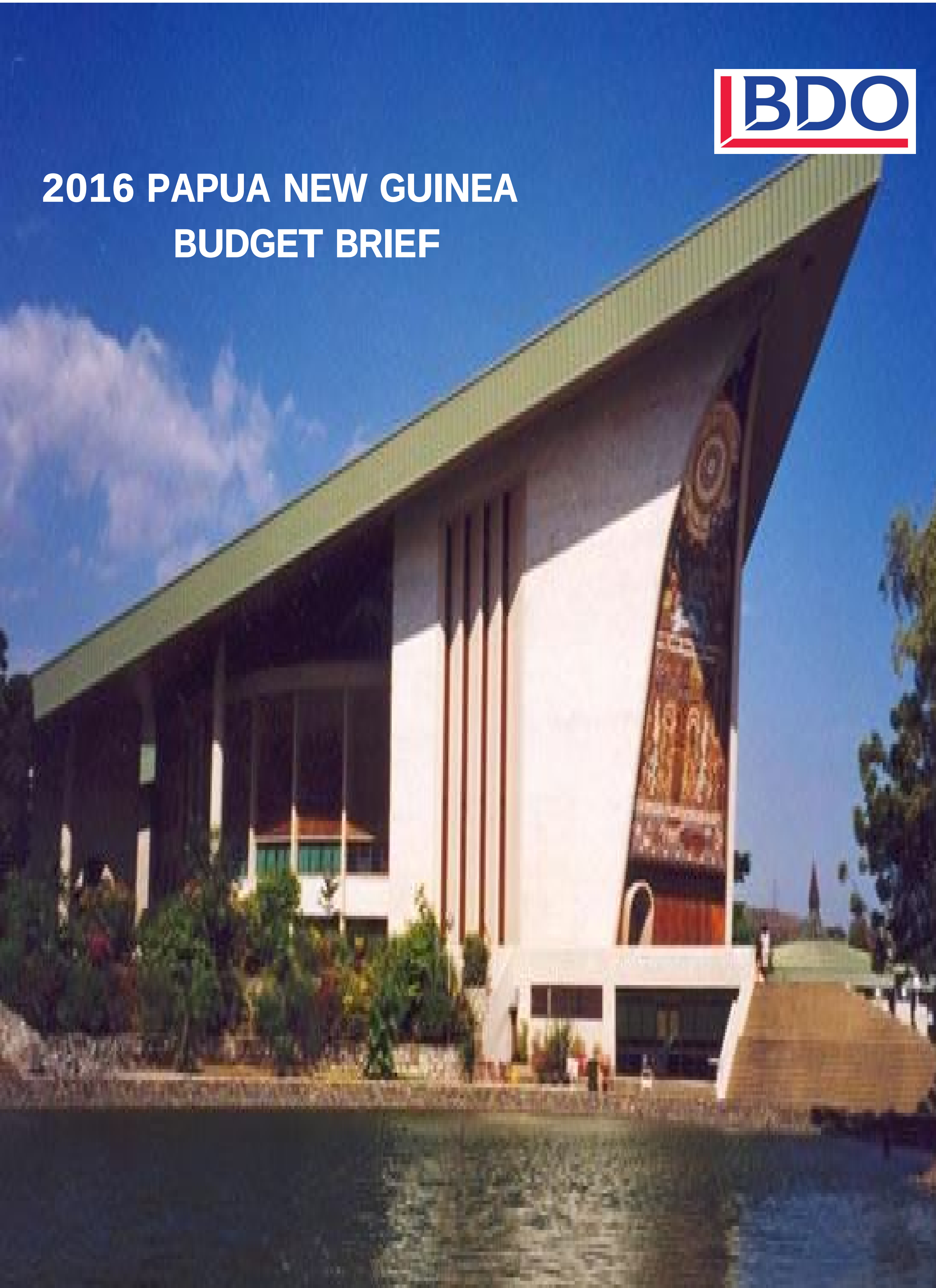
2016 PAPUA NEW GUINEA BUDGET BRIEF



BDO (formerly Guinn PKF) Budget Bulletin is a summary of the important announcements in the Budget and the effects these may have on your personal and business affairs.

Challenging Budget for 2016

The 2016 budget has been framed amidst a weak global economy, relatively slower economic growth that has been constrained by El Nino drought and low commodity prices. The theme of the 2016 budget is "**Supporting Economic Growth Through Fiscal Discipline"**. The 2016 Budget is set at K14,762.5 million (K367.2 million or 2.42% lower from the 2015 revised budget) against a revenue envelope of K12,650.1 million or a deficit of K2,112.4 million. The focus is on

- Enhancing opportunities for the people through an improved investment climate with macroeconomic stability assured with a progressive return to a balanced budget in 2020;
- expenditure prioritisation and improved quality of spending;
- structural reforms among State Owned Enterprises and the size and efficiency of the public sector;
- effective implementation of major projects through improved design, scoping, and implementation processes as well as open and competitive tenders;
- the completion of an extensive independent review of PNG's tax system with the overarching aim of improving the lives of the people of PNG through a more effective tax system;
- Continue to support policy priorities in the Education, Health, Infrastructure, Agriculture, Law and Order and SME sectors; and
- Management of the Government debt profile through capital markets, structural reforms and the issuance of a Sovereign Bond.

