Report of the Auditor General on Head 248 - Excise Department - Year 2016

The audit of the Appropriation Account, Revenue Account and the Reconciliation Statements including the financial records, registers and other records of the Head 248, Excise Department, for the year ended 31 December 2016 was carried out in pursuance of provisions in Article 154 (1) of the Constitution of the Democratic Socialist Republic of Sri Lanka. The Management Audit Report for the year under review was issued to the Commissioner General of the Department on 27 July 2017. The audit observations, comments and findings on the accounts and the reconciliation statements were based on a review of the Accounts and the Reconciliation statements presented to audit and tests of samples of transactions. The scope and extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitations of staff, other resources and time available to me.

1.2 Responsibility of the Chief Accounting Officer and the Accounting Officer for the Accounts and Reconciliation Statements.

The Chief Accounting Officer and the Accounting officer are responsible for the maintenance, preparation and fair presentation of the Appropriation Account, Revenue Account and Reconciliation Statements in accordance with the provisions of Articles 148, 149, 150 and 152 of the Constitution of the Democratic Socialist Republic of Sri Lanka, other Statutory Provisions, and the Public Finance and Administrative Regulations. This responsibility includes the designing, implementing and maintaining internal control relevant to the preparation and fair presentation of Accounts and Reconciliation Statements that are free from material misstatements, whether due to fraud or error.

2. Accounts

2.1 Appropriation Account

Total Provisions and Expenditure

The total net provision made for the Department amounted to Rs. 1,072.45 Million and out of that, a sum of Rs. 983.98 Million had been utilized by the end of the year under review. Accordingly, the savings of the total net provision had been Rs. 88.47 Million or 8.25 per cent. Details appear below.

Expenditure	**As at 31 December 2016**			**Savings as a Percentage of Net Provision**
	Net Provision	**Utilization**	**Savings**	
	Rs. Million	**Rs. Million**	**Rs. Million**	
Recurrent	745.67	743.10	2.57	0.34
Capital	326.78	240.88	85.90	26.29
Total	**1,072.45**	**983.98**	**88.47**	**8.25**

2.2 Revenue Accounts

Estimated and Actual Revenue

The Department had prepared Revenue Estimates totalling Rs. 125,035 Million in respect of 02 Revenue Codes for the year 2016, and during the year under review, Revenue totalling Rs.120,277.89 Million had been collected. It was 96.19 per cent of the estimated Revenue. Details appear below.

As at 31 December 2016

Revenue Code	Estimated Revenue	Actual Income	Excess/ (Deficiency)	Excess/ (Deficiency) as a percentage of the estimate
	Rs. Million	**Rs. Million**	**Rs. Million**	
10:02:04:01	125,000	120,238.07	(4,761.93)	(3.81)
10:02:06:00	35	39.82	4.82	13.77
Total	**125,035**	**120,277.89**	**(4,757.11)**	

2.3 Advances to Public Officers' Account

Limits authorized by Parliament

Limits authorized by Parliament for Advances to Public Officer's Account Item No: 24801 relevant to the Department and the actual values are given below.

Expenditure		Receipts		Debit Balance	
Maximum Limit	**Actual**	**Minimum Limit**	**Actual**	**Maximum Limit**	**Actual**
Rs. Million	**Rs. Million**	**Rs. Million**	**Rs. Million**	**Rs. Million**	**Rs. Million**
38.00	37.98	30.00	31.47	171.00	129.94

2.4 Imprest Account

The balance of Imprest Account No.7002/0000/00/0072/0016/000 of the Department as at 31 December 2016 was Rs. 228 Million.

2.5 General Deposit Account

The balances of the 04 General Deposit Accounts under the Department as at 31 December 2016 totalled Rs. 88 Million. Details appear below:

Deposit Account Number	Balance as at 31 December 2016
	Rs. million
6000/0000/00/0001/0122/000	54.0
6000/0000/00/0002/0178/000	4.0
6000/0000/00/0016/0126/000	17.0
6000/0000/00/0018/0119/000	13.0
Total	**88.0**

2.6 Audit Observation

The Appropriation Account, Revenue Account and Reconciliation Statements of the Excise Department for the year ended 31 December, 2016, had been prepared satisfactorily, subject to Audit Observations appearing in the Management Audit Report referred to in paragraph 1.1 above. The material and significant Audit Observations out of the Audit Observations included in that Management Audit Report appear in paragraph 3.

3. Material and Significant Audit Observations

3.1 Non-maintenance of Registers and Books

It was observed during audit test checks that the Department had not maintained the registers shown below and that two registers had not been maintained in an updated manner.

