

## State Timber Corporation - 2012

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### 1. Financial Statements

#### 1.1 Qualified Opinion

In my opinion, except for the effects of the matters described in paragraph 1.2 of this report, the financial statements give a true and fair view of the financial position of the State Timber Corporation as at 31 December 2012 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

#### 1.2 Comments on Financial Statements

##### 1.2.1 Sri Lanka Accounting Standards

Non - compliance with the following Sri Lanka Accounting Standards were observed.

Reference to Sri Lanka  
Accounting Standard(LKAS)

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Non - compliance

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(a) LKAS - 01

Although all income and expenditure relating to the year of accounts should be shown in the comprehensive income statement, the interest received on staff loan revolving fund had not been included therein.

(b) LKAS - 16

(i) Property, Plant and Equipment belonging to the Corporation had not been revalued. But, a portion of a building stated at Rs. 5 in the financial statements after being written off had been rented out for Rs. 15 million. The value of that building had not been revalued and not shown the fair value in the financial statements. As a result, the assets and the equity of the Corporation had been

understated. Further, as the depreciation for that building had not been adjusted in the financial statements, the profit was also overstated to the value of that amount.

- (ii) Although the possession of 74 lands existed under the Department of Conservation of Forest had been transferred to the Corporation, the value of such assets had not been disclosed in the financial statements for the year under review and as such the value of assets and the equity had been understated.

(c) LKAS - 37

Although the provision or relevant disclosures in respect of contingent liabilities should be stated, the requirements stated in the standard had not been disclosed in respect of the following items.

- The government had sustained a loss of Rs.32,462,148 due to unauthorized felling in the Bagawanthalawa Chapalton commercial thinning plot of land.
- The government had sustained a loss of Rs. 35,169,565 due to discrepancies occurred in removing timber from submerging areas of Rambakenoya reservoir and due to forest offences.
- It had not come to a compromise that the stumpage amounting to Rs. 65,209,269

included in the payable expenditure of Rs. 188,667,206 to be paid to the Department of Conservation of Forest even up to 30 September 2013. It had not been shown as a provision for contingent liabilities and shown as accrued expenses in the accounts.

- Even though the arrears of salaries amounting to Rs. 1,957,174 had to be paid to an interdicted officer who had acquitted from his charges, no provision had been made therefore.

(d) LKAS - 40

A part of the Head Office premises at Battaramulla of the Timber Corporation had been rented out to the Ministry of Environmental and Renewable Energy and to the Department of Conservation of Forest at an annual rental of Rs. 15,154,488 but the value of that building had not been shown under investment assets.

### **1.2.2 Accounting Policies**

Accounting policies on trade and other debtors had not been disclosed in the final accounts.

### **1.2.3 Unexplained Differences**

Even though as per the financial statements of the Corporation, the stumpage to be paid to the Department of Conservation of Forest as at the end of the year under review amounted to Rs. 474,283,658 the amount receivable according to the accounts of the Department of Conservation of Forest amounted to Rs. 560,288,680. As such a difference

of Rs. 86,005,022 was observed between the financial statements of the Corporation and the accounts of the Department and it had not been explained and reconciled.

#### **1.2.4 Accounts Receivables and Payables**

The following observations are made.

- (a) The total trade debtors amounted to Rs. 637,121,375 out of which a sum of Rs. 405,368,846 was more than 90 days representing 64 per cent of the total debtors.
- (b) The debtor balance due from a private institution had included a sum of Rs. 11,873,954 which was receivable from a private company since 1983.
- (c) The Corporation had granted an interest free loan of Rs. 2,000,000 in the year 1988 to the Kataragama Ashthapala Fund. A sum of Rs. 40,000 had been received in the year 2012 and a further balance of Rs. 1,075,000 was due as at the end of the year under review.
- (d) Action had not been taken to settle the Turnover Tax balance of Rs. 398,627 which was brought forward prior to the year 2010 even by 30 September 2013.
- (e) Action had not been taken to bring the refundable tender deposits made by the timber suppliers for providing timber to the Corporation amounting to Rs. 2,270,950 which had been brought forward since the periods ranging from 2 to 4 years in to revenue or to refund them.
- (f) Necessary steps had not been taken to bring into revenue or to settle a sum of Rs. 14,344,600 which was deposited by various suppliers for performance bonds and brought forward from 2 to 6 years.

