

Kalubowitiyana Tea Factory Limited - 2021/2022

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Kalubowitiyana Tea Factory Limited (“Company”) for the year ended 31 March 2022 comprising the statement of financial position as at 31 March 2022 and the statement of profit and loss, 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. My comments and observations which I consider should be reported 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 2022, 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

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 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 intends 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 of the Company.

1.4 Audit Scope (Auditor's Responsibilities for the Audit of the 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 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 the Company 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 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 company has performed according to its powers, functions and duties; and
- Whether the resources of the Company 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 Accounting Standards

Non-compliance with the Reference to Relevant Standard	Comments of the Management	Recommendation
(a) Although it was stated that the interest income received should be disclosed separately in the cash flow statement in terms of Paragraph 31 of Sri Lanka Accounting Standards 07, only a sum of Rs. 5,739,106 out of the total value of interest received during the year under review amounting to Rs. 7,507,766 had been shown in the cash flow statement and accordingly, a sum of Rs.1,768,660 had been under-disclosed.	A sum of Rs. 1,776,466 has been shown in income receivable.	Interest income should be disclosed in the cash flow statement in accordance with Sri Lanka Accounting Standards.
(b) The property, plant and equipment of the company amounted to Rs. 343,017,568 had been revalue during the year under review and the matters relating to Sections (a) to (f) of the above Paragraph to be disclosed in the financial statement, including the effective date of the revaluation, whether an independent assessor was deployed at the time of a class of property, plant and equipment was declared at revalued amounts had not been disclosed in terms of Paragraph 77 of Sri Lanka Accounting Standards 16 .	Actions will be taken to disclose in future.	Matters related to the revaluation should be disclosed in the financial statements in accordance with Sri Lanka Accounting Standards 16 .
(c) Although when an item of property, plant and equipment is revalued, the same class of property, plant and equipment to which the asset belongs should be revalued in terms of Paragraph 36 of Sri Lanka	The revaluation activities of Derangala land is being done and actions will be taken to account for as soon as the revaluation is completed.	Derangala land should be revalued and accounted for in accordance with

Accounting Standards 16, the Derangala land had not been revalued during the revaluation of lands.

Sri Lanka Accounting Standards 16 .

(d) Even though the Commission had sent a letter on 23 September 2021 in order to enter into an agreement on a lease basis to acquire the land on which the Hiniduma Hills Tea Factory has been built belonging to the Land Reforms Commission, that had not been taken over by the end of the year under review in terms of Paragraphs 27 and 86 of Sri Lanka Accounting Standards 37, no disclosure whatsoever had been made in the financial statements regarding the respective matter.

The approval of the Board of Directors was received on 19.03.2019 for the transfer of Hiniduma Hills Tea Factory to Kalubowitiana Tea Factory Company. There is no lease agreement or other legal document for payment of lease from 2012 to 19.03.2019. Therefore, although the Land Reform Commission has been informed in writing to enter into a lease agreement on 19.03.2019 a response has not been received so far. As there is no lease agreement, the lease amount has not been disclosed in the financial statements.

The lease agreement and the contingent liability related to that should be disclosed in the financial statements in terms of Sri Lanka Accounting Standards 37.

(e) Even though the market value of Kalubowitiana and Derangala Tea Factory Assets as at 31 March 2019 had been entered in the books considering as the revalued amount of assets in the year under review as per the Valuation Report No. MRII/LM/3574 dated 25 March 2021 issued by the Southern Provincial Valuation Office, it had not been disclosed in the financial statements in that regard in accordance with Paragraph 77 of Sri Lanka Accounting Standards 16.

Actions will be taken to disclose in future.

Information related to the revalued amount should be disclosed in the financial statements in terms of Sri Lanka Accounting Standards 16.

1.5.2 Accounting Deficiencies

Audit Observation

Comments of the Management

Recommendation

(a) At the time of the transfer of the assets of Hiniduma Hills and Menikdiwela tea factories to the Company, the value of the assets except for the land of the two factories was Rs.44,064,020 and although other assets except the buildings out of these assets had been revalued and accounted for in the year under review, the entire loan amount had been shown under

Although the Hiniduma Hills and Menikdiwela tea factories have been handed over to our Company for operations as per the Decision of the Cabinet of Ministers, necessary activities are currently being carried out to transfer the ownership of the land to the institution and arrangements will be made to take

Adjustment should be made to the loan amount by taking actions to take over the ownership of the tea factories to the Company as per the Decision Cabinet of

