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PAPUA NEW GUINEA

REPORT ON THE OBSERVANCE OF STANDARDS AND CODES (ROSC)

ACCOUNTING AND AUDITING MODULE

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EXECUTIVE SUMMARY

- I. The main purpose of the Report on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A) review exercise, conducted at the request of the Government of Papua New Guinea, is to propose policy recommendations that will strengthen the institutional framework that underpins accounting and auditing practices in the country.** Implementation of the policy recommendations will enhance the quality of financial reporting for corporations – a key pillar that directly contributes to enhancing the business environment and the advancement of governance and financial accountability in both private and public sector entities.
- II. The ROSC A&A review for Papua New Guinea focuses on the strengths and weaknesses of the accounting and auditing environment that influence the quality of corporate financial reporting, and involves both a review of mandatory requirements and actual practices.** The international standards that have been used as reference points for the preparation of this report are International Financial Reporting Standards (IFRS)¹, clarified International Standards on Auditing (ISA)², and international good practice in the field of accounting and auditing regulation.
- III. It is critical at this stage of development that PNG manage its resources well.** The PNG-LNG project shipped its first cargo in June 2014 and it is expected the LNG project to expand GDP by as much as one-quarter in 2014 and 2015, and national income by about 8 per cent. This requires significantly stepping up the quality, compliance, and enforcement of benchmark financial reporting and auditing practices. This is a key development challenge for PNG to channel this windfall revenue into investments that positively impact peoples' lives.

Box 1: Papua New Guinea at a glance

Papua New Guinea (PNG) is an ethnically and socially diverse young nation of seven million people, speaking over 840 languages, poised on the verge of a challenging period of opportunity and risk. It is a lower income country, with a GNI per capita of US\$2,010 in 2013.³

PNG continues to face a number of socioeconomic challenges, which are reflected in its Human Development Index⁴ (HDI) of 0.491 (up from 0.324 in 1980), which gives the country a rank of 157 out of 187 countries with comparable data. The HDI of East Asia and the Pacific as a region increased from 0.457 in 1980 to 0.703, placing PNG below the regional average.

¹ In this report, IFRS refers to the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), the International Accounting Standards (IAS) issued by IASB's predecessor the International Accounting Standards Committee (IASC), and the applicable interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC).

² ISAs are issued by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC).

³ Atlas method, in current US\$. Source: World Bank.

⁴ Each year since 1990, the Human Development Report has published the [Human Development Index \(HDI\)](#) which was introduced as an alternative to conventional measures of national development, such as level of income and the rate of economic growth. The HDI represents a push for a broader definition of well-being and provides a composite measure of three basic dimensions of human development: health, education and income.

IV. In the course of the ROSC A&A review, the team identified areas that require institutional improvement. These include the following:

- i. **Dualistic framework for financial reporting and audit.** There seem to be two parallel systems for accounting, reporting, and audit. One system exists for the large multinational companies (which is driven by international requirements of parent companies and their jurisdictions, as well as the offshore institutions that require/enforce/use this information).

The current dualistic reporting framework has resulted in opaque corporate financial reporting practices that weaken the business environment in PNG.

This system does not depend on the PNG legal system or institutions, and is mostly unaffected by changes in PNG statutes. There is another system for local PNG companies (mostly SMEs and SOEs), which exists mostly on paper but with little enforcement on the part of government, and compliance, on the part of the public sector. The challenge therefore is to create a single PNG Accounting and Auditing system for the corporate sector that is in line with the needs of the country, and that will raise the quality of

financial information of the private sector as a whole. A lot of care needs to be taken not to create a burdensome, overly rigid system which the country does not have the resources to enforce, and the private sector doesn't have the capacity/resources to apply. Currently there are many requirements (on paper), but there is hardly any compliance in practice. The point of having "real" requirements is not only to have clear rules of the game, but also to begin instilling a "compliance culture" in which there may be fewer rules than before, but the ones that remain are actually enforced.

- ii. **Lack of a comprehensive statutory framework for A&A:** While at first glance the laws seemed to be in order, upon closer research it became clear that the necessary implementing measures would need to be enacted. Furthermore, the complication arising from trying to manage and implement parallel legal requirements as they are set forth in law (de jure), which crosses different segments of the corporate sector, contributes to the (de facto) low level of enforcement of these requirements.
- iii. **Lack of operational and effective institutions.** The law grants powers to a number of institutions to act on A&A issues (ARB, ASB, Securities Commission, Insurance Commission, etc.). However, a lack of adequate human and financial resources (funding and staff), hampers capacity to carry out their mandate.

V. The ROSC team has proposed a number of principle-based policy recommendations to address the critical weaknesses identified during the course of the assessment. While a full set of recommendations are detailed in the body of the report, the most critical of these include the following:

- i. **Simplified Standards.** IFRS are the only accounting standards in the country and they apply to all companies. Government should consider accelerating the adoption of IFRS for SMEs for non-public interest enterprises. There is likely more relief that can be extended

to SMEs, but this is a topic that merits a separate and deeper analysis as care needs to be taken to avoid over burdening this growing and critical segment of the economy.

Reconstituting the ASB is one of the most pressing and important issues in modernizing corporate financial reporting practices in PNG.

ii. **Reconstitution of the ASB.** The ASB is the institution most central to the policy reforms needed to improve corporate financial reporting and auditing practices in PNG. The ASB not only needs to promptly reconvene, but it also has to be strengthened with a capable technical secretariat which can conduct detailed analyses on technical issues to inform the ASB and allow it to discharge its duties regularly.

iii. **Clarity of Reporting Requirements.** There is a need to introduce a clear definition of “Public Interest Entity” (PIE) to ensure large enterprises are required to produce annual financial statements which are subject to audit. Similarly, there is a need to group Medium, Small and Micro non-listed companies so that the appropriate policy and statutory requirements can apply and be monitored and enforced.

iv. **Quality Assurance/Public Oversight.** It seems that the auditors are the only group reviewing financial statements and determining the compliance with relevant standards, and that there is little oversight from the regulators to identify compliance gaps between

Without the proper quality assurance function, coupled with the lack of public oversight, there are substantial risks that the significant resource flows will not be appropriately captured, recorded and disclosed.

reporting standards and actual practice (i.e., there is no one “guarding the guards”). In a resource-rich country like PNG, there could be a substantial risk that companies are not accounting for, disclosing and reporting important financial transactions. Auditors/firms who audit the financial statements of PIEs (financial institutions, SOEs, listed companies) should be subject to some form of quality assurance that is not purely peer review based. The quality assurance function could be outsourced to organizations from a neighboring country (e.g., professional accounting organizations from Australia)

while the requisite capacity and skills are developed in PNG institutions.

v. **Building the Capacity of CPAPNG.** There are a 188 member countries of the World Bank Group, and 157 of these countries are full members of IFAC. PNG, as an Associate

Strengthening the ability of CPAPNG to fulfill its IFAC membership obligations is central to building the technical capacity of accounting and auditing professionals in PNG .

Member, may aspire to be recognized among this group of countries that have achieved full IFAC membership. As the institution that perhaps is most central to the technical reforms needed, it is critical that CPAPNG is able to meet the full range of its obligations – covering quality assurance, oversight and enforcement; maintenance of standards; skills development for the profession (including the provision of education and training for practitioners); compliance with the IFAC Statements of Membership

Obligations; etc. In order to achieve full membership, CPAPNG will need to rely on the close partnership and collaboration from a number of other bodies (e.g., ASB, ARB, Department of Finance, etc.) in order to fulfill specific membership requirements.

vi. **Single Regulator for Accounting and Auditing.** The responsibility to develop

A key medium term objective is for the development of a single regulator to supervise and enforce accounting and auditing standards and regulations.

regulations is now scattered amongst various institutions (BPNG, Insurance Commission, Securities Commission, Stock Exchange, Companies Registrar, and IPBC). However, resources and capacity gaps limit the ability of these institutions to review and enforce Accounting and Auditing requirements. Rather, than enhancing the regulator capacity of at least six institutions, it perhaps would be more efficient and effective to have one institution play the leading/central role in developing

these financial regulations (e.g., along the lines as the FRC in Australia), particularly for PIEs. In building this capacity over the medium term, PNG would benefit from learning from a neighboring country like Australia where the public oversight body is recognized as a strong leader supervising corporate financial reporting and audit. Over time, this institution could also be responsible for quality assurance and oversight (see point above).

Currency: Papua New Guinea Kina

PGK 1.00 = US\$ 0.40

ACRONYMS AND ABBREVIATIONS

A&A	Accounting and Auditing
ASC	Accountants Statutory Committee
ADB	Asian Development Bank
ARB	Accountants Registration Board
ASB	Accounting Standards Board
ASF	Authorized Superannuation Fund
BPNG	Bank of Papua New Guinea – Central Bank of Papua New Guinea
BSP	Bank of South Pacific
CPAPNG	Certified Practising Accountants Papua New Guinea
CPE	Continuing Professional Education
CPS	Country Partnership Strategy
FDI	Foreign Direct Investment
FRC	Financial Reporting Council
GAAP	Generally Accepted Accounting Practices
GDP	Gross Domestic Product
GoPNG	Government of Papua New Guinea
IAASB	International Auditing and Assurance Standards Board
IAESB	International Accounting Education Standards Board
IASB	International Accounting Standards Board
IES	International Education Standards
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IPA	Investment Promotion Authority
IPBC	Independent Public Business Corporation
ISA	International Standards on Auditing
LNG	Liquefied Natural Gas
MDTP	Medium Term Development Plan
OIC	Office of Insurance Commissioner
PIE	Public Interest Entity
PNG	Papua New Guinea
POMSoX	Port Moresby Stock Exchange Limited
RoC	Registrar of Companies
ROSC	Reports on the Observance of Standards and Codes
SME	Small & Medium sized Entities
SMO	Statement of Membership Obligations
SOE	State Owned Enterprise
WBG	World Bank Group

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INTRODUCTION

1. **This report is part of a joint initiative of the World Bank and IMF to prepare Reports on the Observance of Standards and Codes (ROSC).** The ROSC Accounting and Auditing review for Papua New Guinea mainly focuses on the strengths and weaknesses of the accounting and auditing environment that influence the quality of corporate financial reporting. It involves both a review of mandatory requirements and actual practices. The international standards that have been used as reference points for the preparation of this report are International Financial Reporting Standards (IFRS), clarified International Standards on Auditing (ISA), and international good practice in the field of accounting and auditing regulation.

