

Tea Shakthi Fund – 2015

The audit of the financial statements of the Tea Shakthi Fund for the year ended 31 December 2015 comprising the statement of financial position as at 31 December 2015 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year ended and the summary of significant accounting policies and other explanatory information was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with section 13(1) of the Finance Act, No 38 of 1971 and section 13(2) of the Tea Shakthi Fund Act, No. 47 of 2000. My comments and observations which I consider should be published with the Annual Report of the Fund in terms of section 14(2) (c) of the Finance Act appear in this report.

1.2. Management’s Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

1.3. Auditor’s Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards (ISSAI 1000-1810) of the Supreme Audit Institutions. Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Fund’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

1.4. Basis for Qualified Opinion

As a result of matters described in paragraph 2.2 of this report, my opinion is Qualified.

2. Financial Statements

2.1 Qualified opinion

Except for the effects on the financial statements of the matters referred to in paragraph 2.2 of this report, I am of opinion that the financial statements of Tea Shakthi Fund as at 31 December 2015 have been prepared in accordance with Sri Lanka Accounting Standards and give a true and fair view of the fund's financial position, financial performance and cash flows for the year then ended.

2.2 Comments on Financial Statements

2.2.1 Re-structural program of the fund

When considering the financial results of the fund for last 5 years it had been made continuous losses other than 2012. Since the Capital grants amounted to Rs.437.5 million received from the Treasury to the fund before 2005 had been adjusted, against Sri Lankan Accounting Standards, to the income from 2012 at an annual rate of 10 per cent, so that low level of loss had been shown and as a result of adjusting government grants, received in last year, of Rs. 25.55 million in comprehensive income statement, lower level of loss had been shown in the year under review. Further, a payable amount of Rs.74 million to Minor Tea Estate Development Authority had been considered as income and due to this profitability had been shown in 2012.

Net assets value of Rs. 553.04 million of the fund in 2011 were been converted as net liabilities valued to Rs.72.42 million in 2014 and this had been increased to Rs.111.65 million by the end of the year under review. Similarly, production in factories of the fund had been stopped by July 2016 and the fund had focused to a Re-structural program.

2.2.2. Sri Lanka Accounting Standards

The following observations are made.

a. Sri Lanka Accounting Standard 10

The date of approval to issue Financial Statements has not been disclosed in financial statements.

b. Sri Lanka Accounting Standard 16

When the carrying amount of a revalued asset is materially dissimilar to its fair value, it needs to be revalued again but the non-current assets of the fund have not been revalued after 2006.

2.2.3. Accounting Policies

The following observations are made.

- a. Even though the fund had prepared its financial statements on accrual basis; interest on investment had been accounted on cash basis. As a result receivable interest on investment for the year under review amounted to Rs. 777,940 had not been accounted.
- b. As per the notes to the Financial Statements, effective life time of tea plantation had as 33 years, however it had been considered as 10 years in accounting.

2.2.4. Accounting Deficiencies

The following observations are made.

- a. Amortization on tea plantation of the fund had been overstated in accounting by Rs. 599,775 for the year under review.
- b. Depreciation on machinery and fittings had been overstated by Rs. 518,627 in accounts for the year under review.
- c. The Tea factory at Yatinuwara had been rented out to an external party and the factory buildings constructed in that premises had not been assessed and taken into accounts under the fixed assets.
- d. A payment of Rs. 8,512,921 related to nine motor vehicles which the legal title does not exist with the fund has been capitalized under non-current assets.

2.2.5 Unexplained Differences

Although a difference of Rs. 96,449 was observed in total amounts to between the cash book balance and the ledger account balance when preparing bank reconciliation statements relating to two bank accounts; actions had not been taken to identify those discrepancies.

2.2.6. Lack of Evidence for Audit

Conformations balance and detail schedules for trade and other receivables amounted to Rs.119,848,226 and trade and other payables amounted to Rs. 34,900,729 at the end of the year under review, had not been presented for audit.

2.3. Accounts Receivable and Payable

The following observations are made.

- (a) An advance payment aggregated to Rs.18,042,351 made in 2001 to construct tea factories at Bulathkohupitiya and Pothupitiya had not been settled even up to the end of the year under review and the construction of factories also been abandoned.
- (b) Though the tea factory at Yatinuwara had been rented out to Kalubowitiyana tea Company and an advance payment of Rs. 10,269,400 made to a private company in the construction stage of the factory in 2005, had been shown under current assets without taking actions to settle it.
- (c) A receivable sum of Rs.1,661,828 to the fund, when demising the Hiniduma tea factory to Kalubowitiyana tea company on rent basis, had been brought forward since 2012 without taking actions for recovery.
- (d) A sum of Rs 2,691,324 for 13 vehicles possessed to estate societies, which had been given to the fund by the Minor Tea Estate Development Authority, had been brought forward and recorded as receivable under current assets without identifying a recoverable party for number of years.

