

## **Kalubowitiyana Tea Factory Company Limited - 2018 /2019**

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### **1. Qualified Opinion**

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The audit of the financial statements of the Kalubowitiyana Tea Factory Company Limited (“Company”) for the year ended 31 March 2019 comprising the statement of financial position as at 31 March 2019 and the statement of comprehensive income, profit and loss statement, statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, 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 provisions of the National Audit Act No. 19 of 2018 and the Financial Act No. 38 of 1971 . My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, except for the effects of the matters described in Paragraph 1.5 of this report, the accompanying financial statements give a true and fair view of the financial position of the Company as at 31 March 2019, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

### **1.2 Basis for Qualified Opinion**

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My opinion is qualified based on the matters described in Paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor’s Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

### **1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements**

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Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Public Sector Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company’s financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared.

#### **1.4 Scope of Audit (Auditor's Responsibility in Auditing Financial Statements )**

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My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause to cease to continue as a going concern.
- Evaluate the structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following.

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company ;
- Whether the it has performed according to its powers, functions and duties; and
- Whether the resources had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

## 1.5 Financial Statements

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### 1.5.1 Non-compliance with Sri Lanka Accounting Standards

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<b>Non-compliance with Accounting Standards</b>	<b>Comments given by the Management</b>	<b>Recommendation</b>
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Although the disclosure of the assets held as collateral should be made in the financial statements in terms of Paragraph 74 (a) of the Sri Lanka Accounting Standards 16, the land on Kalubowitiyana Tea Factory, which the Company had kept as collateral to obtain a working capital loan amounted to Rs. 78,000,000 in the year 2016 had not been disclosed in the financial statements.	It was taken in to notes. Actions will be taken to correct in the next year and make disclosures the assets held as collateral in financial statements.	Disclosures should be made on assets held as collateral as per Sri Lanka Accounting Standards in the financial statements.

### 1.5.2 Accounting Deficiencies

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<b>Audit Observation</b>	<b>Comments given by the Management</b>	<b>Recommendation</b>
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(a) The cost and the cumulative depreciation of the fully depreciated tea dryer cost at Rs. 1,000,000 and sold in	Since there is not enough documents to find the cost of this tea dryer , it has not been excluded and as the assets	Actions should be taken to exclude the cost and the accumulated depreciation of the assets

the year 2014 had not been valuation has already been sold. excluded from the accounts completed in this year, this value at the end of the year under review. will be corrected accordingly.

- (b) A sum of Rs. 59,532,264 incurred by the Company for the construction of a factory at Menikdiwela Land belonging to Tea Shakthi Fund was shown as buildings instead of being taken in to accounts as a receivable balance and the relevant depreciation adjustments had been made. As the approval of the Cabinet of Ministers had been received by now to hand over the relevant factory to our Company, stating of that amount as an assets of the Company is accurate. Prompt actions should be taken to obtain the Menikdiwela Factory to the Company with the approval of the Cabinet of Ministers.

### 1.5.3 Unreconciled Control Accounts or Records

Item	Value as per Financial Statements Rs.	Value as per the Corresponding Records Rs.	Difference Rs.	Comments given by the Management	Recommendation
Balance of 05 Debtor Accounts	7,135,440	5,812,772	1,322,668	The difference is comprise with the total of the value short delivery of tea sent to the stores of the Forbes & Walker and the advance payment made in excess to the Leaf supplied to the Menikdiwela Factory and actions will be taken to correct them in future.	Arrangements should be made to reconcile the balances and to make required corrections.

### 1.5.4 Lack of Evidence for Audit

Item	Amount Rs.	Audit Evidences not provided	Comments given by the Management	Recommendation
(a) Rent payable to B.C.C Lanka	750,000	Rental Agreement	Although the rent payable for this	Actions should be taken to enter into

Company			amounted to an agreement with Rs. 750,000 has an external party to been taken in to obtain buildings on accounts as a lease. payable, a formal agreement has not been signed between B.C.C Lanka Company and our Company.	
(b) Fertilizer Company	728,048	Balance Confirmation Letters	Actions will be taken to rectify in future.	Actions should be taken promptly to correct the balances.
(c) Balance receivable from the Tea Sales Center	2,481,141	Detailed Schedules	An amount worth of Rs. 2,119,800.00 and a sum of Rs. 230,000 send to the tea shop of the Kalubowitiyana Factory from the Derangala and Hiniduma factories respectively has been taken in to accounts as at 31 March 2019 andIt is in due to send these tea stocks to the Marketing Division after being packed .	The Schedules relating to the accounts should be furnished .
(d) Debtor balance	14,641,152	Balance Confirmation Letters	The letters have been sent to those institutions to submit the confirmations to the Audit Division directly .	Actions should be taken to provide balance confirmations for the audit.