#### **1.2.5 Non- compliance with Laws, Rules, Regulations and Management Decisions**

Preliminary reports or final reports to be furnished in terms of Financial Regulations 104(3) and (4) had not been submitted in respect of 19 vehicle accidents even by 30 September 2013.

## **2. Financial Review**

### **2.1 Financial Results**

According to the financial statements presented the net profit before tax for the year ended 31 December 2012 amounted to Rs. 801,681,308 as compared with the net profit before tax of Rs. 603,498,864 for the preceding year. Accordingly an improvement of Rs. 198,182,444 in the financial results was shown. The increase in sales turnover amounting to Rs. 411,346,976 during the year had been the main reason for that increase.

An increase of Rs. 58,265,410 or 36.55 per cent in the non- operating income was shown in the year under review as compared with the preceding year. Increase in interest income by 39.07 per cent and the profit of 505.27 per cent generated from fluctuation of foreign exchange rate had been the reason for it.

### **2.2 Legal Cases Initiated Against the Corporation**

The following observations are made.

- (a) The “B” report had been submitted to the Magistrates Court of Dehiattakandiya by the Department of Conservation of Forest against the State Timber Corporation in respect of losses amounting to Rs. 35,169,565 incurred by the government due to discrepancies occurred in removing timber in the catchment areas of Rambakenoya and forest offences.
- (b) The loss sustained by the Government due to unauthorized felling at Bagawanthalawa Chapalton Commercial thinning plot of land amounted to Rs. 32,462,148 and the Conservator General of Forest had informed that this loss had to be paid by the State Timber Corporation.

## 2.3 Working Capital Management

The following observations are made.

(a) Even though the gross profit ratio of 43.3 per cent had increased to 47.29 per cent by 3.99 per cent in the under review as compared with the preceding year, the net profit ratio had dropped from 10.52 per cent to 5.03 per cent by 5.49 per cent.

### (b) Liquidity Ratios

<u>Liquidity Ratio</u>	<u>Standard Ratio</u>	<u>2012</u>	<u>2011</u>
Current Ratio	2:1	3.74:1	4.38:1
Acid Ratio	1:1	2.75:1	3.24:1

## 3. Operating Review

### 3.1 Performance

#### (a) Timber and Timber Related Products

The actual production of the Corporation for the year under review as compared with the estimated production is given below.

<b>Particulars</b>		<b>Estimated Production</b>	<b>Actual Production</b>	<b>Variance F/(A)</b>	<b>Percentage of Variance F/(A)</b>
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Timber Logs	M <sup>3</sup>	90,713	132,859	42,146	46.46
Sawn Timber	M <sup>3</sup>	6,745	4,955	(1,790)	(26.54)
Transmission Poles	(units)	33,500	30,469	(3,031)	(9.05)
Sleepers	(units)	81,300	117,306	36,006	44.29
Round Pos poles	(units)	59,450	152,837	93,387	157.08
Fence posts	M <sup>3</sup>	46,400	79,608	33,208	71.57
Fire Wood	( Units)	53,350	104,316	50,966	95.53

Wall Panel	(Lme)	30,000	1,850	(28,150)	(93.83)
Elephant Poles	M <sup>3</sup>	34,250	50,674	16,424	47.95
Furniture	Rs .Mn	172.8	156	(16.8)	(9.72)
Imported Timber	(units)	5000	Not stated		

(b) **Sale of Sawn Timber**

A revenue of Rs. 201,351,085 had been earned during the year under review from sale of sawn timber. Even though the budgeted sales amounted to Rs. 425,200,000 that target could not be achieved by Rs. 223,848,915 or 52.6 percent . As the Corporation could not compete with the market competitive prices, the sale of sawn timber during the year under review had been at a very low level even though an island wide sales net work exists.