2.4. Non-compliance with Laws, Rules, Regulations and Management Decisions

The following non-compliances were observed in auditing.

Reference to Laws ,Rules, Regulations and Management Decisions

Non-compliances

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| (a) Financial regulations of the Democratic socialist republic of Sri Lanka
Financial regulation 110 | A register of losses and damage had not been maintained. |
| (b) Establishment code of the Democratic socialist republic of Sri Lanka
Section 13.3 in paragraph II | Though an acting appointment should be given to a permanent position subjected to maximum of 03 months period, two officers had been appointed on acting basis for the posts of accountant and book keeper to the fund from 2012 and 2010 respectively. |
| (c) Treasury Circulars
Circular no. IAI/2002/02 dated 28 November 2002 | A fixed assets register for computer and software had not been maintained. |

2.5. Transactions not confirmed with adequate Authority

A sum of Rs. 25,500,000 received in 2014 from the Ministry of Plantation only for modernization of factory Machineries had not been utilized for the intended purpose and had been spent for recurrent expenditure of the year under review. However, proper authority had not been obtained in this regard.

3. Financial Review

3.1. Financial Results

According to the Financial Statements presented, the financial result of the fund as at 31 December 2015 had been a deficit of Rs. 39,232,292 as compared with corresponding deficit of Rs. 127,823,734 for the preceding year, thus indicating an improvement of Rs. 88,591,442 representing 69 per cent in the financial result of the year under review as compared with the preceding year. The decrease in administration expenses of the year under review by Rs.11,952,188 and adjustment of government grants amounted Rs. 75,550,000 to comprehensive income statement had mainly attributed to above improvement.

When analyzing the financial results of the year under review and last 4 years, a financial deficit had been made in other years except 2012, but the contribution of the fund had been favourable when considering the staff remuneration and depreciation on non-current assets. But the contribution in 2014 had been decreased significantly and it had been increased again by 94 per cent in the year under review.

3.2 Analytical Financial Review

Current ratio and Quick ratio of the year under review were 1.1 and 0.23 respectively and these ratios were not in the best position. Further a depression had been observed in these ratios comparing with the preceding year.

3.3 Legal Actions Instituted against or by the Institution

The following observations are made.

- (a) The fund had filed 11 cases against 11 managerial factories to recover the money receivable to the fund and a case had been filed in district court of Colombo in relation to a cash fraud of Rs. 250,019 in the marketing section of the fund.
- (b) A case had been filed against an external institute to recover a receivable amount of Rs. 19,211,584 to the fund, even though the judgment had been given as favourable to the fund on 20 June 2014, and the Defence had filed an appeal at Commercial High Court of Colombo.

- (c) The workers had filed 8 cases against the fund at Labour Tribunal, even though the judgment had been given as favourable to the fund for a case filed by a worker at District Court the pursuer had filed an appeal.
- (d) Two cases had filed against the fund at District Courts in relation to land disputes of the fund.

4. Operational Review

4.1. Performance

Objectives of the fund in brief, as per the paragraph 7 of the Tea Shakthi Fund Act, no. 47 of 2000 are given bellow.

- Establishment and Improvement of saving habits among minor tea estate owners, and improvement of their economic and social status, and promote investments in relation to tea industry.
- Acquisition of tea factories, development, provision of other facilities to tea factories required in production, provide facilitate to minor tea estate owners in their yield production.
- Take actions which are necessary to enrich the well-being of minor tea estate owners those who are engage in tea production.

Even the fund had not taken new actions in achieving above objectives, only 10 factories and insurance benefit scheme for shareholders in the fund had been continued during the year under review, furthermore the following observations are made.

(a) Factory profit/loss

Even though the fund owned 15 factories only 10 factories were operating during the year under review. According to the factory accounts the loss earned by those factories during the year under review was Rs.88,770,617, further this had been decreased by Rs. 26,712,320 representing 23 per cent, comparing with the preceding year.

The Profit/losses earned by factories, which were in operating condition, from the year ended 2011 to the end of the year under review are given below.