OBJECTIVES

2. **The main purpose of the Report on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A) review exercise, conducted at the request of the Government of Papua New Guinea, is to propose policy recommendations that will strengthen the institutional framework that underpins accounting and auditing practices in the country.** Implementation of the policy recommendations will enhance the quality of financial reporting for corporations (including State Owned Enterprises) – a key pillar that directly contributes to enhancing the business environment and the advancement of governance and financial accountability in both private and public sector entities.

3. **The World Bank Country Partnership Strategy (CPS) for the period of FY2013-2016 rests on three pillars, which are all supported to some extent by the ROSC A&A.** The first pillar focuses on providing increased and more gender-equitable access to inclusive physical and financial infrastructure (including expanded access to finance by SMEs); the second pillar aims on gender-equitable improvements in lives and livelihoods (including a better business environment); and the third, on increasingly prudent management of revenues and benefits (including improving governance). The ROSC A&A is also consistent with an existing operation, the SME Access to Finance Project, as well as with a proposed IFC project to improve corporate governance in the banking sector.

4. **In this context, the Government of Papua New Guinea (GoPNG) is also pursuing a three-pronged approach to support sustainable development in the private sector: Transparency, Governance, and Commercial Accountability.** As such, the GoPNG also expressed interest in the entire suite of ROSCs managed by the World Bank (Corporate Governance, Insolvency and Creditors' Rights, and Accounting and Auditing). The ROSC A&A would be the first of the three.

COUNTRY CONTEXT

5. **Papua New Guinea (PNG) is an ethnically and socially diverse young nation of seven million people, speaking over 840 languages, poised on the verge of a challenging period of opportunity and risk.** The country occupies the eastern half of the island of New Guinea (the western half of which is part of Indonesia), as well as a number of islands in Oceania. It is a

lower income country, with a GNI per capita of US\$2,010 in 2013.⁵ Although there has been some improvement, PNG continues to face a number of socioeconomic challenges, which are reflected in its Human Development Index⁶ (HDI) of 0.491 (up from 0.324 in 1980), which gives the country a rank of 157 out of 187 countries with comparable data. The HDI of East Asia and the Pacific as a region increased from 0.457 in 1980 to 0.703, placing Papua New Guinea below the regional average.

ECONOMIC CONTEXT

6. PNG's economy is dualistic along several dimensions: there is a sharp rural-urban divide, the extractives economy dominates the small non-minerals formal sector, and the contribution and productivity of women is sharply constrained compared to men. PNG is rich in natural resources, including forests, fisheries, oil/minerals and land, but is subject to extreme weather events and natural disasters. The economy is dominated by a labor-intensive agricultural sector and a capital-intensive oil and minerals sector. The formal sector consists of enclave extractive industries, cash crop production, a small import-substituting manufacturing sector, and a growing services and retail sector, while the informal sector is largely subsistence agriculture and local trade.

7. The global downturn of 2009 had only a mild impact on PNG's economy, which expanded by 5.5 per cent, outperforming its regional peers and most other developing economies. This follows several years of six to seven per cent annual Gross Domestic Product (GDP) growth. Much of this growth has been driven by a stream of new investments in the country's productive capacity, in particular, the current US\$16 billion PNG-LNG (liquefied natural gas) project, which shipped its first cargo in June 2014, ahead of schedule. The project is forecast to start generating significant revenues for the government late this decade. Investment decisions on a second LNG project, with even larger production potential, and on a number of other large resource projects, are under discussion.

8. Beyond the energy sector, PNG's minerals sector accounts for a third of value-added and 75 per cent of all exports. It is modern but has few linkages to the local economy. Furthermore, in recent years the non-minerals sector has also benefited from inflows of private investment, particularly in the newly liberalized telecommunications and aviation sectors. The agriculture sector employs 85 per cent of the population; however it consists primarily of subsistence agriculture. The share of manufacturing in GDP has remained at approximately 6 per cent for over a decade.

9. Like many minerals-rich developing countries, PNG struggles to transform increasing national revenues into measurable improvements in household incomes and livelihoods, or individual well-being. In fact, PNG is one of the few countries that are not set to meet any of its Millennium Development Goals by 2015. Further, widespread law and order problems pose a threat to locals, constrain investment, and inhibit the growth of the private sector. Gender

⁵ Atlas method, in current US\$. Source: World Bank.

⁶ Each year since 1990, the Human Development Report has published the [Human Development Index \(HDI\)](#) which was introduced as an alternative to conventional measures of national development, such as level of income and the rate of economic growth. The HDI represents a push for a broader definition of well-being and provides a composite measure of three basic dimensions of human development: health, education and income.

inequality and violence also restrict the ability of women to participate in economic, social and political life, and is a contributing factor to many development challenges in PNG.

10. Translating strong macroeconomic performance and extractive industry revenues into a broad improvement in living standards remains a key challenge. The role of the private sector, especially small and medium enterprises (SMEs) to address this challenge is critical. SME development is notably important in view of low job market participation rate in the formal sector, especially among women and youth. But SME activity and investment are hampered by an array of institutional and structural constraints, among which is the lack of access to finance. To provide stimulus to support the SME sector, the GoPNG has launched a SME Stimulus Growth Package aimed at growing and expanding more local companies with a target to significantly increase locally owned companies in the formal sector from the current 49,000 to over 500,000 by 2050.

11. It is critical at this stage of development that PNG manage its resources well. The PNG-LNG project is expected to expand GDP by as much as one-quarter in 2014 and 2015, and national income by about 8 per cent. Other large resource projects are under discussion. This requires significantly stepping up the quality, compliance, and enforcement of benchmark financial reporting and auditing practices. This is a key development challenge for PNG to channel this windfall revenue into investments that positively impact peoples' lives. The ROSC-AA follows the recent Financial Sector Assessment Program (FSAP), completed in 2011 jointly by the World Bank and International Monetary Fund.

FINANCIAL SECTOR⁷

12. PNG's financial services sector is more robust and well-regulated than many countries of similar age and income, but the dualistic economy has offered incentives to banks to serve elite and corporate clients more effectively and creatively than the rest of the population. Although the financial sector has grown and become more diverse, financial sector inclusion is low. Around 85 percent of the adult population—largely those in rural communities—is excluded from the formal financial sector. Improving access to financial services, particularly for SMEs, remains a very significant developmental challenge.

13. A favorable external environment and the introduction of financial sector reforms after a crisis in the 1990s have provided a strong foundation for financial sector expansion. Total financial sector assets have increased to K37.5 billion (US\$15 billion) at the end of December 2013 from K9.5 billion (US\$3.7 billion) at the end of 2005. There is interest on the part of the private sector in expanding financial services into new markets, as well as of key national authorities, who have led a strong push to achieve expanded microfinance and SME banking services, as well as greater outreach to rural areas.

14. Commercial banks dominate the financial sector, holding over two-thirds of all financial sector assets. Since 2000, when sector-wide reforms were introduced, banking sector assets experienced more than a tenfold increase to more than K27.3 billion (US\$10.9 billion).

⁷ The main source used for this section is the International Monetary Fund and World Bank. Financial Sector Assessment for Papua New Guinea, May 2011. Available at: <http://www.imf.org/external/pubs/ft/scr/2011/cr11163.pdf>

The domestically-owned Bank of South Pacific (BSP) is the largest and is systemically important. It holds over 50 percent of deposits, has operations in other Pacific countries and has issued instruments on foreign exchanges. Other large banks include the subsidiaries of two Australian banks (Australia and New Zealand Banking Group Limited and Westpac Banking Corporation), and a subsidiary of the Malaysian bank, Maybank. In addition, there is a state-owned, non-deposit taking National Development Bank, which has historically provided accessible credit to rural communities but is currently with assets of around 1 percent of total banking assets

15. Authorized Superannuation Funds (ASFs) are the second-largest player in the financial sector, holding more than K8.37 billion (US\$3.3 billion), which is over 80% percent of total nonbank financial assets. Among the four licensed ASFs, Nafund and Nambawan stand out with almost K2 billion (US\$770 million) and K3 billion (US\$1.2 billion) in assets respectively (together holding 87 percent of ASF assets). An authorized “superannuation fund” means an indefinitely continuing fund created for retirement or other related purposes by statute or trust deed or other instrument, including every employer employing or engaging 20 or more employees, and (b) every employee engaged in employment by an employer and receiving pay, whether they make mandatory or voluntary contributions to an ASF. ASFs are created predominately to provide for the retirement of members, with membership evenly spread between statutory bodies and private individuals.

16. There is no material fixed income market other than issues made by the government and the Bank of Papua New Guinea (BPNG), and the stock market exhibits very limited trading and liquidity is thin. The large market capitalization of around K54 billion (US\$21 billion) (over 150 percent of GDP) is a result of substantial cross listings. There are 21 stocks currently listed on the Port Moresby Stock Exchange, including one debt listing, and there were two new equity listings in 2013. There are two stock broking firms.

17. Insurance companies are not considered to be major players in the PNG financial sector and the life sector contributed only 1% to total assets in the financial sector as at the end of 2013. There are five life insurance companies and five life insurance brokers. Ownership is fairly evenly distributed across private companies and individuals. General insurance in PNG includes coverage for fire, household, motor vehicles, marine, third party, medical, and workers compensation. There is one reinsurer (52% State owned, 48% foreign owned), thirteen insurance companies (47% national, 38% foreign, 15 % State owned), seven brokers (over 50% foreign-owned, the rest national), and four insurance loss adjusters (80% foreign owned, 20% national). General insurance premiums are increasing and totaled K439 million for 2011 (US\$175 million), or 9% of GDP.

STATE-OWNED ENTERPRISES⁸

18. Most state-owned enterprises (SOEs) have been corporatized. Of the SOEs, all but one (Bemobile Limited) is 100 percent owned by the State. The assets of SOEs are vested in the Government Business Trust (GBT), which is managed by the Independent Public Business

⁸ *Finding Balance: Benchmarking the Performance of State-Owned Enterprises in Papua New Guinea* (2012)

Corporation (IPBC) which is under the purview of the Minister of Public Enterprise and State Investment.

