

State Contracts - The importance of a valid Contract

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Introduction

The Independent State of Papua New Guinea (State) through its institutions such as the provincial and local-level governments, national government departments and statutory bodies, commonly procure goods and services through contracts. Like any other organization, in order to function, the State is required by law to procure its goods and services from service providers through contractual arrangements. In such instances, some contracts are verbal - for minor contracts, and some are written, for major contracts.

The legal basis for the State to enter into a contract, either domestically or overseas is provided for under Section 247 of the *Constitution*. It reads:

- (1) *Papua New Guinea has power to acquire, hold and dispose of property of any kind, and to make contracts, in accordance with an Act of the Parliament; and*
- (2) *Papua New Guinea may sue and be sued, in accordance with an Act of the Parliament.*

While there are other subordinate laws giving effect to Section 247(1) of the *Constitution*, the primary legislation governing State contracts is the *Public Finance (Management) Act* 1995 (PFMA). This legislation provides the overarching framework for the governance of public funds.

The necessity of entering into a well compliant and lawfully valid contract with the State is imperative. The courts have held that, a person dealing with the State or any of its arm or instrumentality or a public institution, to which the PFMA applies, is bound to comply with the requirements of the Act, and any person deemed to be dealing with such institutions or bodies is deemed to be aware of these requirements.¹

This paper provides a cursory discussion on State contracts and the implications of non-compliance with the requirements of the PFMA. The supplies and tenders board process, the distinction between a major and a minor contract, and an examination of the importance of an Authority to Pre-Commit (APC), and an Integrated Local Purchase Order (ILPOC or Form 4A) under the PFMA will also be presented. A number of relevant and recent case laws will be discussed to demonstrate the present position and the attitude taken by the Courts in clarifying these processes.

The Supply and Tenders Board

The PFMA provides that before a contract is entered into with the State for all major contracts (that is, contract value above K100,000.00), a public tender must be called for the public to bid through the tender process.² Bids are submitted to the Central Supply and Tenders Board (CSTB) for the national Government and Provincial Supplies and Tenders Board (PSTB) for provinces. The CSTB and PSTB are established under Sections 39 and 39B of the PFMA respectively. The Minister of Finance may also establish specialized national supply and tenders boards under Section 39A of the PFMA.

Public tenders involve the widespread advertising of opportunities to supply the government with the required goods or services. The public tender process promotes the principle of competition. This process must be differentiated from selective tenders, expressions of interest and other procurement

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¹ See *Fly River Provincial Government v Pioneer Health Services Ltd* (2003) SC705.

² Section 61 PFMA. See also Part 13 of the Financial Management Manual (2006).

mechanisms. Selective tenders are not allowed under the PFMA as they restrict the level of competition.

The processes available for procurement must also be used for the disposal of items no longer required by the government. In circumstances where a supply and tenders board issues a certificate of inexpediency (CoI), the public tendering process will not apply. A CoI may only be issued in exceptional circumstances as outlined in Part 13, Division 4 of the *Financial Management Manual*.

The role of a supply and tenders board is to ensure that major procurements conducted under its authority; (1) have been carried out in accordance with the PFMA, the Regulations, and Financial Instructions; and (2) represent “value for money” for the government of Papua New Guinea (PNG).

In carrying out this role supply and tenders boards must adhere to the principles of transparency, effective competition, fair and ethical dealing and efficient and effective operation as outlined in Part 11 of the Financial Management Manual. In addition, the CSTB has an additional role to ‘control and regulate’ procurement in relation to ‘minor procurements’, major procurements and PSTB, in accordance with Section 39 of the PFMA. This supervisory role does *not* extend to specialized national supply and tenders boards.

Responsibilities of Departmental Heads in relation to Procurement

To avoid corrupt and illegal dealings, departmental heads are responsible for ensuring compliance with the new changes to the PFMA and the Financial Instructions. Failure to comply with these new provisions could result in serious disciplinary actions against the departmental heads. The head of each spending department or province must ensure that all pre-commitments made by their department or province are included in the annual bids or estimates for the following year (and any subsequent years).

Purchases, Claims and Contracts under K100,000

The Secretary for Finance is not required to approve an APC for amounts less than K100,000 (even though the amendments to the PFMA does make allowance for this). If there are insufficient funds available in a vote to make the purchase using an ILPOC in the current year, the relevant department should make use of available capacity, or seek to have the purchase funded through estimates for the following year. The relevant department or province should not enter into a contract with a supplier if there are insufficient funds available. The relevant department cannot anticipate that funds will be available in the following year (without an APC). These are the cases that Sections 47B, 47C and 47D of PFMA are intended to eliminate (that is, unauthorised officers ordering goods or services without an ILPOC when there are no funds or insufficient funds available).

