

Co-operative Surplus Fund - 2022

1. Financial Statements

1.1 Disclaimer of Opinion

The audit of the financial statements of the Co-operative Surplus Fund for the year ended 31 December 2022 comprising the statement of financial position as at 31 December 2022, and the statement of financial performance, 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 reported to Parliament, appear in this report.

I do not express an opinion on the financial statements of the Fund. Because of the significance of the matters described in paragraph 1.5 of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

1.2 Basis for Disclaimer of Opinion

I expressed disclaimer of opinion on the matters described in paragraph 1.5 of this report.

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 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 Fund'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 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 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 misstatements, 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 scepticism throughout the audit. I also;

- Identify and assess the risks of material misstatement in 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 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 whenever 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 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 Internal Control over the preparation of Financial Statements

The Fund is required to “devise and maintain” a system of internal accounting controls sufficient to provide reasonable assurance that, transactions are executed in accordance with management’s general or specific authorization, transactions are recorded as necessary to permit preparation of financial statements in conformity with the applicable reporting standards, and to maintain accountability for assets, access to assets is permitted only in accordance with management’s general or specific authorization, and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

1.5.2 Accounting Deficiencies

	Audit Observation	Comment of the Management	Recommendation
(a)	Although an amount of Rs. 32,740,634 had been stated as the active loan interest income according to the financial statements, the total of interest income was Rs.33,140,634 in the schedule. Accordingly, a difference of Rs. 400,000 was observed in the interest income and the receivable interest income.	Action will be taken to correct this matter in the current year.	Action should be taken to account for the correct value by carrying out reconciliations.
(b)	As the fixed deposit interest income relating to the year under review had been overstated by Rs.391,781, the income of the year and the receivable interest income had been overstated by that amount.	This situation has arisen due to misstatement of the number of days related to the current year in the calculation of fixed deposit interests. It has been noted down to correct that error in the calculation of interest in the year 2023.	Action should be taken to account for the correct value.

1.5.3 Suspense Account

Item	Amount Rs.	Period of suspense	Comment of the Management	Recommendation
Suspense Account	9,475,735	More than 10 years	The task of settling has been delayed due to difficulties in finding out information.	Action should be taken to identify the balance of the suspense account and settle it.

1.5.4 Lack of Documentary Evidence for Audit

Item	Amount Rs.	Audit evidence not submitted	Comment of the Management	Recommendation
(i) Receivable Co-operative society loans.	590,687,825	Balance confirmations	The relevant societies have been informed to submit balance confirmations as at 31 December 2022	Action should be taken to obtain balance confirmations.
(ii) Receivables from the Co-operative Fund	5,029,486	Balance confirmations	Action will be taken to obtain and submit balance confirmations in the future.	-Do-
(iii) Receivable Treasury Sub Loans	81,871,370	Balance confirmations	-Do-	-Do-
(iv) Payable Treasury Fund	150,000	Detailed Schedule	There are issues in the submission of detailed schedules.	Confirmations that substantiate the balance should be furnished.
(v) Payable National Trustee Fund	3,871,256	Detailed schedules	-Do-	-Do-
(vi) General Deposit Account	7,400,772	Detailed schedules	There are issues in the submission of detailed schedules.	Action should be taken to submit detailed schedules.
(vii) Fixed deposit security creditors	58,918,112	Loan files and balance confirmations	There are issues in the submission of detailed schedules.	Confirmations related to substantiate the balance should be furnished.
(viii) Winding up Accounts (Debit balance)	2,620,473	Copies of the Winding up Account prepared.	As this balance has been carried forward since a period prior to 1990, there are issues in ascertaining the information.	Confirmations related to the balances mentioned in the financial statements should be furnished.

1.6 Accounts Receivable and Payable

1.6.1 Receivables

Audit Observation	Comment of the Management	Recommendation
(a) According to the non-performing loan schedule, out of the loan amounting to Rs. 129,131,173 granted to 69 co-operative societies during the period from 1989 to 2006, a sum of Rs. 89,208,070 remained recoverable as at 01 January 2022 and Rs. 198,991 only had been received as the loan instalments of the year under review. Out of the loan interest of Rs. 102,110,771 as at 31 December 2022, a sum of Rs. 13,674 only had been received.	The loan stated in the non-performing loan register is a very old loan provided by Co-operative Surplus Fund and an arrangement has been made at present to recover this loan.	Action should be taken to recover the loan instalments properly.
(b) Action had not been taken to settle the dishonoured cheques worth Rs. 1,721,566 which had been carried forward since the year 1999 under the miscellaneous assets.	This is a balance that continued to exist over a long period. The officers were instructed to take expeditious action to settle this balance.	Action should be taken to settle the balance of dishonoured cheques
(c) Out of the active loan balance of Rs. 507,312,785 that remained receivable as at 01 January of the year under review, a sum of Rs. 24,962,961 only had been received during the year under review. Although a loan interest of Rs. 216,582,478 was receivable on this loan balance as at 01 January 2022, a sum of Rs. 9,814,450 only had been received during the year under review. No action had been taken to recover any amount from the loan of Rs. 125,271,190 that had been given to co-operative societies and associations before 07 years and included in the above loan balance, even by the end of the year under review.	Most of the loans included in the active loan register are the loans provided before 2018. The sum of Rs. existed 507,312,785 as at 01.01.2022 included the loan instalments to be recovered in the ensuing years. Legal actions are being taken according to the advice of the Attorney General in order to recover the loan granted before 2018. Various measures are currently being taken to recover the other loans and letters have been referred to the relevant Provincial Co-operative Commissioners	Action should be taken to recover the loan.