19. SOEs play a significant role in the PNG economy. They provide a range of essential services, including power, water, telecommunications, air transport, port, and post, all of which are vital to the sustained development of the country. SOEs represented an estimated 10-15 percent of total fixed assets of the economy in 2010, and receive ongoing equity contributions from the government - during the period 2002-2010, GoPNG made equity contributions of approximately US\$400 million. Despite these sizeable investments, the contribution of SOEs to gross domestic product (GDP) was only 1.9 percent in 2012, and only US\$10 million were paid in the form of dividends during the period 2002-2010. Every dollar invested in PNG's SOEs produced seven times less output than the same dollar investment in the rest of the economy.

20. SOEs have been providing essential services in an inefficient manner, and at a significant cost to the economy. Improving financial reporting and audit practices of SOEs would contribute to improved efficiency, transparency, and governance of SOEs, which in turn would result in a number of significant benefits for the economy, including SOEs contributing positively to the fiscal balance (through reduced or eliminated need for government transfers, and increased dividends), as well as improved service delivery in key sectors for the citizens of PNG.

METHODOLOGY AND STRUCTURE OF THE ROSC A&A REVIEW

21. The methodology used to conduct the analytical work for preparing this report includes application of the ROSC Accounting and Auditing diagnostic review. Developed by the World Bank, the diagnostic template questions were complemented by a comprehensive due diligence exercise. A detailed description of the approach and methodology followed in conducting A&A ROSCs can be found at www.worldbank.org/ifa/rosc_aa.html. The World Bank ROSC team met with key stakeholders involved in accounting, auditing, and corporate reporting in Papua New Guinea. Also, several discussion forums were held with groups of preparers and auditors of financial statements, businesses, and regulators.

22. An assessment of actual practice, enforcement and compliance with financial reporting and auditing requirements was also conducted. The team gained an understanding of actual practices through interviews at the due diligence stage, as well as through examining sets of audited financial statements, determining their ease of public availability, and assessing the enforcement practices of supervisors. More specifically:

- (i) A sample of 20 audited financial statements from the financial and non-financial sectors were reviewed to gauge whether they are consistent with the prescribed financial reporting and auditing standards;⁹
- (ii) Audit reports for the financial statements above were reviewed, and discussions with practicing auditors were undertaken to be able to make judgments as to the level of compliance with ISA;

⁹ The sample included four banks, three ASFs, one insurance company, three listed companies, five SOEs, and four non-listed large companies.

- (iii) Monitoring activities regarding the requirements relating to filing and publication of financial statements were reviewed;
- (iv) Actual practices by financial sector supervisors for enforcing financial reporting obligations of regulated entities were assessed;
- (v) The team also researched about the perception of the quality and reliability of financial reporting from users of financial information, such as the business community, credit risk units of banks, and IFC colleagues.

SPECIFIC AREAS OF FOCUS

23. Small and medium-sized enterprises. Given the size and importance of the SME sector in the overall economy of PNG, the ROSC A&A focuses on key broad regulatory aspects that govern financial reporting practices for SMEs. As a follow-up to this ROSC A&A, a dedicated analytical work will review in depth the financial reporting practices of SMEs and application (or the appropriateness and reasonableness) of IFRS for SMEs, among other related topics. The supplemental analytical work represents a common platform through which other parts of the World Bank Group (three to four Global Practices and the IFC) would be brought together to work on the SME agenda. As such this ROSC A&A addresses the following questions:

- Does the regulatory framework relating to accounting, financial reporting and auditing take into account the specific characteristics of SMEs (limited resources available for accounting, fewer external users, etc.)?
- Can the regulatory burden on SMEs relating to accounting be alleviated?
- How can SME accounting and auditing practice be improved to enhance their ability to access financing?

24. State-owned enterprises. SOEs play a significant role in the economy and dominate key sectors such as power, water, ports and aviation in PNG. Therefore, the assessment reviewed the financial reporting and enforcement mechanisms in the SOE sector, including SOEs' and their auditors' compliance with financial reporting and auditing standards; the level of public availability of SOE financial statements and audit reports; as well as whether, or to what extent, the government uses the financial reporting and auditing process as a tool to monitor these entities.

25. CPAPNG capacity and resources. The ROSC A&A analyzed the range of responsibilities of CPAPNG, with a view to identify areas where cooperation or mentoring with other Professional Accountancy Organizations, and assistance from international or regional organizations could bring significant benefit. In particular, the report includes options for introducing a quality assurance system for audits of public interest entities, and ensuring that the weaknesses found in audit practices are used as a basis for building the capacity of the profession, such as through the development of targeted Continuing Professional Education (CPE) courses.

INSTITUTIONAL FRAMEWORK FOR CORPORATE FINANCIAL REPORTING AND AUDITING

A. STATUTORY FRAMEWORK

	Regulator	Accounting Standards	Audit Requirement	Publication
Banks, ASFs, Life Insurance	BPNG	IFRS	Yes. Audit partner rotation every 5 years.	ASFs (others not readily available)
Listed companies	Securities Commission, POMSoX	IFRS	Yes. No auditor rotation	Yes
General Insurance companies	Insurance Commission	IFRS	Yes. No auditor rotation	No
Other companies	IPA Companies Registrar	IFRS	Yes except where exempt. No auditor rotation	Yes, but not readily available *
State-owned enterprises	IPBC (Trustee)	IFRS	Subject to audits by OAG	No

*According to the Companies Act, any member of public may obtain a copy of the audited financial statements from the Companies Registrar. However in practice the documents are either very outdated or not readily available

Companies

26. Business activities in Papua New Guinea are primarily regulated by the Companies Act (1997). The Act sets forth how companies are to be established and how business activities are to be carried out, including provisions on accounting, auditing, and financial reporting. There is no differentiation between legal forms. All entities covered by the Act are “companies”, which may have one or more shareholders and directors, and may or may not have a limitation on liability.

27. The Companies Act classifies companies as either exempt companies or reporting companies. Exempt companies are smaller companies that do not exceed any of the following three thresholds: (a) total assets of K5 million (US\$2 million); (b) 25 shareholders; and (c) 100 employees¹⁰. Exempt companies are not required to follow certain provisions of the Companies Act, including that of undergoing an annual independent audit. Companies that exceed one or two of the above thresholds may also dispense with a statutory audit provided all shareholders agree. Listed companies, their subsidiaries, and overseas companies cannot be exempted, regardless of size. A reporting company is any company that is not an exempt company.

¹⁰ Companies Act 1997 Section 171

28. **There is no legal definition of ‘small’, ‘medium’ or ‘large’ companies in PNG.** The Companies Act only identifies companies as either exempt companies or reporting companies. Classifications into categories can assist policy makers to set financial reporting and audit requirements which are more aligned with the cost-benefits and capacity levels of the companies grouped within each category.

29. **All companies are required to prepare financial statements - both legal entity and consolidated.** Companies are required to prepare annual financial statements comprising a balance sheet, a profit and loss statement, a cash flow statement, and notes¹¹. The legal entity and consolidated financial statements must be prepared within five months of the balance sheet date (normally 31 December)¹². The preparation of the financial statements is the obligation of the directors. The annual report, which includes the financial statements, should be signed on behalf of the board by at least 2 directors.

30. **The financial statements, together with the audit report if applicable, must be sent to all shareholders at least one month before the annual general meeting (AGM)**¹³. The AGM must be held not later than six months after the balance date¹⁴. Companies are required to submit their financial statements, together with the audit report, to the Registrar of Companies within 14 days after the AGM¹⁵.

31. **All company financial statements in PNG must effectively be prepared in accordance with international financial reporting standards regardless of the size of the company.** According to the Companies Act all companies must follow “generally accepted accounting practices” (‘GAAP’). GAAP means¹⁶ a) ‘applicable financial reporting standards’; and b) in relation to matters for which no provision is made in applicable financial reporting standards and that are not subject to any applicable rule of law, accounting policies that –

- are appropriate to the circumstances of the reporting company; and
- have authoritative support within the accounting profession in Papua New Guinea.

32. **PNG has effectively adopted international financial reporting standards as its ‘applicable financial reporting standards’ however there is a lack of clarity as to the precise definition of current GAAP** (refer to Section D below ‘Setting Accounting and Auditing Standards’ for more discussion on this topic). When complying with GAAP, the directors are required to add such information and explanations to ensure that the financial statements give a true and fair view of the matters to which they relate¹⁷.

33. **General purpose financial statements are not used by the PNG Internal Revenue Commission for taxation purposes.** Currently the IRC relies on specific returns to gather the

¹¹ Ibid Sections 177 & 178

¹² Ibid Sections 179 & 181

¹³ Ibid Section 211

¹⁴ Ibid Section 101

¹⁵ Ibid Section 183

¹⁶ Ibid Section 172

¹⁷ Companies Act Section 180 & 182

information needed to meet legislative requirements. However improved accounting and timely reporting will indirectly benefit overall tax compliance.

34. The is scope in the short term to focus on aligning corporate and taxation reporting to ease the administrative burden for smaller/micro entities. In the longer term consideration can be given to convergence of corporate financial reporting and taxation reporting requirements for larger corporations.

35. Foreign companies and their subsidiaries are required to follow the same financial reporting and audit requirements as domestic companies¹⁸. Foreign companies may not be exempted from statutory requirements, regardless of their size. In addition to their parent company financial statements, foreign companies must file a separate set of legal entity financial statements—and consolidated financial statements, if relevant—, specific to the company's PNG business activities, with the Registrar. The Registrar may, however, exempt the company from the requirement to prepare PNG-specific financial statements if it is satisfied with the information contained in the consolidated financial statements of the parent company.

36. Shareholders have the power to decide on the appointment and changes of auditors¹⁹ The Board of Directors of a company is required to ensure that auditors are permitted to attend the AGM, and that auditors are notified of the AGM in advance. An auditor of a company must be registered as a Registered Company Auditor under the Accountants Act 1996.

