



Internal Revenue Commission - Taxation Circular

Taxation Circular TC 2013/3

Subject: Application of Tourism Accommodation Incentive under Division 9B of the *Income Tax Act 1959*

PURPOSE

1. This Taxation Circular clarifies the Commissioner General's view on the application of Tourism Accommodation Incentive under Division 9B of the *Income Tax Act 1959* ("the Act") and will cover:
 - the meanings of a "*large scale tourist accommodation facility*" and a "*substantially improved large scale tourist accommodation facility*" under the Act;
 - what is meant by temporary accommodation for purposes of Division 9B;
 - what it means to be deriving taxable income solely from the operation of a large scale tourist accommodation facility or a substantially improved large scale tourist accommodation facility;
 - the conversion method for transactions where a US Dollar amount must be ascertained for the purposes of Division 9B; and
 - the application process that an eligible taxpayer must follow when applying for this incentive under the Act.
2. All legislative references in this Taxation Circular are to the *Income Tax Act 1959* unless otherwise specified.



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INTERPRETATION

Background

3. The introduction of incentives in Division 9B was part of the Government's initiative to encourage investment in the tourism sector of the economy.
4. Division 9B became effective on 1 January 2007 and applies to qualifying taxpayers who build new large scale tourist accommodation facilities in Papua New Guinea, or taxpayers who improve existing facilities in certain circumstances.

Operative Provisions

5. All qualifying taxpayers who are registered with the Commissioner General are to be taxed at a concessional tax rate of 20%.¹
6. Only taxpayers that derive their taxable income solely from the operation of a large scale tourist accommodation facility, or a substantially improved large scale tourist accommodation facility are eligible to apply for this concession under Division 9B.
7. The concessional tax rate will be applied from the year income was first derived from the operation of the accommodation facility for a period of 14 years.

Large Scale Tourist Accommodation Facility

8. Section 154E provides conditions that need to be met to constitute a large scale tourist accommodation facility for purposes of Division 9B. These conditions are:
 - a) the facility must be a hotel, a motel, ship, inn or another place that is located in Papua New Guinea;
 - b) the taxpayer must use the facility to carry on a business that charges a fee for provision of temporary accommodation;
 - c) the facility must have 100 rooms or more for customer to hire for use as temporary accommodation;
 - d) the construction of the facility must have commenced between 1 January 2007 and 31 December 2011; and

¹ See Section 6D of the *Income Tax and Dividend (Withholding) Tax Rates Act 1984*.



- e) the cost of constructing the facility is US \$7million or more.

Substantially Improved Large Scale Tourist Accommodation Facility

9. Section 154E sets the following conditions for a place to be a substantially improved large scale tourist accommodation facility:
 - a) the facility must be a hotel, motel, ship, inn, or another place located in Papua New Guinea;
 - b) it must be used by the taxpayer to carry on a business that charges a fee for provision of temporary accommodation;
 - c) The facility must have undergone capital works including refurbishment and extension between 1 January 2007 and 31 December 2011;
 - d) the cost of the capital works must be US\$7 million or more; and
 - e) The refurbishment and extension results in the provision of 100 rooms or more at the facility.
10. The Act does not exclude an existing facility with more than 100 rooms from being a “substantially improved large scale tourist accommodation facility” where it satisfies all other criteria set by the Act. Therefore, an existing accommodation facility may have less than, or more than 100 rooms prior to the commencement of the refurbishment and extension exercise. Extensions or refurbishment of the facility may include (but is not limited to) renovations and restyling of rooms, or building of additional rooms on the premises.
11. It is possible for facilities with more than 100 rooms to extend or refurbish parts of the facility such as conference rooms, public bar, restaurant, or any part of the facility that is accessible and used by the in-house guests and still qualify as a substantially improved facility if they meet the other requirements under the definition of a “substantially improved large scale tourist accommodation facility”.
12. The Commissioner General considers the year in which income is first derived from a substantially improved facility as the year in which the extension work or the refurbishment work is completed and that part of the facility becomes available for use by guests.

