

FMM 03.43 Recognition of Commitment Provisions and Contingent Liabilities

43.1 Authority and Prescribed Requirements

- Public Finances (Management) Act 1995 (PFMA):
 - Section 5 mandates Departmental Heads to establish internal controls for accurate recording of financial obligations, including commitments and contingent liabilities.
 - Section 47K, 62 and 68 requires public bodies and statutory authorities and Provincial Governments and Local Level Governments to keep property accounts and records of its transactions and affairs. And to ensure that liabilities are controlled.

43.2 Standards and Supporting Documentation

- International Public Sector Accounting Standards (IPSAS):
 - IPSAS 19 Provisions, Contingent Liabilities, and Contingent Assets
 - IPSAS 1 Presentation of Financial Statements

43.3 Minimum Responsibilities

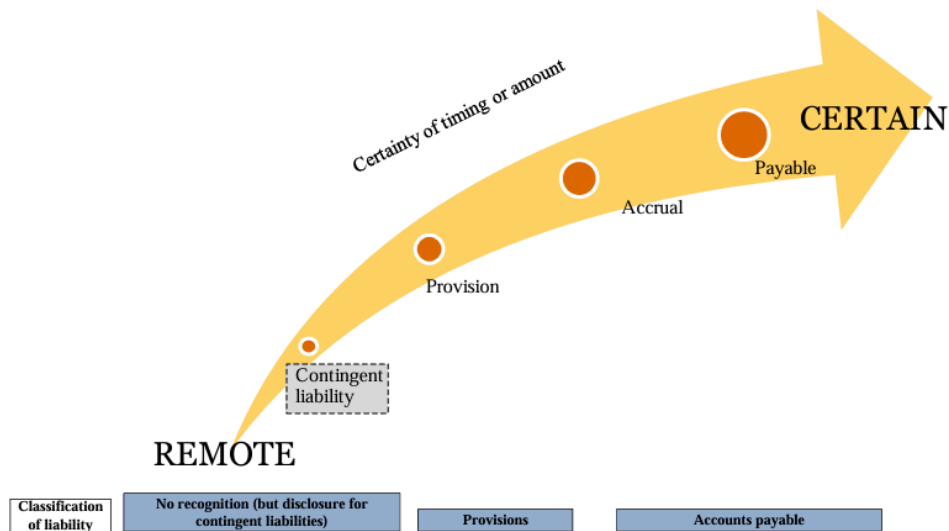
Departmental Heads are to ensure provisions and contingent liabilities are properly identified, recorded, and disclosed. An agency must establish a Contract Register as well as contingent liabilities for financial statement purposes.

Heads of Finance are to establish controls to record and monitor financial provisions and contingent liabilities and the ongoing maintenance to ensure proper classification and documentation of commitments.

The finance department head is responsible for establishing controls to consolidate commitments and contingent liabilities for national reporting purposes and provide technical guidance to agencies on compliance with PFMA and IPSAS requirements.

Internal Audit Units are to review the processes for recording and reporting provisions and contingent liabilities.

43.4 Mandated Policy



1. **Parliament must be notified of the existence of any commitment of possible future liabilities when they are identified or committed.**
2. **Commitment provisions and contingent liabilities must be recognised and disclosed as a note in the financial statements of an agency:**
 - All commitments exceeding K100,000 are to be captured on a commitment register and disclosed as a note for annual reporting purposes.
 - Multi-year commitments must be disclosed in financial reports, including their impact on future liabilities budgets.
 - Contingent liabilities must be reviewed and disclosed in financial statements where there is a possible financial obligation.
 - Unfunded commitments are prohibited, and all financial obligations must be supported by available appropriations.
 - Risk management processes must be in place to assess and mitigate contingent liabilities.
3. **Should a contingent liability give rise to the need for public expenditure, the expenditure requires the authority of an Appropriation Act.**

43.4.1 Exception for commitments incurred without Warrant release

4. In cases where an entity enters into a legally binding contract with an APC but a Warrant has not been issued at the time a claim was lodged by the contractor, the commitment must still be tracked to ensure it is recognised and prioritised when funding becomes available.

43.4.1.1 Establishment of a Commitment Register

5. Each public entity must maintain a Contract/Commitment Register for:

- Legally executed contracts.
- Multi-year contract obligations requiring staged funding.
- Emergency or high-priority expenditures that must be recognised before a warrant is issued.

6. The Contract/Commitment Register must be reconciled monthly and cross-checked with warrant releases to ensure timely recognition in IFMS.

7. Once a warrant is issued, the commitment must be entered into IFMS (or approved finance system) immediately.

8. Heads of Finance must report all commitments in the Off-System Register to the Department of Finance on a quarterly basis.

9. Commitments and Contingent liabilities are recorded as part of the agency's annual general purpose financial statements, and for agencies that form part of the Public Accounts, reported with the Department of Finance for compilation with the Public Accounts.

10. Provisions are recognised in financial statements as a note as they are probable and can be reliably measured (refer to FMM Volume 4).

11. Contingent Liabilities are also disclosed in the notes if the likelihood of an outflow of resources is possible but not probable (refer to FMM Volume 4).

12. Failure to record commitments accurately, leading to arrears or financial misstatements, may result in disciplinary action.

