

Smallholder Plantations Entrepreneurship Development Programme - 2013

The audit of Financial Statements of the Smallholder Plantations Entrepreneurship Development Programme for the year ended 31 December 2013 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 02(a) of Article V of the Loan Agreement No. 712-LK dated 08 May 2007 entered into between the Democratic Socialist Republic of Sri Lanka and (GOSL) and the International Fund for Agricultural Development (IFAD).

1:2 Implementation, Objectives, Funding and Duration of the Programme

According to the Loan Agreement of the Smallholder Plantations Entrepreneurship Development Programme, the Ministry of Plantation Industries is the implementing agency of the Programme. The objectives of the Programme are to strengthen the beneficiaries' institutional capacity and negotiations skills, improve the land tenure status of smallholder-tea and rubber growers, increase producers' profits through improved post-harvest handling, storage, processing and marketing of their products, develop and expand rural finance and credit services and ensure that women improve their living conditions and reduce their poverty.

As per the Loan Agreement, the estimated total cost of the Programme is US\$ 40 million and of this, US\$ 22.5 million, US\$ 3.8 million, US\$ 5.5 million, US\$ 5.2 million, US\$ 2 million and US\$ 1 million were agreed to be financed by the International Fund for Agricultural Development, Government of Sri Lanka, USAID, Wellassa Rubber Company, Participating Financial Institutions and Beneficiary Contribution respectively. The above total cost estimate of the Programme has been proposed to revise on the instructions of the External Resources Department, as USAID and Wellassa Rubber Company were not financing the Programme as well as reduction of Participating Financial Institution's contribution from US \$ 2 million to US\$ 07 million. Therefore the estimated total cost of the Programme had been reduced to US\$ 28 million. The Programme commenced its activities on 06 November 2007 and was scheduled to be completed within a period of 7 years.

1:3 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Generally Accepted Accounting Principles. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

2. Scope of Audit and Basis of Opinion

My responsibility is to express an opinion on these financial statements based on my audit. Audit opinion, comments and findings in this report are based on review of the financial statements presented to audit and substantive tests of samples of transactions. The scope and extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitations of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes the examination on a test basis of evidence supporting the amounts and disclosures in financial statements and assessment of accounting policies used and significant estimates made by the management in the preparation of financial statements as well as evaluating their overall presentation. I have obtained sufficient information and explanations which to the best of my knowledge and belief were necessary for the purpose of my audit. I therefore believe that my audit provides a reasonable basis for my opinion. The examination also included such test of systems and controls, transactions, assets, liabilities and accounting records as deemed necessary to assess the followings.

- (a) Whether the systems and controls were adequate from the point of view of internal control so as to ensure a satisfactory control over Programme Management and the reliability of books, records, etc. relating to the operations of the Programme.
- (b) Whether adequate accounting record were maintained on a continuing basis to show the expenditure of the Programme from the funds of the Government

of Sri Lanka and the Lending Agency, the progress of the Programme in financial and physical terms, the assets and liabilities arising from the operations of the Programme, the identification of the purchases made out of the Loan, etc.

- (c) Whether withdrawals under the Loan had been made in accordance with the specification laid down in the Loan Agreements;
- (d) Whether the funds, materials and equipment supplied under the Loans had been utilized for the purposes of the Programme;
- (e) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Programme;
- (f) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles;
- (g) Whether the initial deposit, withdrawals from and replenishments to the Imprest Fund Account had been truly and fairly disclosed in the books and records maintained by the Programem and the balance as at 31 December 2013 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date;
- (h) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report.
- (i) Whether financial covenants laid down in the Loan Agreements had been complied with.

3. Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, except for the effect of the adjustments arising from the matters referred to paragraph 5 of this report, I am of opinion that,

- (a) the Programme had maintained proper accounting records for the year ended 31 December 2013 and the financial statements give a true and fair view of the state

of affairs of the Programme as at 31 December 2013 in accordance with Generally Accepted Accounting Principles;

- (b) the funds provided had been utilized for the purposes for which they were provided;
- (c) the withdrawals from and replenishments to the Imprest Fund Account for the year under review 2013 had been truly and fairly disclosed in the books and records maintained by the Programme and the balance as at 31 December 2013 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date;
- (d) the statements of expenditure (SOEs) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreements;
- (e) satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (f) the financial covenants laid down in the Loan Agreements had been complied with.

4. Financial Statements

4:1 Financial Performance

According to the Financial Statements and the information made available to audit, the expenditure of the Programme for the year under review amounted to Rs.503,736,265 and the cumulative expenditure as at that date amounted to Rs.1,759,899,896 summary of the expenditure for the year under review and the preceding year and the cumulative expenditure as at 31 December is shown below.

