KPMG

Kundu

March 2022

Foreword

Welcome to the March 2022 Kundu!

This month we analyse BPNG's Monetary Policy Statement. We also focus on what companies could implement to improve their financial management and ultimately the audit opinions issued on their accounts.

Please be mindful that due to technical and other issues there is a current delay in the issuance of work permits.

In the tax world, GST is a hot topic this month with government plans to remove GST on certain products, which may then require suppliers to effect certain system configuration changes. Another area which has generated a lot of interest this week has been the IRC's publication of a comprehensive list of tax offences – quite an interesting read! Finally, please ensure that you as taxpayers are lodging in time and using the correct documentation, while at the same time the usage of the myIRC Portal is also encouraged, as far as is possible.

KPMG in PNG has dedicated in-house specialists in all the following areas: internal audit/risk, visa migration, corporate finance, management consulting, IT advisory, fraud investigation as well as tax and assurance. As such we are well placed to provide a truly multi-disciplined approach to business advisory.

Please enjoy this month's Kundu and reach out to us at kmcentee@kpmg.com.au if you would like to see KPMG cover specific topics in future editions.

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Analysis of BPNG's March 2022 monetary policy statement
by Wayne Osterberg, Director, Advisory Services

The Acting Governor of the Bank of PNG delivered the Monetary Policy Statement (MPS) this week. The recovery in economic activity in 2021 from the ongoing COVID-19 Pandemic is expected to continue in 2022. However, the challenges from the pandemic, supply-chain disruptions, high oil prices and inflation, and the current Russia-Ukraine war could derail the recovery. The Central Bank will maintain the accommodative stance of monetary policy for the next six months to September 2022 to support the economic recovery. It will continue to monitor the ongoing concerns of high inflation and its impact on growth and employment as well as developments in other macroeconomic indicators. The Central Bank may adjust its policy stance if required to achieve its objectives and ensure macroeconomic stability.

Key Area	Comment
Real GDP Growth	Expected to further pick-up in 2022 from -2.4% in 2021 to 2.0% in 2022 reflecting increased activity in both the mineral and non-mineral sectors. In the medium term, growth is expected to continue reflecting the reopening of the Porgera mine. Non-mineral sector growth in 2021 was 2.5% but 2022 forecasts reflect higher production and prices for most export commodities and higher government spending. A delayed restart of Porgera would impact the medium-term outlook.
Central Banking Act	The amendments to the Central Banking Act have broadened the objectives of the Central Bank to include employment and economic growth, and efficient and responsive banking services to the Government. It has also allowed for improvement in the governance framework and increased financing to the Government. The amendments allow for fiscal dominance over monetary policy where BPNG can now fund Government Budget deficit and poses the challenge for monetary policy to pursue these multiple objectives.
Fiscal Policy	The Government continues its expansionary fiscal policy in 2022 with a Budget deficit to be financed mainly from external sources. The level of debt is projected to increase further, raising concerns about debt sustainability. The preliminary fiscal outcome to Nov 2021 showed a deficit of K3.4bn vs K5.6bn for the same period to Nov 2020. It is important that GoPNG improves its revenue raising efforts and prudently manages its expenditures.
FX	FX inflows in 2021 were K22.7bn (K4.9bn in GoPNG borrowings and K17.7bn in export and other flows). Demand amounted to K19.9bn and accordingly Central Bank intervention was required to meet K2.4bn of demand. BPNG is mindful of the imbalance between inflows and demand and is committed to ensure that the FX market will continue to function and that orders are met within a reasonable timeframe.
Money Supply	The projected growth from 11.8% in 2021 to 14.7%in 2022 in total money supply is mainly driven by the expansionary fiscal policy contributing to high liquidity in the banking system. Net Foreign Assets increased due to external borrowing and Net Domestic Assets reflected increased holdings of government securities. Private sector credit and monetary base are projected to increase in 2022 to support the recovery in the non-mineral sector. In the medium term, increase in monetary aggregates will moderate reflecting the Government's fiscal consolidation strategy.
Inflation	The Bank forecasts annual headline inflation to remain elevated at around 5.0% in 2022. The imported inflation from higher oil and food prices would be largely responsible for domestic inflationary pressures. Over the medium term, inflation is expected to ease to around 3.5%.
Balance of Payments	The Bank projects Balance of Payments surpluses of K390m in 2022 and in the medium term due to surpluses in the current account. However, most of the surpluses in the current account, mainly from mineral export receipts, do not flow back into the domestic economy as allowed for under their respective Project Development Agreements (PDAs). For the country to benefit, the State should review the current regime governing the PDAs to maximize gains to the nation. The outlook would improve further if the other major extractive projects (in addition to Porgera) were to come on stream. Foreign reserves at 31 Dec 2021 stood at US$3.2bn vs US$2.7bn at end Dec 2020 – 9 months of import cover.

Source – Bank of Papua New Guinea Monetary Policy statement March 2022 & KPMG Analysis

Plans to improve financial management and audit opinions
by Lizette Theron, Senior Manager, Tax, Transactions and Accounting Services

Financial management means planning, organising, directing and controlling the financial activities of a company. Financial management includes audit readiness preparation, which refers to the strengthening of internal controls and the improvement of financial practices, processes, and systems so there is reasonable confidence that information can withstand an audit by an independent auditor.

