

Customs Officers Reward Fund - 2020

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Customs Officers Reward Fund for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the statement of comprehensive income, 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(3) 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. My comments and observations which I consider should be presented in Parliament, appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the financial statements give a true and fair view of the financial position of the Fund as at 31 December 2020, and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

1.2 Basis for Qualified Opinion

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

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 determines 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 Fund's ability to continue as a going concern, disclosing matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process.

As per Sub-section 16(1) of the National Audit Act, No. 19 of 2018, the Fund 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 of the Fund.

1.4 Auditor's Responsibility for the Audit of Financial Statements

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 Fund'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 Fund'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 the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, 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 Fund and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Fund has complied with applicable written law, or other general or special directions issued by the governing body of the Fund;
- Whether the Fund has performed according to its powers, functions and duties; and
- Whether the resources of the Fund had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Audit Observations on the Preparation of Financial Statements

1.5.1 Non-compliance with Sri Lanka Public Sector Accounting Standards

Non-compliance with reference to the relevant Standard	Comments of the Management	Recommendation
(a) Contrary to paragraph 01 of Standard 1, the revenue from penalties imposed and confiscations had been brought to account on cash basis.	Has not made comments.	Action should be taken in terms of Sri Lanka Public Sector Accounting Standards.
(b) In terms of paragraph 128 of Standard 1, each item on the face of the statement of financial position, statement of comprehensive income and statement of changes in equity shall be cross-referenced to any related information in the notes. However, it had not been so done.	Even though notes relevant to related information in notes, have been presented relating to each item on the face, note numbers have not been cross-referenced by mistake. Officers have been instructed to rectify these shortcomings in presenting accounts in ensuing years.	- do -
(c) In terms of paragraph 54 of Standard 3, in case of correction of prior period errors, matters such as nature of the prior period error should be disclosed in the financial statements. However, disclosures relating to the note of correction of error amounting to Rs.8,687,637 indicated in the statement of changes in equity, had not been made in the financial statements of the year under review in terms of the Standard.	Agreed with observations. It had not been disclosed through a detailed note relating to correction of errors by mistake.	- do -

1.5.2 Accounting Deficiencies

Audit Observation	Comments of the Management	Recommendation
<p>Fifty per cent of the value of penalties and confiscations is credited to the Customs Officers Reward Fund and the said amount is distributed among informants and Customs Officers who had involved in custom investigations. Even though a small percentage out of funds received to the Fund, was allocated to various reserves, information on the value allocated for each reserve had not been revealed in the financial statements. Moreover, the amount received for various small reserves out of funds received to the Fund, had been revealed in the financial statements as the surplus of the Fund. The amount indicated accordingly as the income over expenditure in final accounts (Statement of Comprehensive Income) of the year under review amounted to Rs. 34,143,154.</p>	<p>If any expenses incurred for the said investigation, it is deducted from penalties and confiscated value and 50 per cent of the remainder is credited to the Customs Officers Reward Fund. However, the said total value is not fully distributed among informants and Customs Officers. Out of the value credited to the Reward Fund in accordance with Departmental Orders issued from time to time by the Director General of Customs, allocations are made for each following sub-funds. As such, total balances transferred to the Fund are not distributed.</p> <ul style="list-style-type: none"> • Fuel Fund • Narcotic Fund • 2.5% Reward Fund • Pool payment <p>Moneys so transferred to sub-funds in that manner each year remain accumulated in the Fund. A detailed report thereon has been included in the account as well. Therefore, it cannot be agreed with the audit observation.</p>	<p>It should be brought to account in compliance with accounting systems.</p>

1.5.3 Unreconciled Control Accounts or Records

Item	Comments of the Management	Recommendation
<p>A difference of Rs. 22,406,445 was observed between the balance of the Fund according to the Treasury books and Departmental books as at end of the year under review.</p>	<p>This is a balance brought forward since several years. It was noted to make necessary arrangements by examining thereon.</p>	<p>Reconciliation statements should be prepared by explaining reasons.</p>

