

Paddy Marketing Board-2011

1. Financial Statements

1.1 Disclaimer of Opinion

Because of the significance of the matters described in paragraph 1.2.5 of this report, I have not been able to obtain sufficient appropriate evidence to provide a basis for an audit opinion. Accordingly I do not express an opinion on these financial statements.

1.2 Comments on Financial Statements

1.2.1 Going Concern of the Institution

The Board had sold the stocks of paddy purchased in most instances at lower prices and as such had continued the methodology of obtaining loans from the Treasury and the Banks to finance the purchase of paddy from the ensuing season as well as for the settlement of losses arising from sales. In view of this situation, the going concern of the Board is observed as uncertain.

1.2.2 Non-compliance with Sri Lanka Accounting Standards

The following Accounting Standards had not been complied with

- (a) Even though in terms of Sri Lanka Accounting Standard 5 the stocks of paddy should be brought to account at the lesser value of the cost or the net realizable value, the stock had been valued and brought to account at Rs.4,555,081,250 based on the reports obtained at the year end from the Regional Managers.
- (b) Provision for gratuity had not been made in terms of Sri Lanka Accounting Standard 16.
- (c) Even though the lands and buildings should be separately identified and brought to account in terms of Sri Lanka Accounting Standard 18, land and buildings costing Rs.13,710,714 had been brought to account as one balance. That cost had been depreciated at 2.5 per cent per year.

1.2.3 Accounting Deficiencies

The following observations are made.

- (a) The totals of balances of assets and liabilities that existed before the year 2008 amounting to Rs.277,911,624 and Rs.166,994,520 respectively had been retained in a Suspense Account without being identified while the assets valued at Rs.1,135,701 and liabilities valued at Rs.26,239,640 arisen from the transactions in the years since the year 2009 had also been retained in that Suspense Account.
- (b) Out of the sums of Rs.346,190,000 and Rs.110,000,000 received from the Treasury for the payment of interest on loans and paddy milling and transport charges respectively, sums of Rs.307,263,861 and Rs.91,321,775 respectively had been settled and the balances totalling Rs.57,604,384 had been brought to account as income of the year under review.
- (c) As a result of the erroneous computation of the cost of sales of rice in the Income Statement, the cost of sales had been overstated by a sum of Rs.601,547,073. As such the profit for the year had been understated by that amount.
- (d) In accordance with the decision of the Cost of Living and Food Security Committee and on the instructions of the Secretary to the Line Ministry, rice valued at Rs.1,281,892,217 belonging to the Board had been handed over for storage in the stores of the Department of Food Commissioner. That entire stock of rice had been erroneously brought to account as sales in the year under review. Nevertheless, a stock of rice valued at Rs.611,986,069 out of that stock, remained in the stores without being sold even by 31 December 2011.
- (e) The sum of Rs.182,900,000 received from the Treasury for capital expenditure had been brought to account in the Income Statement as other income and as such the profit for the year had been overstated by a similar amount.
- (f) Lease rent on stores recoverable as at the end of the year under review amounting to Rs.3,697,500 had been omitted in the accounts.
- (g) A sum of Rs.71,076,719 paid for 08 construction works done in the year under review had been shown as advances in the year under review instead of being brought to account under the work-in-progress or the lands and buildings.
- (h) Adequate provision for bad and doubtful debts had not been made for the debtors balances brought forward over a long period.

1.2.4 Accounts Receivables

The following observations are made.

- (a) Out of the sum of Rs.1,086,844,771 receivable from 08 Government Institutions, including a sum of Rs.10,591,838 receivable since the year 2009, the Board had recovered only a sum of Rs.579,247,996 even by 24 September 2013. As such action had not been taken for the recovery of a sum of Rs.507,596,775.
- (b) The Board had not taken action up to 30 September 2013 for the recovery of the advances recoverable from 06 institutions amounting to Rs.150,676,283 including a sum of Rs.20,795,578 receivable since the year 2010.

1.2.5 Lack of Evidence for Audit

The following items of accounts could not be satisfactorily vouched or verified in audit due to the non-submission of the evidence indicated against each item.

Item of Account -----	Value ----- Rs.	Evidence not made available -----
Fixed Assets	13,710,714	Registers of Fixed Assets and Title Deeds
Paddy, Soya Beans, Rice and Stocks in Transit	4,555,191,889	Stock Books, Stock Verification Reports and Confirmation of Balances for stock in transit
Rice, Paddy and Soya Beans Sales Debtors	1,086,844,771	Registers of Debtors, Age Analysis and Confirmation of Balances
Bank Loans and Treasury Advances	5,487,454,030	Age Analyses and Confirmation of Balances
Bank Overdraft	247,131,449	Particulars of Approval obtained, Confirmation of Balances and Age Analyses
Investments	283,044,402	Investment Certificates and Age Analysis
Income from Interest on Investments	14,549,943	Computation of Interest on Investments.