- short-term investments in the financial statements without adjusting the relevant portion to those assets from the total loan amount of Rs. 50 million provided to Tea Shakti Fund.
- (b) Although the cost of living allowances should be added to the basic salary and the contribution amount should be calculated based on the earnings when calculating the contribution to Provident Fund, due to the calculation of Provident Fund contribution by the Company without taking the Cost of Living Allowance into consideration by the year 2017/2018 it was observed in audit that the arrears of contribution to be credited to Provident Fund from the year 2012/2013 to the year 2017/2018 was Rs.1,695,177 and the surcharge to be paid on that was Rs.847,589 and the Company had not made any provision for this expense in the financial statements.
- (c) Actions had not been taken at the end of the year under review to write off the Economic Service Charges receivable which cannot be set off against the income tax payable, the carry forward period beyond 03 years, entitled for the assessment years 2016/2017 and 2019/2020 amounting to Rs. 4,611,778 and withholding tax credits pertaining to assessment years 2016/2017 to 2018/2019 amounted to Rs.2,075,318. Therefore, the current assets had been overstated in the financial statements by the same amount.
- (d) Even though the balance of People's Bank Savings Account had been Rs. 2,704,918 as at 31 March 2022, the interest income earned on it had not been identified and accounted for.
- over this year. Actions will be taken to adjust Rs. 50,000,000 to assets after taking over the possession of the land.
- Since the calculation of Provident Fund Contribution has been done from the year 2012/2013 without taking Cost of Living Allowance into consideration actions will be taken to credit the amount to be credited to the Provident Funds as soon as the financial condition of the Company improves
- Arrangements will be made to correct in future.
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- Ministers.
- The arrears of balance should be credited to the Employees' Provident Fund. Cost of living allowance should be considered while calculating the contribution to the Fund.
- The balance of tax that cannot be recovered or reimbursed should be written off.
- Actions should be taken to identify the interest income and account for.

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| <p>(e) Closing stock value of finished tea at Derangala, Hiniduma and Menikdiwela factories had been shown by understating Rs.23,955 and overstating Rs.807,543 and Rs.159,404 respectively in the financial statements and the total closing stock value of finished tea amounting to Rs. 942,992 had been overstated accordingly.</p> | <p>The final finished tea stock value of Derangala, Hiniduma Hills and Menikdiwela tea factories presented in the financial statements is accurate.</p> | <p>Since a difference is observed between the year-end physical inventory records and the schedules in the financial statements, stock balance should be entered in accounts as per physical stock records.</p> |
| <p>(f) Even though a sum of Rs.22,390,227 had been capitalized in the financial statements as acquisition of property, plant and equipment during the year under review, acquisitions amounting to Rs.15,043,639 had not been included in the Register of Fixed Assets .</p> | <p>The amount of acquisition of property, plant and equipment purchased during the year presented in the financial statements is correct.</p> | <p>Arrangements should be made to include in the Register of Fixed Assets by properly recognizing the non-current assets purchased during the year</p> |
| <p>(g) Bank reconciliation statements of Derangala Tea Factory had not been properly prepared and when comparing account balances as per monthly account statements and bank account statements, a difference in balances was indicted in each month and the difference had been Rs. 657,941 as at 31 March 2022 .</p> | <p>Actions will be taken to correct in future.</p> | <p>Actions should be taken to properly prepare bank reconciliation statements and to correct discrepancies promptly.</p> |

1.6 Accounts Receivable and Payable

1.6.1 Receivables

Audit Observation	Comments of the Management	Recommendation
<p>(a) A sum of Rs. 798,461 receivable to the Company from a private tea broker from the year 2009 was being brought forward and actions had not been taken to recover that even by the date of audit .</p>	<p>A letter dated 17.10.2022 has been issued to the Registrar of Companies to inquire about the shareholders of the Company and actions will be taken to recover this amount accordingly.</p>	<p>Necessary actions should be taken immediately to recover the relevant amount.</p>

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| <p>(b) Actions had not been taken even by the end of the year under review to recover the balance of trade and other receivable and the balance of other advances remaining from the years 2017 and 2018 amounting to Rs. 1,626,269 and Rs. 1,408,881 respectively.</p> | <p>Actions will be taken to correct in future.</p> | <p>Arrangements should be made to recover outstanding balances promptly and to get settled the other advances from responsible institutions and officers.</p> |
| <p>(c) The deposit of Rs. 1,440,000 paid on availing the leased building in which the Company had run its Head Office during the period from 2013 to 08 September 2020 on monthly rental basis had been failed to recover by the end of the year under review although the Head Office was moved to another building.</p> | <p>Actions will be taken to correct in future.</p> | <p>Actions should be taken to recover the deposit amount promptly.</p> |
| <p>(d) Actions had not been taken to settle the outstanding balance for more than 03 years amounting to Rs.949,020 by the end of the year under review in relation to the advances given to bought leaf suppliers of Hiniduma Hills Factory.</p> | <p>Monthly meetings are being held to recover these receivable balances and the arrangements have been made to reduce the receivable balance to Rs.748,322 by now . Further, the police complaints have been made against the respective parties for these outstanding balances and a letter of demand has been sent to the respective parties.</p> | <p>Proper actions should be taken to promptly recover the respective advances or instead, to procure bought leaf from the bought leaf suppliers.</p> |
| <p>(e) A loan amount of Rs. 10,000,000 had been given to B.C.C. Lanka Ltd. in 2003 on the basis of recovery in 12 instalments at an interest rate of 22 per cent and the initial amount was repaid on 22 June 2022 and the interest to be recovered amounting to Rs.51,118,341 at the end of the year under review had not been recovered up to November 2022 .</p> | <p>Actions are being taken to recover the interest due from B.C.C Lanka Company amounting to Rs. 51,118,341 in three instalments.</p> | <p>Actions should be taken to recover the interest amount promptly.</p> |