37. Auditor rotation is not a requirement in the Companies Act however the Act does impose certain safeguards over changes of auditors A company cannot appoint a new auditor in the place of an auditor who is qualified for reappointment, unless (a) at least one month's written notice of a proposal to do so has been given to the auditor; and (b) the auditor has been given a reasonable opportunity to make representations to the shareholders

38. According to the Companies Act, the financial statements, audit reports, annual reports, and other documents filed with the Register of Companies (RoC) are accessible to the public; however this mechanism has limitations in practice.²⁰In order to access the information, an individual must go to the Registrar during business hours, and may request access to the documentation, unless there is a court order in place in which case the documents may be viewed under supervision by an officer of the RoC. The ROSC team found that documents accessed via this method were either several years out of date, or unavailable. A new database system is being developed and, once fully functional, it is expected that all filed documents will be available online, and hence more readily accessible by the public. The new system will also have the capability to issue non-compliance notices to companies that have not lodged documents by the due date. It is anticipated that the new system will be fully functional in early 2015.

39. The Securities Act 1997 regulates the establishment of the Securities Commission, stock markets, and practices relating to the offering of securities to the public. The Act

¹⁸ Ibid Section 390-391 governs financial reporting by foreign companies.

¹⁹ Ibid Division IV Auditors

²⁰ Companies Act Section 398

does not impose any additional financial reporting and audit obligations on listed companies beyond those of the Companies Act requirements. The Securities Act however does provide the legislative foundation for the establishment of the stock exchange, Port Moresby Stock Exchange Limited (POMSoX).

40. All listed companies are required to disclose their audited financial statements to the market in accordance with Chapter 4 of the Listing Rules of POMSoX²¹. Listed companies must lodge their half yearly and full year reports (summarized in a prescribed form) with POMSoX within 75 days after the balance date, which are uploaded on the POMSoX website for public viewing. The company annual report²² must be lodged within 19 weeks after the balance date. Listed companies must also immediately give POMSoX any information that it becomes aware of which a reasonable person might expect would have a material effect on the price or value of the company's securities.

Banks, ASFs, and Life Insurance Companies

41. The BPNG sets prudential standards for commercial banks, ASFs, and life insurance companies²³ An important way the BPNG obtains information for its supervisory purposes is by way of returns submitted by the banks and other regulated entities in accordance with the prudential standards issued under the Banks and Financial Institutions Act 2000 and other relevant Acts²⁴. These periodic financial returns consist of balance sheet, income statement, loan schedule, deposit schedule, capital adequacy, and largest loans. There is no requirement in the BPNG instructions for the returns to be reconciled, or otherwise linked, to the audited annual financial statements. When setting prudential standards, it is advisable to refer as necessary to GAAP, and to avoid establishing corporate reporting and audit rules that may conflict with requirements prevailing in PNG (see also paragraph 107).

42. The commercial banks and life insurance entities are registered companies and must therefore observe the financial reporting and audit requirements of the Companies Act, including the requirement to prepare financial statements within five months after the balance date. The requirement to observe the financial reporting and audit provisions of the Companies Act is reiterated in the Banks and Financial Institutions Act²⁵ and Life Insurance Act²⁶ respectively. Additionally the banks are required to submit their audited financial statements to the BPNG not later than six months after the end of the financial year in accordance with the Banks and Financial Institutions Act. The commercial bank must publish its financial statements and make them available to the public.²⁷ The ROSC team found that only one commercial bank published recent audited financial statements, and life insurance companies' audit financial

²¹ No data was available from POMSoX regarding actual performance regarding compliance, enforcement, etc.

²² Ibid Section 215 Annual return contains details of the company registered address, shareholdings, directors details, principal activities, total of assets & liabilities, number of employees etc. as set out in Schedule 6. For Reporting companies, the audited financial statements must accompany the annual return

²³ The BPNG regulates other types of entities, such as savings & loans societies, finance companies, and microfinance companies, however these are beyond the scope of this ROSC

²⁴ Superannuation Act 2000 and Life Insurance Act 2000

²⁵ Section 4

²⁶ Section 62

²⁷ Schedule 4 of the Banks and Financial Institutions Act 2000

statements were not readily accessible. ASFs are not companies however they are required to comply with the financial reporting and audit provisions of the Companies Acts according to the Superannuation Act 2000 (section 58). The audited financial statements of ASFs are readily accessible by the public.

43. For banks, ASFs, and life insurance companies, under the prudential standards²⁸, the audit report and management letter with respect of an audited entity shall be submitted to the BPNG within 90 days after its financial year-end. A tri-partite meeting of representatives of the bank, its external auditor and the BPNG shall be held within 60 days after receipt of the annual audit report and management letter, although this seldom occurs in practice. A bank's auditor must provide the BPNG, when requested in writing, full access to and/or copies of its working papers, as defined in international auditing standards, with respect to a particular bank audit within 10 days of a request.

44. The prudential standards set out the responsibilities of the board of directors of each bank, ASF, and life insurance company for financial reporting and audit These responsibilities include to (a) appoint and engage a qualified, independent person or firm to prepare the audited financial statements, (b) submit the audited financial statements and other required information to the BPNG, (c) publish its financial statements, and (d) promptly inform the BPNG of any information that is relevant to the supervisory oversight. An auditor may not be engaged where there is an objection by the BPNG. The entity must notify the BPNG within 14 days when an auditor's appointment ceases.

45. The lead audit partner must be rotated after 5 years. There is no regulated 'cooling off' period before the partner may be reappointed however in practice similar guidelines as directors of regulated entities are used, in that the directors are not eligible for reappointment for a period of three years. The banks have audit committees which must have a written charter that outlines their roles and responsibilities, and comprise at least three members, must be non-executive, with a majority of independent directors. The Audit Committee nominates the external auditor and reviews its work to ensure that the financial audited report represent the company's true and fair position and compliance with regulatory requirements. Currently no fines have been imposed except for removal of boards and management on fit & proper grounds, if the matter is serious in nature.

46. Auditors may not be engaged to provide advisory or consulting services while that same auditor/audit firm is engaged for services to conduct the annual audit and related services, except that services related to the preparation of a bank's corporate tax return are not prohibited; or lend any money or other property to its external auditor or audit firm.

General Insurance

47. General insurance companies are required to submit audited financial statements in accordance with the Companies Act, and in addition to the requirements of the Insurance Act 1995 (as amended). Where there is a conflict between the Insurance Act 1995 and the Life Insurance Act, the Life Insurance Act prevails. Licensed entities must annually appoint a

²⁸ Prudential Standards 'External Auditors' 7/2005 (banks); 5/2008 (ASF); and 5/2008 (life insurance)

registered auditor. The auditor shall audit and make a report to the Commissioner on the annual balance sheet and profit and loss account and such other returns and statements which the Commissioner shall determine by notice in the National Gazette as requiring an auditor's report and certification. The Commissioner has issued 'licence requirements' for general insurers in accordance with Sections 18 and 19 of the Insurance Act 1995, which include specific requirements for the appointment of external auditors, audited financial statements, and statutory returns. For the purpose of an audit under this section, the auditor has all the powers of an auditor under the Companies Act.

48. General insurance companies shall submit in the form, time and manner determined by the Commissioner by notice in the National Gazette such reports, returns and other information as the Commissioner specifies in the notice. Licensed general insurance companies are required to submit audited financial statements to the Insurance Commissioner by 31st March each year, in accordance with Circular 08/1 (item 1 (iv)) issued 27 June 2008. They are also included with the Annual Report of the Insurance Commissioner which is submitted to the Minister (Treasury) who tables the report in Parliament. Once approved and passed by the parliament, the report becomes a public document and can be accessed on request by the public. In practice the ROSC team found that the audited financial statements of general insurance companies were not readily available.

State Owned Enterprises

49. "State Owned Enterprise" means a business enterprise in which the State or IPBC owns any assets or any of the share capital. All SOEs and statutory bodies are subject and required under the Audit Act to be audited. SOEs registered under the Companies Act 1997 are required to prepare their financial statements under GAAP and submit their financial statements and annual returns to the Register of Companies within 5 months after year end.

50. IPBC is mandated under the IPBC Act to monitor SOE's. SOE's are governed by the Companies Act plus industry specific legislation for specific industries. For example, NICTA for Telikom & Bemobile, Civil Aviation Act for Air Niugini, Harbour Act for PNG Ports, and Electricity Industry Act for PNG Power, etc.

51. SOE's are required to prepare annual audited accounts including Balance sheets, Statement of Comprehensive P&L and cash flows. IPBC submits to the minister for Public Enterprises and State Investments, who tables the Audit Report in parliament. All SOE's submit to IPBC as the shareholder by 30th June each year. In practice the ROSC team found however that the audited financial statements of SOEs are not readily available.

52. The financial statements of SOEs must be submitted to the Auditor-General for audit. Currently the Auditor General outsources to Registered Company Auditors, including the large global network audit firms, and small to medium practices. The Chief Executive is required to furnish a representation letter as part of the audit process. This provides written confirmation from management to the auditor about the fairness of various financial statement elements. The purpose of the letter is to emphasize that the financial statements are management's representations, and thus management has the primary responsibility for their accuracy. Non-

compliance can be reported to the Minister and Parliament – or referred to the Public Accounts Committee. Where applicable, there is potential for budget funds to be withheld from the SOE.

53. The Auditor-General's report must meet the requirements of the Audit act 1989 (a) whether the financial statements, to which the report relates, are based on proper accounts and records; and (b) whether the financial statements, to which the report relates, are in agreement with the accounts and records and whether they show fairly the financial operations for the period which they cover and the state of affairs as at the end of that period; and (c) whether the receipt and payment and investment of moneys and the acquisition and disposal of assets during the year have been in accordance with the Public Finances (Management) Act 1995; and (d) such other matters arising out of the financial statements, to which the report relates, as the Auditor-General considers should be reported. The Auditor General shall prepare a report to the National Parliament and may send a copy of such report to the Minister and to the Head of the relevant body. This applies to all public bodies and subsidiary corporations notwithstanding any provision to the contrary in any other law.

54. Concerns with timeliness of audited financial statements for SOE 2010-2011 audits for a number of SOEs are still with Auditor General for review. A few SOEs have received disclaimer opinions for misreporting, or for including material inaccuracies in the financial statements.