An ILPOC is the only legitimate evidence that funds are immediately available in the current year. An APC (for amounts over K100,000) is the only legitimate evidence that funds will be made available later in the current year or in a following year. Public officials who deal with suppliers and contractors without an ILPOC or an APC are not acting on behalf of their department or the government. Authorised departmental officers are responsible for obtaining quotations on material or services that are valued up to K100,000 in accordance with the table below:³

<i>Value</i>	<i>Process</i>	<i>Detailed Reference</i>
Less than K5,000	Verbal Quotation	Part 12, Division 2, Financial Management Manual
K5,000 up to K100,000	Written Quotation	Part 12, Division 3, Financial Management Manual

³ Part 12, Financial Management Manual (2006).

Verbal Quotations (for Purchases less than K5,000)

Three verbal quotations are obtained for purchases valued at less than K5000. Quotations are to be recorded in a Quotations Register that includes the following (minimum) information:

- (1) Date of quotation.
- (2) Brief description of the goods, services or works required.
- (3) Price quoted.
- (4) Name of each company providing quote.
- (5) Name of each company's representative from whom the quotation is obtained.
- (6) Name of departmental officer obtaining the quotation.
- (7) Company selected to supply the goods, works or services.
- (8) Reason for selection of the successful company.
- (9) General comments – relating to the quotation.

Each minor purchase is to be ruled off, so that anyone inspecting the Quotations Register can easily determine which quotation relate to a particular purchase. The Quotations Register is to be legible and is to be made available for auditing purposes. Where three suppliers are unable to provide a quote, for example, when proprietary brand items are required, and there is only one supplier, the reason for this is to be recorded in the 'General Comments' section of the Quotations Register. The departmental officer should provide answers to technical questions from suppliers arising during the quotation period. All potential suppliers should be provided with the same information. The departmental officer is to ensure that the goods or services proposed by potential suppliers will meet all relevant technical, delivery and other legitimate requirements of the department.

A contract is to be awarded to the company that meets the relevant technical, delivery and other legitimate requirements of the department, and provides the lowest cost arrangement. Once a supplier is selected, the appropriate requisitions are raised for processing accordingly.

Written Quotations (for purchase valued from K5,000 and less than K100,000)

According to the PFMA, three written quotations are usually obtained for purchases valued between K5000 and under K100,000. Quotations are to be requested from potential suppliers in writing. The department is to provide the potential suppliers a complete 'Description of Requirement', including, but not limited to, quantity, description, delivery requirement, timings, specifications, standards, drawings, special conditions, and any additional information required by the department.

Prices are to be recorded on the Quotations Register, that includes the following (minimum) information:⁴

- (1) Date of quotation.
- (2) Brief description of the goods, services or works required.
- (3) Price quoted.
- (4) Name of each company providing quote.
- (5) Name of each company's representative from whom the quotation is obtained.
- (6) Name of departmental officer obtaining the quotation.
- (7) Company selected to supply the goods, works or services.
- (8) Reason for selection of the successful company.
- (9) General comments – relating to the quotation.

All three written quotations received, and the detailed 'Description of Requirement' are to be attached to the relevant page in the Quotation Register.

Each major purchase is to be ruled off, so that anyone inspecting the Quotations Register can easily determine which quotations relate to a particular purchase. The Quotations Register is to be legible and be made available for auditing purposes. Where three suppliers are unable to provide a quote, for example, when proprietary brand items are required, and there is only one supplier, the reason for this is to be recorded in the 'General Comments' section of the Quotations Register. The departmental officer should provide answers to technical questions arising during the quotation period. All potential

⁴ Part 12, Division 3, Financial Management Manual.

suppliers should be provided with the same information. The departmental officer is to ensure that the goods or services proposed by potential suppliers will meet any relevant technical, delivery and other legitimate requirements of the department.⁵

Purchases, Claims and Contracts over K100,000

Where a department wishes to enter into contracts for amounts of K100,000 or above, and there will be funds available to meet the schedule of payments under the contract (either in the current or subsequent financial years), that department will be able to apply to the Secretary for Finance for an APC. It will be the head of that department's responsibility to ensure that funds are secured in subsequent year's estimates and appropriations through their budget negotiations with the Department of National Planning and Monitoring and with the Department of Treasury.

An application for an APC should be completed by the officials of the relevant department, and signed by the head of that department. All relevant parts of the application form should be completed. The APC must be applied for and obtained by the relevant spending department prior to inviting any tender including applying for a CoI. All other requirements of any relevant supply and tenders board must be complied with after an APC has been obtained. An APC is not required for utility payments.

