

## **Sri Lanka Cashew Corporation – 2016**

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The audit of financial statements of the Sri Lanka Cashew Corporation for the year ended 31 December 2016, comprising the statement of financial position as at 31 December 2016 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 Corporation 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**

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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**

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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 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 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 the 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**

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

## **2. Financial Statements**

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### **2.1 Qualified Opinion**

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In my opinion, except for the effects of the matters described in Paragraph 2.2 of this report, the consolidated financial statements give a true and fair view of the financial position of the Sri Lanka Cashew Corporation as at 31 December 2016 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**

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#### **2.2.1 Sri Lanka Accounting Standards (SLAS)**

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The following non-compliances were observed.

##### **(a) Sri Lanka Financial Reporting Standard 07**

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In terms of Section 08 of the standard, the manner in which financial assets and liabilities were classified and the nature and extent of financial and management risks arising from financial instruments had not been disclosed along with the financial statements.

##### **(b) Sri Lanka Accounting Standard 01**

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- (i) The description of the nature of the capital reserves had not been disclosed along with the financial statements in terms of Section 79(b) of the Standard.
- (ii) The accounting policy used for the recognition and measurement of financial instruments and the recognition and accounting the biotic assets belonged to the Corporation had not been disclosed with the financial statements in terms of Section 117 of the Standard.
- (iii) Except permitted or required by the standard, income and expenditure should not be offset. Nevertheless, income of Rs.127,617 of the papaw project had been off set against its expenditure of Rs.332,262.

##### **(c) Sri Lanka Accounting Standard 02**

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Instead of valuation of stock by computing the cost separately, the stock had been valued at average cost of all products. However, the market price of the cashew related products amounting to Rs.12,411,594 shown in the financial statements had been less than the average cost price.

**(d) Sri Lanka Accounting Standard 16**  
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- (i) In terms of Section 55 of the standard, depreciation of an asset begins when it is available for use. Nevertheless, in depreciating buildings, the policy had been recognised in a manner that depreciation had been made for the entire year, irrespective of the completion date of constructions.
- (ii) As the useful life of non-current assets had not been reviewed, 19 motor vehicles costing Rs.22,921,312 fully depreciated but were being further used. Accordingly, the estimated error arisen had not been revised in terms of Sri Lanka Accounting Standard 08.
- (iii) In terms of Section 73 of the standard, the accumulated depreciation at the beginning of the year under review, the year's depreciation and the depreciation of disposed assets relating to the Property, Plant and Equipment had not been disclosed.

**(e) Sri Lanka Accounting Standard 19**  
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- (i) In terms of Section 57 of the standard, all material post-employment benefit obligations should be assessed by a qualified actuary but it had not been so done.
- (ii) Information with regard to employee benefits to be disclosed had not been disclosed as required by the standard.

**2.3 Accounts Receivable and Payable**  
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The following observations are made.

- (a) The total value of payable balances in the financial statements of the year under review amounted to Rs.16,412,780 out of which the balances totalling Rs.8,929,887 and Rs.600,000 had been older than 5 years and between 3 to 5 years respectively.
- (b) The total value of receivable balances was Rs.22,523,199 out of which the balances totalling Rs.13,230,715 and Rs.5,896,600 had been older than 03 years and between 1 to 3 years respectively.
- (c) Although there was a balance of Rs.1,499,709 in the provision for audit fees account as at the end of the year under review, audit fees had not been paid after the year 2010.
- (d) Lease rental for the land belonging to the Land Reforms Commission possessed without an agreement had not been paid.

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

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The following instances of non-compliance were observed.