55. There is an increasing number of corporate governance measures for SOEs being introduced by the IPBC Boards appointments are approved by the NEC through the nomination of the Minister for Public Enterprises & State Investments. Directors are appointed for a term of 3 years. Audit Committees are set up by IPBC and SOE Boards to assist in discussing relevant issues at Committee level prior to approvals by the Board. Other Board Committees as seen fit to be formed are approved by respective Board to assist in Board meetings. Some SOE's have internal audit teams that have own internal audit charters.

56. Despite the changes to some aspects of SOE management and oversight introduced by IPBC, there are still concerns regarding the effectiveness of critical management and oversight functions. As the team has noted, there are still significant delays in the production of annual financial statements. This not only is a concern for SOE management, but also raises a number of questions regarding the role and functioning of the audit committee of the enterprise's Board. Given the prominent role SOEs play in the economy, and with the projected windfall of revenues due to LNG exports, there is an expectation that increased public investment will flow through many SOEs. Therefore it is important that a corporate governance review of SOEs (individual enterprises) and/or a review of the system of oversight and monitoring of SOEs be undertaken to ensure that these enterprises are functioning effectively and with increased transparency and accountability over their operations in order to best serve the public interest in improving the lives of all citizens across PNG.

B. THE PROFESSION

57. CPAPNG is PNG's only professional accountancy organization and has a growing membership base CPAPNG was incorporated as an association in 1974 and currently has 3,677

members²⁹. Membership of CPAPNG is open to all persons registered under the various categories of the Accountants Act 1996 (Registered Public Accountant, Registered Company Auditor, Registered Liquidator, and Accountants in Employment, Accounting Technicians, Registered Accountancy Graduates, and Registered Accountancy Students). Members can be full members – Certified Practicing Accountant (CPA PNG); Certified Accounting Technicians (CAT PNG); or Fellow - or non-practicing members. Residency is not a requirement and foreign accountants may become members. 74% of members are Papua New Guinean citizens, of which 40% are female. Current breakdown of the total membership base is as follows:

- Honorary Fellow – 3
- Fellow – 21
- CPA PNG – 1,442
- CAT PNG – 11
- Accounting Technicians³⁰ – 808
- Registered Accounting Graduates – 899
- Registered Accounting Technicians – 493

58. Around 1600 applicants on average sit for the entrance examinations each year with an average pass rate of 53%. New admissions average around 100 per annum. The minimum qualifications and experience requirements for the different categories of registration are set out in the rules promulgated by the Accountants Registration Board (ARB). To obtain the CPA designation, a candidate must have completed a diploma³¹ or degree from an approved tertiary institution in PNG – those with a degree with an Accounting major need to successfully pass seven mandatory papers. Those with a degree in another business related discipline or a diploma in Accounting must first complete the requirements for becoming a Certified Accounting Technician (CAT) (see below)

59. CPAPNG administers the examinations which comprise multiple choice and open-ended questions. There is seven year limit to complete professional examinations. Details of the examinations are as follows:

Certified Practicing Accountant (CPA): Seven compulsory papers covering: 1. Foundations of Accounting; 2. PNG Taxation Law and Practice; 3. Strategic Management; 4. Financial Reporting; 5. Financial Risk Management; 6. PNG Business Law; 7. Advanced Audit and Assurance, plus three years of working experience in accounting.

Certified Accounting Technician (CAT): Six papers, five of which are compulsory covering: 1. Foundations of Accounting; 2. PNG Business Law; 3. PNG Taxation Law and Practice; 4. Financial Accounting and Reporting; 5. Management Accounting; 6.

²⁹ Numbers as at 30 September 2014

³⁰ Accounting technicians – refers to candidates admitted prior to 2010. This comprises candidates with a Diploma in Accounting or non-accounting degree holders. Registered Accounting Technicians are the same however it refers to candidates admitted from 2010. Once these candidates complete the required 6 subjects, the candidate is conferred CAT status.

³¹ A tertiary qualification below degree-level

Accounting Concepts and Principles or Business Finance, plus three years of working experience in accounting.

60. CPAPNG developed its own code of ethics in 1997 which is in need of updating in line with the current Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA). Members are required to observe the CPAPNG code however it is not legally enforceable.

61. CPAPNG became an associate member of IFAC in 2007 and is now actively seeking full membership of IFAC A key monitoring tool in attaining full membership is the IFAC Statement of membership obligations³² (SMO) from which CPAPNG has developed a ‘roadmap’ of required actions to achieve full membership.

62. There is no existing Quality Assurance program to review the quality of audits conducted by CPA members. A regular program of audit quality assurance reviews ensures that members maintain a professional standard and can identify areas for improvement. This leads to an overall improvement in audit quality which underpins an effective corporate reporting and audit environment.

63. CPAPNG capacity needs to be increased if it is to meet its full current obligations, and to sustain an expanded role under full IFAC membership. CPAPNG has adequate resources to support its regular functions however more resources are needed to conduct the full due diligence needed to ensure compliance with member obligations and maintain the integrity of the CPA PNG designation. Areas to strengthen capacity include due diligence to confirm new members’ level of experience, and strengthening systems to ensure current members maintain their minimum CPE hours. Expansion into areas such as providing capacity building programs for Small and Medium audit practices (SMPs) or development and implementation of programs to assure that members are maintaining minimum professional standards will also require additional capacity within CPAPNG.

64. In order to achieve full membership, CPAPNG will need to rely on the close partnership and collaboration from a number of other bodies (e.g., ASB, ARB, Dept. of Finance, etc.) in order to fulfill specific membership requirements. There are a 188 member countries of the World Bank Group, and 157 of these countries are full members of IFAC. PNG, as an Associate Member, may aspire to be recognized among this group of countries that have achieved full IFAC membership. As the institution that perhaps is most central to the technical reforms needed, it is critical that CPAPNG is able to meet the full range of its obligations – covering quality assurance, oversight and enforcement; maintenance of standards; skills development for the profession (including the provision of education and training for practitioners); compliance with the IFAC Statements of Membership Obligations; etc.

³² There are seven SMOs – SMO 1 Quality Assurance; SMO 2 International Education Standards for Professional Accountants and Other Pronouncements issued by the IAESB; SMO 3 International Standards and Other Pronouncements issued by the IAASB; SMO 4 IESBA Code of Ethics for Professional Accountants; SMO 5 International Public Sector Accounting Standards and Other Pronouncements issued by the IPSASB; SMO 6 Investigation and Discipline; SMO 7 International Financial Reporting Standards and Other Pronouncements issued by the IASB. PNG’s action plan is available on the IFAC website <http://www.ifac.org>

65. **All persons providing accountancy services in PNG are required to be registered with Accountants Registration Board (ARB)** as established under the Accountants Act 1996. All persons registered with ARB must be a member of CPAPNG as a prerequisite of registration. The ARB is chaired by the Auditor-General (*ex officio*) and consists of the President of CPAPNG (*ex officio*), five accountants from each of the categories of registration (including two Registered Company Auditors), two persons from academia, and a practicing lawyer. Board members are appointed for a period of up to three years and are eligible for reappointment. There is a Secretariat, led by the Registrar of Accountants, which carries out administrative functions required under the Act.

66. **The categories of registration are Registered Public Accountant, Registered Company Auditor, Registered Liquidator, and Accountants in Employment³³.** The latter comprises persons with a relevant diploma, degree, or professional qualification and employed in government, by a statutory body, or by a private organization, and performing accounting-related duties. For Accountants in Employment it is the prospective employer who must apply for the accountant's registration, although anecdotal evidence indicates that the compliance rate is low.

67. **The ARB prescribes the minimum qualifications and experience required for each category of registration** A person may apply to the ARB for registration in one or more of the above categories provided they furnish evidence to the satisfaction of the Board of their qualifications, work experience, competence, and character, together with evidence of Professional Indemnity Insurance, and evidence of any other matter reasonably required by the Board. Registration for each category is generally renewable annually for prescribed fee and a list of all registered accountants (and their category) is published annually.

68. **A non-resident may apply for registration** and the ARB at its absolute discretion shall grant approval upon such conditions as the Board thinks fit. The Board may enter into a reciprocal arrangement with the accountants' board or other competent authority in any country for (a) the recognition of the status of a person registered by that board or competent authority to practice as an accountant, and (b) similar recognition or registration, licensing or authorization in that country of persons registered in PNG.

69. **The ARB may cancel registration in a number of circumstances** where a person (i) has been convicted of an offence a) punishable by imprisonment of one year or more, or b) in the opinion of the Board render them unfit to practice accountancy, or (ii) is convicted of an offence relating to their duties or functions as an accountant; (iii) is of unsound mind; or (iv) is found guilty of certain misconduct.

70. **The ARB does not meet regularly and suffers from capacity constraints which hamper its effectiveness** The Board met only once in recent years which is not adequate for the volume of registrations and adds to the burden of the Secretariat and delays in actions. The Secretariat comprises the Registrar and only a few administrative staff and therefore lacks the resources and technical skills to fully discharge tasks such as due diligence of applicants and follow up actions

³³ Accounting technicians, Registered Accounting Graduates, Registered Accounting Technicians are not registered with ARB but are members of CPAPNG

and fines. The lack of resources is apparent in the long lead times to process registration renewals.

71. The ARB would benefit from more sophisticated tools & reliable databases to track registrations and compliance The Secretariat's systems are in need of upgrade in order to improve data collection and tracking of registrations to monitor compliance and performance. Connectivity with databases such as CPAPNG and the Registrar of Companies could enable comparison of membership bases (including checking that CPE obligations are up to date) and highlight irregularities and discrepancies in registrations and statistics.

72. Improved information systems can form the basis of awareness campaigns and enhance transparency of the Board's operations There is a need to inform accountants of requirements of the legislation and mandatory registration. The deliberations of the ARB are not widely publicized which deprives professional accountants of basic information and adds to the general lack of awareness.

73. Membership requirements are monitored and enforced by the Membership, Ethics and Disciplinary Committee. It meets once every 2 months to consider, deliberate and process Council agenda and related issues before each Ordinary Council Meeting. No disciplinary actions have been undertaken by the Committee in recent years

74. There is also an Accountants Statutory Committee (ASC), according to legislation³⁴, however it rarely meets. The function of the ASC is to inquire into complaints against a registered person for disgraceful and improper conduct in the practice of accountancy. The Committee comprises the Chairman of the Membership, Ethics and Discipline Committee of CPAPNG; three registered, practicing accountants; a qualified person drawn from academia; and a lawyer engaged in private practice. The ASC may make a number of orders in cases of serious misconduct, including admonishment; payment of costs; enforceable undertakings; fines up to K10,000 (US\$4,000); suspension of registration up to one year; cancellation of registration; order refusal of an registration application.