The 2016 Budget is accompanied by the 2015 Supplementary Budget, comprised of reductions in expenditures of K1.378 million and additional revenue measures. Cuts were made to projects that are behind in schedule in terms of implementation and idle funds that had not been used.

Economic growth in 2016 is expected to be at 4.6% (2015: actual of 9.9% and budget of 15.5%), driven by a rebound in the mining and non-mining sectors after the disappointing performance in 2015.

Inflation is expected to be 5.7% (2014: 5.5%) reflective of the expected improvement in global economy and the pickup in commodity prices.

Inherent risks in the 2016 Budget

- Global commodity price fluctuations and impacts on agricultural growing conditions, fishing and forestry sector;
- Approving of tax exemptions to individual tax payers without a guiding policy or on an ad hoc basis as well as approving Infrastructure Tax Credits without proper costing and policy advice;
- Heavy reliance of the Budget on domestic borrowings; and
- Natural phenomena such as the current El Nino event and its impact on 2016 crop for PNG's agricultural commodities, as well as water and electricity supply in the capital city and other parts of the country.

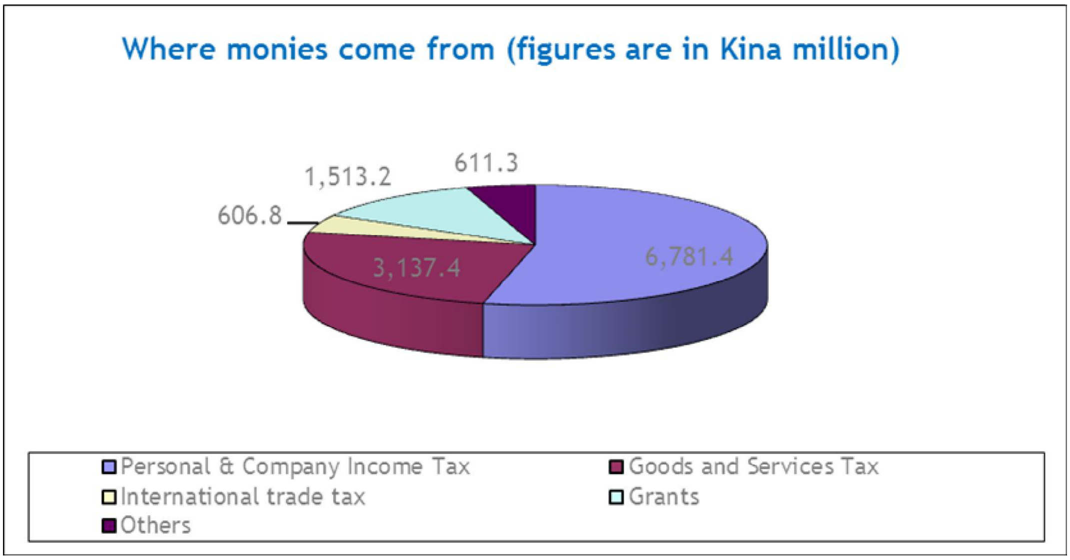
Key Economic Indicators

The key economic indicators for 2016 are projected as follows:

Real GDP growth	4.3%
Real non-mining GDP growth	3.4%
Inflation	5.7%
Interest rates (Treasury bills)	6.25%
Inscribed stock (3 years yield)	9.7%
Oil Price (US$ per barrel)	54
LNG (US$ per thousand cubic feet)	11.7
Copper price (US$ per tonne)	5,149
Gold price (US$ per ounce)	1,157
Nickel (US$ per tonne)	10,302
Cobalt (US$ per tonne)	30,000