Factory	For the years ended 31 December				
	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Deniyaya	(11,735)	(11,913)	(7,777)	(7,349)	(4,126)
Walahanduwa	(12,245)	(14,068)	731	(2,297)	(3,312)
Mawarala	(7,614)	(10,279)	(10,229)	(6,108)	(3,653)
Elpitiya	(14,675)	(13,482)	(3,409)	(7,990)	(16,604)
Raigamkoralaya	(13,737)	(15,885)	(7,479)	(7,579)	2,191
Kothmale	(8,092)	(9,683)	(6,933)	(6,132)	(8,901)
Keppitipola	(4,000)	(5,628)	5,421	(1,285)	(5,223)
Passara	(1,643)	(1,769)	5,772	6,640	2,345
Mahaweli	(4,360)	(10,054)	(13,079)		245
				(899)	
Deraniyagala	(10,669)	(22,722)	(8,770)	(3,989)	-
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	(88,770)	(115,483)	(45,752)	(36,988)	(37,038)
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In order to purchase more buds for minimizing factory losses a high price had been paid for tea buds from 2010 continuously. However the objective had not been achieved and an extra cumulative cost incurred there on was Rs. 73,494,328.

(b) Tea production

The information presented in relation to tea production is as follows.

Factory	production cost per tea Kg		Production		Machine capacity (over production)	Amounts Produced from tea buds used in production (standard percentage 21.5)	Average net sale per tea Kg
	(Rs)	(Rs)	(Kg)	(Kg)			
	2014	2015	2014	2015	(Kg)	% 2015	(Rs) 2015
Deniyaya	527.22	498.72	146,651	115,894	451,500	20.51	373.02
Deraniyagala	474.62	447.46	250,966	174,912	387,000	20.94	346.96
Kothmale	488.36	-	80,351	4,837	451,500	-	-
Passara	382.53	349.31	209,097	309,379	387,000	22.57	326.68
Walahanduwa	537.70	513.05	148,814	108,880	516,000	20.65	372.49
Keppitipola	391.10	360.08	206,235	270,036	387,000	21.70	324.54
Mahaweli	428.92	357.36	188,065	275,144	774,000	21.82	329.23
Elpitiya	565.26	447.96	102,435	159,632	516,000	20.04	327.52
Raigamkoralaya	483.02	431.76	316,688	358,525	516,000	20.16	373.68
Mawarala	644.51	-	55,380	-	322,500	-	-

The following observations are made.

- (i) Capacity of machines in the whole factory system of the fund was under-utilized during last 3 years and the tea production in 6 factories had decreased more than 50 per cent out of their tea production capacity and 3 factories had utilized the capacity only up to 80 per cent during the year under review. Accordingly, the cost of manufacturing per tea kilo had been increased due to factory overhead cost of production.
- (ii) The production in Mawarala tea factory had been ceased in 2015 and the tea factory in Kothmale was not in operational condition since March. Out of 8 factories that are in operational condition 5 factories were failed to achieve the optimum level of tea production of 21.5 per cent and due that the direct expenses on raw tea bud had increased.

As per (i), (ii) above, the cost of production per tea kilo had exceeded the net average selling price per tea kilo in the factories of the fund.

- (c) The production of tea according to the action plan and performance reports for the year under review is as follow.

Factory	Targeted purchase of raw tea buds as per the action plan	Actual purchase of tea buds	Targeted production of tea as per the action plan	Actual production of tea	Percentage of variance
	(kilo grams)	(kilo grams)	(kilo grams)	(kilo grams)	
Deniyaya	1,200,000	565,013	258,000	115,894	55.08
Walahanduwa	1,130,000	527,228	242,950	108,880	55.18
Mawarala	1,016,800	-	218,655	-	-
Elpitiya	950,000	796,446	204,250	159,632	21.84
Raigamkoralaya	1,800,000	1,778,508	387,000	358,525	7.36
Deraniyagala	1,484,650	835,151	319,200	174,912	45.20
Kothmale	1,168,000	128,396	251,100	4,837	98.07
Keppitipola	1,395,000	1,244,335	299,925	270,036	9.96
Passara	1,334,500	1,370,669	287,000	309,379	(7.8)
Mahaweli	1,700,000	1,261,161	365,500	275,144	24.72
Total	13,178,950	8,506,907	2,833,580	1,777,239	

As per the action plan for the year under review, though it was expected to purchase 13,178,950 kilo grams of raw tea buds, only 8,506,907 kilo grams of tea buds had been purchased since the percentage variance was 35.45. As per the action plan for the year under review, the targeted tea production was 2,833,580 kilo grams, whereas the actual production was 1,777,239 kilo gram that is 62.72 per cent. When factory vice considered, the variance was in a range of 25 per cent to 98 per cent in factories at Deniyaya, walahanduwa, kothmale and Deraniyagala.

(d) Local tea sales section

Although it was planned to achieve a sale of Rs.9,286,555 from the local tea selling section, the actual sales was Rs. 3,713,253 and it was 40 per cent of the targeted amount of the year under review.

(e) Fertilizer section

Although the targeted manure sales for the year under review, were 3,827 metric tons the actual sales were 679 metric tons which is only 17 per cent. Nevertheless in an event of targeted fertilizer sales of 8,525 metric tons for the year representing 16.89 per cent at an amount of 1,440 metric tons had been sold; Accordingly there was a drawback in setting targets as well as in progress during the year under review.

