KPMG

Kundu

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Foreword

This month we share our thoughts on the potential economic impact of COVID-19 that has now reached PNG shores. Given that many companies are now undergoing their annual reporting and audit periods; we also discuss the important role every CEO plays in financial reporting. As always, we cover the latest IRC developments and tax return deadlines.

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

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

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PNG's economic outlook in 2021

by Wayne Osterberg, Director, Advisory Services

In Papua New Guinea the impact of the second COVID-19 lockdown is creating substantial uncertainty. There is no doubt that the wave of COVID-19 anticipated last year probably did not materialise and that the current wave of positive tests in likely an indicator of both increased testing and the high incidence of transmission. Australian authorities have identified a PNG strain which appears to be less virulent than certain other strains, which is good news but should not allow complacency to set in.

The economic impact is still difficult to fully formulate as the drivers are still playing out.

The health sector is massively impacted by the number of cases and treatment required. The vaccine rollout will provide a greater level of protection for frontline health workers but a full nationwide rollout is still some way off and will rely to a large degree on our ability to source, fund and deploy vaccines in sufficient quantity.

The mining sector has managed the crisis fairly well, but the current wave is definitely having an impact, with the current closure of OK Tedi. Porgera remains shut due to non COVID-19 issues and prior to the current wave the government appeared to be making some progress towards advancing the major projects required for more sustainable economic growth and activity. However, the impact of the current wave is not likely to be quantified for some time.

The restricted travel activity between PNG and Australia will make it more difficult for miners and all entities in both the public and private sectors, to source skills required for specific projects or ongoing business. They make it more difficult for skilled nationals to return to PNG from Australia and have the potential to become a more enduring obstacle to the free flow of skills between the nations.

The travel and hospitality sector is the most obvious and hardest hit victim of the pandemic and the reimposed travel restrictions between provinces. The Port Moresby hotels have been beneficiaries of the domestic quarantining system operated by the mines for staff travelling to site, but this is skewered towards those establishments approved by the operators. Quarantining of international arrivals will drop until some semblance of normality returns to international travel, particularly with Australia.

The hospitality and brewing sectors will be negatively affected by the current lockdown with activities in certain hospitality offerings materially curtailed and a resultant knock on effect for the stability of employment and the short term loss of earnings for employers and employee, which may become more structural if conditions worsen or do not improve.

The property sector has longer term, more rooted, considerations at play and the outlook is driven by supply, demand and the economic activity that supports demand. Supply has grown in recent years – upper end of the residential and office markets. Demand at the upper end has not been sufficiently strong to absorb that supply, with pressure on yields and thus valuations. Demand for affordable housing is strong but has not been sufficiently matched by supply.

The retail and manufacturing sectors remain driven by prevailing economic conditions and the consumer confidence and spending that they generate. The current climate will subdue activity and the lack of major project spending will depress the sectoral demand. Government funded projects are likely to be delayed and impacted by the prevailing restrictions and the focus the pandemic requires.

The banking sector is fairly resilient but the additional demands resulting from the pandemic in terms of logistical difficulties; reduced staffing complements; and the necessity to ensure safety in branches will push up operational costs.

It is a little early to make any strong calls on the outlook other than to say that 2021 is likely to be another challenging year in Papua New Guinea.

Financial reporting for CEOs

by Lizette Theron, Senior Manager, Tax, Transactions & Accounting Services

Any company's success depends in large part on sound financial management. The ultimate responsibility for a business's financial management belongs to the chief executive officer (CEO). In any business, the CEO assumes the main role of overseeing operations of the entire company, holding the highest position, and only reporting to the board of directors. A financially aware CEO is better equipped to guide the business and to remain productive and profitable.

Information is a key factor to success and it needs to be accurate, available and timely. Accurate and timely financial reports allow accurate forecasts, the ability to plan ahead and the opportunity to make adjustments quickly. Monthly internal financial reporting is essential, adapted in accordance with the specified requirements of the CEO and other leaders in the company, to get financial information that helps them manage the company.

Each company has key performance indicators that the CEO may consider to be more indicative of the health of the business than any other. Moreover, there are performance standards that the CEO may try to highlight by doing a more frequent review, for example having sales figures from each branch updated every week or even every day, in order to monitor whether earnings challenges will arise. Internal reporting requirements will vary in frequency and detail from company to company, and the issues that are reported to the CEO vary, based on what the CEO wants to emphasize to the company as the highest priorities.