Reference to Laws, Rules, Regulations and Management Decisions	Non-compliance
(a) Inland Revenue Act No,10 of 2006.	Action had not been taken to prepare tax returns or to pay income tax for the assessment years of 2011/2012, 2012/2013, 2013/2014, 2014/2015 and 2015/2016.
(b) Value Added Tax Act No.14 of 2002 and National Building Tax Act No,9 of 2009.	An entity which supplies or manufacturers wholesale and retail goods and the quarterly turnover is over Rs.3.75 million or the annual turnover is more than Rs.15 million that entity should register for Value Added Tax and Nation Building Tax. Action had not been taken accordingly.
(c) Guideline 5.4.8 of the Government Procurement Guidelines of 2006.	Eventhough a contract for Rs.1,350,000 had been awarded for the deforestation of 100 acres at Rs.13,500 per acre in the Kondachchi Estate, a performance bond had not been obtained. As that contractor had failed to commence the work, that task had been subsequently awarded to another party deviating the Procurement Guidelines on the decision of the Board of Directors on 30 August 2016. A sum of Rs.1,500,000 had been paid on 30 April 2017 for 100 acres at Rs.15,000 per acre.

## 3. Financial Review

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### 3.1 Financial Result

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According to the financial statements presented, the operation of the Corporation for the year under review had resulted in a deficit of Rs.36,525,411 as compared with the deficit of Rs.47,728,042 for the preceding year. Accordingly, the deficit had decreased by Rs.11,202,631 as compared with the preceding year. Increase of revenue in the Commercial Division by Rs.19,609,086 and the decrease of expenditure in the Service Centre by Rs.3,406,450 had mainly attributed to this decrease.

In analyzing the financial results of the year under review and the 4 preceding years, there was a net profit of Rs.44,233,832 for the year 2012 and it had continuously deteriorated since then and the net loss for the year 2015 amounted to Rs.47,728,042. As adjustments had been made in the year 2016 for the compensation received for lands which was a non-operational income and the over provision of gratuities totalling Rs.22,746,506, the net loss for the year 2016 had reduced to Rs.36,525,411. However, in considering employees remuneration and depreciation on non-current assets, the contribution of Rs.121,065,660 of the Corporation in the year 2012 had decreased to Rs.87,183,875 in the year 2016.

## **4. Operating Review**

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### **4.1 Performance**

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In terms of the State Agricultural Corporation Act No.11 of 1972, the main objectives of the establishment of the Corporation are Plantation, Production, Processing and Sale of Cashew, Preparation of Plans for Marketing, conducting investigations and researches collection, preparation, Publication and distribution of information on marketing and others, training of persons required for processing Cashew related products and the promotion of demand for products for the World Market.

In order to achieve the above objectives, the Corporation has a network, comprising of 7 Cashew estates, 04 breeding centres, 07 Central Plant nurseries which produces but plants, 02 Cashew Processing Centres, 03 Sales Centres, 02 reaserch centres and 51 Marketing agents network. Audit examination carried out in respect of the main activities of the Corporation observed the following matters.

#### **(a) Production in the Cashew Estates belongs to the Corporation**

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According to the information made available for audit, the observations on the production in the Cashew estates belonging to the Corporation and the extent of cultivation of lands are given below.

- (i) Replanting in the Kondachchi estate, 6,000 acres in extent, had been commenced in the year 2014 and Cashew Plants had been cultivated in 450 acres by March 2017. However, the cultivation had not been properly maintained.
- (ii) It was observed that reap of harvest can be done in the year 2017 from Cashew Plants Cultivated in the year 2014, but the necessary facilities had not been provided to store the harvest properly and to dry the harvest after reaping.
- (iii) The fertile land of the Kondachchi estate, 4,350 acres in extent, had been idle and the attention of the Management was not drawn to replant by increasing necessary equipment, supervisory staff and Labourers under a proper plan.
- (iv) Out of the land, 960 acres in extent, in the Achchige estate in Puttalam, 760 acres were suitable for cultivation and a minimum crop of 14,641 kg field weight of Cashew had been obtained during the year under review. Eighty seven acres had been utilized for replanting.  
Eventhough the number of bud Cashew plants cultivated in a land of 673 acres in extent amounted to 53,840, the number of Cashew trees already cultivated amounted to 3,286 only. As such a land 50,540 acres in extent where Cashew can be cultivated had been idle without being utilized for cultivation.