The application should be delivered to the First Assistant Secretary (Expenditure and Cash Management Division) of the Department of Finance, where it will be registered. If the application form is not complete, the application will not be registered or accepted and will be returned to the relevant department if such omissions are subsequently discovered. The First Assistant Secretary will evaluate the application according to the established criteria.

The results of this evaluation are then considered at the weekly APC Committee meeting. The committee include heads of the relevant divisions of the Treasury Department and the Department of National Planning and Monitoring in order to jointly ascertain the merits of the APC request and the likelihood of funds becoming available to fund payments under the contract. The First Assistant Secretary, in his capacity as Chairman of the APC Committee, makes recommendations to the Secretary for Finance as to whether an APC should be approved, together with a recommended maximum amount of pre-commitment.

If approved by the Secretary, the First Assistant Secretary will allocate an APC number, and the APC details will be entered into the register accordingly. The APC will be in triplicate – white (original for the supplier or contractor); blue - Department of Finance copy, and green - implementing department's copy. For all APCs the Department of Finance will make and retain a photocopy of the APC form.⁶ The entire APC form is then passed on to the nominated contact officer of the implementing department.

This officer will then make a photocopy of the form and forward the entire APC form, together with any requisition (FF3), to the relevant supply and tenders board. The relevant supply and tenders board will not proceed to tender or grant a CoI unless an APC has first been obtained from and approved by the Secretary for Finance. The relevant supply and tenders board will write their file number on the original of the APC, and place their stamp and date over the top of that file number.

When a notice of successful tender or CoI has been issued by a supply and tenders board, it will fill in the name of the successful contractor or supplier. The board will make and retain a photocopy of the APC and return the blue copy to the Department of Finance, and the original (white) and the implementing department copy (green) to the nominated contact officer on the APC. The officer will then forward the original APC to the successful supplier or contractor.

An APC/ILPOC

Section 47D of the PFMA provides the definition of an APC and an ILPO. APC is defined as:

⁵ Ibid.

⁶ At this stage the supplier or contractor has not filled out the form.

Authority to Pre-commit Expenditure means an Authority to Pre-commit Expenditure issued under Section 47B.

ILPOC is defined as:

Integrated Local Purchase Order or Claim (ILPOC) means Finance Form 4A – Integrated Local Purchase Order or Claim issued in accordance with the Financial Instructions.

The APC process was introduced to bring under control the problem of 'arrears.' The APC process is contained within Sections 47B, 47C, and 47D of the PFMA. The amendments to the PFMA in 2016 is aimed at limiting the validity of contracts with the government to:

1. Those that are authorised by a PGAS generated ILPOC or Form 4A. [The national Department of Works shall continue using its ORACLE based computer generated ILPOC], that is, where funds are available in the current year, or,
2. Where there is a need to commit expenditure in advance of funds becoming available, those that are authorised by the Secretary for Finance as evidenced by his signature on an APC or Form5A.

The 2016 amendments provided that unless contracts with the government are supported by one of these two forms of authority, those contracts will be null and void and will not be enforceable against the government.

The purpose of the APC process is to ensure proper accounting, management and reporting on the Pre-Commitment of Expenditure is maintained at all levels of the national, provincial and local-level governments.

Section 47B of the PFMA provides for the legal basis for APC. It is set out in full:

47B. Authority to pre-commit expenditure.

(1) The Departmental Head of the Department responsible for financial management may issue to a Departmental Head an Authority to Pre-commit Expenditure in relation to the purchase of property or stores or to the supply of goods or services where the Departmental Head of the Department responsible for financial management is satisfied that-

- (a) in the case of proposed expenditure exceeding K100,000.00-
 - (i) in the provisions of this Part have been complied with in relation to the purchase or supply; and
 - (ii) funds will be available to meet the proposed schedule of payments for the purchases or supply; and
- (b) in the case of proposed expenditure not exceeding K100,000.00, the circumstances of the proposed expenditure are such that it is appropriate to authorize the Department, to the Departmental Head of which the Authority to Pre-Commit Expenditure was granted, to enter into a contract for the purchase of property or stores or for the supply of goods or services notwithstanding that the full amount of funds to meet the payment required under the contract is not immediately available but it is within the appropriation for the year to which the Authority to Pre-commit Expenditure relates for the item to which it relates.

(2) An Authority to Pre-Commit Expenditure under Subsection (1) shall specify-

- (a) the purchase of property or stores of the supply of goods or services to which it relates; and
- (b) the maximum amount to which the Authority extends.