1.6.2 Payables

Audit Observation	Comments of the Management	Recommendation
(a) Cheque cancellation and Pay As You Earn surcharge for more than five years amounted to Rs. 903,380 and Rs.59,344 respectively had been entered in the accrued expenses account and actions had not been taken even by the end of the year under review to settle.	Actions will be taken to correct in future.	These balances should be settled promptly.
(b) A total of Rs. 3,710,375 had been accounted for as payable to Tea Shakti Fund and two other private companies since more than five years and actions had not been taken even by the end of the year under review to settle. Failure of claiming for these amounts by the creditors is observed as a controversial matter.	Actions will be taken to correct in future.	Steps should be taken to settle promptly or if it does not claim, then to verify and credit to the income.
(c) Actions had not been taken even by the end of the year under review to settle a balance remaining under trade creditors from more than five years valued at Rs. 1,582,797.	Actions will be taken to settle this trade creditor balance in future.	Steps should be taken to accurately identify the parties to be paid and settle promptly or if it does not claim, verify it and credit it to the income.

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

Reference to Laws, Rules, Regulations	Non-compliance	Comments of the Management	Recommendation	
(a) Public Enterprises Circular No. PED/12 dated 02 June 2003	(i) Section 8.2.2	Although the concurrence of the Minister of Finance and the approval of the respective Minister should be obtained in the investment of funds and even though	Kalubowitiana Tea Factory Company, has been established under the Companies Act and the decision making of the Company is being done by the Board of Directors. Accordingly,	Investments should be made with the approval of the respective Minister and the concurrence of the Finance Minister.

the Company had the short-term invested investments of the Rs. 110,119,465 in Company have been short-term deposits as made with the at 31 March 2022, approval of the Board necessary approvals of Directors. had not been obtained for that.

(ii) Section 9.14

Although a procedure manual related to the formulation of rules for Human Resource Management should be prepared and approval of the Secretary of the Treasury should be obtained, actions had not been taken accordingly.

The procedure manual related to the formulation of rules and regulations for Human Resource Management has been prepared and submitted to the Board of Directors.

A procedure manual should be prepared promptly and necessary approvals should be obtained.

2. Financial Review

2.1 Financial Results

The financial result for the year under review was a deficit of Rs. 2,764,772 and the corresponding deficit for the preceding year was Rs. 15,144,959. Accordingly, a decrease in deficit by Rs. 12,380,187 was observed as compared with the preceding year. Decrease of administrative and financial expenses by Rs. 12,104,410 as compared to preceding year and increase in other operating income by Rs. 4,763,170 had mainly attributed for this decrease.

2.2 Trend Analysis of Major Income and Expenditure Items

The sales income of the Company had decreased by 11 per cent as compared to the preceding year and it is observed that the 29 per cent decrease in sales income at the Hiniduma Hills Factory and the 12 per cent decrease in sales revenue at the Kalubowitiana Factory had mainly attributed for this decrease. Similarly, due to decrease in fixed deposit interest income as compared to the preceding year, the financial income of the year under review had declined by 26 per cent. It was also observed in cost component analysis that the other major expenses, including cost of sales, had decreased from 11 per cent to 62 per cent as compared to the preceding year.

2.3 Ratio Analysis

The current ratio of the year under review and the previous year had remained unchanged at 2:1 and it was observed that the quick assets ratio which was 1.6: 1 in the previous year was 1.4: 1 in the year under review. Similarly, considering the gross profit ratio of the Company, the amount of 1.4 per cent in the previous year remained unchanged in the year under review and it was observed that the net profit ratio which was negative at 1.2 per cent in the preceding year had continued to be negative at 0.7 per cent in the year under review.