Many business failures have been attributed to the inability of financial managers to plan and control properly all aspects of financial management. In particular, small and medium-sized entities (SMEs) are facing difficulties in their development due to the lack of financial resources and management experience.

The SME-accountant relationship is regarded by many as a necessity, because SMEs are required to produce documentation such as audited financial reports to comply with laws and regulations, and SMEs are obliged to engage accountants to produce these reports and potentially to interpret and analyse financial statements.

The need to prepare a complete set of financial statements increases as an entity progresses from small to medium size. It is at the medium-size stage that financial reporting will be useful to internal and external users. External users include lenders and suppliers of assets and inventories. In most cases owner-managers prepare financial statements in SMEs and many are not financially literate.

They may encounter several challenges that hinder their development opportunities, such as poor managerial skills, unqualified staff and reduced access to finance due to reporting and information deficiencies. While access to finance is critical for SMEs to survive and grow, unfavourable audit reports contribute to lenders' reluctance to provide finance to SMEs.

Financial institutions and investors take audit opinions seriously and will be reluctant to do business with companies with adverse audit opinions and disclaimers of opinion. In order for SMEs to improve their financial management and obtain more favourable audit opinions, corrective actions must be taken to address control weaknesses, non-compliance and other audit findings.

An audit action plan (AAP) will assist companies in preparing corrective actions specifically to address audit findings, questionable transactions, reportable conditions, and material weaknesses mentioned in the audit report. Other issues such as non-compliance with laws and regulations, absence of documented policies and procedures or non-adherence to best practices in internal controls can be addressed in a financial management improvement plan (FMIP).

Preparation of a FMIP will inform company management of the deviations and challenges that exist in the company's financial management status quo, measured against accounting and internal control best practice, as well as the audit findings.

The main purpose of a FMIP is therefore to list the tasks that need to be undertaken to successfully achieve full compliance and audit readiness. This could contribute towards enabling auditors to obtain sufficient audit evidence as a basis for a more favourable audit opinion than in previous years.

A typical FMIP (which may incorporate an AAP, focusing on specific audit findings) should address at least the following:

- Governance, monitoring, and communication
- Asset management
- Supply chain management
- Risk management
- Control activities
- Internal audit management
- Information systems management

Whether the FMIP is developed in-house or by external consultants, in order to ensure smooth implementation and timely monitoring, each specific finding or weakness to be addressed should give rise to planned activities, further divided into manageable steps, and assigned to individuals or external consultants, with specific due dates for completion.

A well-prepared FMIP provides clear outputs and timelines. Management would use the FMIP to review progress and manage actively the implementation of activities by organising regular meetings to check on progress, constraints, risks faced by their teams in the implementation of the tasks, and solutions to address these.

Change to GST rate on certain products

Proposed GST changes mentioned by the Treasurer in Parliament last week have attracted some attention by media and industry bodies. The Treasurer announced that to address inflationary pressures for the public they intend to remove GST on certain products such as rice, cooking oils, fuels, tinned fish, feminine hygiene products and other food staples. Although no legislation has been tabled as yet is it expected the reduction may be introduced in April and last around six months. Usually this would be achieved through the application of a zero rate of GST to these products. The change will only be effective if the reduction is actually passed on to consumers. For suppliers it would mean a re-configuration of their system to ensure the zero rate is applied.

IRC publish schedule of tax offences and penalties

In line with its increased focus on tax compliance IRC have published a guide to the various tax offences and their associated penalties. The penalties may be criminal and/or administrative in nature. The guide is pretty comprehensive and runs to 38 pages covering offences under the Income Tax Act, GST Act, Stamp Duty Act and Tax Administration Act. For taxpayers who are behind on their taxes or otherwise in default this is a reminder that it is better to proactively bring taxes up to date as it can lead to more favourable treatment and penalty outcomes.

Tax return forms and income tax deadlines

IRC issued a recent reminder to taxpayers to ensure they are using the correct tax forms as their systems are not configured to deal with the older forms and may lead to input errors. On this note, the IRC recently issued the new Form C for the 2021 income tax returns. This is available on the IRC website and is broadly similar to recent years. IRC also published the expected due dates for taxpayers lodging through a tax agent – tax returns for a 31 December period are due by 30 June 2022 (taxable returns) or 31 July 2022 (non-taxable returns). Taxpayers should plan to meet these deadlines as IRC have been much stricter in recent years in granting individual taxpayer extensions and we cannot expect that the Covid extensions of recent years will be available again this year.

myIRC portal

While IRC continue to encourage the use of the myIRC portal it currently has limited functionality and allows payment through certain cards only (and not through bank transfers). We understand that some of these issues will be addressed over time. On the positive side IRC and the software developers have been open to meeting with and hearing from tax agents on their user experience and areas for improvement.

Potential delays in work permit approvals

Recent weeks saw the breakdown of the work permit card printing machine which led to delays in the issue of work permit cards. Now it seems this is to be followed with further delays lasting possibly one to two weeks due to a change in signatories internally. As ever, it is important to lodge applications and renewals for work permits and visas well in advance of the date required to cater for these sorts of eventualities which unfortunately can often arise

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Our social media presence

As usual, you may access our regular multi-disciplined thought leadership pieces, newsletters and updates on our KPMG PNG LinkedIn page. Also connect via our webpage www.kpmg.com.pg and Facebook https://www.facebook.com/pngkpmg/

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