(3) Subject to Subsection (4), an Authority to Pre-commit expenditure under Subsection (1) authorizes the execution, in accordance with and subject to compliance with the procedures specified in this Part, of a contract for the purchase of property or stores or for the supply of goods and services specified in the Authority to the extent of an amount not exceeding the maximum amount specified in the Authority.

- (4) A contract under Section 47 shall not be entered into unless –
 - (a) an Authority to Pre-commit Expenditure under Subsection (1) relating to the contract has been issued; and
 - (b) all other requirements of this Part relating to the contract have been complied with.

Section 47C and 47D PFMA make it clear that contracts which have not complied with the Act are null and void. Section 2A of the *Claims By and Against the State Act* 1996 (CBASA), reinforces this position.

The recently enacted *Public Money Management Regularization Act, 2018* (PMMR) takes it one step further in its application by ensuring that the requirement of the APC and ILPOC is made applicable to all statutory bodies. Section 11 of the PMMR is in the following terms:

11. CLAIM AGAINST THE STATE AND STATUTORY BODIES NOT ENFORCEABLE IN CERTAIN CIRCUMSTANCES.

(1) A claim for payment, compensation, restitution, damages or any other form of relief, including injunctive or declaratory relief, against the State or a statutory body based on equity or equitable principles in respect of the value of works, goods or services rendered to the State or a statutory body shall not be enforceable through the Courts or otherwise, unless the seller of the property or stores or the supplier of the works, goods or services produces-

- (a) a properly authorized ILPOC; or
- (b) an Authority to Pre-commit Expenditure,

relating to the property or stores or works, goods or services, the subject of the claim, to the full amount of the claim.

(2) A claim for payment, compensation, restitution, damages or any other form of relief, including injunctive or declaratory relief, against the State or a statutory body based on the undertaking or promise of any person, whether or not that person had the actual, implied or ostensible authority of the State or statutory body to give or make that undertaking or promise, shall not be enforceable, through the courts or otherwise, unless the person making the claim produces -

- (a) a properly authorized ILPOC; or
- (b) an Authority to Pre-commit Expenditure,

relating to the undertaking or promise, the subject of the claim, to the full amount of the claim.

(3) The Court shall, on application by the State, stay a claim specified in Subsections (1) and (2), if the person making the claim cannot produce, on demand by the State -

- (a) a properly authorized ILPOC; or
- (b) an Authority to Pre-commit Expenditure,

relating to the subject of the claim, to the full amount of the claim.

The message is clear from the legislature. Any person doing business with the State must show that he or she has a valid APC and ILPOC to perform the contract. Without a valid APC or ILPOC, the purported contractual arrangement is invalid.

Suppliers and contractors cannot seek to be paid for any goods or services they have provided, where they did not first obtain an ILPOC or an APC. Departments are reminded that normal procurement procedures apply for amounts under K100,000. This includes obtaining three written quotes and the issuance of an ILPOC. The only exemption to the above will be the use of a FF4 for purchases in genuine emergency situations up to a maximum amount of K300. Examples could include purchase of food items for a large and unexpected police cell intake in a remote area. Fixing a dripping tap, purchase of stationery and other such examples cannot and do not constitute an emergency. This provision may not be used to substitute for poor planning and preparation by a department.

Implications of non-compliance - ILPOCs & APCs

The courts have taken an obstinate approach to safe guard the provisions of the PFMA (Sections 47B, 47C and 47D) for purported contracts with the State, particularly the requirement to produce a valid ILPOC for minor contracts and an APC for major contracts.⁷ In the recent decision in *Ray (Trading as Bara Construction) v Numara* (2018) N7380, Hartshorn J, dismissed the proceedings for failing to comply with the requirements of Sections 47B, 47C and 47D of the PFMA and Section 2A of the CBASA. His honour made the following observations:

In regards to the submissions by Jhelson that a General Expenses Form and a Requisition for Goods and Services were endorsed in support of the contract, that a Certificate of Completion was issued and therefore the contract is valid and enforceable, ss 47D PFMA and 2A Claims Act are quite clear. A contract purportedly entered into for and on behalf of the State without full compliance of the PFMA is null and void and shall not be enforced in any court and any property, goods or services supplied under such a contract may not be sued upon and no claim is enforceable in respect of them, in any court. Further such a claim shall not be enforceable through the court unless the supplier of the services produces the requisite Integrated Local Purchase Order and Claim (ILPOC) or Authority to Pre-Commit Expenditure (APC).

Here there is not in evidence an APC or ILPOC issued under s 47B PFMA. There is no pleading in the statement of claim to the effect that either an APC or ILPOC were issued for the contract. The General Expenses form and Requisition for Goods and Services are not the necessary APC or ILPOC. I note further the General Expenses form and Requisition were both purportedly signed after services were purportedly provided. Jhelson has not produced the requisite APC or ILPOC. His claim is unenforceable under s 47D PFMA and s 2 Claims Act.

