

IV. Accounting and Auditing Standards

This chapter describes the accounting and auditing standards that govern the preparation of external financial reports and the audit of those reports. The chapter is structured as follows:

- 1 – Introduction
- 2 – International Public Sector Accounting Standards
- 3 – Accounting Standards Board
- 4 – International Accounting Standards
- 5 – PNG Accounting Standards
- 6 – Auditing Standards

1. Introduction

International Accounting and Auditing Standards, and PNG Accounting Standards are reviewed or drafted by the PNGIA, and recommended for adoption by the Accounting Standards Board.

At this stage, every International Accounting Standard (IAS) issued by the International Accounting Standards Committee and every International Standard on Auditing issued by the International Federation of Accountants, have been adopted in full. Two PNG Accounting Standards have been developed which specifically relate to PNG circumstances; these are Plantation Accounting and Currency Reporting. A gazettal notice has not yet been issued which is required for the enforcement of the Standards.

2. International Public Sector Accounting Standards

The International Federation of Accountants has released the first eight International Public Sector Accounting Standards (IPSASs) designed to enhance the accountability and financial management of governments worldwide. The release of these documents means that for the first time there is an authoritative set of independent financial reporting standards for governments. The Standards are based on Cash or Accrual, there are no Standards for Modified Cash or Modified Accrual.

IPSASs 1-8 are the first in a set of accrual-based accounting standards applicable to the public sector and will contribute significantly to the provision by governments of comparable, relevant and understandable financial information.

The IPSASs are based on the International Accounting Standards (IASs) issued by the International Accounting Standards Committee

(IASB). The IASs are adapted as necessary to reflect their application to the public sector.

The Public Sector Committee (PSC) of the International Federation of Accountants (IFAC) also recognizes that many governments may not yet be in a position to adopt the accrual-based IPSASs. To assist these governments, the PSC has developed an exposure draft ED *Financial Reporting under the Cash Basis of Accounting*. This sets out the requirements for the presentation of the primary financial statement under the cash basis of accounting, as well as the statement's structure and minimum content requirements. The requirements that are likely to emerge in this standard should lead to transparency where governments remain on the cash basis of reporting.

Building on the momentum of the recently released first set of final International Public Sector Accounting Standards (IPSASs), the International Federation of Accountants (IFAC) Public Sector Committee (PSC) released a further six new exposure drafts. The exposure drafts are another key step in the PSC's efforts to develop a comprehensive body of international accounting standards for governments around the world.

In addition to the new standards and exposure drafts, the Public Sector Committee has released a study, *Governmental Financial Reporting: Accounting Issues and Practices*. The new study aims to assist governments in the preparation of their financial reports and contains a detailed description of the common bases of accounting used by governments: cash accounting and accrual accounting, as well as a brief discussion of common modifications to the cash and accrual bases. The study also provides examples of actual financial statements prepared under each basis of accounting. A Summary of PSC Study 11, IPSASs 1 – 8 and EDs 9 - 15 are as follows:

- IFAC PSC Study 11 *Governmental Accounting Issues and Practices* aims to assist governments in the preparation of their financial reports and contains a detailed description of the common bases of accounting used by governments: cash accounting (including modified cash accounting) and accrual accounting (including modified accrual accounting). The Study also provides examples of actual financial statements prepared under each basis.
- IPSAS 1 *Presentation of Financial Statements* prescribes the overall considerations for the presentation of financial statements, guidance for the structure and minimum requirements for the

content of financial statements prepared under the accrual basis of accounting.

- IPSAS 2 *Cash Flow Statements* requires the provision of information about the historical changes in cash and cash equivalents of an entity by means of a cash flow statement, which classifies cash flows during the period from operating, investing and financing activities. Cash flow information allows users to ascertain how a public sector entity raised the cash it required to fund its activities and the manner in which that cash was used.
- IPSAS 3 *Net Surplus or Deficit for the Period, Fundamental Errors and Changes in Accounting Policies* requires the classification and disclosure of extraordinary items and the separate disclosure of certain items in the financial statements. It also specifies the accounting treatment for changes in accounting estimates, changes in accounting policies and the correction of fundamental errors.
- IPSAS 4 *The Effect of Changes in Foreign Exchange Rates* deals with accounting for foreign currency transactions and foreign operations. IPSAS 4 sets out the requirements for deciding which exchange rate to use and how to recognize in the financial statements the financial effect of changes in exchange rates.
- IPSAS 5 *Borrowing Costs* prescribes the accounting treatment for borrowing costs and generally requires the immediate expensing of borrowing costs. However, the Standard permits, as an allowed alternative treatment, the capitalization of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset.
- IPSAS 6 *Consolidated Financial Statements and Accounting for Controlled Entities* requires all controlling entities to prepare consolidated financial statements that consolidate all controlled entities on a line-by-line basis. The Standard also contains a detailed discussion of the concept of control as it applies in the public sector and guidance on determining whether control exists for financial reporting purposes.
- IPSAS 7 *Accounting for Investments in Associates* requires all investments in associates to be accounted for in the consolidated financial statements using the equity method of accounting, except when the investment is acquired and held exclusively with a view to its disposal in the near future in which case the cost method is required.