Starting Date for Construction and Capital Works

13. The starting point for the construction of a facility, refurbishment, or extension of a facility, is to be determined from the contract for works between the taxpayer and the contractor(s) for the works.



14. If there is no date specified in the contract for works, then the taxpayer bears the burden of demonstrating to the Commissioner General the date on which construction, refurbishment, or extension actually commenced.

Sole Taxable Income

15. The Act requires a taxpayer to derive all his taxable income from the operation of a “large scale tourist accommodation facility” or a “substantially improved large scale tourist accommodation facility” in order to be eligible for the incentive under Division 9B.
16. The Commissioner General is of the view that the taxpayer who operates the facility as a temporary accommodation facility need not necessarily own the facility in order to operate a business that provides temporary accommodation. The provision is wide enough to cover arrangements where the facility is leased to another person (taxpayer) to operate it as a place where temporary accommodation is provided to guests for a fee (refer to Example 4).

Income from Related Activities within the Facility

17. The Commissioner General understands that many taxpayers which operate tourist accommodation facilities may derive income from a broad range of activities undertaken within the facility and not just from the provision of rooms. Where these are integral to the provision of temporary accommodation, then this would still fall within the “sole taxable income” requirement. Such activities may include on-site restaurants or cafes, laundry services, leasing of part of the facility for ATMs or artifact shops, bars, souvenir shops, or provision of wireless internet services. Taxable income derived from these activities logically comes from the operation of the facility. Conferencing facilities may also be acceptable, but these will be a matter of fact and degree and will depend upon the nexus with the provision of short term accommodation in the facility.
18. However, if a taxpayer carries on any business operation that derives income, but is distinctly independent from the provision of temporary accommodation within the facility, then the sole income requirement would be breached. This may arise intentionally or unintentionally where the other operations are not incidental to the provision of temporary accommodation (refer to Example 7).
19. Each case would be determined on its own facts when such a situation arises. Taxpayers are encouraged to discuss their specific circumstances with the Commissioner General should there be any doubt.

Investment and Other Sources of Income

20. It is likely that some taxpayers will have small amounts of cash in operating accounts with commercial banks and may derive some form of income from interest received on such



accounts. This is logically part and parcel of operating a tourist accommodation facility and would not breach the sole taxable income requirement. However, income received from term deposits, shares, or other forms of investment will most likely be considered as breaching the sole taxable income requirement under the Act. In the event of dispute, the onus is on the taxpayer to demonstrate that the income received meets the “sole taxable income” requirement.

21. Theoretically, it may be possible for a taxpayer to operate two accommodation facilities if both facilities qualify under the Act. Although, practically that may be a rare possibility and taxpayers must note that the term of the concessions would cease when the earliest qualifying facility’s term ceases if the two facilities qualify for concession at different points in time (Refer to Example 6).
22. Furthermore, the sole taxable income requirement may require some taxpayers who currently operate more than one accommodation facility (where only one is a qualifying facility), or where they would otherwise breach the “sole taxable income” requirement to undergo a corporate restructure to ensure that the tourist accommodation facility is the only source of income for the taxpayer who is operating it.

Temporary Accommodation

23. The phrase “*temporary accommodation*” is not defined anywhere in the Act and therefore assumes its ordinary meaning. Ordinarily, it would mean that the rooms would be provided by the taxpayer to a guest for a limited time, that is, to satisfy a passing need for that room by a guest.
24. The Oxford Dictionary² defines “temporary” as “lasting or meant to last only for a limited time”.
25. The Oxford Dictionary³ also defines “*accommodation*” as “*lodgings; a place to live*”.
26. The combined meaning of the two words when read together would mean a place to live for only a limited time. The Commissioner General is of the view that this is the intended meaning of the term “*temporary accommodation*” as used in Division 9B.
27. The temporary nature of the accommodation provided by the taxpayer allows for the guest to be entitled to occupy the facility for a short term. The guest need not actually occupy the facility for his right to occupy it to exist. However, the right to occupy the facility does not extend to cover situations where the guest can use the facility as his residence.