3. Operational Review

3.1 Management Inefficiencies

Audit Observation	Comments of the Management	Recommendation
(a) Although 15 unauthorised residents had occupied the 3.31 hectare land in between 1989-1996 valued at Rs.23,000,000 on which the Kalubowitiana Tea Factory is located, legal actions had not been taken till the end of the year under review to remove them.	The complaints have been made to the Divisional Secretary about the presence of unauthorised residents . The Divisional Secretary had carried out the surveys of the land through the Government Surveyors Department and actions are being taken to take legal actions by examining the legal ownership held for the land of unauthorised residents based on that report.	Unauthorised residents should be evicted by taking legal actions.
(b) The Hiniduma Hills and Menikdiwela tea factories established under the Tea Shakti Fund were handed over to Kalubowitiana Factory Company for operational activities in 2012 and 2015 respectively and due to difficulties in maintaining the Tea Shakti Fund by the Company a loan of Rs. 50 million had been given to the Fund on 09 April 2015 . Although the approval had been given to legally transfer the ownership of Hiniduma and Menikdiwela tea factories to the Company for this amount as per the Decision of the Cabinet of Minister No CP/19/0743/117/024 dated 19 March 2019, the legal ownership of the factories had not been vested even by the end of the year under review.	Although Hiniduma Hills and Menikdiwela tea factories have been handed over to our Company for operations as per the decision of the Cabinet of Ministers, necessary arrangements are currently being carried out to transfer the ownership of the land to the Company and actions will be taken to take over this year.	According to the Decision of the Cabinet of Mimisters, immediate steps should be taken to take over the ownership of the tea factories to the Company.

- (c) Since the repairs and maintenance of the circuit bungalow located in the Kalubowitiana Tea Factory premises have not been carried out systematically, a huge cost has to be incurred for the repair due to long-term existence of this condition and it was observed during the audit that it had adversely affected the effective life of it as well .
- The relevant building had been converted into a circuit bungalow in the year 2017 and the maintenance works of the circuit bungalow had been carried out in the years 2017 and 2018 and roof renovation had not been done at that time. Even though it has been mentioned in the last few years in the Annual Estimate regarding the renovation of the quarters, the renovation works have not been carried out in the quarters considering the financial condition of the Company. Accordingly, as the financial status of the Company is good in the year 2022/2023 actions will be taken to complete the repair and maintenance works in the year 2022/23 by following the procurement process.
- Steps should be taken to protect the assets by systematically carrying out maintenance and repairs

3.2 Operational Inefficiencies

Audit Observation

The Decision of Cabinet of Minister No. CP/19/0743/117/024 dated 19 March 2019 had informed that by handing over the production of Hiniduma Hills and Menikdiwela tea factories, where the Tea Shakti Fund was established, the company should carry out all the necessary activities to run these two factories profitably without burdening to the General Treasury. After handing over these factories to the Company in the year 2015, there was a continuous unprofitable situation up to the year under review and although the annual loss of the two factories has decreased by 06 per cent in the year under review as compared to the previous year, the accumulated loss at the end of the year under review had been Rs. 131,185,760 .

Comments of the Management

A formal feasibility study has not been carried out before commencing the respective factories. Failure of receiving adequate bought leaf to this Factory to match with the production capacity, occurrence of continuous losses has affected for this. However, it has been able to attract many bought leaf suppliers from the 2022/2023 financial year through welfare programme promotion methods. A financial performance indicator has been introduced to the Factory and job targets have been given for each staff member. The allowances and other privileges of the staff are determined based on the amount of marks received for the performance of the work at the end of the year. Further, the factories have been modernized and the factories are controlled through MIS,CCTV System. Further, actions have been taken to get bought leaf of Sri Lanka State Plantation Company to Menikdiwela Factory.

Recommendation

All necessary steps should be taken by the Company to run tea factories profitably without incurring any cost to the General Treasury as per the Decision of Cabinet of Ministers.

3.3 Idle or Underutilized Property, Plant and Equipment

Audit Observation

Although about 21,050 tea bushes according to the total area of the tea field can be grown in the tea field of Kalubowitiyana Tea Factory, it is observed that there are less than 13,100 tea plants in the tea plantation area of the factory and the expected yield of fresh leaves was less than 35 per cent due to the lifespan of the tea plants in that field was about 17 years old. It was observed that the maintenance works had also not been done in the field of tea.

Comments of the Management

The tea field of Kalubowitiyana Tea Factory is now more than 17 years old and more than 06 cycles of pruning have been done so far. Accordingly, approximately 5 per cent die in one pruning season and due to that reason, it has not been possible to get the yield at the optimal level. Further, the lack of workers for work in the factory sector and the insufficient wages paid by the Factory have also directly affected this. Applications for replanting of tea have been forwarded through the Tea Small Holdings Development Authority and preliminary plans are being carried out for replanting activities.

Recommendation

Replanting should be done in time and attention should be drawn on alternative methods instead of using labour.