

## **Smallholder Agribusiness and Resilience Project - 2024**

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The audit of financial statements of the Smallholder Agribusiness and Resilience Project for the year ended 31 December 2024 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 9.03 of the Loan Agreement No. 2000003227 and Grant No. 2000003226 dated 10 June 2021 entered into between the Democratic Socialist Republic of Sri Lanka and the International Fund for Agriculture Development (IFAD). My comments and observations which I consider should be reported to Parliament appear in this report.

### **1.2 Implementation, Objectives, Funding and Duration of the Project**

According to the Loan Agreement, the Ministry of Agriculture is the Executing Agency and the Project Management Unit established for SARP is the Implementing Agency of the Project.

The objectives of the Project are to build resilience and market participation of 40,000 rural smallholder households in the project area. The activities of the Project are implemented under three components namely Capacity Building for Climate Resilience and Inclusive value chains, Investment for Climate Resilience and Inclusive value chains and Project management and coordination.

As per the Loan Agreement, the estimated total cost of the Project was US\$ 81.98 million equivalent to Rs 14,756.40 million and out of that US\$ 42.76 million equivalent to Rs 7,697.88 million was agreed to be financed by International Fund for Agriculture Development. The balance amount of US\$ 12.60 million equivalent to Rs. 2,268 million is expected to be financed by the Government of Sri Lanka.

The Project had commenced its activities on 10 June 2021 and scheduled to be completed by 10 June 2027.

### **1.3 Qualified Opinion**

In my opinion, except for the effects of the matters described in the 2.1 section of my report, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2024, statement of expenditure and its cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

### **1.4 Basis for Qualified Opinion**

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 opinion.

## **1.5 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.

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

## **1.6 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 scepticism 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 internal control of the Project.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- 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.

I communicate with those charged with governance regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

## 2. Comments on Financial Statements

### 2.1 Accounting Deficiencies

Accounting Audit Issue	Deficiency / Amount Rs. Mn	Response of the Management	Auditor's Recommendations
As per the Section 43(a) of Sri Lanka Public Sector Accounting Standard 05, assets and liabilities for each statement of financial position should be translated at the closing foreign exchange rate of the date of the statement of financial position. However, the Parity adjustments amounting to Rs.114.52 Mn relating to the foreign loan of the project had not been accounted for the year under review as per above requirement.	114.52	In line with guidance in State Accounts Guideline No. 03/2024 dated 22.02.2024, parity adjustments were not included in the project's financial statements for the year 2024.	Adhere to the Sri Lanka Public Sector Accounting Standards.

### 2.2 Non Compliance with Laws, Rules and Regulations

Reference to the Laws Rules and Regulations	Non Compliance/Audit Issue	Response of the Management	Auditor's Recommendations
Circular No CGIR/2019/03-1(Ins. & Cir) dated 09 July 2019 and Circular No CGIR/2021/02-02 dated 09 April 2021 issued by the Department of Inland Revenue	All government entities should send to the Department of Inland Revenue the details regarding to VAT payments to supplier before 15th of next month after quarter. But Project had not prepared and sent the details to Department of Inland Revenue from the beginning of the project.	The necessary steps have been taken by the project to ensure that outstanding VAT payment information is submitted to the Department of Inland Revenue, in accordance with the relevant circular and the guidance provided by the authorities.	Necessary actions should be taken to send relevant VAT details to Department of Inland Revenue.

### 3. Physical Performance

#### 3.1 Physical and Financial Progress of the Activities of the Project

Component	As at 31 December 2024	Delay/ Audit Issue	Reasons for delays	Response of the Management	Auditor's Recommendations
	Expected physical performance Percentage	Performance achieved percentage			
Overall Physical performance	40.19	15	Raising uncertainty about the project's ability to meet its objectives within the remaining implementation period.	Delay to commence in commencement of the project	Comments have not been received. The activities of the project should be completed within planned time frame.