75. Pecuniary penalties for non-compliance with the Accountants Act are quite lenient. For example, the fine for non-compliance with a rule under the Accountants Act is K200 (US\$ 80). A person who pretends to be registered or qualified is subject to a fine of up to K5,000 (US\$2,000).

C. PROFESSIONAL EDUCATION AND TRAINING

76. There are six tertiary education institutions across PNG³⁵, with between 80 and 100 students graduating with accounting-related degrees each year. The largest education institution, the University of Papua New Guinea (UPNG), is also offering two years Diploma³⁶ in

³⁴ Accountants Act 1996 Section 54

³⁵ University of PNG, University of Technology, Divine Word University, Pacific Adventist University, Institute of Business Studies, University of Goroka

³⁶ A Diploma course is usually offered to those students who passed secondary level but do not meet the pre-requisites for the (higher level) degree courses. A Diploma course is often an additional step toward entry to achieving a full degree.

Accounting through its School of Business Administration. On completion of Diploma in Accounting with minimum grade level, a person will be eligible to apply for Bachelor of Accounting. Total years of study for both Diploma and Bachelor are four years. Both the programs are offered through face-to-face (internal) and through distance education mode. Furthermore, the UPNG will be offering Bachelor of Public Sector Accounting from the academic year 2015. This program is targeted towards members of staff of Public Service. Those who have completed Diploma in Accounting with a minimum of five years of experience in Accounting or Treasury areas of Public Sector are eligible to apply.

77. International Financial Reporting Standards (IFRS) are covered in detail in the Bachelor of Accounting degree course however there is little coverage of technical aspects in Diploma courses. It was conveyed to the ROSC team that there is a lack of printed materials and textbooks for students

78. A process of regular dialogue between universities and the accounting profession and business would provide critical feedback to help strengthen the university curriculum. In the past from time to time there have been interactions between the universities, the profession, and business representatives to update and improve the curriculum however these have lapsed in recent years. Without a process of ongoing feedback, the university curriculum can become outdated and disconnected with the needs of the profession or business. A structured exchange of dialogue between the three groups can provide feedback on such as areas as current changes in global accounting practices; quality of accounting graduates and areas in need of strengthening; technical capacity in IFRS and fundamental accounting principles.

Continuing professional education (CPE)

79. The CPAPNG CPE requirement is forty hours total each year, with CPAs and CATs required to undertake a minimum of twenty structured and twenty unstructured CPE hours

80. There is a lack of accredited CPE providers with only CPAPNG providing CPE courses with support from major accounting firms. CPAPNG lacks the capacity to provide a regular number and standard of CPE courses to meet the demand from members. Structured CPE hours via in-house courses must be approved by CPAPNG.

81. CPE hours are monitored through the annual renewal application however CPAPNG lacks the capacity and systems to conduct more in-depth due diligence. Failure to maintain CPE hours leads to non-renewal of memberships and a potential breach of rules which would be addressed by the CPA PNG Membership, Ethics and Disciplinary Committee although the latter action has not been taken to date.

82. Small and Medium audit practices (SMPs) are heavily reliant on CPAPNG to keep their practices up to date with international standards and practices. SMPs often are not affiliated with global networks that regularly provide necessary training and feedback.

83. PNG policy makers are focusing on the need to build skills and accreditation of public sector accountants and to bring these more into line with the private sector. A coordinated

approach to implement this policy can include tailored CPE programs comprising topics relevant to public sector accountants. Around 20% of CPA members are employed in Government.

D. SETTING ACCOUNTING AND AUDITING STANDARDS

84. The Accounting Standards Board (ASB) established under the Companies Act is responsible for setting financial reporting standards, issuing guidance on their application, and other relevant tasks. The Act however does not expressly refer to the function of setting auditing standards. ASB is chaired by the Registrar of Companies, and comprises 6 additional members: (a) the Auditor-General, (b) two representatives of CPAPNG, appointed by the Minister; (c) one representative of the Accountants Registration Board, appointed by the Minister; and (d) two suitably qualified persons appointed by the Minister (although there is no guidance on the nomination and appointment process for (d)). Board members are appointed for a maximum term of five years.

85. Despite its key role, the ASB is not operational and has not held a meeting since 2006. A media release in early 1998 by the ASB expressed the need for uniform accounting standards for PNG companies, and stipulated the adoption of International Accounting Standards.³⁷ An announcement was also issued (undated) by the ASB referred to 'directives' and 'policy statements' approved in 2001 and 2002. The announcement also advised that the Standards Committee of CPAPNG may recommend the new international financial reporting standards for adoption by the ASB, or may issue financial reporting guidelines from time to time, without being approved by the ASB or published in the National Gazette. Such recommendations or guidelines issued by the Standards Committee of CPAPNG are considered to have the authoritative support within the accounting profession in PNG and therefore form part of PNG GAAP. The Standards Committee has not met for a number of years pending the reconvening of the ASB.

86. The ASB lacks the capacity to carry out its functions. A Secretariat is operating within the Registrar of Companies office however there is no formal establishment of a Secretariat in legislation, and the Board does not have the necessary skills, resources or funding. Under the Companies Act, modified audit opinions and cases of non-compliance raised by auditors are required to be referred to the ASB. There is no process within the RoC and ASB to implement this, and it also raises a question as to whether the role of the ASB includes an enforcement element.

87. The reconstitution of the ASB must be seen as a priority. The ASB is the institution most central to the policy reforms needed to improve corporate financial reporting and auditing practices in PNG. The ASB not only needs to promptly reconvene, but it also has to be strengthened with a capable technical secretariat which can conduct detailed analyses on technical issues which will inform the ASB and allow it to discharge its duties regularly.

88. The ASB would benefit from additional advisory or policy work to help modernize its core function. The ASB must not only be active but it must also regularly communicate with stakeholders and constituents. Apart from having technical secretariat supporting key functions

³⁷ Together with one PNG accounting standard PNGAS3

of the ASB, the ASB would also need to properly establish various procedures to ensure adequate due process and consultations on technical issues related to standards, outreach and communications, etc., as well as ensuring that adequate implementation guidance accompanies the issue of new and amended standards.

89. There is a conflict between the provisions of the Accountants Act and Companies Act in relation to the role of standard setting. The Companies Act establishes the Accounting Standards Board to set accounting and auditing standards, however similar and overlapping functions are assigned to the CPAPNG under the Accountants Act (Section 24).

90. PNG is moving toward adoption of the IFRS for SME however the consultative process has not included the wider accounting profession. It would be worthwhile gauging broader opinion as to whether smaller companies will have the capacity comply with the IFRS for SME standard. Also, care needs to be taken with regard to adoption of the IFRS for SME standard as consideration is needed to ensure that any future standard is appropriately contextualized to fit the SME environment in PNG.

E. ENSURING COMPLIANCE WITH ACCOUNTING AND AUDITING STANDARDS

91. A number of regulators supervise the financial sector in PNG: For listed companies, the Securities Commission (SC) has a broad regulatory function related to ensuring the conduct of an orderly stock market; whilst day-to-day processing of lodged audited financial statements, and other company documents, is performed by the Port Moresby Stock Exchange under its Listing Rules. BPNG (the central bank) supervises banks, ASFs and other financial institutions, and the Insurance Commission, under the Department of Treasury, supervises non-life insurance companies. All companies, including State Owned Enterprises, must lodge their audited financial statements with the Registrar of Companies (RoC) which has the responsibility to monitor compliance with the Companies Act. For SOEs, the IPBC provides an additional layer of oversight through its role to as manager and trustee of the GoPNG's significant investment in public enterprises.

Companies

92. To date there has been no effective monitoring and enforcement of company audited financial statements in PNG. Due to the large volume of transactions the RoC operates primarily as a registry, receiving company documents lodged under the legislation, using largely outmoded systems and with limited resources. The RoC is aware of the issues and is introducing electronic lodgment (filing) systems which have the capability to analyze and compare databases. For example the RoC in collaboration with the (former) Small Business Development Corporation is developing a simplified, automated mechanism for small businesses to lodge their annual returns. Other regulators currently do not consider the review of audited financial statements to be either within their scope of supervision or they lack the necessary expertise to carry out this function.

93. The regulators do not have function in place to review financial statements and audits for compliance with relevant standards and regulations. The RoC has also been seeking to build up its monitoring capacity however despite its role and responsibilities under the

Companies Act, the RoC still lacks the capacity (staffing, funding and systems) and the technical expertise to review compliance of audited financial statements with the accounting and auditing standards. There is a checklist in place to review audited financial statements however it forms more of a completeness check than a technical review; and there is no follow up of overdue reports and no fines applied for late lodgment etc. Given this history of non-enforcement, there is little incentive therefore for companies to comply and no deterrent to penalize those who fail to observe the standards.

94. Lack of a systematic collection of relevant data to monitor compliance is a common shortcoming. Basic data such as the number and profile of companies, auditors, and level of non-compliance are not maintained due to the resource and system constraints. Compilation of such data would provide important information for policy action and enforcement activities, as well as the basis for imposing fees and fines under the legislation. Areas which could be monitored are late lodgments, appointment/removal of auditors, and statistics by category of company (small, medium, large). Collaboration and data checks across the systems of different agencies (for example the RoC, ARB and Internal Revenue Commission) would aid in the identification of non-compliance (for example, auditor signing a report lodged with RoC is not registered with ARB).

95. Improved information can form the basis for generating awareness campaigns and strengthened communication by the regulators. Up to date and relevant information assists in identifying cross-cutting issues and non-compliance. This can form a more robust basis for targeted awareness campaigns to promote good governance and understanding and to publicize cases of non-compliance both as a deterrent and for educational purposes.

96. The standard setting process in PNG does not facilitate regulatory oversight or compliance. The lack of clarity of what constitutes GAAP in PNG, as well as the applicable auditing standards, diminishes the legal backing of the requirements. This hampers the supervisors' capacity both to educate stakeholders and to enforce the requirements. Non-compliance can increase if there is widespread opinion that the requirements are too uncertain or too flexible to be enforced.