(f) Welfare section

The tea factories have not settled the loans of Rs. 118,300,000 until the end of the year under review, which was given by the welfare fund of the members of minor tea estate society at Tea Shakthi Fund from 2000 to 2003 in order to fulfill the financial needs in tea factories of Tea Shakthi Fund. Though the expected interest on this loan during the year under review was Rs. 16,244,777, the settlement of loans and interest has been uncertain due to continuous losses in factories.

- (g) As at 31 December 2015, 94,425 shareholders possessed shares valued at Rs. 206,014,150. The fund had not been operated in order to give benefits to these shareholders since 2007 to the year under review. Though the vision of the institute is to become the best institute that devoted itself for uplifting socio economic condition of minor tea estate owners, by increasing the share capital value of members, it was unable to fulfill the goal due to above mention particulars.

4.2. Management Activities

After closing down the factory at Balangoda, due to weak supervision of the management, 18.59 perches in 6 plots of land were captured by external party and a case in this regard was been examined in district court at Balangoda.

4.3 Idle and underutilized Assets.

The following observations are made.

- (a) Nearly 47 acres out of the land of 97 acres which belongs to Mawarala tea factory had not been cultivated; meanwhile a paddy field valued at Rs. 240,000 owned by the same factory had not been cultivated and remained idle.
- (b) Though a fertilizer mixing machine, valued at Rs. 2,197,447 to mix fertilizer at store premises of the fund, had been purchased and this machine was remained idle due to having higher expenditure and time taken to mixing.
- (c) After closing the factory at Balangoda the Residency and the lavatory system of the factory had been destroyed due to weak maintenances of buildings. At the end of the year under review, the factory land at Balangoda valued at Rs. 1,350,000 and buildings valued at Rs. 10,000,000 had been remained idle without using for any purpose.
- (d) A computer software system valued at Rs. 2,435,000 had been purchased in 2010 to prepare consolidated accounts for the head office and all factories of the fund; this had not been used for preparing accounts even up to 20 December 2016.

4.4. Damages and Losses

The following observations are made.

- (a) Although a sum of Rs. 2,105,980 for purchasing spare parts and a sum of Rs.438,819 renovating the machines of the tea factory at Walahanduwa had been spent in 2013, renovation work had not been completed so as to bring the drying machine to an operational condition even up to the reporting date.
- (b) According to the reports of Sri Lanka Tea Board, 7,247 kilograms of tea valued at Rs.3,242,743 had been destroyed in the tea factory at Deraniyagala, during the year under review due to an un-eligible condition for human consumption.
- (c) Actions had not been taken to charge from officers those who are responsible in shortage of tea bulks in factories at Elpitiya and Deniyaya, valued at Rs. 1,669,613 and Rs.1, 258,758 respectively.

4.5 Land and Buildings which were not formally taken over.

Even though the value of factory buildings were recorded as Rs. 81,655,360 in accounts, actions had not been taken by the fund to take over the ownership of the land where those buildings are located, even up to the end of reporting date.

4.6 Personnel Administration

The approved cadre to the fund was 90, while the actual staff was 47 there were 43 vacancies including 20 staff officer vacancies as at 31 December of the year under review. Being the approved cadre for factories were 199 and actual factory staff was 77, there were 122 vacancies including 19 technical officers so as 53 per cent vacancies had existed.

5. Accountability and Good Governance

5.1 Presentation of Financial Statements

Even though the financial statements should be presented to the Auditor General within 60 days after concluded of the financial year according to paragraph 6.5.1.of the Public Enterprises Circular No. PED/12 of 02 June 2003, the financial statements for the year under review had presented to audit on 19 October 2016, after a delay of 233 days. Moreover, the draft annual report had not been presented to audit even up to 20 December 2016.

5.2 Internal Audit

Even though an internal audit unit to the fund had been established only two officers had been appointed to that section.

5.3 Budgetary Control

According to the budget of the fund, variances of 22 per cent to 100 per cent were observed between budgeted income and expenditure and actual income and expenditure, thus observing that the budget had not been made use of as an effective instrument of management control.

6. Systems and Controls

Weaknesses in the systems and controls observed during the course of audit were brought to the notice of the Chairman of the fund from time to time. Special attention is needed in respect of the following areas of control.

Systems and Controls areas	Observations
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(a) Accounting	Delays in presenting financial statements
(b) Receivable and Payable Balances	Existence of receivables and unsettled balances from long term
(c) Budgetary control	Significant variances were observed between budgeted and actual figures
(d) Financial control	Bank Overdraft facilities had been taken
(e) Operational control in the factories	All the factories earn losses
(f) Utilization of assets	Existence of idle assets