair as tax is imposed on wages/salaries and then on the retirement fund.

### **Recommendation**

It is recommended that tax imposed on retirement funds especially when it comes to the component on employer's contribution should not be heavily taxed as it becomes a disincentive for employees to contribute to these super funds. If tax were to be imposed it is suggested that the contribution be taxed when the contribution is made fortnightly rather than the tax being imposed on the lump sum. Interest being accrued over time should be tax free.

It is strongly recommended that the current tax rate be reviewed to ensure that it provides an opportunity for retiring employees to build a life outside their formal employment. Otherwise, the current tax rate may contribute to the decimation of their savings and as a result most of the workers may not be able to survive after retirement. In the same vain this may discourage voluntary savings from informal economy participants.

**4) *Lack of transparency when contributions by employers are made on a lump sum basis.***

Currently most firms are making their employees contribution on a lump sum basis. It is a concern for the employee whether the firm is honest in remitting the appropriate amount to the superfunds.

**Recommendation:**

Contribution from employees and employers (excluding informal economy participants) into Superfunds should be made on a “real time” fortnightly basis rather than through a “lump sum” half yearly/quarterly basis. This is more transparent compared to the current approach. Equally important is the need for NASFUND to penalize those employers who have failed to make regular contribution into the super funds. IRC could look at imposing certain tax burden on these firms or remove certain privileges as penalty for non-compliance. IPA could look at penalties in relation to their company registration.

**5) *Financial Inclusion drive in PNG is lacking effort to build confidence among Papua New Guineans***

Financial Inclusion drive in PNG seriously needs the government to increase the level of confidence among the populous. Complaints regarding bank’s unfair policies especially when it comes to charging of fees are seen as barriers towards bringing many people into the formal financial system.

**Recommendation:**

The government through the Bank of Papua New Guinea needs to strengthen its supervision division to ensure “fair play” by financial institutions when it comes to investigating customer complaints.

The government through the Central Bank could look at introducing a Banking Ombudsmen to independently investigate customer complaints rather than allowing complaints to be “internally investigated”.

## TAXATION ON FORMAL SECTOR

### 1) *Generally Papua New Guineans lack information on tax contribution*

Most Papua New Guineans don't know how much tax they actually contribute to the government coffers. Having no sense of the enormity of the amount of money that they pay as tax they care less about what happens to public money. Subsequently without this knowledge they don't demand accountability and transparency from their leaders allowing public funds to be vulnerable to corruption.

#### **Recommendation**

It is recommended that IRC look into the idea of making available on periodic basis information on individual tax contribution within a certain period (every 6 months or annually) to strengthen the process of accountability and transparency. This will also encourage tax payers to hold their leaders and decision makers accountable for their decisions regarding the use of large sum of public money.

### 2) *The current declared maximum dependency for taxation purposes is outdated.*

The current maximum dependency of four (4) does not do justice to the rising cost of living in PNG and the fact that most households comprise of on average of 6 to 8 people. When undertaking this particular exercise it is important to take into consideration that the number of families living on average in a household in an urban setting may be different from a rural or semi-urban setting

#### **Recommendation**

It is recommended that IRC work with NSO to update the number of dependencies of a household regularly to ensure that the individual tax payers are able to contribute to tax based on the number of dependencies.

It is recommended that this exercise be done separately from the regular HIES undertaken by NSO given the HIES is undertaken every 10 years. It is important to update the information regularly within a reasonable timeframe like every 5 years. Lack of accurate information concerning the average number of dependence in a typical PNG home will not do justice to a lot of working class Papua New Guineans who may feel that they have been unfairly taxed given they are taking care of more dependents than anticipated by IRC or the government.

Information with regard to tax rebates need to be made public so as to allow those working class Papua New Guineans who are legitimately incurring huge cost burdens (tax payment being one of them) are able to be compensated by the government through IRC. At present not a lot of Papua New Guineans know that such a thing exist and for those that know it, the processes and the requirements may not be clear to them.

3) *The proposed increase of GST to 15% is not feasible*

The committee should not increase the GST Tax because of the number of reasons. Firstly, our informal economy is not yet developed as it is dominated by one or two industries most notably betelnut and tobacco. Increasing GST does not do justices to those majority of Papua New Guineans that thrive on other forms of informal economic activities.

Support the informal economy will provide opportunities for formal sector workers in PNG to resort to the sector to generate additional income to supplement their fortnightly wages. Thus it is unfair when the government is not supportive of the sector and yet it wants to increase GST. Increasing the GST while nurturing the growth of the informal economy should go hand in hand. The current situation indicates that any decision to increase the GST will be a total mis-match thereby adding to the high cost of living experienced by average wage and income earning Papua New Guineans. Simply increasing GST will further add to cost burden that is currently incurred by unemployed, self-employed and average income earning Papua New Guineans. Secondly, GST should not be increased as there is very little proof to show that GST has translated to improvement in the lives of the majority of the people. Most of our people in the rural areas of the country still live a life that is almost pre-historic given the progress that urban PNG and the world at large has gone through. The imbalance in terms of living standards is primarily due to corruption where much of the resources are locked-up and squandered in major urban centres of PNG. Corruption still remains a huge challenge in PNG and it is unfair when simple Papua New Guineans are required to pay for corruption rather than service delivery. Therefore, it would be deemed fair if the government addresses corruption as part of the tax reform exercise. Having a transparent and accountable government encourages the public to pay tax compared to one that is corrupt.

