

State Timber Corporation -2011

1. Financial statements

1:1 Qualified Opinion

In my opinion, except for the effects of the matters described in paragraph 1:2 of this report, the financial statements give a true and fair view of the financial position of the State Timber Corporation as at 31 December 2011 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1:2 Comments on Financial Statements

1:2:1 Sri Lanka Accounting Standards

According to the provisions of the Sri Lanka Accounting Standard No. 21, the net difference of the foreign exchange difference in the Non-resident Foreign Currency Account amounting to Rs.492,868 should be shown separately in the Income Statement. Instead, it had been shown under the other income in the Income Statement.

1:2:2 Accounting Policies

The total expenditure of Rs. 27,362,375 of the Mechanical Workshop which supplies services to all the Divisions of the Corporation had been shown as cost of sales instead of allocating among the respective Divisions which obtained the services.

1:2:3 Accounting Deficiencies

The following observations are made.

- (a) The opening and the closing stock of raw material and stock of finished goods of the Furniture Division had not been shown separately and as such the cost of production of the furniture produced could not be separately identified.
- (b) The Economic Service Charge paid for October to December 2010 had been considered as the Economic Service Charge for the year 2011 in

accounting for Economic Service Charges Tax and the non-disclosure of the Economic Service Charge amounting to Rs.8,110,676 for October to December 2011 as a payable for the year 2011 in the accounts had resulted in the understatement of the Economic Service Charge by a sum of Rs.178,846.

- (c) The sum of Rs.205,594 received from the disposal of motor cycles in the year under review had been credited to the Sundry Income Account instead of being credited to the Assets Disposal Account.
- (d) Fines amounting to Rs.286,934 recovered from the officers of the Corporation had been shown in the accounts as an amount payable.
- (e) The advances amounting to Rs.17,724,680 received from external institutions in the year under review had been shown as a deduction from the debtors balance and as such the current assets and current liabilities had been understated by that amount.

1:2:4 Accounts Receivable and Payable

The following observations are made.

(a) Debtors

- (i) Even though the Chairman had informed that action will be taken to obtain the Treasury approval for the write off of the sum of Rs.11,873,865 remaining receivable from a private company from the year 1983, that approval had not been received up to the end of the year under review.
- (ii) The debtors balance older than 05 years relating to the year under review amounted to Rs.13,871,024.
- (iii) The advances paid to external institutions in the years 2008, 2009 and 2010 amounting to Rs.705,458, Rs.77,138 and Rs.15,895 respectively had not been settled even p to 31 December 2011.

(b) Creditors

Action had not been taken either to settle or write back to income creditors balances amounting to Rs.107,750 old between 02 to 05 years shown under the refundable tender deposits.

1:2:5 Lack of Evidence for Audit

The schedules relating to the balance of Rs.12,832,130 in the Work-in-progress Account had not been furnished to audit and that balance could not be satisfactorily vouched.

1:2:6 Non-compliance with Laws, Rules, Regulations and Management Decisions

The following instances of non compliance were observed.

Reference to Laws, Rules, Regulations etc.	Non-compliance
(a) Financial Act, No. 38 of 1971 Section 8(2)	Even though the approval of the appropriate Minister given with the concurrence of the Minister of Finance and the Minister of Planning should be obtained for capital expenditure exceeding Rs. 500,000, an agreement had been entered into with a private company for the construction of a two storeyed steel building valued at Rs. 12,724,917 at the Kaldemulla Complex, without obtaining such approval.
(b) Public Enterprises Circular No.PED/12 of 02 June 2003 Section 4.2.5	Even though the following statements should be reviewed monthly by the Board of Directors for the efficient management of the working capital, it had not been so done. (a) Debtors and Creditors Age Analysis (b) Age Analysis of Stocks (c) Statement of old, obsolete and slow moving stocks and other items.

1:2:7 Irregular Transactions

The General Manager had entered into an agreement with the supplier on the bid of Rs.570,914 on 21 June 2011 for the printing of the Annual Report for the year 2009 before the grant of the approval by the Procurement Committee. The approval of the Procurement Committee had been received only on 23 June 2011.

2. Financial Review

2:1 Financial Results

The operating result of the Corporation for the year under review before income tax amounted to a net profit of Rs.603,498,864 as compared with the pre-tax net profit of Rs.877,623,257 for the preceding year, thus indicating a decrease of Rs.274,124,393 in the net profit. A profit of Rs.444,444,459 had been earned from the preliminary operations of the Corporation and that as compared with the preliminary operating result of Rs.615,230,379 for a preceding year indicated a decrease of Rs.170,785,920. The major reason for the decrease in the profit had been the decrease of the sales for the year by a sum of Rs.440,312,420 and the increase of the selling and distribution expenses by a sum of Rs.61,662,903.