97. Pecuniary penalties are legislated under the Companies Act however imprisonment is not available for serious offences. The penalty for noncompliance is up to K100,000 (US\$ 40,000) per company director. This applies for example if the financial statements—legal entity and consolidated—are not prepared and signed within the five-month deadline; if the financial statements do not comply with the applicable financial reporting standards; or if the financial statements are not duly audited. If a company's annual return is at least six months late; or if it fails to submit the required documentation to the Registrar within 18 months of the time required for submission (e.g., financial statements, audit report, annual report), a company may be removed from the Register of Companies. The Court may impose additional penalties up to the value of any benefits derived by a person when committing an offence. Certain acts are specified as offences, including false statements and falsification of records, leading to automatic prohibition from managing companies for a period of five years. The Registrar, and the Courts, can also prohibit persons from managing companies.

Listed companies

98. **The Securities Commission does not have the legal or physical capacity to supervise the audited financial statements for listed entities.** The current law does not provide for powers for the SC to deal with reporting, compliance & disclosure requirements. Three new bills are being prepared which address this. These will improve the institutional independence and regulatory capacity of the SC as well as updating the legislation relating to PNG capital markets.

99. **The POMSoX asserts that the listing rules are strictly enforced and met in a timely manner** (according to its website). This includes disclosure of material information in timely manner; lodgment of periodic reports; however this does not extend to ensuring that audited financial statements comply with relevant standards and legislation.

100. **Penalties for non- compliance for listed entities under the Securities Act are more onerous and include imprisonment.** Under the Securities Act, both the Securities Commission and the Registrar of Companies have powers to inspect books, papers, and other documents under the Act. There are a number of offences under the Securities Act including where any person makes a false or misleading statement likely to induce trade in securities or affect the market price (a fine of up to the greater of K200,000 (US\$80,000) or ten times the benefit derived, or up to five years imprisonment , or both); a person who falsifies records, or makes false or misleading statements or reports to the Commission, the Registrar, or the stock exchange (a fine of up to K50,000 (US\$20,000) , or up to two years imprisonment); or a director who fails to take reasonable steps to ensure that the body corporate complies with the Act, or fails to take reasonable steps to ensure the accuracy and correctness of any statement submitted under the Act (a fine of up to K50,000 (US\$20,000) , or up to two years imprisonment).

Banks, ASFs, and Life Insurance Companies

101. **The BPNG's has a strong reputation for its regulation and supervision in the banking, life insurance, and superannuation sectors, however it conducts only limited reviews for compliance of audit financial statements.** The BPNG focusses on ensuring the maintenance of prudential standards and promoting good governance. BPNG has around 40-50 staff engaged in monitoring and enforcing compliance with the respective Acts, prudential standards, licensing conditions and any other directives issued by BPNG from time to time. Submission of annual audited financial statements are monitored, and issues followed up where contained in an audit qualification or where significant and raised by the auditors in the management letter. However there is no review for compliance with accounting standards as BPNG does not have the depth of up-to-date specialized skills (e.g. financial instrument valuations, actuarial) to do this.

General Insurance

102. **The Office of Insurance Commissioner (OIC) is responsible for monitoring and conduct oversight of general insurance companies.** The OIC has strengthened its prudential oversight via the introduction of Risk Based Capital supervision in which OIC monitors and ensures that the requirement on capital adequacy and solvency of the insurance companies are met. Five staff undertake 'at desk' assessment and evaluation of insurance companies, and additional on-site inspections and enforcement activities. Insurance companies are 'encouraged'

to comply with legislative requirements. However compliance with the requirement to submit annual audited financial statements by 31 March is generally poor and the OIC has no enforcement powers under the Insurance Act 1995 to penalize breaches.

103. The OIC is proactively building its oversight function however there is still room for further strengthening and capacity building. Areas for strengthening include regular coordination with other regulators (particularly the BPNG); building IFRS and industry-specific technical expertise to review the quality of audited financial statements; building capacity in terms of resources and systems; monitoring compliance with submission of audited financial statements; and consider taking a role in the appointment and rotation of auditors.

State Owned Enterprises

104. Although legally a trustee rather than a regulator, the IPBC plays an important role in monitoring the quality and timeliness in SOE financial reporting. The IPBC undertakes a number of functions including holding and monitoring State owned assets and ‘majority-owned’ SOEs; undertaking the function of planning, coordinating and managing State assets, infrastructure and projects; determining policies regarding the conduct of its affairs and the affairs of any of the Trusts³⁸; and setting policies and objectives for SOEs on any matter or on behalf of the Trusts, the State or any State Owned Enterprises. In the event of a contravention of these requirements, the IPBC may dismiss the director(s) of the majority-owned SOE; any dismissed director is ineligible to be appointed as a director of a majority-owned SOE for a period of 3 years.

105. The IPBC views audited financial statements as very important for ‘dividend’ purposes, regulatory purposes, and for the public accountability. A team of five officers manage the IPBC portfolio (portfolio managers) each overseeing up to four groups of SOEs. Quarterly reports are received and are assessed (against benchmarks) by the portfolio managers. Recently a Compliance and Risk Unit was formed, with duties including reviewing financial statements.

³⁸ Section 8 of the Independent Public Business Corporation of Papua New Guinea Act 2002

ACCOUNTING STANDARDS AS DESIGNED AND PRACTICED

106. Whilst it is generally acknowledged that international financial reporting standards are applicable in PNG, the current definition of GAAP lacks clarity. The ASB approves the ‘applicable financial reporting standards’ for PNG. A 1999 directive from ASB stipulated International Accounting Standards as the applicable financial reporting standards and a subsequent (undated) ASB announcement stated that the ASB has approved all International Accounting Standards and IFRS 1 to 7. There is no information as to whether any IFRS have been approved subsequent to IFRS 7³⁹. In addition it is not clear whether the specific PNG accounting pronouncements⁴⁰ are still current, and whether there have other policies adopted which have authoritative support in PNG.

107. BPNG-regulated entities (specifically ASFs and Life Insurance companies) must also comply with financial reporting requirements of the BPNG prudential standards Prudential standard 3/2008 for ASFs sets out the financial statements components (Statements of Changes in Net Assets; Statement of Net Assets; Statement of Cash Flows; a Summary of Significant Accounting Policies; and Notes to the Financial statements), as well as a number of note disclosures, for example fair value of investments; returns on investment and to members; exposures; details of investment managers and actuaries etc. Prudential standard 4/2006 sets out the policy that ASFs must follow for the provisioning for bad and doubtful debts. For Life Insurance companies, prudential standard 6/2008 sets out the financial statement components and classifications (Operating statement, Statement of Assets and Liabilities, etc.), as well a number of note disclosures, for example, fair value of investments, valuation bases, returns on investments). Prudential standards 2/2005, 3/2005 and 4/2005, link the valuation of liabilities, assets, and solvency requirements to the financial statements.

108. A review of a sample audited financial statements by the ROSC team found a high level of compliance. The review focused on compliance, based on a desk review of the presentation and disclosures included in the selected sample of audited financial statements. The review noted the following:

- Segment Reporting. There was inconsistency in the disclosures around segment reporting mainly IFRS 8 ‘Operating Segments’ paragraph 22 to 32. The matters around presentation and disclosures that were not adequately disclosed are as followings:
 - General information
 - Information around profit and loss, assets and liabilities
 - Measurement
 - Reconciliation of reportable segment profit and loss, assets and liabilities to entity’s profit and loss, assets and liabilities
 - Entity wide disclosures around:

³⁹ IFRS 7 “Financial Instruments Disclosures”

⁴⁰ ASBD 1 “Directors and Employees Remuneration”; ASBD 2 “Reporting Currency”; ASBPS 1” Exemption of overseas companies”

- Information about products and services
- Information about geographical areas
- Information about major customers
- Instances of accounting policy notes did not disclose application and potential impact of new and revised standards as required by IAS 8 paragraph 28 a, b, c and d.
- Disclosures around IFRS 7 paragraphs 33 to 39 not fully considered. These are around the following areas:
 - Qualitative disclosures – exposure to risk and how they arise, its objectives, policies and processes for managing the risk and the methods used to measure the risk
 - Quantitative disclosures - summary quantitative data about its exposure to that risk at the end of the reporting period. This disclosure shall be based on the information provided internally to key management personnel of the entity
 - Credit risk - the amount that best represents its maximum exposure to credit risk at the end of the reporting period without taking account of any collateral held or other credit enhancements
 - a description of collateral held as security and other credit enhancements, and their financial effect
 - Financial assets that are either past due or impaired
 - Inconsistency in the inputs used on sensitivity analysis in comparison to entities in the same industry.

109. There were omissions noted for the disclosures required under the PNG specific standards. A number of financial statements reviewed did not include the disclosures according to two PNG standards ASBD1 and ASBD 2.

AUDITING STANDARDS AS DESIGNED AND PRACTICED

110. Auditing standards are not specified in PNG legislation however the Companies Act⁴¹ sets out the information that must be contained in the auditor's report, including the work done by the auditor; the scope and limitations of the audit; whether the auditor has received all the explanations and information required; and whether, in the auditor's opinion:- proper accounting records have been kept; the financial statements comply with generally accepted accounting practice and where they do not, the respects in which they fail to comply; and the financial statements and any group financial statements give a true and fair view of the matters to which they relate, and, where they do not, the respects in which they fail to give such a view.

111. Similarly the BPNG prudential standards for banks, ASFs, and life insurance companies, sets out how audit services must be performed, that is, with the objective to examine, verify, confirm and evaluate the financial statements and other information prepared in accordance with appropriate criteria to enable the auditor to express an opinion as to whether the financial statements are prepared, in all material respects, in accordance with an identified financial reporting framework and that, in the auditor's opinion, give a true and fair view, or present fairly, in all material respects the financial condition of a bank etc.

112. International auditing standards, although not formally adopted in PNG, are widely regarded across the accounting profession and audit industry as the applicable auditing standards. Although the Companies Act does not expressly refer to the setting of auditing standards, the ASB issued PNG Audit Guidance Statement No.1 in November 2002, which provides guidance on the form and content of audit reports consistent with ISA 700 'The Auditor's report on financial statements'.