Items of Expenditure	Expenditure for the year ended 31 December		Cumulative Expenditure as at 31 December 2013
	2013 Rs.	2012 Rs.	Rs.
Civil Works	15,382,670	66,354,327	183,221,239
Motor Vehicles			32,377,365
Equipment and Goods	3,707,482	3,031,823	19,585,215
<u>Recurrent Cost</u>			
Training and Workshops	15,047,179	10,406,602	43,456,332
Technical assistance and academic activities	1,685,778	5,853,510	16,945,227
Contract with Service Provider	8,486,292	5,359,273	20,560,787
Agricultural Outlay	68,616,617	82,346,464	336,709,110
Subsidies and adjustments grant	121,962,641	130,701,016	464,894,001
Loans for Farmers	164,796,264	57,429,736	272,536,000
Salaries and allowances	29,504,040	27,476,219	146,456,988
Operation and Maintenance	14,036,072	13,999,290	81,526,182
Beneficiary Contributions	19,312,163	21,265,461	77,747,450
Contribution of the participating credit institutions	41,199,066	14,357,434	61,884,000
Social Responsibility fund			2,000,000
Total	503,736,264	438,581,155	1,759,899,896

4:2 Imprest Fund Account

According to the financial statements and the information made available, the total replenishments, the withdrawals therefore and the balance as at 31 December 2013 are as follows.

	<u>US Dollar</u>	<u>Rs.</u>
Balance as at 01 January 2012	7,097	902,411
<u>Add</u> : Replenishments	3,720,153	480,084,531
Foreign Exchange Gain	--	1,813,495
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	3,727,250	482,800,437
Less : Withdrawals	3,157,735	408,334,713
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Balance as at 31 December 2013	569,515	74,465,724
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5. Audit Observations

5:1 Non-compliance with Laws, Rules and Regulations

Details relating to advances, part payments and cheques issued for final payments were not available in the related road construction files in terms of Financial Regulations 260 and 286. It was observed that cheques had been personally delivered to Divisional Secretariats.

5:2 Management Inefficiencies

The following observations are made.

- (a) Tea Small Holders Development Authority provides financial assistance to small estate owners under 4 stages. According to the laws and regulations of the Authority, proper activities should be carried out for payment of future financial assistance. However, without doing so, the financial assistance due for the next stage had been granted.

- (b) Newspaper advertisements had been published by spending Rs.1,095,628 to recruit persons for vacancies of certain posts. However, recruitment had not been made for the posts of Financial Assistant Rubber Specialist and Accountant at the divisional offices at Gampola and Monaragala.
- (c) Goods valued at Rs. 1,512,893 purchased under the Smallholder Plantation Entrepreneurship Development Programme during the year 2012 had not been distributed among the beneficiaries even as at 31 March 2013.

5:3 Uneconomic Transactions

The Project should have granted money due for 4 stages to the Tea Small Holder Development Authority based on the successful completion of each stage. However, financial assistance of Rs. 9,773,711 had been granted for the successive stage without supervising the previous unsuccessful stages. There was no evidence to show that the payments had been effectively made use of.

5:4 Control over Vehicles

The following observations are made.

- (a) Though it was able to utilize 2 vehicles during the month of December of the year under review according to the agreed monthly payment of hire charges, 2 vehicles had been made use of, by spending Rs. 420,260. As such, it was observed that the ability to save significant amount had been averted.
- (b) The front wheel of a vehicle had broken due to technical defects before completing 3 years from the date of purchase and a sum of Rs. 706,415 had been spent to repair this. However, the amount obtained as insurance coverage was Rs.149,327. Accordingly, the loss caused amounted to Rs. 557,087. The distance performed was 81,000 kilometres only. In this connection, the secretary had informed that certain repairs carried out were not relevant to the accident.

5:5 Budgetary Control

The following observations are made.

- (a) During the year 2013, 96% of the provision for the mid country Sub-Programme amounting to Rs.145 million had been spent. However, out of the money provided for Civil Works, Technical assistance and academic activities, Contract with Service Provider 100 per cent, 100 per cent and 64 per cent remained unspent.
- (b) Out of the Rs.348 million provided for the Monaragala Sub Programme during the year 2013, a sum of Rs.352 million representing 101 Per cent had been spent. 29.34 Per cent had been spent for Agricultural Outlay, exceeding the amount provided and 1.2 Per cent had been spent for Contract with Service Provider. Out of the sum of Rs. 149,050,000 provided for civil works, furniture and equipment, service provider contracts and salaries and wages a sum of Rs. 82,032,364 had been spent. The percentage of savings relating to those items ranged between 25 to 78 per cent.
- (c) The amount estimated for the period of programme was Rs. 2857 million. However, a sum of Rs.1254 million representing of 43% alone of the amount targeted had been spent by the end of 2012 although 3 years had exceeded since the year of commencement. The objective remained to be achieved during the 2 ensuing years by spending Rs.1603 million representing 57 %. In this connection, the Secretary had informed that the target could be achieved in future.

6. Physical Performance

The following observations are made.

