KPMG

Kundu

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Foreword

This month we explore value-creation through understanding asset management; share our understanding of the new proposed production sharing contract regime in the oil & gas and minerals sectors; provide the insights from our recent Pandemic Fraud Risk Management Survey conducted; and as always provide tax regime updates.

With our dedicated in-house specialists in internal audit/risk, visa migration, corporate finance, management consulting, IT advisory, fraud investigation as well as tax and assurance, we are well placed to provide a truly multi-disciplined approach to PNG business compliance and advisory.

Please enjoy this month's Kundu and reach out to us at +675 321 2022 if you would like to see KPMG cover specific topics in future editions.

Zanie

Are we managing assets cohesively?

by Lizette Theron, Senior Manager, TTA

'Asset Management' versus 'Fixed Asset Management'

These terms appear to be the same, although the major distinction lies in the operational versus the financial management of assets. The terms above are therefore not merely a semantic preference but a difference in meaning in real terms. It is important to understand the distinction and how companies, in order to most efficiently manage their assets, need to ensure the cohesion between operations and finance insofar as they manage their assets.

'Asset management' is *'systematic and coordinated activities and practices through which an organisation optimally and sustainably manages its assets and asset systems, their associated performance, risks and expenditures over their lifecycles for the purpose of achieving its organisational strategic plan'.*

This is a definition from the Institute of Asset Management, while other sources describe 'fixed asset management' as an *accounting process* that seeks to track fixed assets for the purposes of financial accounting, preventive maintenance, and safeguarding from theft.

Over the past two decades there has been continuing calls for the integration of asset management and fixed asset management or *'asset accounting'*. To some extent this has been based on a desire for accountants and asset managers to speak the same language, reduce confusion and produce efficiencies from using the same information.

Effective asset management, including fixed asset management, enables an organisation to realise value from assets in the achievement of its objectives. Valuation, depreciation, asset management planning and pricing decisions should be based on a consistent understanding of the asset lifecycle and asset condition, and how this information should be utilised for fixed asset management and accounting.

Benefits of asset management

There are many advantages to taking a global, holistic view of asset management to ensure cost-efficient operations and the achievement of objectives. In particular, asset management can help:

1. **Tracking of assets –** the easiest task to accomplish in asset management is the compilation of a complete list of what the business owns and leases, including where assets are located, how they are used, and when changes were made. Such a comprehensive list provides the basis for the other benefits.
2. **Operational efficiency** – realising efficiencies depends on aligning needs and requirements with existing capabilities. An organisation needs to know, for example, what can be utilised before more spending is considered, and what can be eliminated to save money. Asset management puts a full understanding of assets, their capabilities, lifecycle, upgrade expectations, maintenance requirements, etc., at the disposal of management.
3. **Integration of branches or sites** – organisations with multiple locations can more easily create asset reports and provide other asset information that may be required by insurers, auditors, and management.
4. **Financial reporting** – asset management can ensure that relevant and up-to-date information is available for financial statements to fully disclose these details. Accounting for asset acquisitions, expenditures on upgrades and maintenance, and depreciation rates are examples.
5. **Asset recovery** – the majority of assets have a limited lifespan or useful life. Some assets will eventually be refurbished, or moved from a central location to a remote office or used for a secondary purpose. Others will be sold or scrapped. These changes, as well as use of consumables and spares, need to make it to the accounting system and financial reports.
6. **Risk management** – controlling assets inherently entails risk, and asset management helps identify where those risks lie and what types of proactive solutions can be employed to avoid them.
7. **Forecasting** – having an accurate acquisition history and understanding what is being utilised now empowers an organisation to identify trends. This can provide a basis for predicting fixed asset needs and budgets.
8. **Accuracy** – it is a challenge to keep track of all items that comprise an organisation's assets. With strong asset management, it becomes easier to tell when items are lost or stolen and deal with the underlying causes, and reduce vulnerabilities.

Fixed assets accounting

There is still confusion surrounding the accounting for fixed assets. Most organisations have fixed assets, used in the production of goods and services to customers - this can range from a single laptop to a fleet of trucks to an entire manufacturing facility or an apartment building for rent.

For organisations where fixed assets represent a significant capital investment, it is critical that, in addition to the physical management and maintenance of the assets, *fixed assets accounting* be applied correctly.

Some important considerations for organisations to keep in mind are:

- Consideration of all costs at time of acquisition or construction, and capitalisation of costs such as sales tax or freight incurred on a fixed asset purchase.
- Adopting a capitalisation policy, depending on the size of the organisation.
- Basing estimated useful life for depreciation on an asset's estimated service life, i.e. not using depreciable lives based on Internal Revenue Commission rules for financial reporting purposes.

- Taking note of changes in an asset's use or service; asset impairment may need to be considered.
- Considering and re-evaluating estimates of useful lives on an ongoing basis.
- Considering asset impairment when significant events or changes in circumstances occur.
- Considering whether an asset will have value at the end of its service life, then basing depreciation on cost, less estimated salvage value (residual value).
- Retention of depreciation records in sufficient detail so assets can be accurately tracked when physically moved and/or disposed.
- The new lease accounting standard (IFRS 16) and, in this regard, lease accounting to determine proper life - taking care not to automatically depreciate a leased asset over its useful life.
- Insurance recordkeeping requirements when recording and tracking fixed assets.