- (v) As the age of 15,195 Cashew trees in the Puttalam, Kandamaluwa and Hardy estates had been older than 30 years, the yield of them was at a low level. The yield of a Cashew tree in the Mankerny, Suduwathura ara and Oyamaduwa estates had been less than 2 kg as compared with the maximum yield of 4.93 kg of field weight in the Eluwankulama Estate.
  - (vi) In the Puttalama Estate, 800 seeds plants and 4000 bud plants had been cultivated in the years 2012 and 2013 respectively and 28 per cent of them were destroyed according to the census in 2015.
- (b) Proper statistical records had not been maintained in an updated manner in respect of Cashew trees in the Cashew estates of the Corporation by identifying Cashew trees.

(c) **Implementation of the subsidy programs**  
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The Cashew plantation subsidy scheme had been implemented since 2000 island wide with the objective of extending Cashew cultivation and to improve the National Product. By the end of the year under review 2,383,620 and 1,200,640 bud Cashew plants and seed cashew plants respectively totalling Rs.3,584,260 had been distributed among the farmers under this subsidy scheme, and the following observations are made in this connection.

- (i) Sums of Rs.62.9 million and Rs.222 million had been spent as capital expenditure and recurrent expenditure respectively during the past 5 years, therefor. The cash for fertilizer subsidy had been given prior to the year 2013 and a sum of Rs.16 million had been granted as fertilizer subsidy from the year 2007 to 2013 but the Corporation had not taken follow up action about the successfulness.
- (ii) Cashew plants of 34,240 had been distributed in the year 2014 among the 275 farmers in 09 Divisional Secretarial Divisions in the Puttalam District. In the first check carried out observed that 46 per cent plants of them had destroyed whereas in the second check observed that 65 per cent of them had destroyed. In the year 2015, Cashew plants had been distributed to 201 farmers in 09 Divisional Secretariat Division in the same district and it was observed in the first census, 31 per cent of them had destroyed.
- (iii) Cashew plants of 36,000 had been distributed among the farmers in 11 Divisional Secretarial divisions in the Kurunegala District in the year 2014. By the time of the first check and the second check 58 per cent and 71 per cent of them respectively had destroyed. In the year 2015, 28,000 Cashew Plants had been distributed among 248 farmers in 10 Divisional Secretarial Divisions out of which 43 per cent of them had destroyed by the year 2016.
- (iv) Cashew plants of 32,000 had been distributed among 412 farmers in 14 Divisional Secretarial Divisions in Anuradhapura District in the year 2014. By the time of the second check, only 9,948 or 31 per cent of them had remained.

- (d) According to the physical test check carried out in Divisional Secretariats of Puttalama and Arachchikattuwa in Puttalam District. Nikaweratiya in Kurunegala District and Nochchiyagama in Anuradhapura District the following matters were observed.
- (i) All 640 plants given to 3 farmers had destroyed and out of 3,120 plants given to 28 farmers, only 824 plants or 26 per cent had succeeded.
  - (ii) Most of the Cashew estates had overgrown with weeds and not properly maintained. Furthermore, action had not been taken to protect the plants from animals.
  - (iii) Eventhough nearly 5 years had elapsed by now for Cashew Plants given in the year 2012, any cultivated land whatsoever which reaping harvest was not observed at the physical verification.
  - (iv) Even though a proper supervision had to be carried out in order to achieve the objectives of the Cashew subsidy program, supervisory functions were difficult as the cultivated lands were not located so as to easy supervision of the Cashew Development Officers.
- (e) In the production of Cashew during the year under review there were 27,935 kg of rotten and empty Cashews. Although the rotten and empty Cashews should be 15 per cent of the field weight of 1 kg, the rotten and empty cashew percentage of Eluwankulama Kamandaluwa and Nalanda estates had ranged from 19 to 57 per cent of the field weight of the harvest received.
- (f) The Corporation had sold 30,598 kg of Cashew in the year under review. Of them 22,022 kg of Peel Cashew and 7,029 kg of Cashew flesh had been purchased from the external persons. Accordingly, 11,430 kg of Cashew had been purchased from outside and as such the estates of the Corporation had reached a Cashew production as low as 20,000 kg.

(g) **Research and Development**

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A sum of Rs.4,631,970 had been spent for the Kansamalawa and Puttalam Research Centres in the year under review and the following observations are made in this regard.