## **Recommendation**

The tax review committee should not increase the GST tax

### ***4) Tax imposed on locally owned firms and foreign owned business are not at parity***

There is a need to ensure that tax contribution from Papua New Guinean firms and multinational companies are at parity. As it is, multinational companies are offered all the incentives in terms of tax breaks (tax holidays), tax credits schemes and etc. This does not make sense when these are well established international firms who have the capital and financial muscle to finance investments regardless of its size and magnitude. It is understandable that these incentives are required to enable investment in key sectors of our economy to spur economic growth yet by providing incentives such as tax holidays for a period of 10-15 years these multinational companies are earning more than what they are expected to earn. However, it is also important that Papua New Guinean firms are able to get a similar treatment depending on their level of investment and risk involved so that we create a level playing field for competition to thrive within our economy. Currently, the government is in the process of developing an SME Policy and Masterplan to stimulate the SME Sector. However, if the tax regime in place is not able to allow Papua New Guinea entrepreneurs to operate “formally” they may resort to operate “informally” as a means to avoid the high cost of doing business which could be attributed to the high level of tax apart from other things.

## **Recommendation**

Tax review committee/IRC should set-up/facilitate a special working group comprising of the Department of Trade, Commerce & Industry, SME Corporation, BPNG, CIMC, IPA, Constitutional Law Reform Commission (given they are currently taking the lead in reviewing the INFORMAL SECTOR DEVELOPMENT & CONTROL ACT 2004) and Department of Community Development & Religion to agree on the definition of SME and informal economy in PNG for the sake of taxation in PNG.

Furthermore, the above committee should work on addressing various aspects of the informal economy that has tax implication.

Tax regimes imposed on businesses needs to be fair and most importantly informed by industry analysis of the constraints and opportunities.

## TAXATION AND THE INFORMAL ECONOMY IN PNG

### *1) Lack of data on informal economy contribution to the economy*

There is no accurate data on the size and scale of the informal economy and subsequently its contribution to the economy. GDP as a measure is not able to capture the informal economy. Determining the scale, size and scope of the informal economy is very important in informing the government on decisions concerning tax reforms in the country like should it tax the informal economy.

### **Recommendation**

The tax review committee/IRC need to undertake an urgent national audit of all informal economic activities to determine the size, scale and scope of the informal economy. Taxation review committee/IRC and the government of PNG in general should support CIMC and the Department of Community Development with their proposed study to undertake a nationwide stock-take of the informal economic activities in the country. The survey will be a follow-up to the 2001 survey that looked at the constraints affecting the informal economy (sector at that time). The findings from this survey may well assist the government to review the CPI Basket to ensure that it is up to date in order to generate a more up to date inflation figures.

The government to explore the use of other measurement aside from GDP to measure non-market contribution of the informal economy into the PNG Economy

### *2) The imposition of tax/fees or charges on the informal economy is unfair as it is more targeted at suppliers than consumers*

Any attempt to tax the informal economy in PNG should note that the informal economy is an outcome of the dynamics of supply and demand and its emergences and subsequent growth is usually instigated by the failure within the capitalist market system to create employment opportunities for an exponentially rising population growth. Therefore, policy responses in terms of taxation reforms should look at addressing both the demand and supply side of the problem impacting the informal economy. Its growth is also aided by the fact that it is “unregulated” and as such it escapes the strict rules and regulations that are usually developed and put in place for

compliance purposes by the government. For instance taxation and company registration laws.

### **Recommendations:**

There needs to be a “balance” when it comes to imposing tax on informal economy. It is recommended from the outset that tax being imposed on the informal economy participants should be at most done at a “minimum level” to allow its growth until its transition into the formal sector in order to broaden the tax base which at present is small and may only comprise of 15-20% of the formal sector in PNG.

On the demand side, tax should be imposed through the usage of facilities such as market facilities (which includes water, toilet, electricity, access to space), the issuance and usage of permits or licenses to operate within minimum requirements/standards in place. The UNWOMEN/NCDC Safe Cities Market Programme which has developed an electronic bill pay system allows the relevant authorities to collect fees through the use of mobile phone banking concept (in this case Nationwide Microbank “Micash”).

On supply side, tax breaks should be provided to those companies who are willing to source locally produced fresh produce, homemade bakery products and artisan products such as crafts. It is also recommended that the government encourage downstream processing and value chain through subsidizing or reducing tax for those firms that are involved in sourcing and providing technical know-how in producing quality goods and services to local farmers or micro-enterprises.

### ***3) Collection of taxes/fees for informal economy vendors is done in an ad hoc manner***

Most informal economy markets in PNG are not properly set-up and there is no proper fee collection system in place. Subsequently, there is gross misuse of these fees by purported market inspectors which has led to LLGs (both rural and urban) missing out on revenues.