2:2 Analytical Financial Review

The gross profit percentage of the Corporation for the year under review amounted to 42.86 per cent and the pre-tax net profit percentage amounted to 18.49 per cent, and the corresponding gross profit percentage and the pre-tax net profit percentage for the preceding year amounted to 41.39 per cent and 14.07 per cent respectively. Thus a decrease of 1.47 per cent in the gross profit percentage and a decrease of 4.42 per cent in the net profit percentage were observed. The major reasons for the decrease of the net profit had been the decrease of sales by 13.35 per cent and the increase of as establishment, sales and distribution expenses by 7.65 per cent.

2:3 Working Capital Management

Liquidity Ratio	Standard Ratio	2011	2010	2009
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Current Rates	2:1	2.93:1	2.26:1	20.2:1
Quick Assets Ration	1:1	1.8:1	1.71:1	1.35:1

The current and quick assets ratios of the Corporation had gradually increased resulting in the existence of all excess working capital status.

3. Operating Review

3:1 Performance

(a) Import of Sawn Timber

Even though the Corporation had planned the import of 5,000 cubic metres of sawn timber and earn an income of Rs.487.5 million there from, timber had not been imported in the year 2011.

(b) Household Furniture Unit

(i) According to the financial statements, the actual sale of household furniture in the year under review amounted to Rs.121.74 million and that indicated a decrease of Rs.81.38 million from the budgeted sales amounting to Rs.203.12 million. The loss of the Household Furniture Division of the Corporation for the year under review amounted to Rs.34.22 million. This Division had incurred a loss due to the increases of the cost of production by 46.53 per cent and the increase of the establishment and administrative expenditure by 30 per cent as compared with the preceding year.

(ii) According to the Corporate Plan of the State Timber Corporation, plans had been made for the increase of the sales income of the

Household Furniture Division by Rs.180 million in the year 2010, Rs.190 million in the year 2011 and Rs.200 million in the year 2012. Nevertheless, the actual household furniture sales in the year under review amounted Rs.121.74 million and as compared with the preceding year indicated an improvement of 83.35 per cent. Nevertheless, it had not been possible to reach the expected targets of the Corporate Plan.

(iii) A successful arrangement had not been launched in 2011 for the promotion of the sale of the household furniture of the Corporation.

(c) No action whatsoever had been taken in the year in connection with the activities such as agricultural products, processing forest related produce, import of cane, by-products from timber and sale and export of finished and semi-furnished goods included in the objectives of the Corporation. The Chairman informed that the Corporation had not ventured into those products as those were not favourable profit-wise.

(d) Timber and Timber related Products

A reconciliation of the actual production of the year under review with the budgeted production for the year under review revealed that the actual production of sawn timber, sleepers, wall panels and the household furniture had been at 64.5 per cent, 48.45 per cent, 92.36 per cent and 29.85 per cent levels respectively.

3:2 Management Inefficiencies

The following observations are made.

(a) The sales value of rejected sleepers of the Oil Impregnation and Seasoning Division amounted to Rs.8,957,819 and as compared with sales of the year 2010 amounting to Rs.3,970,334 represented an increase of 225.6 per cent. As such a stock of sleepers with a considerable value had been rejected.

(b) The Accpac Accounting Information System used by the Corporation for the preparation of the accounting and financial statements is being used from the year 1992 up to the year under review. The existence of

deficiencies from the date of introduction of the system up to 31 December 2011 was observed and it was further observed that there were delays in the preparation of final account due to the absence of a proper accounting information system.

- (c) Even though the Handbook on Sustainable Forest Management should have been supplied in 30 days, it had taken more than 07 months. As such the Handbook could not be released on the Green Month that fell on 15 October as expected.
- (d) A sum of Rs.300,000 had been paid to a lawyer for handling the legal matters in connection with the summon issued on the Chairman in connection with action taken contrary to a Court Order.
- (e) In addition, a sum of Rs.275,000 had been paid as lawyers' fees in connection with the case No. SC/FR/567/2010 filed in the Supreme Court by a Non-Governmental Organization in connection with the failure of the officers of the State Timber Corporation to follow the relevant laws and rules. A sum of Rs.52,030 had been paid to a lawyer to appear for a case filed by the Commissioner General of Labour for the failure to take action in accordance with the decisions of an Arbitrator.

3:3 Uneconomic Transactions

The following observations are made.

- (a) A loss of Rs.6,266,409 had been caused due to the import and use of sub-standard creosote from an Indian Company in the year 2007. A sum of Rs.4,256,977 (US\$37,497.49) had been paid to that company without reaching a final agreement in that connection. No action whatsoever had been taken up to date on the Letter of Credit obtained on the payment of a further sum of US\$54,490.
- (b) Even though 40 carpenters, 30 polishers and 03 painters are in service, a sum of Rs.194,450 had been paid at Rs.3,150 per chair for spraying 63 conference hall chairs of the Head Office of the State Timber Corporation. The Chairman informed that the work had to be done from an outside source due to the lack of employees with experience in polyurethane in the Corporation.

