

Sri Lanka Cashew Corporation - 2015

The audit of financial statements of the Sri Lanka Cashew Corporation 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 then ended and a 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 23 of the State Agricultural Corporations Act, No.11 of 1972. My comments and observations which I consider should be published with the Annual Report of the Corporation 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 of Supreme Audit Institutions (ISSAI 1000 – 1810). Those Standards require that I comply with ethical requirements and plan 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 Corporation'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 Corporation'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 financial statements. Sub-sections (3) and (4) of Section 13 of the Finance Act, No.38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

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

My opinion is qualified based on the matters described in paragraph 2.2 of this report.

2. Financial Statements

2.1 Qualified Opinion

In my opinion, except for the effects of the matters described in paragraph 2.2 of this report, the financial statements give a true and fair view of the financial position of the Sri Lanka Cashew Corporation as at 31 December 2015 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.2 Comments on Financial Statements

2.2.1 Sri Lanka Accounting Standards

Instances of non-compliance with the Accounting Standards are given below.

- (a) Sri Lanka Accounting Standard 01

- I. The basis adopted for the preparation and presentation of financial statements had not been disclosed.
- II. Even though the other requirements should have been disclosed in terms of Section 138, the following information had not been disclosed.
- (i) Addresses of the registered office or the principal business premises.
- (ii) Operations and key functions of the Corporation.
- (b) Sri Lanka Accounting Standard 02

- Instead of valuing the stock by separately computing the cost, the stock had been valued at the average cost of all the products. As such, the market price of the cashew related products had been lesser than the cost.
- (c) Sri Lanka Accounting Standard 10

- Since the date approved for the issue of financial statements in accordance with Section 17 is important for the users of the financial statements, the approval dated of the financial statements should be disclosed. Nevertheless, the Corporation had not disclosed the approval date of the financial statements.
- (d) Sri Lanka Accounting Standard 16

- I. Fully depreciated 19 vehicles were further being used, whereas action had not been taken to revalue and bring to account in order to show their fair value.
- II. The accumulated depreciation as at the beginning of the year under review, depreciation relating to the year under review and the depreciation of the assets disposed of relating to property, plant and equipment had not been disclosed.

- (e) Sri Lanka Accounting Standard 19

The requirements that should be disclosed on the employees' benefits had not been properly disclosed in terms of the Standard.
- (f) Sri Lanka Accounting Standard 37

The contingent liabilities should be disclosed in the financial statements. Nevertheless, the cases filed against the Corporation by two officers who had served in the Corporation claiming compensation had not been disclosed in the financial statements.
- (g) Sri Lanka Accounting Standards 41

The biological assets of the Corporation, that is, cashew trees, had not been brought to account at the fair value in accordance with the Standard and the following disclosures had not been made.
- I. The financial risk strategies relating to the agricultural activities.
 - II. Each biological assets category and the nature of activities.
 - III. The physical quantities of each biological asset and the non-financial pre-measurement estimates relating to yield harvested during the period.

2.2.2 Accounting Deficiencies

The following observations are made.

- (a) The interest amounting to Rs.43,968 receivable for the year under review for the fixed deposits had been understated in the accounts.
- (b) Expenditure of Rs.364,664 relating to the year under review had not been brought to account as accrued expenditure and the amount payable for the laboratory equipment valued at Rs.53,000 purchased by the Nedagamuwa Processing Centre in September 2015 had not been accounted under the creditors.
- (c) (i) A loan amounting to Rs.3,500,000 obtained under 6 per cent annual interest from the Treasury through the Ministry of Agriculture, Marketing Development, Cooperative Development, Hindu Religious Affairs and Auxiliary Education and Vocational Training on 08 April 2005 had not been shown under the long term debts and it had been shown under the current liabilities in the accounts.
- (ii) Allocation for the interest of Rs.210, 000 payable for that loan for the year under review had not been made and the interest of Rs.2, 240,000 payable up to 31 December 2015 had not been shown as current liabilities.

- (d) The sum amounting to Rs.791,465 payable for the Crop Insurance had been shown as current liabilities in the accounts instead of being shown under the long term liabilities.
- (e) Although the total value of the Agrarian Well constructed at the commercial nursery, Mihinthale was Rs.517,507, that value had been shown as Rs.465,756 under the fixed assets. Accordingly, fixed assets had been understated by Rs.51,751.