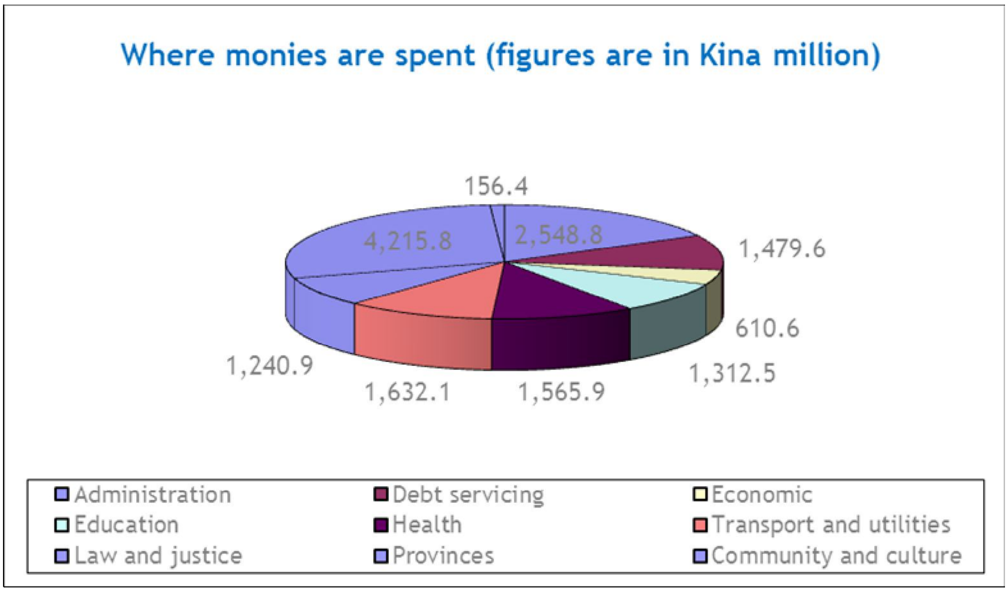
Revenue

The total revenues and grants for 2016 are anticipated at K12,650.1 million which is K12.2 million higher than the 2015 revised estimate of K12,637 million. The slight increase in revenue estimate is attributed to tax revenue and grants, which more than offsets the decrease in other revenue.



Expenditure

Total expenditure in 2016 is estimated to be K14,762.6 million. This represents K367.2 million or 2.4 per cent decrease over the 2015 Revised Budget of K15,129.7 million. The level of spending resulted in a budget deficit of K2,029.7 million or 3.7% of GDP and will bring total debt in 2016 to 35.8 per cent of GDP. The source of funding for the above expenditure will be as follows: (a) Government funds of K12,698.3; (b) loans of K922.0 million; and (c) Donor funds of K1,142.2.



Taxation

Tax amendments are effective 1 January 2016 unless an alternate date is specified.

Introduction of a GST deferral scheme for imports

The current GST Act provides for GST to be imposed on goods that are imported. The GST paid by importers is later refunded to the taxpayer after they lodge their GST return. The above arrangement reduces cash flow for businesses and creates unnecessary administration costs for IRC and PNG Customs.

Under the new scheme, the payment of a GST liability on imports would be delayed until the business lodges its next GST return with the IRC, at which time there would be a GST credit available.

Removal of discretionary GST exemptions by the Head of State

Currently, the Head of State, acting on the advice of NEC, is able to exempt or reduce the rate of GST. Such discretionary power has been repealed to ensure that the application of GST remains efficient, non-distortionary and prevents revenue leakage.

Suspension of the negotiation of Double Tax Agreements (DTAs)

DTAs are designed to remove double taxation that can act as a barrier to international investment. These agreements facilitate collaboration between tax authorities, especially through providing the legal basis for exchange of taxpayer information. PNG has DTAs with Australia, Canada, China, Fiji, Malaysia, Singapore, Korea and the United Kingdom.

The Government will postpone entering into new DTA negotiations until after the Base Erosion Profit Shifting report can be fully considered. Once the BEPS report has been fully considered, it may also be appropriate to renegotiate PNG's existing DTAs to ensure PNG gets its fair share from the treaties.

The Multilateral Convention on Mutual Administrative Assistance in Tax Matters

The Multilateral Convention on Mutual Administrative Assistance in Tax Matters allows collaboration between tax administrators to address offshore tax evasion. PNG has recently become a member of the Global Forum on Transparency and Exchange of Information, which is a prerequisite to joining the Multilateral Convention.

Technical and Administrative Amendments

All technical and administrative amendments are effective 1 January 2016 unless an alternate date is specified.

Repeal of Section 6A of the Income Tax Act 1959 (ITA)

Section 6A of the ITA provides for the removal of the Commissioner General from office. This is now provided for in the Internal Revenue Commission Act 2014 (IRC Act) and should have been repealed when the IRC Act commenced. This amendment will repeal section 6A of the ITA to remove the duplication of the removal process of the Commissioner General.

Repeal of Section 6B of the ITA

Section 6B provides for the appointment of the Commissioner for Taxation. This is now provided for in the IRC Act. This amendment will repeal section 6B of the ITA to remove the duplication of the appointment process for the Commissioner for Taxation.

Amend Section 196B of the ITA

Replace the reference 'Section 196D(1)' with the word 'Division'. This will make the law clear that the income derived from a prescribed contract defined in Division 14A is income sourced in PNG and is subject to PNG tax.

Amend the Income Tax Regulation 1959 (IT Regulation)

Repeal regulation 91A(2) and paragraph (b) of the definition of 'eligible payment' in section 354K. When changes were made in 2013 to limit the industries that required a Certificate of Compliance, Regulation 91A(2) was inadvertently not removed. Contracts for the hire or leasing of equipment no longer require a COC.

Amend the GST Act paragraphs 72(1)(a) and 72(1)(b)

Clarify that the IRC has four years to amend a GST return from either the date the return is lodged or the date of the assessment, whichever is the earlier.

Papua New Guinea Taxation Review

The Tax Review Committee undertook an extensive review of PNG's taxation system, with the aim of improving the lives of the people of PNG through a more effective tax system. New tax measures as a result of the tax review will be available in the 2017 budget.

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