- (a) A sum of Rs. 4,924,298 had been paid up to 31 December 2012 to the Department of Conservation which comes under the Smallholder Plantations Entrepreneurship Development Programme for activities such as to survey and allocate land, planting poles and administration. But, a physical verification revealed that activities such as survey and allocation of land, planting poles and payment of salaries to labourers had not been properly carried out at Kosgodamulla, Karametiya, Puranwelyaya, Polgahapitiya, Ellayaya, Kumbukmandiyayaya and Kanawegalla.

- (b) The labour charges for planting poles as at 31 December 2012 amounted to Rs. 3,463,320. A comparison of 1444 poles planted revealed that the expenditure incurred as planting a pole was Rs. 2,398. The estimated amount for planting a pole was Rs. 1,250.
- (c) The following overpayments were observed at a physical verification of 13 roads at mid country.
- (i) Three roads coming under the authoritative area of Ganga Ihala Divisional Secretariat had been renovated by using a concrete mixture of 1:2:4 without soil testing. Polythene had not been spread on the roads before concreting and as a result of not complying with the standards certain roads had broken. The status control report too had not been obtained before making payments.
 - (ii) Information such as estimated amount for each item, whether estimate had been prepared for all items paid whether the required labour contribution had been provided etc., were not in the files maintained at the project office with regard to the estimates relating to the roads renovated by the Divisional Secretariat.
 - (iii) A sum of Rs.853,117 had been overpaid with more labour charges of Rs.400,452 for less work done at the mid country office with regard to 11 roads renovated in 2011 and 2012. The total overpayment was Rs. 1,253,569.
- (d) The following matters were observed at a physical verification carried out with regard to roads constructed by Sub offices.
- (i) The Monaragala sub office of the Smallholder Plantations Entrepreneurship Development Programme had spent Rs. 39,677,670 during the year 2012, to renovate 34 roads. Twelve of these roads had been physically verified in audit was revealed that a sum of Rs. 2,342,991 had been paid for unsatisfied work and work not upto specifications.

- (ii) The maximum amount that could be paid for renovating kilometer of road is between Rs. 500,000 and Rs. 1,000,000, as per Project Appraisal Report. But, the Monaragala sub office had spent Rs. 10,844,943 in excess in the year 2012 for 17 roads. (Details in Annexure 01).
- (e) During the year under review, a sum of Rs. 1,050,000 had been spent to distribute passion fruit plants among beneficiaries through a society under the Smallholder Plantations Entrepreneurship Development Programme. A test check was carried out in this regard and it was revealed that the orange cultivation of 3 beneficiaries had been spoilt and about 50% of the orange plants of another beneficiary had died. This society had not exercised care to get the barbed wires given for the orange cultivation. As a result, the cultivation of passion fruits of other beneficiaries too had failed. Meanwhile, 35 of the 100 plants given to a beneficiary of the society had not been planted even as at the time of inspection.

In this connection, the Secretary had informed that a hundred per cent success cannot be expected in development programems of this nature and the plants that had not been planted at the time of inspection had not been planted.

- (f) The following matters were observed with regard to the extension of rubber cultivation at the Monaragala sub office.
 - (i) The Monaragala sub office had cultivated 3,827 hectares of rubber from 2008 to 2011. Of these. 23% of the cultivation representing 892 hectares had become a failure. The reason for the failure of rubber cultivation had not been sought out. The management could not furnish to audit the details such as, whether subsidy had been granted and whether spoilt plants had been given for cultivation.
 - (ii) Subsidy is granted for properly maintained cultivations and there was no necessary methods to examine those cultivations. As such, it cannot be ruled out in audit that stoppage of subsidy payable to 30% of the total cultivation representing 1154 hectares could end up in unsuccessful cultivation.
- (g) Test checks carried out with regard to animal husbandry revealed the following matters.
 - (i) Fifteen chickens for beneficiary had been given under the Poultry Management Project. Field inspection revealed that out of the chickens

given to 2 beneficiaries, 9 and 3 chickens respectively had died. It was observed in audit that these chickens had died, as a result of not preparing safe poultry cages. In this connection, the secretary had informed that the beneficiaries had been in situated to buy chickens in lieu of the deed ones, at their non expenses.

- (ii) A yoghurt sealing and filling machine had been purchased with the intention of forming a preparatory centre for value added goat milk. However, the technical evaluation committee had three phase machine instead of a single phase machine. As a result, this project could not be successfully operated even as at 2 March 2013.
- (iii) Thirty eight goats valued at Rs. 498,150 had been given to the Narangala Balungala society under the project for offering goats to beneficiaries. 24 goats had been sold even as at 22 March 2013 and 11 other goats had died. As such, the objective of offering goats to this society had not been achieved.
- (iv) A sum of Rs. 2,016,000 had been spent in 2012 to purchase 6,600 chickens. A test check carried out in audit revealed that many of the birds given to the beneficiaries had died and more male chickens, than the female chickens, had been given to beneficiaries and as such the objective of this project had not been properly achieved.