There is no doubt that embarking on total 'whole-life' asset management will be an immense undertaking for some organisations.

Many organisations face a significant challenge in tracking the location, quantity, condition, maintenance and depreciation status of their fixed assets, and although many organisations in PNG may not yet have mastered 'asset management' as a whole, the accounting for assets or 'fixed asset management' (as a minimum) need to be improved by the finance team and asset managers.

It is therefore beneficial for organisations to engage early with consultants to assist with the compilation of and accounting for fixed assets for financial reporting and audit purposes.

PNG's proposed production sharing regime

by Wayne Osterberg, Director, Advisory

The Minister for Petroleum has published clarification on the new proposed production sharing contract regime (PSC) to replace the current royalty / tax concessionary regime (RTS) in the oil & gas and minerals sectors. The new regime is detailed in the Organic Law on Papua New Guinea's Ownership and Development of Hydrocarbons and Minerals and the Commercialisation of State Businesses 2020 (2020 Organic Law). This replaces the 2016 Organic Law and has now been passed by Parliament.

The new regime aims to achieve four critical goals:

1. Replacement of the RTS regime with the PSC regime in both the oil & gas and the mineral sectors;
2. Enshrine Kumul Minerals Holdings Limited (KMHL) as the national mining company of PNG and Kumul Petroleum Holdings Limited (KPHL) as the national oil company of PNG;
3. Restate and reaffirm clear corporate governance, board independence, and protect the commercial integrity of KMHL, KPHL, and Kumul Consolidated Holdings (KCH); and
4. Introduce a National Petroleum Authority (NPA) to replace the Department of Petroleum & Energy with clearer functions relative to the PSC regime.

The key features of the new regime, explained by the Ministry, are:

- Title and ownership of the resource will be retained by 'PNG' (being KMHL, KPHL, KCH) throughout exploration and development to point of sale.
- Management and control of the exploration and production chain will be retained by 'PNG' throughout to point of sale.
- The State, through KMHL or KPHL, will be 100% owners of projects and will contract developers to undertake exploration and development. With respect to financing, all costs incurred will be incurred by the developer and be recovered by them from the project revenues (net of royalties).
- There will be no cash call obligations for 'PNG' unless the State elects to participate with the developers.
- All operational, commercial and technical data will be owned by PNG, which will directly participate in any operation.
- PNG will own all project infrastructure and facilities built by developers, whom have a right of use and will recover the costs thereof from the project revenues.

The rationale for the change is stated as being that PNG has historically had to buy its ways into its own projects by meeting historic and future costs. This required the State to borrow to fund its participation thus reducing its share of revenues and its ability to borrow to meet socio-economic obligations. The changes will allow PNG to retain ownership of its natural resources and engage with the developers as equals.

The Minister has detailed a number of other countries which use production sharing and the benefits that such a changed regime will bring to PNG.

The new regime represents a material shift in the sectors and is consistent with the 'Take back PNG' initiative. It is likely to be controversial and the PNG Chamber of Mines and Petroleum expressed concern at the lack of consultation at the time the proposed legislation was published and has stated that the changes "will cause significant uncertainty for the industry" and that "changes of this gravity and significance require careful and extensive assessment".

PNG pandemic fraud risk management survey

We recently conducted the KPMG PNG Pandemic Fraud Risk Management Survey where respondents shared their experience across critical areas of their business over the past few months. In our survey:

- Only 35% of respondents said their suppliers are using shadow IT in their organisation to ensure their data is not being transferred over insecure channels.
- 70% of respondents said they have a business continuity plan in place to address remote working and account for potential infrastructure failures.
- 35% of respondents did not have backup personnel for key roles and reporting lines if staff are unable to work.
- 70% of respondents have not implemented a recruitment freeze.
- Only 65% of respondents said fraud and financial crime detection systems are included in business continuity and disaster recovery plans.

Insights from our survey include:

- Determining whether any of your supplier services or technology have been impacted by the ongoing pandemic and assess whether that affects its delivery of services and/or technology.
- Communicating with suppliers directly around whether their business continuity plans support remote work for key services and technology.
- Identifying critical roles within your business unit including backup personnel to ensure business continuity.
- Incorporating detection systems into your business continuity and disaster recovery plans to identify potential fraud incidents early and implementing appropriate preventative controls to prevent reoccurrence.

Tax deadlines and penalties

A reminder that the income tax deadline for taxable returns is 31 August 2020 while non-taxable returns are due 30 September 2020 (due to Covid extensions).

Since July we have seen the IRC impose substantial penalties on the payment of monthly compliance taxes, even for being a day late. With SWT penalties running at 20% flat tax plus 20% interest per annum and GST at 10% flat tax plus 20% interest per annum it is imperative that these taxes are paid on time.

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