- (i) Though a research proposal before being conducted researches should be approved, proposals for only 2 researches in the Puttalama Research Centre had been furnished.
- (ii) Continuous and formal progress reports, enabling to evaluate the research progress had not been presented.

## **4.2 Transactions of Contentious Nature**

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- (a) Instead of using a proper computer software, suitable for accounting purposes, a software to which all accounting data could not be input had been used, and as such a Computerized Trial Balance had not been prepared and it had been manually prepared instead.
- (b) One rupee is charges per kg of peel Cashew from the Private imports of Peel Cashew on the decision of the Board of Directors and a sum of Rs.2,150,000 had been recovered in the year under review and it had been brought to accounts under miscellaneous income in the financial statements.

## **4.3 Management Activities**

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Although the Corporation had cultivated Cashew in 15 estates, 17,650 acres in extent, of them, 200 acres of an estate belonged to the Department of Agriculture, 1,874 acres of 3 estates, 15,280 acres of 6 estates 151 acres 135 acres and 10 acres belonged to the Land Reform Commission, Government, Department of Conservation of Forest, Elkaduwa Plantation Company and the Livestock Development Board respectively, action had not been taken to acquire those lands to the Corporation.

## **4.4 Idle and Underutilized Assets**

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The following observations are made.

- (a) The boiler and related equipment used for boiling Peel Cashew in the Cashew Processing Centres in Nadagamuwa and Puttalama had been idle for more than 10 years. As such, more wastages occurred when cutting Peel Cashew.
- (b) Sixteen motor cycles which could be used in the Nathagamuwa Cashew Processing Centre had been idle. Had they been not used for the functions of the Corporation, necessary action had not been taken to dispose of them properly.
- (c) Estate Superintendents' bungalows in the Kandachchi estate, 328 buildings of Store Keepers and Labourers and buildings including the school had destroyed. Those properties included vehicle service station, 3 water tanks with 20,000 liter capacity and one cultivation well.

## **4.5 Personnel Administration**

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The following observations are made.

- (a) The approved and actual cadre of the Corporation stood at 224 and 184 respectively and as such 40 vacancies had existed. Two officers had been recruited to the Post of Labour Supervisors in excess of the cadre and 9 employees had been recruited on contract basis.



- (b) Without the approval of the Department of Management Services, a market promotion officer had been recruited on the decision of the Board of Directors met on 28 October 2016.
- (c) Two executive grade officers of the Corporation had been recruited, contrary to the qualifications stated in the scheme of recruitment.

## **5. Accountability and Good Governance**

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### **5.1 Tabling the annual reports**

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The annual report of the Corporation for the year 2014 had not been tabled in Parliament and a draft annual report had not been presented in accordance with, Public Finance Circular No.PF/PE/21 dated 24 May 2002.

### **5.2 Budgetary Control**

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In comparing the budgeted figures with actuals in the year under review for 17 items variances ranging from 14 per cent to 765 per cent were observed, thus the budget had not been made use of as an effective instrument of financial control.

## **6. Systems and Controls**

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Weaknesses in systems and control 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.

<b>Areas of systems and control</b>	<b>Observations</b>
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(a) Personnel Administration	Although more staff had been employed to the extension Division than the staff employed to the Cashew Plantation, the expected objectives had not been achieved.
(b) Assets Control	<ul style="list-style-type: none"> <li>(i) Not taking action to acquire the legal ownership of Cashew estates.</li> <li>(ii) Not taking action to get the maximum productivity from Cashew estates belonging to the Corporation.</li> </ul>
(c) Stock Control	Stock of Cashew purchased from external parties by the Cashew Processing Centre at Nadagamuwa had not been entered in a proper register.

- (d) Accounting
  - (i) The software system used for accounting purposes had not been updated to suite the Corporation.
  - (ii) Non-preparation of a consolidated Trial Balance.
  - (iii) Deviation from Sri Lanka Accounting Standards.
  
- (e) Debtors Control
  - Action had not been taken to recover the debts receivable from sale of Cashew on time.