The kind of reporting that a CEO should expect, as a minimum, to be able to monitor and measure the business's performance, financial position and cash flows, includes the following:

- Cash flows
  This details a business's cash flows during certain time periods and indicates if a business made or lost cash during that period of time.
- Profit & loss accounts (Income statement)
  This indicates the revenue a business earned over a certain period of time and shows a business's profitability. It includes a net income equal to the revenues and gains minus the expenses and losses.
  Some ratios that could be monitored include the following:
  - Operating expense ratio: this indicates the operational efficiency of the business through the comparison of operating expenses and total revenue. Essentially the lower the operating expenses the more profitable the business.
  - Net profit margin: this measures the business's profit minus operating expenses, interest, and taxes divided by total revenue.
- Financial position (Balance sheet)
  This displays a business's financial status at the end of a certain time period. It offers an overview of the business's liabilities, assets and shareholder equity.
  Ratios that could be monitored include the following:
  - Return on assets (ROA): shows how profitable the business is compared to total assets.
    ROA = net income divided by total assets.
  - Return on equity (ROE): calculates the profit generated by the company for the shareholders. It is used to compare profitability amongst businesses in the same industry. ROE = net income divided by shareholder's equity. Working capital: a financial key performance indicator focused on financial stability, this will help monitor performance based on the company's assets and liabilities. Working capital ratio = total current assets divided by total current liabilities.
  - Quick ratio/acid test: this ratio serves up critical information concerning liquidity.
    Quick ratio = (Current Assets – Inventories – Prepaids) divided by Current Liabilities.
  - Aged receivables
    The aging schedule is used to identify clients that are late in paying their invoices. If the bulk of the overdue amount is attributable to a single client, the business can take necessary steps to ensure that the customer's account is collected promptly. If there are several customers with overdue amounts that extend beyond 60 days, it may signal the need to tighten the credit policy towards the existing and new clients.
    Accounts receivable days is a formula that helps work out how long it takes to clear accounts receivable.
    Accounts Receivable Days = (Accounts Receivable / Revenue) x Number of Days in the Year (or month).
    The aging schedule also identifies any recent changes and spot problems in accounts receivable. This can provide the necessary answers to protect the business from cash flow problems.
    The accounts receivable aging method is used to estimate the amount of uncollectable debts which includes the approximate amount of the receivables that may not be collected. While the percentage is different for each group and is based on past experience and current economic conditions, the general rule of thumb is that the longer an account receivable remains outstanding, the less are the chances of its collection.
  - Aged payables: this schedule shows how quickly the business pays off suppliers and other bills. Accounts Payable Settlement Days = (Accounts Payable / (Expenses) x Number of Days in the Year (or month).
- Budget
  Helps with both planning and controlling the finances of the business, to ensure that the business has money for future projects. The budget variance serves to express the difference between budgeted and actual figures, in total or for a particular accounting category.

Financial reporting which is good for auditors, is more often than not of little use to management, and the CEO must work with the chief financial officer to configure internal financial reporting to meet the needs of the people driving the company. It is not expected of the CEO to do their own accounting but, in order to make the best decisions for the future of the business, every CEO needs to have a good working knowledge of the company's financial situation.

IRC developments and tax return deadlines

by Karen McEntee, Partner, Tax, Transactions & Accounting Services

With IRC on a skeleton staff at the moment due to Covid protocols there has been a knock on effect on services. For good reason IRC are no longer allowing visitors to the building. Other measures include hard copy tax lodgements being left in a box for later collection of the stamped document and currently, it is taking some time to get the stamped version back. Our recommendation is that even if a taxpayer is lodging a hard copy for stamping, they should also submit the soft copy by email and save the email as evidence of the lodgement deadline having been met. This would help the taxpayer in cases where, due to service delays, the IRC do not stamp the document until after the tax deadline. We have suggested the IRC move to a form of electronic stamping, if possible, and we look forward to seeing if this eventuates.

Unfortunately, IRC have not as yet issued the 2021 Tax Agent Bulletin which sets out the timelines for lodgement of 2020 tax returns. Usually this is issued by early February each year. However, in line with previous years taxable returns are likely to be due by 30 June if the taxpayer uses a tax agent (if the taxpayer does not use a tax agent then the tax return is already overdue and they should consider using a tax agent). Given the operational uncertainties that lie ahead for all businesses as a result of Covid lockdowns, isolations and employee illnesses we strongly recommend that taxpayers give adequate time to plan for and to meet their tax deadlines.

On another matter, IRC issued new 2020 IRC forms this week. The new returns are completely different in format to the old tax return forms and pose some issues. Unfortunately, many taxpayers have already prepared their tax returns based on the old forms. We are seeking clarity from IRC in relation to the forms, whether they will be revised and when they are required to be implemented.

Our social media presence

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Contact us

Zanie Theron Managing Partner ztheron@kpmg.com.au	Herbert Maguma Partner hmaguma@kpmg.com.au	Karen McEntee Partner kmcentee@kpmg.com.au	Pieter Steyn Partner psteyn@kpmg.com.au

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