### **Recommendation:**

IRC should establish a similar system like the Bill Pay system put in place by Nationwide Microbank for fees collection in Gerehu Market to collect tax for informal

market vendors. The option would be for IRC to utilize the Bill Pay system platform to collect tax by building tax into the market fees paid by vendors to NCDC or other market authorities.

The government needs to develop a policy to priorities the establishment and maintenance of existing markets as a development priority. This is because markets provide an avenue to link both formal and informal economy. This allows relevant authorities such as town and urban authorities the opportunity to tax the informal economy for the facilities that are using within the market. Right there is no law apart from the NCDC Act 2001 that clearly identifies who is responsible for the building, maintenance and upkeep of markets although common knowledge will dictate that it is the responsibility of the town and urban authorities. There is a need for the government to introduce a separate piece of policy and legislation on Market development in PNG.

While the government's focus is on setting up physical market infrastructures in strategic node areas it should also regulate mobile traders and peddlers operating within the informal economy.

*4) The government at present is not supporting the implementation of the NATIONAL INFORMAL ECONOMY POLICY 2011-2015*

The government should take full carriage of the implementation of the National Informal Economy Policy 2011-2015 and the revised Informal Sector Development & Control Act 2004 to grow the informal economy. The informal economy as it is now is too small (interms of scale and scope) for it to be taxed and needs support from the government to grow and be taxed. The informal economy is also less commercially driven as it is more driven on the "survival basis".

**Recommendations**

Given the reason stated above it is recommended that at present the informal economy (except betelnut and tobacco) should not be heavily taxed or should not be taxed at all. The government by supporting the informal economy will increase diversification and specialization within the sector. This will play to the strength of our people given most of them are agriculturalists.

The government should now give its full support to the implementation and review of the NATIONAL INFORMAL ECONOMY POLICY 2011-2015 and the review of the INFORMAL SECTOR DEVELOPMENT & CONTROL ACT 2004.

The taxation committee/IRC and the government of PNG in general should support initiatives currently undertaken by UNWOMEN and CIMC to group informal economy market vendors into groups/associations. The association will play a critical role in disseminating information regarding tax to the market vendors as well as provide opportunity for IRC to pursue regular surveys on informal economy Participant's perception on tax.

IRC should also provide its thoughts on the draft submission on the review of the Informal Sector Development & Control Act 2004 currently spearheaded by CLRC, CIMC and Department of Community Development & Religion.

#### *5) Informal squatter settlements lack of property rights for tax purposes*

Squatter settlements in cities like Port Moresby and Lae and other urban centres towns are increasing at significantly faster rate due to rapid rural urban drift given rise to by high level of economic activities. Although settlements are blamed for social ills in the society more and more settlements are now providing affordable housing to urban dwellers. Subsequently, it is helping to ease the pressure on average Papua New Guineans in the time when housing is in a total mess. Government should explore policies and legislation that addresses properties rights issues when it comes informal squatter settlements in urban towns and cities.

### **Recommendation**

The tax review committee/IRC should consult the UN Habitat, Office of Urbanisation and NCDC on the National Strategy that they are putting in place to address settlements in NCDC.

#### *6) Tax reductions are not effectively been passed onto consumers by firms*

It is a major concern in PNG that whenever the government undertakes a decision to reduce tax especially GST it does not trigger a domino effect down to the consumers. As a result inflation is exponentially rising every year.

## **Recommendation**

There is a need for IRC to develop a system where it can able to monitor and evaluate the impact of tax cuts or tax holidays on the level of inflation in the economy. At present, reduction in taxes do not necessarily lead to a reduction in costs of goods and services as often times most shops either keep the prices the same or increase it even further. IRC is encouraged to liaise with ICCG to ensure that the “trickling down effect” does take place when it comes to tax cuts.

## **TAXATION AND WAGES**

### ***1) Wage spiral indexation***

With the recent government announcement to increase the tax thresholds to K10,000 and further move to increase that level even further, we are seriously in danger of falling into the trap of “*wage spiral indexation*”. The government is encouraged not to rely heavily on increasing wages as a remedy to combat rising rate of tax and inflation in general.

### **Recommendation**

The government should instead look at other alternative such as tax breaks to combat rising imported inflation.

### ***2) Increasing Minimum Wage level can kill the tradeable sector like agriculture***

Wages increases should not only be biased towards the non-tradeable sectors like construction, retailing and manufacturing industries but should also take into consideration the tradeable sectors especially those within the informal economy and agriculture sector. Unreasonable wage increases could severely impact the agriculture sector whose revenue/profits are determined by movements in the commodity prices.

### **Recommendation**

The government should not rely heavily on wage increases to overcome inflation problems but should take a more holistic approach by addressing lowering high cost structure of the PNG Economy to ensure that the costs borne by businesses in the

country are reasonable. Currently, the high cost structure of the economy attributed to such factors as imported inflation, the limited availability of alienated land for development purposes and the increase in population have driven up the cost of doing business in PNG. Such factors then drive the need for wages to be increased which then leads on to an increase in prices of goods and services and the need for tax to be increased to reign in the rise in the level of inflation.