- (d) Out of the loan amounting to Rs. 75,000,000 granted to the Buildings Materials Corporation on 08 May 2013, a sum of Rs. 62,091,372 remained recoverable as at 31 December 2022 and the relevant interest to be recovered was Rs. 75,500,840. Although a period of 10 years had elapsed, the loan amount and the interest totalled Rs. 137,592,212 had not been recovered even by 31 December 2022.
- Information is reported to the effect that the relevant Cabinet paper for the recovery of that amount from the Building Materials Department has been prepared by the State Ministry and referred to the Cabinet Ministry on 28.03.2022.
- Action should be taken to proceed with follow up actions and recover the loan.

1.6.2 Payables

Audit Observation	Comment of the Management	Recommendation
(a) The balance of Rs. 6,017,551 that remained payable to the surplus fund and stated under the miscellaneous liabilities in the statement of financial position had not been settled from the year 2009.	The task of settling has been delayed due to difficulties in finding out information. However, officers have been instructed to take measures to settle these balances expeditiously.	Action should be taken to settle the payables.
(b) No action had been taken to settle the excessively recovered Rs. 196,201 continued to exist from the year 2009 under the payable liability and the transfer of account balance of Rs.100,000 continued from the year 2018.	The task of settling has been delayed due to difficulties in finding out information. However, officers have been instructed to take measures to settle these balances expeditiously.	Action should be taken to settle the payables.

2. Financial Review

2.1 Financial Result

The operating results for the year under review was a surplus of Rs. 230,070,179 as compared with the corresponding surplus of Rs. 105,727,365 for the preceding year. Accordingly, an improvement of Rs. 124,342,814 was observed in the financial results. This improvement was mainly due to increase in the interest income by Rs. 152,039,040.

3. Operating Review

3.1 Management Inefficiencies

Audit Observation	Comment of the Management	Recommendation
(a) As the management did not take action to recover the annual loan interests and instalments relating to the loans granted from the Co-operative Surplus Fund during the years 2010,2012 and 2013	After restructuring the loans and writhing off of the interests, interests and loan instalments will be duly paid in the future.	Action should be taken to recover the loans in accordance with the agreements.

according to the agreements, an interest of Rs. 48,664,475 had been written off from the profit during the year under review.

- (b) Although there are provisions in that Act to provide loans only to the co-operative societies, contrary to that, an interest free loan of Rs. 13,969,497 had been granted to the Co-operative Wholesale Establishment in 05 April 2012. Although the respective institutions have been notified in this connection, no favourable response has been received thus far. Action should be taken to grant loans in accordance with the provisions of the Act.
- (c) Despite the existence of loan balance of Rs.19.5 million granted to the Sri Lanka Co-operative Sales Association in the year 2006 as non-performing balance, without being recovered the loan, a loan of Rs.7.5 million had been provided by the Co-operative Surplus Fund in the year 2022. The grant of loans without being so recovered the previous loans was questionable to the Audit. The loan granted to the Co-operative Sales Association is shown in the non-performance loan register and prior to the release of the loan in the year 2022, written notifications have been made to settle the loans due from the Co-operative Sales Association Limited. However, on 04.08.2022, that Association has informed us in writing that it has not obtained a loan of Rs. 19,500,000. If the relevant Association confirms that there is no such loan amount, relevant corrections should be made after analytically examining based on the relevant documents of the Surplus Fund as to how such loan came into being.
- (d) In order to establish a dairy super market while giving priority to increase the local milk production, an interest free loan of Rs. 15,587,000 had been granted on 06 August 2007 to construct a building and open a sales stall. The Department of Co-operative Development had signed an agreement with the Milk Producers' Cooperative Society for this purpose. The following observations are made in this connection. In terms of Section 7 of the agreement, it had been stipulated that the monthly instalment of Rs. 65,765 should be paid before 15 of every month. However, only Rs. 737,250 had been paid despite the lapse of 15 years, and it was accordingly observed that money had been paid only for 11 months. It had been stated according to Section 12 of the agreement that the ownership of the building in which the supermarket is housed will be owned by the Co-operative Development Department if the payment is not settled within the prescribed period (within 20 years). Nevertheless, action had not been taken to take over the ownership. Since the project became inactive, the association also became inactive consequently. As a result, this loan amount has not been settled. The officers of the association discussed this matter with the then honourable minister and no proper solution was given. Since the CWE possesses the ownership of the land, the ownership of the building has not been vested in the Department. Action should be taken to recover the loans in accordance with the loan agreements.

According to Section 11 of the agreement, an officer of the Co-operative Department should be appointed to specifically examine whether this loan is properly utilized, whereas it had not been so done. As a result, the General Association of the Sri Lanka Milk Producers Co-operative Society had been identified as an inactive society and its registration had been cancelled by 31 January 2023. Therefore, a sum of Rs. 14,849,750 due from this society was revealed as an unrecoverable loss.

Due to excessive involvement of the employees and the officers for the above project, it created problematic situations in maintain the stalls owned by the association. As a result, the association became inactive. The then General Manager is dead at present. Employees also have left the association. Therefore, action has been taken to cancel the registration since a number of years have elapsed from the association being inactive.

Action should be taken to ensure the adherence to the matters contained in the agreement.

- (e) The cancellation of registration of the inactive co-operative societies had been identified in the Action Plan, 2022 as a strategy to strengthen and develop the co-operative societies, which is the main objective of the Co-operative Surplus Fund. Nevertheless, guidelines on the specific procedures to be followed in winding up of co-operative societies and associations had not been introduced to carry out that work more properly.

The guidelines related to the winding up activities are scheduled to be implemented from 01.06.2023.

Guidelines should be prepared for winding up activities.