3:4 Weaknesses in the Control of Motor Vehicles

The following observations are made.

- (a) A double cab motor vehicle had met with accidents in 04 instances and the loss not covered by insurance cover amounted to Rs.162,323. The Corporations had not conducted inquiries against the employees responsible for the accidents. No follow up action had been taken on the action taken by the Police on the accidents.
- (b) An accident had been caused to a motor vehicle resulting in a loss of Rs.1,258,557 to the motor vehicle while being driven by the Working Director who is not an officer of the Corporation and the Corporation had not held an inquiry into it in that connection. The Chairman informed that a Committee in terms of Financial Regulation 104 had been appointed and the necessary steps will be taken after the receipt of the report.
- (c) A double cab motor vehicle valued at Rs.7,684,456 had become a total loss due to an accident caused on 24 August 2010 and the Corporation had not held an inquiry in this connection. In addition, disciplinary action had not been taken against the driver for the failure to prevent the accident to the motor vehicle.
- (d) The National Insurance Trust Fund had decided on 11 August 2011 to condemn the double cab motor vehicle which met with an accident on 30 April 2010 and the cost of repairs would exceed 50 per cent of the insured value or Rs.800,000. An inquiry in that connection had not been held up to date.

3:5 Resources of the Corporation Supplied to External Parties

The expenditure on insurance for a motor vehicle used by an external party from periods commencing prior to the year 2008 amounting to Rs.83,517 had been incurred by the State Timber Corporation.

4. Accountability and Good Governance

4:1 Corporate Plan

The following observations are made.

- (a) A Corporate Plan had been prepared for the period 2008-2012.
- (b) Copies of the Corporate Plan for the period 2008-2012 approved by the Board of Directors should be furnished at least 15 days before the commencement of the financial year to the line Ministry, the Department of Public Enterprises of the General Treasury and the Auditor General. Nevertheless, an updated Corporate Plan for the period 2010-2014 had not been furnished to audit.
- (b) The particulars of the progress of the expected products and the imports for the year under review according to the Strategic Plan are given below.

Objective and Programme	Expected Quantity according to the Strategic Plan	Actual Quantity according to the Quarterly Reports	Difference	Percen- tage
4.1 Production of Sawn Timber	6,000 Cubic Mteres	3,753 Cubic Metres	2,247	(37.45)
4.2 Import of Sawn Timber	5,000 Cubic Metres	--	5,000 Cubic Metres	(100.00)
5.1 Production of Sleepers	120,000 Units	66,699	53,301	(44.4)
5.1 Import of Sleepers	30,000 Units	--	30,000	(100.00)
5.2 Production of Transmission poles	60,000 Units	31,863	28,137	(46.90)

01.1	Production of Traditional Household Furniture	Rs.36 million	} 140 198 (58.5)
1.3	Increase of Production of Complexes at Kaldemulla, Ampara and Boossa.	Rs.120 million	
3.1	Production of Parts of Household Furniture	Rs.7 million	
7.2	Increase the Turnover by the establishment of Household Furniture Showrooms	Rs.175 million	

4.2 Action Plan

Even though an Annual Action Plan for the year 2011 had been prepared, the following deficiencies therein were observed.

- (a) The Action Plan had been prepared with the sole objectives of the production and sale of timber and attention had not been paid for its preparation covering all the Divisions of the Corporation.
- (b) Even though the officers assigned with the responsibility for the achievement of the objectives and targets during the relevant year should be specifically indicated, it had not been so identified in the Action Plan for the year 2011.

4:3 Internal Audit

The following matters were observed.

- (a) In terms of Financial Regulation 134(3), copies of Internal Audit Reports should be furnished to the Auditor General. But none of the Internal Audit Reports had been furnished to the Auditor General.
- (b) Even though staff of the Internal Audit comprised 54 Internal Audit Officers including the professionally qualified Chief Internal Auditor recommendations for the improvement of the internal control system had not been made by reviewing them. Instead, officers had been attached to the Regional Offices and deployed non-audit duties.
- (c) The half yearly reports had not been furnished to the Auditor General in terms of Section 13(5)(d) of the Finance Act, No. 38 of 1976.

4:4 Procurement Plan

A Procurement Plan for the year 2011 had not been prepared.

4:5 Budgetary Control

A reconciliation of the budgeted income and expenditure for the year under review with the actual income and expenditure revealed income variances ranging from negative 100 per cent to negative 39.98 per cent and expenditure variances ranging from 0.12 per cent to 686.55 per cent, thus indicating that the budget had not been made use of as an effective instrument of management control.

5. Systems and Controls

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

- (a) Presentation of Financial Statements
- (b) Debtors Control
- (c) Creditors Control
- (d) Budget
- (e) Fixed Assets
- (f) Contract Files
- (g) Corporate Plan
- (h) Purchases