(c) **Furniture unit**

- (i) According to the Financial Statements the actual furniture sales of the Corporation during the year under review amounted to Rs. 126.218 million and it was less than Rs.121 million of the budgeted sales of Rs. 247.214 million. The net loss of this unit was Rs. 13.12 million. As compared with the preceding year Increase in sales by 3.67, per cent increase of establishment and administrative expenditure by.22.63 per cent, and the increase in selling and distribution expenditure 43.9 per cent had been the reasons for the loss of this unit.
- (ii) Non-minimizing the cost of furniture had been the main reason for the loss of this unit.

(d) **Timber Depots**

According to the Profit and Loss Account prepared for depots the net profit earned during the under review was Rs. 408,883,574 whereas it was Rs. 303,550,284 during the preceding year.

The sale of timber logs during the year 2012 had exceeded by Rs. 317,310,858 or 22.72 per cent than the budgeted sales of Rs. 1,396,845,000 representing 52.43 per cent of the total sales income. A few timber logs had been received from private lands and as donations and the entire balance had been obtained from the forest cultivations of the Department of Forest Conservation. Cutting and transport of these timber logs had been done through private contractors. A sum of Rs. 226,322,521 or 13 per cent of the sale of timber logs amounting to Rs. 1,739,141,867 in the year 2012 had been spent for cutting and transport of timber logs.

(e) **Sale of Sleepers**

The overall sale of Sleepers during the year under review amounted to Rs. 728,996,144 and it was an improvement of 8.69 per cent of the budgeted sale which amounts to Rs. 670,725,000. The monopoly of the manufacture of local Sleepers vests with the Corporation and the entire stock is purchased by the Department of Railway.

**3.2 Management Inefficiencies**

(a) **Payment of Retirement Gratuity – coupe officer**

A coupe officer who was in probation period and sent for remand custody due to a discrepancy made in supplying timber had been interdicted in June 2002 and reinstated without holding any disciplinary inquiry. Further he was convicted by the Magistrate Court and then he had been interdicted again on 05 December 2005. According to an appeal made he was acquitted in November 2010. In the mean time he had gone abroad without approval and he was discharged by the



disciplinary inquiry held after 9 years from charges and reinstate in service with back wages. After 7 days he had vacated the service and gone abroad again.

Instead of dismissing him from service on the ground that he had gone abroad during the probation period without approval. A sum of Rs. 119,160 as gratuity and a sum of Rs. 1,957,174 as salaries, Employees Provident Fund and Employees Trust Fund contributions had been paid to him. This payment had been treated as a result of an inefficiency of the management in audit.

**(b) Payment for the Supply of Timber**

Advances totalling Rs. 12,843,873 had been paid from time to time to timber suppliers as a part of the value of supply in receiving timber and timber related products to the depots. Although the final payment should be made after recovering the advance payments to the timber suppliers who had completed the orders, it had not been so done and as such the timber supply advances had been shown in the Financial Statements. Accordingly, it was observed that the internal control over the payment for timber supply was at a weak level.

**(c) Procurement of an Accounting Information System**

A sum of Rs. 3,425,341 had been paid to a private company for the procurement of computerized accounting information system. The following observations are made in this regard.

- i. Other additional modules required for the efficient operation of the Computerized Accounting Information System, consist of several modules had not been supplied even by 30 September 2013.
- ii. While there is an Information Technology Division consists of 10 officers under a Deputy General Manager (Information & Technology) and there was a requirement that the supplier Technical Institution should have been presented a technical proposal by identifying the Corporation requirement, an external person had been deployed on assignment basis as

a coordinating officer relating to procurement and a sum of Rs.312,500 had been paid to him.

- iii. Without purchasing servers in the installation of complete system, such facilities had been obtained from a telecommunication firm on a monthly lease rental basis and a sum of Rs. 611,933 had been paid during the year 2012.

### **3.3 Operating Inefficiencies**

- (a) Incurring a loss of Rs. 35,169,565 to the Government as a Result of Discrepancies made in Removing Timber from Catchment Areas of Ampara Rambaken Oya Reservoirs and Forest Offence.

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The following observations are made in this regard.