As Jhelson has failed to meet the requirements of ss. 47B, 47C, 47D PFMA and s.2A Claims Act, a reasonable cause of action is not disclosed and his claim is frivolous as it is bound to fail. When a proceeding is bound to fail, it has been held to be frivolous: *Tonny Wabia v BP Exploration Operating Co Ltd* [1998] PNGLR 8, *Kiee Toap v The State* (2004) N2731, N2766, *Lerro v Stagg* (2006) N3050 and *Tompion v Anderson* [1973] VR 321. Consequently, the proceeding should be dismissed. Given that it is not necessary to consider the other submissions of counsel.

Her Honour Polume, J in a consolidated hearing on 9th November, 2018 in *WS No. 1119 of 2015, WS No. 1121 of 2015, WS No. 1120 of 2015, WS No. 1122 of 2015* and *WS No. 1188 of 2015* reinforced the ruling in *Ray v Numara* and dismissed the foregoing proceedings, for non-compliance with Sections 47B, 47C, and 47D of the PFMA and Section 2A of the CBASA for the plaintiff's failure to produce a valid APC and ILPOC.

His Honour Justice Hartshorn J, very recently on 31 July, 2019, in a number of 19 different education contractor claims further reaffirmed the position in *Ray v Numara* by dismissing the foregoing claims for non-compliance with Section s 47B, 47C, and 47D of the PFMA and Section 2A of the CBASA⁸.

⁷ A similar provision is reproduced as Section 2 in the *Claims By and Against the State Act* and Section 11 of the *Public Money Management Regularisation Act*.

⁸ (1) WS 1378 of 2015 – Onaga Kokoa trading as 3JS Construction & Ors; (2) WS 1434 of 2015 - Pana Bara trading as Bex Maintenance Services & Ors; (3) WS 1342 of 2015 - Oka Rau trading as Rakaru Construction & Ors; (4) WS 1345 of 2015 – Nima Baro trading as ENhay Construction & Ors; (5) WS 1382 of 2015 – Poini Waigi trading as Pik Construction & Ors; (6) WS 1504 of 2015 - LaksyVagi trading as Wanimaro Construction & Ors; (7) WS 1432 of 2015 – Boi Baro trading as BNK Construction & Ors; (8) WS 1433 of 2015 – Boi Baro trading as BNK Construction & Ors; (9) WS 1428 of 2015 - Beau Biau trading as Timothy Numara & Ors; (10) WS 1517 of 2015 - Wasco Levi trading as Barulu Construction Ltd & Ors; (11) WS 1405 of 2015 - Trasa Suki Trading as Amaka Construction & Ors; (12) WS 1407 of 2015 - Trasa Suki trading as Amaika Construction & Ors; (13) WS 1307 of 2015 – Rupuna Pikita trading as Creative Network Marketing & Ors; (14) WS 1372 of 2015 - Les Willie treading as LW Maintenance & Ors; (15) WS 1568 of 2015 - Kini Roy trading as Balavuali Construction & Ors; (16) WS 1390 of 2015 -

The cases highlighted so far are contractor claimants alleging to have done work for the Education Department in NCD through some purported contractual agreements. Even as some produced very strong evidence of work done and clear service rendered to the Education Department on behalf of the State, the mere fact that there was non-compliance with the PFMA, the proceedings were dismissed on those bases alone.

Conclusion

The consequences of contracting with the State without fulfilling the requisites of the law can be devastating. The celebrated Supreme Court case of *Fly River Provincial Government v Pioneer Health Services Ltd*⁹ is on point which affirms that a failure to comply with the mandatory requirements of the PFMA will no doubt render such contract illegal, and therefore null and void and unenforceable in court.

The recent dismissal of more than 20 education contractor claims by the court clearly indicates the present approach by the courts that compliance of the law, particularly the PFMA and the CBASA is mandatory and therefore imperative. The onus is on the person dealing with the State or any of its arm or instrumentality or a public institution to which the PFMA applies, to ensure that there is full compliance of the requirements of the Act as the law demands that any person deemed to be dealing with such institutions or bodies are deemed to be aware of these requirements.

⁹ Kema Investments Ltd & Ors; (17) WS 1377 of 2015 - Kaina Investment Ltd & Ors; (18) WS 1519 of 2015 - Jhelson Ray trading as Bara Construction & Ors; and (19) WS 1166 of 2015 - Havaik Ltd & Ors.
Ibid.