#### 3.2 Underutilized Resources

	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	When considering the progress of utilization of funds as at 31 December 2024, it was observed that the project utilized only USD 1.85 Mn funds from USD 41.74 Mn of total allocation by the IFAD Loan. As a percentage, it was 4.4 per cent. Therefore, the utilization of funds is ineffective when considering the rest of two and half year time period with balance funds.	Since the inception of the project, several challenges have contributed to its slow physical progress. These include delays in obtaining approval for key staff recruitments, unfilled positions within the project cadre, a high rate of staff turnover, and changes in project activities.	Tasks of the project should be completed planned time frame and funds should be utilized efficiently.
(b)	Total agreed contribution of government of Sri Lanka for SARP is USD 12.60Mn, the cumulative use of government	GOSL funding has been utilized primarily for tax-related payments directly linked to IFAD-financed activities,	Tasks of the project should be completed planned time frame and funds should be utilized

fund as at the year under review is only USD 0.21Mn and it is equivalent to 1.66 percent of agreed amount. This project is to be ended on 10 June 2027 and use of remaining 98 percent of agreed government fund in next two and half years is uncertain. particularly those related to tank rehabilitation and other eligible expenditures. The lower physical progress of the project has also resulted in a lower-than-expected utilization of GOSL financing. efficiently.

- (c) It was observed that the project has utilized only Rs.404.67 Mn from allocation for the reimbursable foreign loan of Rs.891.02 Mn for the year under review. Therefore, allocation of Rs.486.35 Mn representing 54.6 percent of the total allocation had not been utilized by the project. Agreed. The limited physical progress of the project was a key factor contributing to this underperformance, which also resulted in lower-than-expected utilization of GOSL financing. Tasks of the project should be completed planned timeframe and funds should be utilized efficiently.

### 3.3 Matters in Contentious Nature

Audit Issue	Response of the Management	Auditor's Recommendation
The project was originally planned to commence in the year 2020, with a total implementation period of six years. However, the formal financial agreement necessary for the project's execution was not signed until 10 June 2021, resulting in an initial delay in mobilization. Despite of the signing of the financial agreement in mid of 2021, it was noted that the project's financial and operational activities did not begin until August 2022 over a year later. This delay in commencement effectively reduced the available timeframe for implementation within the originally intended six-year period.	Comments have not been received.	Tasks of the project should be completed within the predetermined time frame.

### 3.4 Issues Related to Human Resources Management

Cadre Position	No of Posts		No. of vacancies	Response of the Management	Auditor's Recommendation
	Approved	Actual As at 31 December 2024			
Agriculture Specialist position	06	00	06	At present, a revised cadre proposal has been submitted, and once approved, the currently unfilled positions will be filled accordingly.	Necessary Vacant cadre positions should be filled without delay.
Area Coordinator position	03	02	01		
Office Assistant position	02	00	02		

### 3.5 System and Controls

Audit Issue	Response of the Management	Auditor's Recommendation
A Purchase Order (PO) was issued to Soft Vision Technologies (Pvt) Ltd on 10 October 2022 for the installation of the Busy Accounting System, valued at Rs.1,470,000. As per the terms and conditions of the PO, all installation activities were to be completed within 26 days from the date of issuance. As at 16 February 2023, Rs.1,102,500 which 75 percent of the total contract amount had been paid for the establishment of the accounting system. Although the installation process was reported as completed, it was observed that essential components such as the preparation of system specifications, IFR, Justification Reports and financial statement preparation had not been included in the delivered solution. This indicates non-compliance with the agreed deliverables and raises concerns regarding the adequacy and completeness of the system implementation.	To date, only 75 percent of the total contract value has been paid, with the remaining 25 percent withheld due to the supplier's failure to fully deliver the agreed-upon components. However, the project has since engaged in negotiations with the supplier, and necessary improvements are currently being made to the system. It is expected that all contractual deliverables will be fulfilled.	All requirements regarding to accounting system should be completed and used it without delay.