- i. According to the letter No. FIM/HC/01/05 dated 27 August 2012 of the Conservator General of Forest, 1,196 trees had been removed within the area of 431,310 cubic decimeters beyond the limit of Kadiyampitiya reservation, Nellyyadda forest and Nuwaragala reservation without authority.
- ii. Trees were cut and fallen in unauthorized areas and a large amount of trees in lands belonging to the Monaragala District which had not been vested in the State Timber Corporation in any grounds had been cut down and felled in the plots of land.
- iii. In analyzing data obtained, the location of inceptives of unauthorized fallen trees by using GPS many fallen trees were located exceeding the water level of reservoir in catchment areas.
- iv. A considerable income had been deprived by the government due to under valuation and sale of timber provided by the coupe itself and degrading of best quality timber (determination as low quality timber)

- v. Lots of timber obtained from trees cut down outside the coupe and collected at various places had been recorded in the relevant books as timber available at coupes.
- vi. Priority had been given to way side sales than supplying timber depots. According to the computation of the Department of Conservation of Forest 2676.57 cubic meters of luxury class timber degrade as class No: 2 timber had been sold way side instead of selling through depot and as a result the amount deprived to the government was Rs. 35,169,605.

**(b) Clear Falling of Teak Plantation in Monaragala Palaruwa**

The period between the dates determined by the tender board to hand over coupe to contractors and the dates of commencement of supply of timber in the coupe had ranged from 14 days to 115 days. Before the validity period of agreements entered into with the timber supply contractors was elapsed short term work agreements had been entered in to with contractors again by covering the validity period of the previous agreements.

**3.4 Transaction of Contentious Nature**

**(a) Purchase of Finger Jointing Machine for the Boossa Furniture Complex**

Although a finger jointing machine had been purchased by paying a sum of Rs. 6,169,950 more than one year's ago no any products had been sent to the market and no feasibility study had also been carried out before the project was initiated. It was stated that further sum of Rs. 54.4 million had to be spent for other required machines. Finger jointing products had not been determined and fixed selling prices after doing a cost analysis.

- (b) Although the warranty period of 1 ½ years had elapsed, production had not been commenced and as such the technical defects could not be identified in operating the machine. As a result the rectification of such technical defects through the agent had been precluded

- (c) In considering all facts such as the expenditure incurred for the Finger Jointing machine up to now, other machinery required for the machinery system, electricity supply and the factory accommodation, this investment had not been an economically viable project.

### **3.5 Fruitless Investments**

The following observations are made

- (a) The Corporation had commenced a joint venture by incurring an initial expenditure of Rs. 468,000 in the year 2001 and a sum of Rs.3,000,000 had been invested in the Lanka Timber Plantation Company. Nevertheless no any return what so ever had been obtained even by 30 September 2013.
- (b) The Corporation had not obtained any benefits from the share investment of Rs. 500,000 made in the Land Reclamation and Development (pvt) Ltd on 26 September 1985 even up to 30 September 2013.

### **3.6 Uneconomic Transactions**

#### Printing and Supply of Cash Sale Invoice Books

- (a) The loss of Rs. 1,870,000 was sustained by the Corporation due to purchase of printed books at Rs. 1,250 per book which was the highest quoted price.
- (b) Any inquiry had not been made from the Government Printer for printing matters and the prior approval of the Secretary to the line Ministry had not been obtained before handing over to a private printing firm.

### **3.7 Personnel Administration**

The approved cadre by the Treasury amounted to 2364 whereas the actual cadre as at the end of the year under review amounted to 2187.

### **3.8 Vehicle Utilization**

The reported number of accidents caused to Corporation's vehicles during the year 2012 was 19 out of which a sum of Rs. 1,268,637 had been spent for the repair of only 9 vehicles. Although the amount of insurance indemnity received for those 9 vehicles was Rs.1,081,354, the damages occurred to the vehicles during the year 2012 had not been computed and brought to accounts.

## **4. Accountability and Good Governance**

### **4.1 Presentation of Financial Statements**

Even though, in terms of paragraph 6.1.1 of the Treasury circular No. 01/2004 dated 24 February 2004 and paragraph 6.5.1 of the Public Enterprises circular No.PED/12 dated 02 June 2003 Financial Statement should be submitted to the Auditor General within 60 days after the end of the financial year, the Financial Statements for the year under review had been submitted only on 06 May 2013.