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

Non-compliances observed are given below.

Reference to Laws, Rules, Regulations and Management Decisions	Non-compliance
(a) Section 13(5)(d) of the Finance Act, No.38 of 1971	Even though a minimum internal audit programme should be prepared and implemented in concurrence with the Auditor General, the Board had not taken action accordingly.
(b) <u>Financial Regulations of the Democratic Socialist Republic of Sri Lanka</u>	
(i) Financial Regulations 135-139	The Board had not carried out assignment of duties and the delegation of authorities for financial control.
(ii) Financial Regulation 188(2)	Even though the Chairman informed the audit that legal action had been taken in connection with seven cheques valued at Rs.12,140,745 deposited in the Banks during the year under review had not realized even by August 2012, those cheques had not been settled even by 30 September 2013.
(c) Decision of the Cabinet of Ministers No.07/1199/315/031 dated 25 July 2007	Even though the Sri Lanka Agricultural Products Marketing Authority should have been liquidated and the Board re-established on 25 July 2007 should have taken over all the assets and liabilities of the Authority, the Board had taken over only the assets such as fixed deposits, savings deposits, cash in hand and staff advances amounting to Rs.184,658,970. Action had not been taken even up to 31 December of the year under review for the takeover of the other assets and liabilities and for liquidating the Authority.
(d) Paragraph 6.5.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003	The Draft Annual Report had not been presented with the Financial Statements.

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| (e) Treasury Circular
No.1A1/2002/02 of 28 November
2002 and Financial Regulation
756 | Fixed assets value at Rs.13,710,714 had not been surveyed over a period exceeding 06 years. |
| (e) Decision of the Cabinet of
Ministers
No.CM/10/2762/447/013 dated
16 December 2010 | Even though action should be taken for the settlement of the advances amounting to Rs.2,000 million granted by the Treasury, from the money collected from the sale of rice, action had not been taken for the settlement of those advances from the sum of Rs.708,232,048 collected from the sale of rice in the year under review. |
| (g) Chapter VI of the Establishments
Code | The personal files of 04 officers recruited had been incompleated and the medical reports, approvals of salary increments, reports on work and conduct, etc. had not been included therein. |
| (h) Declaration of Assets and
Liabilities Act, No.74 of 1988 | The above mentioned 04 officers had not submitted the Declarations of Assets and Liabilities |

2. Financial Review

2.1 Financial Results

According to the financial statements presented, the operation of the Board for the year under review had resulted in an operating profit of Rs.264,125,792 as against the operating loss of Rs.346,747,035 for the preceding year, thus indicating an improvement of Rs.610,872,827 in financial results. Had the overstatements of the profit amounting to Rs.247 million as shown in (b) to (f) of paragraph 2.2.3 of this report been adjusted, the profit of Rs.264 million for the year under review would be reduced to a profit of Rs.17 million.

2.2 Abnormal increase in Expenditure

The total financial cost incurred by the Board on loans amounting to Rs.329,644,154 in the year 2011 represented 52 per cent of the total income for the year amounting to Rs.631,978,105. However, the income for the year 2011 included the grants amounting to Rs.554,090,000 received from the Treasury. If that amount is eliminated and compared with the net operating income of Rs.77,888,105, the total financial cost would amount to 423 per cent of the total income.

3. Operating Review

The following observations are made.

- (a) According to the information furnished, targets had been set for the purchase of 400,000 metric tons of paddy at a cost of Rs.11,955 million while only 80,144 metric tons of paddy had been purchased at a cost of Rs.2,278 million and that represented 20 per cent of the target. Purchase of paddy as compared with the preceding year indicated a deterioration of 47 per cent.
- (b) Out of the paddy purchased in the Yala and Maha Seasons of the year 2011, the Board had purchased nadu paddy representing 78 per cent and 84 per cent respectively. The Board had not taken action for the purchase of Samba paddy which commands a very high consumption locally. The percentages of the varieties of paddy purchased by the Board are given below.

Season	Samba	Nadu	Total Purchased	Percentage of Purchase out of the total Purchased	
				Samba	Nadu
	Metric Tons	Metric Tons	Metric Tons	%	%
Yala	16,516.9	60,103.9	76,620.8	22	78
Maha	556.6	2,967.4	3,524.0	16	84

- (c) According to Paddy Purchase Programme, the targeted plan of the Government is to purchase a minimum of 5 per cent to 10 per cent of the overall paddy production by the Board direct from the farmers. But the Board had failed to reach that target. According to the information furnished, the purchases of paddy from the total production, except in the case of Yala Season 2011, had been at a level, below 5 per cent. Details appear below.