Type of Register	Relevant Regulation	Observations
Register of Losses	Financial Regulation 110	Not updated
Vehicle Log Books	Financial Regulation 1645 (a)	Log Books had not been maintained for 28 vehicles
Register of Fixed Assets	Treasury Circular No 842 of 19 December 1978	Not updated

3.2 Lack of Evidence for Audit

A Distress Loan balance totalling Rs.322,849 could not be satisfactorily scrutinized, as 6 Distress Loan files were not produced in audit.

3.3 Replies to Audit Queries

Even by 10 July 2017, no replies had been submitted for an audit query sent to the Department during the year under review, and the reckonable value of the transactions relevant to this query was Rs. 140,099.

3.4 Appropriation Account

Budgetary Variance

The following observations are made.

(a) Additional provisions of Rs. 82,787,553 had been obtained through Supplementary Estimates for 10 Objects due to the non-preparation of Estimates fully and accurately. In accordance with Financial Regulation 50, and this had ranged between 11 per cent to 200 per cent of the estimated provisions relating to these Objects.

(b) Additional provisions totalling Rs. 67,097,916 had been obtained for 06 Objects by way of Rs. 38,420,000 through Supplementary Estimates and Rs. 28,677,919 through Financial Regulation No 66, and this was 21 per cent of the basic estimated Provisions of those Objects.

(c) Even though provisions amounting to Rs. 18,600,000 had been appropriated through Supplementary Estimates without appropriating provisions through basic estimates for Object No. 2502, there had been a saving of the provisions amounting to Rs. 18,470,197 being 99 per cent of it. Further, 24 per cent or a sum of Rs. 64,649,613 had been saved from the provisions appropriated under building and constructions, due to the unusual delay in the construction activities of a building.

3.5 General Deposit Account

Action had not been taken in terms of the financial Regulation 571 relating to 19 deposits totaling Rs. 985,000 which had lapsed over a period ranging from 2 years to 5 years.

3.6 Revenue Accounts

The duties relating to the preparation of Revenue Estimates, collection of Revenue, Accounting and the presentation of Accounts relating to 02 Revenue Codes had been assigned to the Head of the Department as the Revenue Accounting Officer. The following observations were made during the course of the test audit of those Revenue Codes.

(a) Revenue Code No 10.02.04.01 – Excise (Liquor)

Following observations are made.

(i) According to the Revenue Account submitted for audit, there were arrears of revenue totalling Rs.2,544.81 Million, and these arrears of revenue had belonged to a period ranging from 1 year to 5 years.

(ii) In the export of liquor, it is only the customs export note submitted by the exporter that is based by the Department for the grant of export tax rebates. However, the Department had not introduced a proper methodology to decide the quantity actually exported.

(iii) The Excise Department did not have a methodology to inquire into the types of raw materials and their quantities used by the Lion Beer Company for the manufacture of malt liquor.

(iv) An analytical report had not been obtained from the Government Analyst's Department regarding whether physically harmful substances were present in malt liquors and the percentage of sugar therein.

(b) Revenue Code No 10.02.06.00 – Tobacco Tax

Following observations are made.

(i) The actual revenue for the year under review had increased by Rs. 05 Million compared to the actual revenue for the previous year.

(ii) While the Department issues licenses for the export of cigarettes, the Department had not devised an appropriate methodology to establish whether the quantity of cigarettes to be exported have actually been exported.

(iii) The Department has not yet devised a methodology to establish the correctness of the type of beedi leaf imported in the manufacture of beedies.

3.8 Reconciliation Statement on the Advances to Public Officers Account

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The following deficiencies were observed during the course of audit test checks done on the Reconciliation Statement of the Advances to Public Officers Account as at 31 December 2016 relating to objective No 24801.

(a) While, in accordance with the Reconciliation Statement submitted to audit, the total of the balances in arrears as at that day had been Rs.2,858,223, the Department had failed to recover these outstanding balances, even though these outstanding balances had been continuing for a period ranging from 01 year to 20 years.

(b) No action had been taken to recover a sum totalling Rs.420,993 due from six Officers who had retired on 31 December of the year under review, when their Pension Gratuities were being settled.

(c) Loan balance amounting to Rs. 1,224,830 remained recoverable from 15 interdicted officers as at 31 December of the year under review. Sums of Rs. 206,920 and Rs. 28,700 which had lapsed over 3 years and 20 years respectively had been included in that loan balance.