### **4.2 Corporate Plan & Strategic Plan**

The following observations are made.

- (a) In terms of paragraph 5.1.1 of the Public Enterprises circular No.PED/12 dated 02 June 2003 a Corporate Plan should be prepared for the period not less than 3 years. Nevertheless, the State Timber Corporation had prepared a Corporate Plan only for the period from 2008 to 2012.
- (b) In terms of paragraph 5.1.3 of the above circular, the copies of the updated Corporate Plan approved by the Board of Directors should be presented to the Line Ministry, Treasury, Department of Public Enterprises and to the Auditor General at least 15 days before the commencement of the financial year. Accordingly, the Corporation had not taken action to prepare a Corporate Plan covering the year 2013 and not submitted to the relevant institution.

- (c) The following objectives stated in the Gazette Notifications under strengthening the functions of the Corporation had not been included under objectives stated in the Corporate Plan and the strategic plan.
- (i) Production and marketing of timber by products
  - (ii) Scientific control of forestation, reforestation and forest plantation
  - (iii) Agricultural production
  - (iv) Processing of forest related products
  - (v) Export of cane

#### **4.3 Action plan**

The following observations are made.

- (a) Although an action plan including the Information and Technology Personnel and Administration etc should have been prepared, the action plan prepared by the Corporation had been a document including only manufacture and sale of timber and timber related products.
- (b) As different values of items had been indicated in the Strategic Plan, action plan and the quarterly reports prepared by the Corporation, it was difficult to determine which values would be utilized for the measurement of actual performance.

#### **4.4 Procurement Plan**

The procurement plan had not been prepared in conformity with the budget.

#### **4.5 Budgetary Control**

Significant variances between the budgeted and actual revenue and expenditure were observed and as such the budget had not been made use of as an effective instrument of management control e.g. the sawn timber turnover stated in the budget was Rs.425,200,000 whereas the sawn timber turnover stated in the action plan was Ra.1,050,200,000.

#### **4.6 Fulfillment of Environmental and Social Responsibilities**

In releasing blocks of lands for falling of trees, action should be taken to protect forestation and forest cover as much as possible there were instances where the Corporation had not complied with those requirements. Particulars are given below.

##### **(a) Falling 392 Trees in a Natural Forest in the Sampath Nuwara Area**

A case had been filed in the Court of Appeal against the Corporation by a Non-Governmental Organization in respect of the above, cited the State Timber Corporation as the respondent and the Court ordered the Timber Corporation stating that even for falling one tree it should have been in complied with the law.

##### **(b) Unauthorized Falling at Bangalawatta Chapalton Commercial Thinning Block of Land**

The following observations are made in this connection.

- (i) In falling timber at Bangalawatta Chapalton Commercial thinning block of land, trees valued at Rs.32,462,148 had been fallen and action had not been taken to stop such unauthorized fallings by the State Timber Corporation and 9 charges had been framed stating that officers of the Timber Corporation had directly connected with issuing licenses for those and converted timber in to sleepers.
- (ii) A committee consisting of 6 officers had been appointed by the Ministry of Environment to inquire into these matters. That committee had confirmed on 15 May 2012 that discrepancies had been happened on all charges framed by the Department of Conservation of Forest and for additional 5 charges.
- (iii) According to the letter dated 12 June 2012 of the Deputy General Manager (Operations) of the State Timber Corporation addressed to the General Manger 4 recommendation were submitted. Accordingly there was no evidence to prove that necessary action had been taken to implement recommendations No 1 to 3.

- (iv) Similarly, disciplinary actions had not been taken against the officers responsible for forest offence occurred as confirmed by the Conservator General of Forest on 25 April 2012.

**5. Systems and Controls**

Deficiencies in systems and controls were brought to the notice of the Chairman of the Corporation from time to time. Special attention is needed in respect of the following areas of control.

- (a) Debtors control
- (b) Creditors control
- (c) Budgetary control
- (d) Fixed assets control
- (e) Procurement
- (f) Vehicles control