1.6 Non-compliance with Laws, Rules, Regulations, Management Decisions etc.

Reference to Laws, Rules, Regulations etc.	Non-compliance	Comments of the Management	Recommendation
<p>-----</p> <p>Section 153(2)(b) of the Customs Ordinance No.17 of 1968</p>	<p>-----</p> <p>Even though a suitable methodology should be prepared for the distribution of rewards from the Reward Fund by obtaining the approval of the Minister of Finance, a sum of Rs.16,520,215,868 for officers as cash rewards and a sum of Rs.1,997,381,541 for the informants had been distributed during the period of 22 years from the year 1999 to the year 2020 without evidence for obtaining the approval of the Minister of Finance for the Departmental Order No.PL 118 of 28 January 1988.</p>	<p>-----</p> <p>It is not agreed with your observations regarding the payment of cash rewards in terms of Section 153(2)(b) of Customs Ordinance No. 17 of 1869. It can be assumed that the Order of the Custom Department, No.118 of 1988 has been issued by obtaining the approval necessary therefor and further investigation is required in this regard. A committee has been appointed by the Ministry of Finance for reaching a decision regarding further activities.</p>	<p>-----</p> <p>A suitable methodology should be prepared for the distribution of rewards.</p>

2. Operating Review

2.1 Management Inefficiencies

Audit Observation	Comments of the Management	Recommendation
<p>-----</p> <p>(a) In the investigations conducted on custom offence, recovery of minimum tax revenue receivable to the Government on imports under general condition and crediting to the Government revenue had been disregarded and penalties on custom offences had been imposed including the revenue so deprived of while it had been proposed to pay 50 per cent of</p>	<p>-----</p>	<p>-----</p>

the penalties imposed, for the payment of rewards to officers. Even though the adverse effects resulting therefrom had been pointed out by Audit for many years, it had not been looked into. Consequently, an increase in the cash rewards distributed among the officers were observed. Following observations were made in this regard.

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| <p>(i) There had been a necessity of making amendments to the Customs Ordinance as well as to the legal provisions of these Funds in a proper and updated manner in line with the complexity of imports and exports occurred due to the prevailing liberal economic policies in the country.</p> | <p>Appropriate amendments have been made to the Customs Ordinance and to the legal provisions of the Funds from time to time and attention will be drawn towards making amendments as relevant in future as well.</p> | <p>Necessary amendments should be made.</p> |
| <p>(ii) As cited in Section 162 of the Customs Ordinance, discretionary powers have been assigned to the Director General of Customs on matters relevant to violation of Customs regulations. However, the emphasis laid by Sri Lanka Customs on securing the Government revenue had not been at a satisfactory level.</p> | <p>All relevant steps will be taken to secure the Government revenue when earning Customs revenue.</p> | <p>Emphasis should be laid on securing the Government revenue.</p> |

(b) Collection of Arrears of Penalty Revenue

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| <p>(i) Penalty revenue in arrears amounting to Rs.2,051,340,784 not accounted but in arrears as at 31 December of the year under review, comprised of a sum of Rs.561,540,349 between 1 year and 5 years and a sum of Rs.182,762,354 over 05 years.</p> | <p>A committee has been appointed to regularize collection of arrears of penalty revenue and it was noted to implement a proper methodology for such issues once the committee proposes and formulates them.</p> | <p>Action should be taken to account arrears of penalty revenue.</p> |
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<p>(ii) File relating to Custom Investigation No.CINT/HQB018/2013 had been misplaced with a balance of Rs.2,212,586 after paying Rs.1,955,942. Moreover, a balance of Rs.350,000 remained as arrears in penalties relating to Custom Investigation No.ENSP/CASE/2009/09 as at the date of audit. However, this file had also been misplaced. Action had not been taken in terms of Financial Regulations 103(1) and 104 (1) relating to the said files.</p>	<p>It was noted to record after looking into the matter.</p>	<p>Action should be taken in terms of Financial Regulations.</p>
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2.2 Operating Inefficiencies