(d) A loan balance of Rs.190,160 was due to be recovered as at 31 December 2016 from Officers who had vacated services of the Department. Even though this had been outstanding over a period ranging from 6 years to 9 years, the Department had not taken adequate steps to settle these loan balances.

(e) There was a loan balance of Rs.526,068 due to be recovered from Officers who had been dismissed from service. This is outstanding over a period ranging from 7 years to 20 years.

3.9 Good Governance and Accountability

Internal Audit

There was no substantial evidence to establish that a formal audit had been conducted based on Departmental directives, notifications and other provisions. Accordingly, it has not been observed that a sufficient performance had taken place according to the Internal Audit Plan for 2016.

3.10 Assets Management

The following deficiencies were observed during the course of audit test checks done on the assets of the Department.

(a) A stock of library books valued at Rs.77,690 had been idling for 04 years.

(b) While the Department had been using 02 motor vehicles belonging to other institutions, appropriate action had not been taken to vest the ownership of these vehicles.

(c) The Department had not taken action to formally vest the lands relevant to 10 Excise Stations where Regional Offices are being maintained.

(d) Even though Annual Boards of Survey had been held in the Regional Offices of the Department for the year under review, no Board of Survey had been held in the Head Office.

3.11 Non-compliances

Non-compliance with laws, rules, regulations etc
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Instances of non-compliance with laws, rules and regulations observed during the course of audit test checks are analyzed below.

Reference to laws, rules, regulations etc	Non compliance
(a) Section 17 of the Tobacco Tax Act No. 08 of 1999	Even though a Tobacco Tax Reward Fund has to be set up, no action had been taken to do so.

(b)	Excise Notification No. 818 of 04 March 1998	No approved and written methodology had been established for the payment of cash rewards to Excise Officers, informants and others from the Excise Reward Fund.

3.12 Performance

The observations on the progress of the Department according to the Annual Budget Estimate 2016 and Action Plan are shown below.

(a) <u>Budgetary Estimates and the Action Plan</u>

The following observations are made.

(i) While it had been estimated to collect Rs.125,000 Million as revenue in respect of the Excise Revenue Code, a revenue of Rs.120,238 Million had been collected at the end of the year under review. It was 96 per cent of the estimated revenue.

(ii) Even though there are 22 companies registered in the Department manufacturing strong liquor, 92 per cent of the total revenue had been contributed only by 05 companies. The contribution to revenue of the balance 17 manufacturing companies had been at a level as low as 7 per cent. Accordingly, it has been observed during the audit that the strong liquor market of this country is dependent on 05 companies manufacturing strong liquor.

(iii) While 53.8 Million litres of strong liquor had been manufactured in the year 2011, by the year 2014, it had come down to 43.9 million litres, being a 18 per cent decrease. This decrease had been reported continuously from the year 2011 to the year 2014. However, compared to the year 2014, during the year 2015 it had gone up again to 51.8 Million litres, being an increase of 18 per cent, and compared to the year 2015, during the year 2016, it had increased further by 7 per cent. According to this information, it has been observed that the quantity of strong liquor subject to manufacturing taxes had decreased continuously, and that it had been on the increase again since the year 2015. Even though at present a higher rate of taxes has been imposed on the manufacture of liquor, the reasons for these unusual variations in the manufacture of liquor had not been submitted to audit.

(iv) The revenue from taxes on strong liquor which was Rs.47,002 Million in the year 2011 had gone up to Rs. 103,496million in the year 2015, being a 120 per cent increase. However, the manufacture of strong liquor which was 53.8 Million litres in the year 2011, had gone up to 55.5 Million litres in the year 2016, being only an increase of 3 per cent. Similarly, according to the available information, Rs.874 being the average of the manufacturing tax for 1 litre in the year 2011, had by the year 2016 gone up to Rs.1,865, being an increase of 113 per cent. Accordingly, it was observed that what had happened during that period was the imposition of a higher tax rate by the Government for increasing the revenue of the Excise Department.

(v) While revenue of Rs.133.51 Million had been earned through 4,593 Excise technical crime raids during the year under review, in the previous year revenue of Rs.178.51 Million had been earned through 4,932 Excise technical crime raids. Accordingly, it has been observed that compared to the previous year, during the year under review, there had been a drop by Rs. 45 Million or a 25 per cent decrease and raids by 339 or a 7 per cent decrease in respect of technical crimes.

(vi) Compared to the year 2016, during the year under review there had been a drop by Rs.887,800 or a decrease of 20 per cent in respect of revenue from cigarette fines.