	2009/2010	2010	2010/2011	2011	Total
	Maha	Yala	Maha	Yala	
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	Metric Tons	Metric Tons	Metric Tons	Metric Tons	Metric Tons
Total Production	2,630,000	1,671,000	1,996,000	1,879,000	8,176,000
Purchase of Paddy by the Board	73,192	115,714	3,524	76,621	269,051
Paddy Purchased by the Board as a Percentage of the Total Production	2.8	6.9	0.2	4.1	3.3

- (d) According to the Standard practice of the Board, old stocks of paddy should be issued first for the production of rice. Nevertheless, there were instances of the issue of new stocks of paddy despite the availability of old stocks in the stores. The following observations are made in this connection.

- (i) Contrary to the above Standard, 3,032,005 kilogrammes of new paddy stocks valued at Rs.85,048,150 had been issued disregarding the availability of 2,626,113 kilogrammes of old stocks of paddy valued at Rs.73,548,914 in the stores.
- (ii) In view of the retention of old stocks of paddy in the stores without being issued, the Board had to incur additional costs for maintenance resulting from discolouration, damage by insects, outdating of stocks, spoilage, destruction of stocks and mixing with dirt.

3.2 Management Inefficiencies

The following observations are made.

- (a) A loss of Rs.369.49 million had been incurred due to the sale of rice belonging to the Board stored in the stores of the Department of Food Commissioner at lower prices to 04 private companies. The Chairman of the Board informed the audit that the Board did not sell the rice but it had been done by the Food Commissioner on the approval of the Secretary to the Line Ministry.

- (b) According to Sections 3 and 10 of the Paddy Marketing Board Act, No.14 of 1971, registration of private rice mills should be done for the maintenance of a business for the milling of paddy and rice, polishing and processing. But the Board had not taken action accordingly. Nevertheless, paddy valued at Rs.1,340,648,888 had been issued in the year to the millers selected improperly. Out of that, rice relating to stocks of paddy valued at Rs.67,706,816 had not been received by the Board even up to the end of the year under review. This stock of paddy had been shown as stocks in transit in the financial statements.

3.3 Transactions of Contentious Nature

The following observations are made.

- (a) Legal action had not been taken in the year under review to secure the title to the stores, buildings utilized by the Board and the 142 premises relating to those stores and for the securing the clear title to the 44 buildings which are being utilized without authority by external parties.

- (b) Even though the Board had paid a sum of Rs.3,255,329 in the year under review to an insurance company for insuring stocks of paddy, the Board that failed to obtain compensation for the losses and damage caused to stocks of paddy due to the failure in storing paddy in accordance with the instructions and standards specified by the insurance company.

3.4 Irregular Transactions

The following observations are made.

- (a) Even though the lease agreements of 07 stores buildings out of the 19 stores buildings of the Board leased out on lease agreements had expired, action had not been taken either to renew the leases or to recover the possession of the properties. As a result the lessees had been utilizing the buildings even up to 30 September 2013 without making payment.
- (b) The lease rent of 16 buildings out the 19 buildings had been outstanding even by the end of the year under review and the outstanding lease rent amounted to Rs.5,173,950. Out of that a sum of Rs.3,641,250 had been outstanding for periods ranging from 02 years to 05 years. Adequate steps for the recovery of the outstanding lease rent had not been taken even up to 14 October 2013.
- (c) The lease rent of 04 stores buildings for the year 2011 only had been recovered without recovering the old outstanding lease rents totalling Rs.3,036,400.
- (d) A private company had spent a sum of Rs.6,314,659 to modernize a building without the prior approval of the Board and the company had been allowed to set off a sum of Rs.30,000 monthly from the lease rent. As such the total lease rent deprived of to the Board amounted to Rs.360,000.

3.5 Apparent Irregularities

The following irregularities were observed in relation to the stocks of paddy issued by the Board to the millers.

- (a) Even though the Board should obtain an unconditional Bank Guarantee valid for 90 days from an accepted Bank in accordance with the agreement before the issue of stocks of paddy to the millers, such guarantee had not been obtained from any of the millers. In lieu of the Bank Guarantee, the Board had obtained undated blank cheques of no value and had issued stocks of paddy valued at Rs.1,340,648,888. Nevertheless, the possibility of the misuse of Government money through that process cannot be ruled out in audit.

- (b) The Banks had rejected payment on cheques issued by certain millers due to various reasons. No legal action whatsoever had been taken against those millers even by 14 October 2013. According to a test check, the value of the cheques on which the payment had been rejected amounted to Rs.3,742,220.
- (c) Opportunities had been provided for committing different types of frauds and irregularities due to reasons such as the failure to take follow up action by comparing the copies of Issue Orders with the Issue Advices issued by the stores for the issue of paddy, non-maintenance of proper records, irregular selection of millers and the non-introduction of proper control methodologies.