Audit Observation -----	Comments of the Management -----	Recommendation -----
<p>In terms of Section 153 (2) (b) of the Customs Ordinance No.17 of 1968, various penalties imposed on custom offences and sums equivalent to 50 per cent of proceeds from sale of confiscated goods, are credited to the Customs Officers Reward Fund and this Fund has been established for payment of rewards to officers and informants with the intention to expose, control and prevent custom duty frauds. The following observations are made on the payments made by the Fund during the period from the year 2012 to the year 2020.</p> <p>(a) A sum totalling Rs.12.249 million had been distributed among officers and informants from the year 2012 to the year 2020 and out of that, a sum of Rs.10,807 million representing 88.22 per cent had been paid to the officers.</p>	<p>Agreed with audit observations.</p>	<p>Attention should be paid towards handling of funds.</p>

- (b) Even though the sum paid to officers and informants in the year 2012 amounted to only Rs.787 million, it had increased up to Rs.1,400 million by 2019 representing 78 per cent. Moreover, the import export sale had been at a considerably low level due to restrictions imposed in the year 2020 and the Covid 19 pandemic. However, rewards amounting to Rs.985 million and Rs.124 million had been paid respectively to officers and informants during the year 2020.
- The sums of Rs.985 million and Rs.124 million paid during the year 2020, are not sums paid for the investigation files relating to the year 2020, but sums paid for files relating to years 2017, 2018 and 2019 of which investigations were concluded. Moreover, one of the key objectives of this Reward Fund is accurately identifying custom frauds and motivating officers therefor. As such, even though custom duty frauds are exposed through this rewards scheme, direct control or reduction of such frauds as a whole is not possible. Specifically, it is observed that carrying out well planned frauds and irregularities in groups using computers and other advanced technology have increased around the world as a whole. Accordingly, the increase of the tendency in earning money by fraudulent means is apparent in our country as well. Moreover, filing appeals by importers and taking court measures have mainly attributed to the delay in investigations.
- (c) A sum of Rs.33,528,128 had been credited in the year under review to the Fuel Fund being a sub fund of the Reward Fund. Even though the objective of establishing the said Fund had been stated as to meet the expenditure on fuel required for custom investigations, the cost of fuel incurred on custom investigations has been a burden of expenditure to the General Head of Expenditure of the Department. As such, no expenditure whatsoever had been incurred from the said Fund during the year under review. Nevertheless, money had been collected to this Fund
- Agreed with the observations. However, the establishment of the said Fuel Fund had been mainly focused on prevention activities of custom offences in case of a certain excess fuel requirement and to fulfill the fuel requirement of the Marine Unit deployed for prevention activities of custom offences, implemented by the Department of Customs before the LTTE war situation. The balance of the said Fund has been accumulated due to non-function of the said Unit as a result of the war situation which prevailed.

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continuously disregarding reasonable requirements and as such, the balance therein had been Rs.588,807,229 as at the end of the year under review.

- (d) An increase of Rs.9,753,579 was evident in the year under review in the Drugs Prevention Fund (Narcotics Fund) for the payments for officers participating in raids on drugs which is a sub-fund of the Reward Fund. However, the sum paid during the year had been only Rs.3,414,100. In terms of Departmental Circulars, monies relevant to the sub-fund have been transferred. Monies so transferred should be recorded as Rs.13,167,679.61 and not as Rs.9,753,579. Relevant payments have been made for requests made during the year based on Departmental Circulars. -do-
- (e) A sum of Rs.17,908,423 had been credited in the year under review to the Fund of 2.5 per cent established for payments for officers of support service supply divisions despite direct non-contribution to investigations and the balance of the said Fund as at 31 December 2020, was Rs.182,494,596. The balance of the 2.5 per cent sub-fund as at 31.12.2020 should be recorded as Rs.182,494,596 and not as Rs.116,044,277. -do-