(b) Planning

Shown below are the instances where action had not been taken in accordance with the Action Plan for 2016.

(i) During the year under review, while a net provision of Rs. 18.60 Million had been apportioned to activate the automatic tax calculation system, only about one per cent of it had been spent. The cause for this had been the delay in action because of the failure to plan without identifying its requirements prior to the commencement of the system.

(ii) Even though provisions totalling Rs. 500.00 Million had been apportioned during the years 2015 and 2016 for the construction of the Head Office (Rajagiriya) of the Excise Department, even by the end of the year under review, construction had not been completed.

(iii) A net provision of Rs.15.00 Million had been apportioned for staff training during the year under review. Out of it, Rs 2.47 Million or 16 per cent had been saved due to action not been taken to train the staff in the expected manner.

(c) Key Functions not executed adequately

While key functions of the Department had not been executed adequately, several such instances observed are shown below.

(i) The Department had not implemented a suitable methodology to establish/obtain confirmation whether the respective toddy rental license fees are being paid in time by toddy rental licensees.

(ii) In accordance with Section 4.5 of Excise Notification No 818 dated 04 March 1994, Rs.200,000 had been set apart during the year under review for acts of bravery or acts of special recognition. From the year 1994 to the year 2016, no payments had been made by the Department for such acts.

(iii) During the year under review, Rs.4,500,000 had been set apart from the Excise Reward Fund for the training and educational matters of the Officers. Rs.2,331,515 or 52 per cent out of it had been spent only for providing meals to the new Officers who had received training. Also, the balance amount of Rs.2,168,485 had not been spent for any training purposes. Accordingly, no formal plan had been prepared for the training and educational matters of the Officers of the Department.

(iv) In accordance with provisions of Section 13 of the Excise Ordinance of 2009, an Excise pass (D28 pass) should be obtained in that behalf when spirits are imported or when spirits are transported from a distillery or ware house. A copy of that transport pass should also be available at the Excise Office where the distillery is located. However, it was observed during the course of audit test checks that there were instances where such transport passes had not been obtained. Accordingly, during the audit it was not possible to be satisfied that proper monitoring was being done about stocks received by the distillery

3.13 Transactions of a contentious nature
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Some of the transactions done by the Department were of a contentious nature. Details of several such transactions revealed during the course of audit test checks are shown below.

(a) Even though it is stated in accordance with condition 27 of Gazette Extraordinary of the Democratic Socialist Republic of Sri Lanka No 1544/17 dated 10 April 2008, that no approval should be granted to relocate a premises licensed to sell liquor, based on a license issued in the year 1996 to run a foreign liquor shop in the city of Matale, authority had been given in the year 2010 to operate that foreign liquor shop in the city of Thunukkai in the District of Batticaloa. Further, arrears of license fees in respect of this foreign liquor shop had not also been collected.

(b) A private company had submitted a project proposal and a pre-feasibility report for the manufacture of ethyl alcohol using grain (grain based distillery) on 23 March 2015 to the Department. The Additional Director General of the Ministry of Finance had given authority for it to be implemented as a pilot project. According to the project report, even though it should have been started in the Kurunegala District, contrary to it, the distillery had been started in the Kalkudah area (Batticaloa). Also, information about what types of grain were being used for the industry had not been specifically stated in the project report. Further, information had also not been submitted about the input and output ratio of the raw materials. A technical report about the generation of ethyl production when using grains as raw materials also had not been submitted. A complete report about the proposed still and a report about the criteria used in silent spirits and rectified spirits also had not been submitted. Documents such as the approval of the Local Government Authority, Environmental Reports, reports about the title of the land and boiler certificates had also not been submitted along with the project report. Granting approval for the project in such a situation was a matter of contentious nature.

(c) Even though a private institution in the Boralesgamuwa area had applied for a FL 08 Excise license, the Excise Department had decided that this license could not be issued due to various reasons. However, the issue of the relevant license later with effect from 01 October 2016, was a contentious matter during the audit.

(d) According to letter no CSA/4/5/38 dated 06 June 2016 of the Secretary to the President, the prior approval of the Secretary to the President has to be obtained in the issue of excise licenses. It was observed during the course of audit test checks that 11 licenses of FL 07 and FL 08 types had been issued without obtaining approval in that manner.

(e) Even though the Divisional Secretary, Ambalangoda had reported that the stipulated distance regarding places of religious worship had not been fulfilled, disregarding this fact, a FL 11 license has been issued to a hotel, based on the copy of a private survey report.