3.6 Uneconomic Transactions

The following observations are made.

- (a) The Savings Account opened in the year 2008 for depositing the money collected from the sale of paddy by the Sri Lanka Agricultural Products Marketing Authority had been transferred to the Board with effect from 26 April 2010 and the balance as at that date amounted to Rs.5,338,284. That money had not been effectively invested since that date up to 30 September 2013.
- (b) A sum of Rs.127,000 invested by the Board in the shares of the Associated Newspapers of Ceylon Ltd. had been credited as at 31 December 2011 to a Suspense Account. Action had not been taken to obtain as return on that investment.

3.7 Identified Losses

The following observations are made.

- (a) The Board had spent a sum of Rs.22,380,293 as interest on Bank overdrafts and a sum of Rs.307,263,860 as interest on Bank Loans during the year under review due to the non-settlement of Bank overdrafts and the Bank loan balances.
- (b) The Board had not taken action to conduct annual survey of stocks of paddy by adducing the high costs as the reason. The computation of stock shortages after the issue of entire stocks of paddy purchased had been the procedure adopted by the Board. Nevertheless, the stocks of paddy purchased from the Maha Season 2009/2010 after reactivating the paddy purchase operations had been fully issued by certain stores even

by 15 June 2012 and the shortages of stocks of paddy of that season could be ascertained in audit. As such the shortages of stocks of paddy amounting to 296,876 kilogrammes valued at Rs.8,312,528 was detected at the inspection of 12 stores in the Anuradhapura Zone. Accordingly, the possibility of such shortages in the other 130 stores cannot be ruled out in audit.

3.8 Non-implementation of Directives of the Committee on Public Enterprises

The following observations are made on the non-implementation of Directives of the Committee on Public Enterprises.

- (a) According to the Directive Nos. 06 and 15 made by the Committee on Public Enterprises at the meeting held on 05 December 2012, a Chief Internal Auditor should be appointed and until then, the audit should be done by the Internal Audit Division of the Line Ministry. But none of the Internal Audit Reports had been furnished to audit even up to 30 September 2013.
- (b) According to Directive No.14, a committee should have been appointed to identify the unidentifiable and the recoverable debtors' balances existing from the period prior to the year 2008 and a new balance sheet should have been prepared after writing off those on the recommendation of such committee and with proper approval, such action had not been taken.
- (c) Even though it had been expected to prepare registers for the fixed assets and other assets identified in the preparation of the future financial statements of the Board in accordance with the above directives, the Board had failed to submit the detailed schedules in respect of the items indicated in the financial statements submitted to audit. As such that requirement remains without being fulfilled.

3.9 Staff Administration

Even though the approved staff of the Board stood at 134, the accurate information on the actual staff and the vacancies as at 31 December 2011 had not been furnished to audit.

- (a) Even though 07 posts of Regional Managers in the Middle Management level had been approved, all those posts remained vacant. Even though periods exceeding 03 years had elapsed after the appointment of the Assistant Regional Managers to cover the duties of those posts, no action had been taken for filling those vacancies.

- (b) Even though the Board is utilizing about 180 stores for the storage of stocks of paddy, only 78 Assistant Regional Managers and Assistant Stores Officers had been deployed for the efficient discharge of stock control functions. Attention had not been paid for obtaining approval for new posts.
- (c) Even though an officer had been recruited on 03 May 2011 for the post of General Manager which is one of the Chief Executive posts of the Board, it had been done irregularly. Nevertheless, the recruitment had become a contentious issue as the officer had not fulfilled the educational qualifications and experience relevant to the post.

4. Accountability and Good Governance

4.1 Presentation of Financial Statements

According to Section 6.5.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003, the financial statements for each financial year should be presented for audit within 60 days after the close of the relevant financial year. Nevertheless the financial statements for the year 2011 had been presented for audit only on 13 May 2013, that is, after a delay of 15 months.

4.2 Budgetary Control

A budget showing the income and estimated cash flow statement had not been prepared in terms of Section 5.2.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003. The classification of expenditure in the budget did not agree with the classification in the financial statements. As such the variance between the estimated expenditure and actual expenditure could not be computed. As such the budget had not been made use of as an effective instrument of management control.

5. Systems and Controls

Weaknesses in systems and controls observed during the course of audit were brought to the notice of the Chairman of the Board from time to time. Special attention is needed in respect of the following areas of control.

- (a) Accounting
- (b) Financial Control
- (c) Assets Control
- (d) Stores Control
- (e) Budgetary Control
- (f) Staff
- (g) Issue of Licenses to Millers