- IPSAS 8 *Financial Reporting of Interests in Joint Ventures* specifies proportionate consolidation as the benchmark treatment for accounting for such joint ventures entered into by public sector entities. IPSAS 8 also permits – as an allowed alternative – joint ventures to be accounted for using the equity method of accounting.
- ED 9 *Financial Reporting under the Cash Basis of Accounting* sets out the overall considerations for the presentation of the financial statements under the cash basis of accounting, guidelines for their structure, and minimum requirements for their content.
- ED 10 *Revenue from Exchange Transactions* proposes requirements for the accounting treatment of revenue arising from exchange transactions and addresses the issue of revenue recognition for these transactions.
- ED 11 *Inventories* proposes the accounting treatment for inventories under the historical cost system.
- ED 12 *Construction Contracts* proposes requirements for the accounting treatment of revenue and costs associated with construction contracts.
- ED 13 *Financial Reporting in Hyperinflationary Economies* proposes requirements for financial reporting under conditions of hyperinflation.
- ED 14 *Property, Plant and Equipment* proposes the accounting treatment for property, plant and equipment, including the timing of their initial recognition, and the determination of their ongoing carrying amounts and related depreciation.
- ED 15 *Leases* proposes requirements for the accounting treatment of leasing transactions.

3. Accounting Standards Board

The Accounting Standards Board (ASB) is established under the Companies Act, 1997. It has the following functions:

- to develop, approve, amend, and revoke financial reporting standards for the purposes of this Act in respect of reporting companies, exempt companies or all companies;
- to make determinations on the application of any approved financial reporting standards; and

- to give directions as to the accounting policies that have authoritative support within the accounting profession in Papua New Guinea.

The ASB comprises:

- the Registrar of Companies (who is Chairman of the Board)
- the Auditor-General
- two representatives of the PNGIA
- one representative of the Accountants Registration Board
- two persons appointed by the Minister.

4. International Accounting Standards

The following International Accounting Standards have been approved for application in Papua New Guinea, effective for accounting periods commencing on or after 1 July 1999:

IAS 1	Presentation of Financial Statements
IAS 2	Inventories
IAS 7	* Cash Flow Statements
IAS 8	Net Profit or Loss for the Period, Fundamental Errors, and Changes in Accounting Policies
IAS 10	Events After the Balance Sheet Date
IAS 11	Construction Contracts
IAS 12	* Income Taxes
IAS 14	Segment Reporting
IAS 16	Property, Plant, and Equipment
IAS 17	Leases
IAS 18	Revenue
IAS 19	Employee Benefits
IAS 20	Accounting for Government Grants and Disclosure of Government Assistance
IAS 21	The Effects of Changes in Foreign Exchange Rates
IAS 22	Business Combinations
IAS 23	Borrowing Costs
IAS 24	Related Party Disclosures
IAS 25	Accounting for Investments (<i>withdrawn effective 1 January 2001</i>)
IAS 26	Accounting and Reporting by Retirement Benefit Plans
IAS 27	* Consolidated Financial Statements and Accounting for Investments in Subsidiaries
IAS 28	Accounting for Investments in Associates

IAS 29	Financial Reporting in Hyperinflationary Economies
IAS 30	Disclosure in the Financial Statements of Banks and Similar Financial Institutions
IAS 31	Financial Reporting of Interests in Joint Ventures
IAS 32	* Financial Instruments: Disclosure and Presentation
IAS 33	Earnings Per Share
IAS 34	Interim Financial Reporting
IAS 35	* Discontinued Operations
IAS 36	Impairment of Assets
IAS 37	Provisions, Contingent Liabilities, and Contingent Assets
IAS 38	Intangible Assets
New International Accounting Standards Not Yet Effective:	
IAS 39	* Financial Instruments: Recognition and Measurement, effective 1 January 2001
IAS 40	Investment Property, effective 1 January 2001)
* These standards are not applicable to exempt companies (i.e., companies which are not required to file their annual returns with the Registrar of Companies).	

5. PNG Accounting Standards

The following PNG standards have been issued and approved by the Accounting Standards Board:

PNGAS 3	Accounting for Plantations
PNGAS 4	Reporting Currency

6. Auditing Standards

All International Standards on Auditing, which have been drafted by the International Auditing Practices Committee and issued by the International Federation of Accountants, have been accepted for use in the Private Sector by the Accounting Standards Board.

The Auditor-General's Department is a member of the International Organisation of Supreme Audit Institutions (INTOSAI) and Government auditing is undertaken in accordance with INTOSAI Standards.