² Australian Concise Oxford Dictionary, 5th Edition, Oxford University Press (2011).

³ *Ibid*



28. Where parts of the facility are occupied as a residence, or are intended to be occupied as residence, that facility will not be considered as temporary accommodation facility for purposes of Division 9B⁴. This point is based on the Commissioner General's view that "a residence" clearly implies a building with a significant degree of permanence of occupation.⁵
29. The intention of the taxpayer must be to provide temporary accommodation to his guests. That intention is a factual matter which will be inferred from the manner in which the taxpayer operates the facility. Other factors that may be taken into account by the Commissioner General include (but not limited to) –
- a) Characteristics of the Rooms – the form and fit-out of the rooms.
 - b) The types of services provided to the rooms – meals, house-keeping, etc.
 - c) Status of the occupant – lessee, licensee, tenant, guest, etc. This can be drawn from the legal relationship of the occupant with the temporary accommodation provider.
30. The Commissioner General would generally not raise any issue where a guest is entitled to stay in the tourist accommodation facility continuously for less than three months.

Conversion of US Dollar to PNG Kina

31. One of the conditions under the Act for a taxpayer to be eligible for concession under Division 9B is for the taxpayer to spend a minimum of US \$7 million on the construction or capital works on the tourist accommodation facility. The Act does not provide how the Commissioner General will convert Papua New Guinea Kina into the US Dollar for purposes of Division 9B.
32. Generally, a taxpayer should convert the value of its expenses that were incurred using the daily exchange rate for the date of payment. The Commissioner General understands that this practice might be administratively burdensome for some taxpayers and would accept the use of half-yearly average rate or the annual average rate where the taxpayer has made multiple payments within a half-year period or the entire year, provided the payments were made consistently throughout the period and represent a fair calculation of the costs in US Dollars.

⁴ The Commissioner General understands that some tourist accommodation provider provides onsite accommodation for some of their critical employees. Such arrangements would not disqualify the facilities from being a large scale tourist accommodation facility or a substantially improved large scale tourist facility.

⁵ *Marana Holding Pty Ltd v Federal commissioner of Taxation* [2004] FCA 233 per Beaumont J at paragraph 21; *Urdd Gobaith Cymru v Commissioner of Customs and Excise* [1997] V & DR 273 (at 279).



33. The annual and half-year average exchange rates can be calculated from the daily exchange rates that are available from the Bank of Papua New Guinea and can be accessed online through their website: www.bankpng.gov.pg. The rate to be used is the mid-market rate.

Registration Process for Taxpayers

34. Any taxpayer that wishes to utilize this concession must make a written application to the Commissioner General providing the following details:
- the name of the taxpayer;
 - the name and location of the tourist accommodation facility;
 - the ownership structure of the tourist accommodation facility;
 - financial statements for prior years where relevant;
 - any other assets owned by the taxpayer;
 - the number of rooms to be used for tourist accommodation within the facility;
 - the date when the construction or extension or refurbishment of the facility commenced and proposed date of completion;
 - a summary of the proposed development or extension or refurbishment and anticipated outcome when the works are completed;
 - a summary of the cost of construction, refurbishment or extension of the facility;
 - the preferred method of currency conversion from PNG Kina to US Dollar or vice versa that would be used by the taxpayer and why that methodology would be appropriate in the circumstances.
35. The Act does not indicate that a specific form be used for purposes of making an application for this concession. A standard letter addressed to the Commissioner General with supporting documents would be sufficient as an application.