13. The Register must be audited annually to ensure compliance with PFMA and government financial policies.

43.4.2 Definitions

Commitment provisions are recognised when an agency has a present obligation that arises from past events, which will likely result in an outflow of resources or payments. Provisions are recognised in the financial statements because the amount and timing of the obligation are certain. Examples of Commitment Provisions:

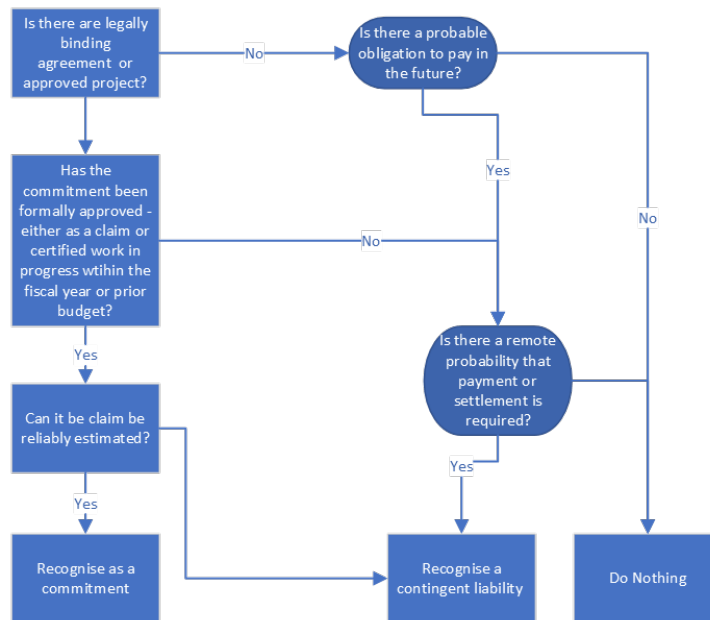
- Contractual obligations for goods or services received but not yet paid, or claims lodged but unpaid (these can be recorded in or outside of IFMS and the approved finance system).
- Court order legal settlements where the outcome and amount are reliably estimable.

Contingent liabilities represent potential obligations that arise from past events but are dependent on future events not wholly within the entity's control.

Examples of Contingent Liabilities:

- Pending litigation where the outcome is uncertain.
- Guarantees provided to third parties, where payments may be required depending on future events.

43.4.3 Difference Between Provisions and Contingent Liabilities



43.5 Non-Mandatory Guidance

Nil

Further Information	frcd@finance.gov.pg
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FMM 03.44 Accounting for Leases – Operating and Finance Leases

44.1 Authority and Prescribed Requirements

- Public Finances (Management) Act 1995 (PFMA)
- National Procurement Act 2018

44.2 Standards and Supporting Documentation

- IPSAS 43 – Leases

44.3 Minimum Responsibilities

Treasurer only has the authority to approve finance leases (defined below) as it is a form of financing by the State.

Departmental Heads must ensure all lease arrangements are assessed for classification and financial impact and are therefore, responsible for ensuring cost-benefit analysis is undertaken and documented before entering into lease agreements.

44.4 Mandated Policy

44.4.1 Definition of a Lease

A lease is an agreement whereby the lessor (owner) conveys to the lessee (user), in return for a payment or series of payments, the right to use an asset for an agreed period. Leases are generally categories as either an operating or finance lease.

44.4.1.1 Operating Lease

- An operating lease does not transfer the ownership of the asset at the end of the term of the lease or have a clause or opportunity to take over the ownership of the lease during or at the end of the lease term.

1. As an operating lease, the lease is not recorded as a liability nor is the leased asset recorded as an asset.

- 2. For any lease or service agreement, the total value of the lease or agreement must be approved by a delegated within their delegated authority, not a portion. Only the delegate can sign the lease or agreement.**

For example, if an officer seeks to hire a vehicle, then the total days that the vehicle is to be leased must be specified and approved by the delegate. The vehicle cannot be approved for hire based on number of days or based on day rate alone, the total value needs to be approved for the lease term.

- 3. An operating lease does not require the Treasurer approval as a borrowing, guarantee or loan by the State.**
- 4. Payments are recognised as an expense over the lease term when paid. Outstanding lease payments are recognised as a commitment on the commitment register (refer to FMM 03.20 Expenses).**

44.4.1.2 Finance Lease

- A finance lease transfers substantially all the risks and rewards incidental to ownership, even if title is not transferred. A finance lease usually includes an arrangement where the lessee will have the asset transferred to them (to the State) or provides an option for the lessee to pay for the asset to be transferred to them after a period of time of leasing.
- A finance lease is essentially a financing agreement or form of borrowing to acquire and asset. Typical indicators of a finance lease include:
 - Ownership transfers to the lessee at the end of the lease.
 - Option to purchase the asset with or without a residual payout amount.
 - Lease term covers most of the asset's useful life.
 - Present value of lease payments equals or exceeds fair value of the asset.
 - The leased asset is of a specialised nature usable only by the lessee.

5. Both the value of the asset and total expected value of the lease liability must be recorded in the approved accounting system of the agency. The liability is equal to the present value of minimum lease payments and the asset is registered on the asset register.
6. The lease is a form of borrowing and must have approval of the Treasurer prior to entering into the agreement (refer to FMM Volume 3 on Loans, Borrowings and Guarantees for further details).
7. Before entering into any lease, agencies must:
 - Conduct a cost-benefit analysis comparing leasing to purchasing;
 - Evaluate risks such as technological obsolescence, maintenance obligations, or ownership value;
 - For long-term, high-value or recurring lease costs, assess the risk of creating long-term liabilities without appropriate budgeting.

44.5 Non-Mandatory Guidance

Nil

Further Information	frcd@finance.gov.pg – general information enquiries@treasury.gov.pg for assistance on finance leases
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