113. Compliance with applicable auditing standards differs among audit firms of different sizes. In order to assess actual auditing practices, the ROSC team interviewed practicing auditors and senior leaders of the auditing profession. Facilitated discussions were conducted with the representatives of accounting firms operating in PNG, including global network firms, together with local medium-sized and small accounting firms. It appeared that tier one and tier two firms associated with international accounting firm networks had the capability to adhere to International Standards of Auditing. In case of these firms, ISA is built into their audit methodology and they are subject to the process of quality control from their international partners. The international partners also provide technical support and training to their counterparts in the country. The small practices, however, expressed they faced challenges in adhering to International Standards of Auditing.

114. For the local medium sized and small accounting firms, there are limited training opportunities on ISA. CPAPNG organizes an annual conference and a few seminars around the year on topical issues and these are the only opportunities for most of the local practices to catch up on the latest developments in auditing standards and practices.

⁴¹ Section 200

115. A review of a sample of audit reports demonstrated a strong degree of compliance with the requirements. However the review was limited to a desk review and the audit reports of SOEs were not provided to the ROSC team. In addition the sample consisted primarily of audits conducted by the major audit firms.

PERCEPTION OF THE QUALITY OF FINANCIAL REPORTING

116. During the course of the ROSC preparation, the following perceptions were commonly raised in discussions with key actors in PNG's corporate reporting and audit environment:

- **Challenges in applying full IFRS** – the full range of IFRS are considered too complicated for all companies, and entities reporting in accordance with the Companies Act, to apply. There is also a general lack of understanding by users of the financial statements. The full IFRS contain complex valuation techniques, judgments and assumptions which many financial statement preparers have difficulty in applying. Also a lack of guidance can lead to inconsistencies of interpretation and application. This causes errors requiring re-work which leads to delays in preparation of the financial statements.
- **Technical competencies at various levels** – the ROSC team was informed that recently graduated accountants lack the necessary technical and 'soft' skills e.g. (office skills, interpersonal skills, report writing etc.) requiring training before they fully assimilate into the workforce. Qualified CPA members can lack the higher technical skills required to competently apply the more complex requirements of IFRS.
- **Challenges in conducting audits-** the audit environment is challenging due to a range of factors, including lack of adequate substantiating documentation; difficulty in obtaining 3rd party confirmations; high costs of conducting the audits; frequent long delays in signing financial statements, particularly where there has been a change in management or change in auditor.
- **Compliance across non-listed companies** – There is a concern that non-listed companies may not be fully compliant with the financial reporting and audit requirements, particularly small and medium enterprises, or those companies audited by smaller audit firms. This may include late lodgment of documents or lack of compliance with the relevant standards. The difficulty in obtaining up to date audit financial statements for non-listed companies supports this perception. Also potentially significant entities may avoid an audit under the 'exempt' company provisions of the Companies Act.

POLICY RECOMMENDATIONS

117. The broad policy recommendations made in this ROSC emerge from the review findings and from the valuable inputs received from various stakeholders. The policy recommendations are interrelated and mutually supportive and are designed to collectively improve the corporate financial reporting environment in PNG.

118. The guiding principles behind the recommendations are to build on the existing systems of accounting and auditing. The future developments should be carried out in a manner that does not jeopardize the achievements of the framework and systems in place and be implemented through collaboration among the government, financial sector regulatory agencies, accountancy profession, and international development partners.

RECOMMENDATIONS FOR THE SHORT-TERM

119. ***Improving the Statutory framework.*** Updating and clarifying the legal framework is an essential and immediate first step in improving the quality of corporate financial reporting (accounting and auditing) practices in PNG. In doing so, the government is making a significant contribution to provide clarity to the business community (foreign and domestic firms) regarding the regulatory practices and requirements.

- The Accountants Act needs be reviewed to ensure it is consistent with the Companies Act. A number of Acts are in the process of being updated and these revisions must take into consideration the need to ensure clarity and consistency of financial reporting and audit requirements across PNG's statutory framework.
- The ASB should promptly be reconstituted to issue an announcement to clarify GAAP in PNG and the applicable auditing standards. It will take time to establish a single regulator or change legislation, yet the need to clarify applicable financial reporting and audit standards is urgent and critical.
- Additional policy and advisory work to support the ASB is also recommended. At a minimum, this work should explore options to establish (i) the role and organization structure of the ASB – including the process for appointment of the Board; (ii) modern procedures for the ASB's operations – including establishing due diligence and consultative processes, communications and outreach; (iii) a technical secretariat to conduct detailed technical analyses in support of the ASB.

120. ***Clarifying and Simplifying the Accounting and Auditing Statutory Framework.*** Providing greater clarity regarding the application of appropriate standards to easily distinguishable segments of the corporate and business sectors is another essential step in improving the business and regulatory environment in PNG.

- Develop a means to group Medium, Small, and Micro non-listed companies as basis to introduce a single set of policies and regulatory requirements commensurate with the capacity and significance of companies.⁴²
- Introduce a definition of ‘Public Interest Entity’ as this will help ensure that publicly significant entities are required to produce general purpose financial statements which are subject to audit.
- An additional study on IFRS for SMEs should be conducted to determine whether there is a suitable threshold below which a simplified approach for financial reporting can be considered and applied to small, medium and ‘micro’ enterprises. Given the importance the SME sector represents in terms of contribution to GDP, employment, future economic growth, this study would provide the government with key analysis and recommendations to bring this growing segment of the business community into the formal economy. This work should also be considered in conjunction with other initiatives such as the automation of annual returns for small businesses.

121. *Improving Compliance and Enforcement with Accounting and Auditing Standards.* Once the statutory and legal frameworks have been updated, and once the rules and requirements have been clarified, the next step is to ensure compliance with the new (or updated) laws and regulations. It will take time to establish the culture of compliance, but enforcement of new rules and regulations must be seen as a *sine qua non* to improving the business and regulatory environment through improved corporate practices that are increasingly aligned with international standards and benchmarks.

- A program of quality assurance reviews must be introduced by CPAPNG. This quality assurance program will focus on confirming that professional standards for audits are maintained by audit firms licensed to operate in PNG. While this program will require time to be developed internally, there may be opportunities to partner with (or outsource to) other professional bodies to assume this function during the immediate time period when skills and capacity are being developed.

122. *Building the Capacity of the Profession.* Ensuring adequate capacity to operate, manage and oversee the profession is another critical aspect of improving the quality of corporate financial reporting practices. Laws, standards and directives can certainly be updated but without the ability to implement them properly (i.e., if the critical technical skills are not developed to supply businesses) there will be no means by which to ensure corporations and business are deriving the maximum benefit from modern accounting and auditing practices.

- The capacity of the CPAPNG must be increased to meet its full range of functions in addition to supporting an active quality assurance program for its members, CPAPNG needs to strengthen in other important areas including introducing

⁴² The National Financial Inclusion and Financial Literacy Strategy 2014-15 includes an action item to ‘Assist Department of Trade , Commerce and Industry to establish a national definition of Micro, Small and Medium Enterprises (MSME) by 2015

professional programs to develop SMPs and public sector accountants, adequate due diligence to confirm new member experience levels etc.

- A review of the Accounting Registration Board, in conjunction with the assessment of CPAPNG, is a key step in identifying structural capacity gaps to regulate the profession. The reason for the relative inactivity of the ARB should be assessed, including identification of funding and capacity constraints, and any revisions needed to the Accountants Act. This can include an assessment of the existing disciplinary mechanisms and sanctions, including the operation of the ASC. Systems enhancements should also be considered as a basis for close collaboration between ARB and CPAPNG, and to use as a basis for membership awareness campaigns.
- CPAPNG's existing code of ethics must be updated to align with the IESBA code of ethics for professional accountants.

123. Conduct a Corporate Governance ROSC Assessment. Through the course of this ROSC assessment, the team found that the BPNG and IPBC are introducing mandatory codes of corporate governance, such as requiring audit committees, internal audit, corporate ethics etc. Moreover, there are serious concerns regarding the timeliness and quality of annual financial statements prepared by SOEs. This in turn brings into question not only the technical capacity to produce the statements but more importantly the quality of management and corporate practices within the SOE as well as the role of the Board and other aspects of oversight that permit a weak financial control environment to persist.

RECOMMENDATIONS FOR THE MEDIUM-TERM

124. Establish a 'Financial Reporting Council' (FRC) – PNG has the basic foundation for sound corporate financial reporting and audit however this is a missing 'enabler' with a clear focus to drive the implementation of framework and to ensure quality. The Council could contain representatives from each regulator (BPNG, Insurance Commission, Securities Commission), Auditor-General, Registrar of Companies, ARB, CPAPNG, IPBC, and be established under its own Act. The role of the FRC may include:

- Adopt financial reporting and audit standards based on international standards, and issue relevant policies and guidance.
- Review the application, quality and publication of financial reporting and audit in practice.
- Provide input to amendments to various legislation and regulations to ensure uniformity of financial reporting and audit requirements; adherence to the policies established for PNG; and adequacy of sanctions.
- Build awareness amongst regulators, preparers, users of financial statements, and other stakeholders.

125. ***The capacity of regulators should be reviewed to ensure adequate resources*** are available to conduct their financial reporting and audit oversight functions. The RoC in particular needs adequate resources to ensure the prompt lodgment and follow up of audited financial statements and enable their efficient retrieval. Critical data such as number of companies, profiles, and compliance statistics, must be developed and maintained as a basis for effective supervision and monitoring, and for education and awareness purposes.

126. ***Reinstitute a structured collaboration between educational institutions, CPAPNG, and business.*** This collaboration can provide important feedback on the competencies of graduates in practice which will help inform areas in the curriculum in need of strengthening. The group can also assess the estimated volume of professional accountants need to support the economy and consider strategies to meet the targets. An assessment of the curriculum should be made in alignment with the IAESB International Education Standards.

127. ***The number of accredited CPE providers should be increased, and should include courses tailored for public accountants*** currently only CPAPNG provides CPE programs and the range of providers should be increased to increase the range of CPE options for members.

128. ***CPAPNG must strengthen its monitoring to ensure members maintain minimum CPE hours*** currently CPAPNG lacks the capacity and systems to conduct detailed due diligence to confirm CPE hours of members.