EXAMPLES

Example 1

36. Grog's Hotel is in Port Moresby. The construction began in February 2008 and was completed in August 2011. It has 120 rooms for temporary accommodation, and was built at the cost of K73



million. Grog's Hotel meets the definition of a large scale tourist accommodation facility in the Act because:

- It is a facility that charges a fee for temporary accommodation.
- It has more than 100 rooms.
- Its construction commenced between 1 January 2007 and 31 December 2011.
- The cost of constructing the facility is more than US\$7 million using the annual average rates of K1= US\$ 0.35 (2008), K1= US\$ 0.33 (2009), K1=US\$ 0.37 (2010), for each year and K1 = US\$ 0.37 for the last half-year of construction (first half of 2011) in which expenses were incurred.

37. The calculations for the above conversion in the example would be as follows:

FINANCIAL YEAR	AMOUNT COST IN KINA	USD CONVERSION
2008	K10 million	PGK 10,000,000 x 0.35 = USD 3,500,000
2009	K45 million	PGK 45,000,000 x 0.33 = USD 14,850,000
2010	K15 million	PGK 15,000,000 x 0.37 = USD 5,550,000
2011	K3 million	PGK 3,000,000 x 0.37 = USD 1,110,000
TOTAL	K73 million	USD 25,010,000

38. The annual and half-year average exchange rates were used because many payments were made over the course of a single year and it would be onerous on the taxpayer to use the daily rate for the date of payment of each expense incurred over the course of the construction.

Example 2

39. Kirikiri Hotel has 85 rooms in 2008. In March 2009, the facility underwent an extension. The extension was for an additional 70 rooms to be built. The total cost was slightly over US\$8 million. The work on all additional rooms was completed in December 2010. Two installment payments totaling K22 million were made to the main contractor. The first payment of K10 million (at the exchange rate of K1= US\$ 0.4032) was on 12 January 2009 and the second payment of K12 million (at the exchange rate of K1= US\$ 0.3367) was on 26 June 2010. The taxpayer used the daily exchange rate for each respective date the payments were made.



40. The facility charges a fee for providing temporary accommodation to guests. It was refurbished and extended between 1 January 2007 and 31 December 2011. There are more than 100 rooms that are available for use as temporary accommodation.
41. Kirikiri Hotel therefore meets the definition of a substantially improved large scale tourist accommodation facility under the Act.

Example 3

42. Beaver Falls Resort in Tari has 85 rooms which are let out to customers for temporary accommodation. In November 2009, it decided to extend the facility to include a casino to cater for an anticipated increase in royalty payments from the PNG LNG Project. Work commenced immediately and the casino was completed and operational in January 2011. The casino operations have since become the major source of income for the hotel, generating approximately K10m of taxable income annually, while the other components of the Beaver Falls Resort have not generated any taxable income for the past several years.
43. The total cost of the extension was US\$25 million based on the annual average exchange rates for each respective year of construction that expenses were incurred.
44. Beaver Falls Resort is not eligible for incentives under Division 9B because it fails to meet to the requirement for 100 rooms. Furthermore, the casino operations have now become the major source of income for the hotel and it is arguable that this is effectively a separate operation from the provision of accommodation in the Beaver Falls Resort.

Example 4

45. Jolly Limited owns a resort facility on the island of Newton. The facility meets the definition of a large scale tourist accommodation facility.
46. Jolly limited leases the resort facility to Victory Limited to operate as a hotel which provides temporary accommodation to guests. The income derived by Jolly Limited is from the leasing of the resort facility to Victory Limited (Head Lessee), thus, it is not eligible to apply for concession under Division 9B.
47. Victory Limited, as the operator of the facility and derives its taxable income solely from the operation of that facility. Victory Limited is therefore an eligible taxpayer for purposes of Division 9B.