## 1.6 Accounts Receivable and Payable

### 1.6.1 Receivables

Audit Observation	Comments given by the Management	Recommendation
Even though a loan amounted to Rs. 10,000,000 had been granted to the BCC Lanka Company in the year 2003 at a 22 per cent interest rate on a recovery basis in 12 installments, as it could not recover at least one installment, the total amount due as at the end of the year under review was Rs. 52,910,605	As the 6 acres of lands owned by B.C.C Lanka Ltd. has been handed over to the Ministry of Prison Reforms, once the amount is received by BCC Lanka, they have pledged in writing to settle this amount to us.	Actions should be taken to recover the loan promptly with both parties agreement.

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

Reference to Laws, Rules, Regulations, etc.	Non-compliance	Comments given by the Management	Recommendation
(a) <b>Public Enterprises Circular No. PED / 12 of 02 June 2003.</b>			
(i) Paragraph 9.3.1. (V)	Although, appointments should be made on a temporary basis until a permanent appointment is made, an officer has been appointed as the Assistant Manager (Marketing) on acting basis in the Head Office of the Company on 22 March 2017, without making a permanent appointment.	An employee of the institute was deployed in the post of Assistant Manager (Marketing) on acting basis to minimize the cost. As there has been some improvement in the Marketing Division at present, it has been submitted for approval to fill the vacancies in the post of Assistant Manager (Marketing).	Action should be taken to obtain a permanent appointment for the post of Assistant Manager (Marketing) with the relevant approvals.

(ii) Paragraph 9.14	Although a procedural manual should be prepared for obtaining the approval of the Secretary to the Treasury to formulate rules for Human Resource Management the Company had not acted accordingly.	Actions will be taken to formulate a relevant procedural manual for Human Resource Management.	It should prepare a Procedural Manual and obtain the approval.
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**(b) Public Enterprises  
Circular No.  
01/2015 dated 25  
May 2015**

(i) Paragraph 3.2.1	Although the approval of the Secretary to the Line Ministry should be obtained for additional fuel by the Chairman, in cases where the monthly fuel allowance is not sufficient to perform the duties, the approval for additional fuels exceeding the approved fuel limit amounted to Rs. 243,854 had not been obtained by the Chairman of the Company.	It has been stated in the letter dated 12.10.2016 by the Secretary to the Ministry that there was no objection of the Ministry for the payment of the fuel by the approval of the Board of Directors. The Board of Directors has approved the reimburse of 91 liters of fuel per month at the meeting of the Board of Directors on 25.05.2017. Accordingly, the expenditure incurred on fuel for the additional runs for the official duties has been reimbursed.	It should focus on operating within the monthly approved fuel limit and actions should be taken to obtain approval in accordance with the Circulars obtaining additional fuel.
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(ii) Paragraph 3.2.2	Although the approval of the Board of Directors should be obtained before reimbursement of additional fuel to the Executive Directors	The reimbursement of fuel is done with the approval of the Chairman and the Managing Director.	It should focus on operating within the monthly approved fuel limit and actions should be taken to obtain approval in
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and other Officers, the approval had not been obtained for the additional fuel amounted to Rs. 157,411.

accordance with the Circulars for obtaining additional fuel .

- (c) Financial Regulations of the Democratic Socialist Republic of Sri Lanka.  
F.R .387
- Although the paying officer should constantly monitor whether his bank balance is sufficient for payment by cheque, since the cheques were written without verifying that the bank balance is adequate, a sum of Rs. 12,168,970 had to be paid as overdraft interest for the overdraft balance of Rs. 81,708,981 by the end of the year.
- Providing a bank overdraft amounting to Rs. 50 million to the Tea Shakthi Institute with the direct intervention of the Minister of Plantation Industries and the Ministry in the year 2015 received and due to factors such as the construction of Menikdiwela Factory under the 100 day programme (Rs. 76 million), the Company's bank balance caused a bank overdraft and since the Hiniduma Hills and Menikdiwela factory were making continuous losses and also availability of a negative cash flow through these factories, it has been impossible to minimize the continuous cash balances remained on a bank overdraft .
- Actions should be taken to make payments preparing the plans for monthly cash flow of the Company whilst making payments by cheques.