(f) The liquor for sale in two liquor shops subjected to audit test checks were not consistent with the stipulated potency. It was not observed that monitoring had been done by Excise Officers to ensure that production had been carried out in accordance with the stipulated specifications.

3.14 Losses and Damages

A loss of Rs.600,465 had been incurred due to a vehicle belonging to the Department met with an accident on 08 August 2007. Although legal action had been taken to recover the damage from the driver responsible for the accident, even by the end of the year under review it had not been possible to recover the damage.

3.15 Management Weaknesses

The following weaknesses were observed during the course of audit test checks.

(a) During the year under review, a sum of Rs.12,870,756 had been spent for maintaining offices in rented out buildings, as a result of the further delay in the construction work of buildings necessary to maintain the Offices of the Department.

(b) In Chapter 4 of Gazette Extraordinary of the Democratic Socialist Republic of Sri Lanka of 18 April 2002, under the rules governing denatured spirits, it had been notified that in order to transform/render the active and regular use of alcohol unfit for human consumption, denaturing should be done using a denaturing agent such as Britex. However, it had been established that the denaturing agent Britex had not been used for denaturing in respect of spirits obtained by a private company for industrial purposes up to March 2016. Even though 500 grams of the denaturing agent Britex had been obtained by the respective distillery on 01 March 2016, no evidence was produced to audit that the Excise Department had issued the above denaturing agent to this institution during the years 2014 and 2015. Formal/proper corroboration/confirmation had also not been obtained regarding the stocks of spirits obtained for production purposes being denatured.

(c) In accordance with Excise Notification No 988 dated 02 March 2016, an Excise Duty is payable on imported spirits. However, it had been observed in the course of the audit that a quantity of 10,604.6 litres and 6,455.7 litres of spirit had been brought into this country during the years 2015 and 2016 respectively, in excess of the quantity of spirits for which duty had been paid. While information whether Excise Duty had been levied for the quantity of spirits so brought in excess was not produced before audit, evidence was also not adduced to the effect that the quantity of spirits brought to this country had been monitored by the Officers of the Department. Further, entries and reports about the receipt of spirits and stocks of spirits were not produced to audit.

(d) According to the contents stated in Chapter 2 of the Liquor Industry Hand Book, the Superintendent of Excise should examine the documents of ware houses in his area of authority, compare and verify the balances in the stock books with other balances monthly. However, according to the Inspection Log Book, it had been observed that during the year 2016, the relevant Superintendent of Excise had not taken part in the monitoring of distilleries in the Kalutara District.

3.16 Contract Administrtion

The following observations are made in this regard.

(a) The Department of Buildings functions as an Advisor regarding the construction of buildings of the Excise Department. However, even prior to the selection of contractors in the proper manner, the Department had, based on the basic/preliminary estimate, released provisions to the Department of Buildings for building construction purposes. Accordingly, it had been observed during the course of the audit that other parties were improperly utilizing provisions received by the Department for constructions. During the year under review and the previous year, amounts released had been Rs.41,000,000 and Rs.50,000,000 respectively.

(b) Total provisions amounting to Rs. 61.84 Million, being the amount estimated for the construction of the Kandy and Nuwara Eliya Excise Offices, had been released to the Department of Buildings on 15 June 2016. However, even by May 2017, construction work had not been completed.

(c) Even though a sum totalling Rs.377.07 Million had been spent from the year 2013 to year 2016 for the construction of 05 buildings for the Department, by 31 December 2016, none of the building constructions had been completed. By 31 July 2017 construction work of only two buildings had been completed.

3.17 Human Resources Management
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Approved Cadre and Actual Cadre
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The position on the cadre as at 31 December 2016 had been as follows:

	Category of employees	Approved Cadre	Actual Cadre	Number of Vacancies
(i)	Senior Level	64	40	24
(ii)	Tertiary Level	433	379	54
(iii)	Secondary Level	818	662	156

(iv)	Primary Level	172	166	06
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	Total	**1487**	**1247**	**240**
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The following observations are made.

(a) 07 posts, by way of 04 posts of Deputy Commissioner of Excise and 03 posts of Assistant Commissioner of Excise, being posts at senior level directly contributing to the mission of the Department, were lying vacant. Further, proper action had not been taken to fill 13, 13 and 27 vacancies respectively in the posts of Superintendent of Excise, Chief Inspector of Excise and Inspector of Excise.

(b) It was not observed that Human Resources Management had been carried out taking into consideration obtaining an efficient service through the allocation of duties and the transfer of duty subjects from time to time within the organizational structure and strengthening internal control.