

**Small and Micro Industries Leader and Entrepreneur Promotion Project III (SMILE-III)
- 2010**

1. Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, except for the effects of the adjustments arising from the matters referred to in the paragraph 3 of this report, I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2010 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2010 in accordance with Generally Accepted Accounting Principles,
- (b) the withdrawals from and replenishments to the Special Yen Account during the year ended 31 December 2010 had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2010 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,
- (c) the statements of expenditure (SOEs) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement,
- (d) satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (e) the financial covenants laid down in the Loan Agreement had been complied with.

3. Audit Observations

3.1 Presentation of Financial Statements

Following observations are made.

- (a) Progress of sub-loans for each component of the technical assistant loan and the general loan had not been disclosed separately in the financial statements.
- (b) Cumulative disbursement summaries of loans in district wise as well as in sector wise had not been disclosed in the financial statements.

3.2 Lack of Evidence for Audit

Following observations are made.

- (a) Information relating to issue of Eligibility Clearance and approval granted for sub-loans by the PMU during the year under review were not made available to audit.
- (b) A fixed assets register or any other adequate records with regard to the fixed assets amounting to Rs. 5,498,356 had not been made available to audit. Further, documentary evidence relating to handing over of such assets to the Ministry of Industry and Commerce, which is the present implementing agency of the Project, by the then Ministry of Enterprise Development and Investment Promotion, which was the former implementing agency, had not been made available to audit. Accordingly, the existence and valuation of such assets could not be ascertained in audit due to lack of proper evidence.
- (c) Even though, a sum of Rs. 4,239,778 had been paid as personal emoluments for the year under review, appropriate records such as attendance records, salaries and wages records, overtime and holiday pay records, etc. were not made

10.9 million or 6.9 % had been disbursed up to the end of the year 2009. However, the details of utilization of Technical Transfer loan during the year under review were not made available to audit.

- (ii) As per Section 1(4)(a) of Schedule 1 of the Loan Agreement, the scope of the general loan is to improve the productive capacity of small and micro industries. According to the information made available, the pattern of disbursement of loans in sector wise were as follows.

Sector -----	Disbursements made during the year 2010 ----- Rs. Million	Disbursements as a percentage ----- %
Services	69.79	25
Construction	25.08	9
Metal Products	18.35	6
Garments	5.22	2
Agro Industries	9.9	4
Wood and Wood Products	12.72	4
Animal Husbandry	13.37	5
Food Processing	67.01	24
Miscellaneous	9.5	3
Rubber Products	7.46	3
Textiles	9.91	4
Transportation	12.25	4
Plastic Products	3.82	1
Printing and Paper Products	14.68	5
Chemical	3.50	1
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Total	282.7	100
	=====	=====

According to the above information, out of total loan disbursements of Rs. 282.7 million made during the year under review, a sum Rs.173.01 million or 61.19 % of the total disbursement had been distributed only in three Districts, while the balance disbursement of Rs. 109. million had been distributed among other 10 Districts, which shows an unequal distribution of funds, and also, it was revealed that, no any amount of loan had been distributed among the balance 12 Districts.

(b) Loan disbursement issues

Total loan disbursements as at the end of the year under review was Rs. 9,321.2 million and out of that the disbursement made during the year under review was Rs. 282.7 million. Following observations are made in this regard.

- (i) According to the information made available, adequate records, files and other documentations had not been maintained by the PMU to enable to vouch the disbursements made during the year under review satisfactorily. Accordingly, number of applications received for sub-projects, project appraisal reports, eligibility clearance reports, loan approval and reasons for rejection of applications, delays in approvals of loans, delays in disbursements, quarterly progress reports, etc. had not been made available for audit.
- (ii) Loans amounting to Rs. 282.7 million had been granted to 166 persons during the year under review. However, out of the 166 loan documents including loan applications documents for 17 loans amounted to Rs.41.6 million or 14.7 % only had been submitted to audit.
- (iii) Out of the loans amounting to Rs. 282.7 million disbursed during the year under review, a sum of Rs. 272.1 million or 96% had been disbursed within 5 months period from 01 January to 31 May 2010 and the balance amounting to Rs. 10.7 million or 4 % had been disbursed during the period of 7 months from 01 June 2010. Therefore, it was

3.4 Human Resource Management

Following observations are made.

According to Section 2:2 of the Management Services Circular No. 33 of 05 April 2007, D WHDP LGHQWLILHG DV ³&RUH 3URMHFW 6WDII´ FRQVL may be deployed to ensure smooth and timely implementation of the project. However, according to the information made available, it was observed that in several instances the aforesaid instructions had not been followed. Details are given below.

- (a) The implementation of SMILE III Project had been transferred from the then Ministry of Enterprise Development and Investment Promotion to the Ministry of Industry and Commerce during April 2010. However, a team identified as ³&RUH 3URMHFW 6WDII´ FRQVLVWLQJ RI WKH 3URM been appointed to ensure smooth and timely implementation of the Project.
- (b) Before transferring the Project to the Ministry of Industry and Commerce, Key posts of Senior Environmental Officer, Disbursement Officer and Statistical/ MIS Officer had not been recruited. Further, seven employees including the posts of Accounts Assistant, Driver, Data Entry Operator, Office Assistant and three Trainees had been recruited exceeding the approved cadre without obtaining the proper approval from the Department of Management Services.

3.5 Unresolved Audit Issues

According to the information made available it was revealed that the following audit issues identified and reported to the management of the Project in my previous years ¶ audit reports had not yet been rectified.

- (a) Before transferring the Project to the Ministry of Industry and Commerce, following issues were made relating to the recruitment of staff to the PMU of the Project.