Example 5

48. Star Fish Resorts operates one hotel each in Kimbe, Rabaul, and Alotau.



49. In 2009, their hotel in Rabaul underwent major extension and refurbishment. The extension and refurbishment work made the hotel in Rabaul fall within the definition of a substantially improved large scale tourist accommodation facility, except that Star Fish Resorts was deriving income from two other hotels that do not meet the definition of a “large scale tourist accommodation facility”, or a “substantially improved large scale tourist accommodation facility.”
50. Before applying for the concession, Star Fish Resorts underwent a corporate restructure. Blue Fish Limited was incorporated as a subsidiary of Star Fish Resorts and the hotel in Rabaul was transferred to Blue Fish Limited. Blue Fish Limited is now eligible to apply for concession under Division 9B, since it now meets the sole taxable income requirement.

Example 6

51. Numori Hotels operates one hotel each in Kavieng and Vanimo.
52. In March 2007, their hotel in Kavieng underwent a major extension and refurbishment. The extension and refurbishment work was completed in July 2008. The extension and refurbishment made the hotel in Kavieng fall within the definition of a “substantially improved large scale tourist accommodation facility.”
53. Numori Hotels Ltd was granted the tourism concession for the hotel in Kavieng effective from 1 January 2009 by the Commissioner General and its taxable income was taxed at 20%. (Note: Since the hotel qualified for only part of the 2008 year of income, the Commissioner General’s view is that the concession can only be applied to the following year of income. This is because Submarine Motels would not have satisfied the sole taxable income test in the 2008 year of income.)
54. In December 2009, Numori Hotels Ltd began constructing a new hotel in Vanimo. In December 2011, construction for the hotel in Vanimo was completed and the hotel derived its first income in January 2012. The hotel in Vanimo meets the definition of a large scale tourist accommodation facility and was granted the concession under Division 9B effective from 1 January 2012.
55. Despite a gap of three income years between the grant of concession for the hotel in Kavieng and the hotel in Vanimo, Numori Hotels still satisfy the sole income requirement in the 2012 year of income.
56. However, taxpayers should note that the concession for both hotels would cease at the expiration of the concession originally granted to Numori Hotels Ltd in relation to its hotel in Kavieng. This is because when the concession for the hotel in Kavieng expires, it will mean that Numori Hotels Ltd would not be deriving their taxable income solely from a “large scale tourist accommodation facility” or a “substantially improved large scale tourist accommodation



facility” even though the hotel in Vanimo would still be eligible if it were in a separate holding company.

Example 7

57. Kapul Limited runs a large scale tourist accommodation facility known as Palai Resort located on the beachfront on Manus Island. They operate a dive boat which berths at Palai Resort and caters for dive tours for guests and non-guests at Palai Resort.
58. Kapul Limited is deriving income from the operation of a large scale tourist accommodation facility and also from the dive tours. Kapul Limited is not eligible for incentive under Division 9B because Kapul Limited has breached the sole income requirement under the Act. The dive tours are distinct from and not incidental to the provision of temporary accommodation at Palai Resort.

DATE OF EFFECT

This Circular represents the preliminary, though considered view of the Commissioner.

This Circular applies to arrangements that were begun to be carried out from 1 January 2007.

AUTHORISATION

Authorised by BETTY PALASO - Commissioner General of Internal Revenue Commission

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BETTY PALASO, OBE

ISSUED

30th July 2013



REFERENCES

Related Taxation Circulars:

NIL

Subject References:

- Tourism Accommodation Incentive
- Substantially improved large scale tourist accommodation facility
- Large scale tourist accommodation facility
- Sole Taxable Income
- Temporary Accommodation

Legislative References:

"Income Tax Act 1959"

"Income Tax and Dividend (Withholding) Tax Rates Act 1984"

Case References:

Marana Holding Pty Ltd v Federal commissioner of Taxation [2004] FCA 233

Urdd Gobaith Cymru v Commissioner of Customs and Excise [1997] V & DR 273

Other References:

Australian Concise Oxford Dictionary, 5th Edition, Edited by Bruce Moore, Oxford University Press (2011)