2.3 Non-compliance with Laws, Rules, Regulations and Management Decisions

The following instances of non-compliances were observed.

Reference to Laws, Rules, Regulations, and Management Decisions	Non compliance
(a) Inland Revenue Act, No.10 of 2006	Even though the Corporation is an institution liable for income tax, action had not been taken for the preparation of Income Tax Returns for the years of assessment 2011/2012, 2012/2013, 2013/2014 and 2014/2015 or for the payment of income tax.
(b) Value Added Tax Act, No.14 of 2002 and Nation Building Tax Act, No. 9 of 2009	Where the institution supplying wholesale and retail sale goods is the manufacture of the same goods and where the turnover per quarter exceeds Rs.3 million or the annual turnover exceeds Rs.12 million, the institution should register for Value Added Tax and Nation Building Tax, but action had not been taken accordingly.
(c) Section 3.5 of Chapter XXIV of the Establishments Code of Democratic Socialist Republic of Sri Lanka	In the payment of Distress Loans, instances in which loan had been granted exceeding the 40 per cent deduction limit of the debtors and the guarantors were observed.
(d) Public Enterprises Circular No.95 dated 14 June 1994	Even though the benefits specifically approved by the Ministry of Public Administration or the General Treasury only could be paid to the employees under the approval of the Board of Control, contrary to that, transport allowance amounting to Rs.2,368,801 at the rate of Rs.5,000 and Rs.1,500 per month for the officers at managerial level and the other employees respectively had been paid up to October of the year under review.

(e) Paragraph 10 of the Public Finance
Circular No. 02/2015 dated 10 July 2015.

As stipulated in the circular instructions with regard to the transfer of vehicles and sales income, the vehicle sales income should be credited to the Consolidated Fund. Nevertheless, income of Rs.5,306,351 earned by the sale of vehicles of the Corporation during the year under review had not been remitted to the Treasury.

3. Financial Review

3.1 Financial Results

- (a) According to the financial statements presented, the operations of the Corporation for the year under review had resulted in a deficit of Rs.47,728,042 as compared with the deficit of Rs. 26,057,641 for the preceding year. Accordingly, as compared with the preceding year, an increase of the deficiency by Rs.21,670,401 was observed. The decrease of the expenditure of the Commercial Division by Rs.40,073,524 and the increase in the expenditure of the Cashew Project Service by Rs.9,254,364 and increase in the expenditure of nurseries by Rs.12,114,885 had been the main reasons for this deficit.
- (b) In analyzing financial results of the year under review and three preceding years, the financial results of the year 2012 amounting to a net profit of Rs.44,233,832 and it had ceaselessly deteriorated to a net loss of Rs.47,728,042 in the year 2015. However, when taking into consideration employees' remunerations and depreciations, contribution in the year 2012 amounting to Rs.100,906,166 had decreased to Rs.41,851,749 or by 141 per cent in the year 2015.
- (c) The payments for the employees' remunerations of the Corporation in the year 2012 was Rs.45,592,055, whereas it had been Rs.71,884,727 during the year under review thus showing a 57 per cent increase.

3.2 Analytical Financial Review

(a) Operations

- I. The gross profit ratio of the Commercial Divisions of the Corporation in the year 2015 was 27 per cent and it was 46 per cent in the year 2014. Accordingly, a 19 per cent decrease was observed as compared with the year 2014.
- II. When comparing sales income of the cashew related products of the year 2015 with sales income of the years 2011 to 2014, a decrease in the sales income in the year 2015 was observed.

4. Operating Review

4.1 Performance

In terms of State Agricultural Corporations Act, No. 11 of 1972, the main objectives of the establishment of the Corporation were the cultivation, production, processing and purchase of cashew, preparation of marketing plans, conduct of investigations and researches, collecting, preparing, publishing and distributing information on marketing and other information, training of persons required for processing cashew related products and promotion of the demand for the productions in the international markets. However, the following matters were observed on the achievement of the objectives.

(a) Action had not been taken to train persons required for processing cashew related products and to promote global markets for the cashew products.