## 2. Financial Review

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### 2.1 Financial results

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The financial results for the year under review was a deficit of Rs. 50,211,574 and the corresponding deficit for the preceding year was Rs. 3,285,757. Accordingly, a deterioration of Rs. 46,925,817 was observed in the financial results. The increase in

the cost of sales over the sales income during the year under review had mainly attributed to this deterioration.

### 3. Operating Review

#### 3.1 Management Inefficiencies

Audit Observation	Comments given by the Management	Recommendation
(a) An officer who works full time in a permanent post as a manager of another government agency and receiving the salary and allowances relevant to that post was appointed as the Executive Director of this Company and the Executive Director's allowance and fuel allowance amounted to Rs. 718,825 had been paid by the Company during the year under review.	An Executive Director has been appointed with effect from 16 July 2018 at the Board Meeting held on 19 July 2018. Accordingly, the incentives and benefits of the post have been granted according to Circular No. PED 3/2015 . From April 2019, upon the oral request of the Executive Director, 50 per cent of the monthly allowance will be paid.	An officer working full-time in an another government agency should not be paid full salary in the post of Executive Director.
(b) Even though a sum of Rs. 938,922 had been paid as interest by obtaining a sum of Rs. 93,679,116 as a short-term loan on the value of the made tea sent to a broker to be submitted to the auction , the approval of the Board of Directors had not been obtained.	These funds are obtained from the brokers with the approval of the Chairman of the Institute for maintaining the cash flow of the institution. Since the Board Meeting is held once a month, it is impractical to seek the approval of the Board of Directors for expenditure.	Actions should be taken to obtain loans with the approval of the Board of Directors.
(c) A member of the Board of Directors who was not eligible for official vehicles had been assigned a vehicle and paid an allowance of Rs. 152,760 in the year under review.	One member of the Board of Directors has been entrusted with the task of supervising the production activities of the newly opened Tea Factory at Menikdiwela and overseeing the process of obtaining tea leaves by a letter signed by the Chairman dated 04.01.2018. A car has been given to facilitate transportation for these duties and fuel is provided depending on the distance traveled for the	The management should take actions to comply with the Circular provisions, to recover the allowances granted to officers who were not entitled to official vehicles.

official purpose.

- (d) Even though a worker can only be paid a bonus of Rs. 3000 each, only a sum of Rs. 252,000 can be paid as bonus considering sympathy for employees of companies that have reported a loss in the financial year 2016 and failed to reduce their profitability in financial year 2017 in terms of the Public Enterprises Circular No. PED 03/2018 of 07 December 2018, a sum of Rs. 559,719 had been paid as bonus exceeding that amount.
- The collapse of the entire tea system has resulted in the profitability of the tea industry has been declined. However, this has been paid with the approval of the Board of Directors, since the employees should be encouraged and their economic background needs to be improved.
- Actions should be taken to pay bonus to the officers according to the Circulars.

### 3.2 Operating Inefficiencies

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Audit Observation	Comments given by the Management	Recommendation
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(a) A sum of Rs.2,167,569 had been paid as incentives to leaf suppliers for the implementation of green leaf promotion programme with the objective of increasing production at Menikdiwela Tea Factory during the year under review and even though a Board Member had been appointed to supervise the programme, the purchase of green leaf had declined by 74,540 kgs as compared to the previous year. Accordingly, the desired objectives had not met through the implementation of the promotional programmes .	Even if green leaf incentives are provided, it is difficult to find quality suppliers. Due to this, green leaf incentives have been discontinued in the year 2019/2020 .	The Management should work towards achieving the targeted objectives.
(b) Although the Company had paid incentives amounted to Rs. 672,028 to the green leaf suppliers to uplift the green leaf yield of the Hiniduma Tea Factory and the also the obtaining of green leaf yield for the year under review had dropped by 349,704 kg as compared to the preceding year, the	In the event of a decline in the price of made tea in the market, the quantity of green leaf purchased to reduce production was also deducted. Thereby the losses of Company were reduced. Further, since the Management decided to buy	Management should be responsible to meet the Company's desired objectives whilst providing incentives.

management had not taken the high quality green leaf, the necessary measures for that. incentives were paid to buy high quality green leaf.