(b) Cashew Cultivation

(i) Even though Puttalam Cashew Plantation had a land area 960 acres in extent, only 240 acres had been utilized for the cashew cultivation. Accordingly, 720 acres remained idle.

(ii) Cashew trees that standing on Puttalam, Kamandaluwa and Hardy Estates had exceeded 30 years and as such yield had been at a minimal level.

(c) Implementation of Subsidy Programme

For the purpose of propagation of cashew, 560,000 plans comprising 200,000 grafted plants and 80,000 cashew seedlings had been distributed per year among the farmers in the years 2014 and 2015. The following observations are made in this connection.

(i) Grafted cashew plants amounting 34,240 and 36,000 had been distributed in the year 2014 by spending Rs.2,054,400 and Rs.2,152,800 for 09 Divisional Secretariats in Puttalam District and 11 Divisional Secretariats in Kurunegala District respectively. It was observed at the physical verification conducted that the expected targets had not been achieved as 22,204 or 65 per cent cashew plants in Puttalam District and 13,027 or 36 per cent cashew plants in Kurunegala District had perished.

(ii) It was observed that out of 280,000 cashew plants distributed, only 130,303 plants had been successful and as such the expected outcome of the Cashew Subsidy Project had not been achieved.

(iii) Even though cashew plants for 4500 acres had been supplied under the subsidy programme in the year 2014, it was observed that there was not even a single cashew plant in 422 acres.

(d) **Research and Development**

A sum of Rs.3 million had been allocated for research and development of the year under review and out of that Rs.2.894 million had been spent. The following matters were observed in the examination of implemented research programmes,.

- (i) Although a research proposal should be presented and approval obtained before carrying out researches, action had not been taken accordingly.
- (ii) Regular and proper progress reports had not been presented so as to enable the progress of the researches to be evaluated and progress reports had been presented in the form of monthly work done reports.

4.2 Management Inefficiencies

The following observations are made

- (a) Financial Regulations and Administrative Procedural Rules had not been prepared for the Corporation and in respect of employees' arrival and departure and office hours, the Establishments Code and Public Administration Circulars and in respect of the payment of overtime, the provisions in the Shop and Office Employees Act, had been adopted in favourable manner.
- (b) The Corporation had maintained cashew cultivation in 9 estates comprising 15,329 acres in extent and out of which one estate of 200 acres, three estates of 1874 acres and five estates of 13,255 acres belonged to the Department of Agriculture, Land Reform Commission and the Government respectively and action had not been taken to acquire those lands to the Corporation.
- (c) A sum of Rs.9,466,200 was due from the Ministry of Economic Development as at 31 December 2015 in respect of providing cashew plants to the Divinegume Programme in the years 2012 and 2013 and a Ministry named the Ministry of Economic Development does not exist at present. Accordingly, the recovery of above money is questionable and steps had not been taken to recover that sum during that period itself.

5 Accountability and Good Governance

5.1 Annual Reports

Annual Reports of the Corporation pertaining to the years 2013 and 2014 had not been tabled in Parliament and the draft Annual Reports for the year 2015 had not been furnished along with the financial statements in accordance with Public Finance Circular No. PF/PE/21 dated 24 May 2002.

5.2 Budgetary Control

- I. Although the Budget for the relevant year should be prepared so as to enable the budget figures to be reviewed with the actual expenditure of the preceding year,

Budget presented by the Corporation for the year under review had not included the actual expenditure of the preceding year.

- II. A variance between the budgeted expenditure and actual expenditure of 26 budgeted items ranging from 20 per cent to 1102 per cent was observed and as such the budget had not been made use of as an effective instrument of financial management control.

6. Systems and Controls

Deficiencies in systems and controls observed during the course of audit 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) Staff Administration

Financial and Administrative Procedural Rules had not been prepared for the Corporation and recruitment and promotions of employees had been carried out deviating from the approved scheme.

- (b) Budgetary Control

A formal Budget approved by the Board of Directors had not been furnished.

- (c) Assets Management

Action had not been taken to take over the legal possession of the estates.

- (d) Financial Control

Action had not been taken to recover the loans due from the sale of cashew plants of the Corporation within the relevant period.