

Paddy Marketing Board – 2014

The audit of financial statements of the Paddy Marketing Board for the year ended 31 December 2014 comprising the statement of financial position as at 31 December 2014 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information 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 13(1) of the Finance Act, No. 38 of 1971 and Section 30 of the Paddy Marketing Board Act, No. 14 of 1971. My comments and observations which I consider should be published with the Annual Report of the Board in terms of Section 14 (2) (c) of the Finance Act appear in this report.

1.2 Management’s Responsibility for the Financial Statements

The management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

1.3 Auditor’s Responsibility

My responsibility is to express an opinion on these financial statements based on the audit conducted in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000-1810).

1.4 Basis for Disclaimer of Opinion

As a result of the matters described in paragraph 2.2 of this report, I am unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded items, and the elements making up the statement of financial position, statement of comprehensive income, statement of changes in equity, and cash flow statement.

2. Financial Statements

2.1 Disclaimer of Opinion

Because of the significance of the matters described in paragraph 2.2 of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

2.2 Comments on Financial Statements

2.2.1 Going Concern of the Board

As the stocks of paddy purchased by the Board had constantly been marketed at prices less than the market price and the cost, action had been taken to obtain loans annually from the Treasury and a state banks in order to fund the purchase of paddy in the next season, and settle the losses sustained. By 20 June 2017, a sum of Rs. 18,645.3 million together with an interest thereon amounting to Rs. 420.8 million remained payable in respect of the loans and advances obtained from 03 state banks for purchasing paddy and operating expenses during the period 2009-2014. As such, it could not be ruled out that there had been no effect on the risk affecting the going concern of the Board.

2.2.2 Disclosure of Transactions with the Connected Parties

Payments totalling Rs. 298,889,804 had been made to the C.W.E. Construction and Engineering (Private) Limited in the year under review by awarding the constructions of the Board to that institution for which the Chairman of the Paddy Marketing Board had served as a founder member of the Board of Directors. Nevertheless, those transactions had not been disclosed in the financial statements.

2.2.3 Sri Lanka Accounting Standards

Sri Lanka Accounting Standard 07

Due to the following observations, the tallying of the cash flow statement was questionable in audit.

- (a.) Although the cash flows in respect of Property, Plant and Equipment amounted to Rs. 2,853,054 in the year under review, it was shown as Rs. 26,664,302 under investment activities of the cash flow statement.
- (b.) Prior year adjustments amounting to Rs. 18,520,161 shown in the statement of changes in equity, had been adjusted to the operating profit in the cash flow statement.

2.2.4 Accounting Deficiencies

The following observations are made.

- (a.) The sum totalling Rs. 8,286,422 paid for the construction of stores complex in Meethotamulla, of which the construction had been complete, and renovation of stores in Wellawaya and erecting the fence of the land, had been shown in the Work in Progress Account instead of being capitalized in the Lands and Buildings Account. As such, depreciations on the lands and buildings had also been understated by a sum of Rs. 207,160.
- (b.) Furniture and equipment valued at Rs. 4,849,303 purchased in the year under review had been brought into the Work in Progress Account instead of being shown in the relevant account. As such, the depreciation on furniture and equipment had been understated by a sum of Rs. 969,860.
- (c.) When making payments for the construction of buildings, sums of Rs. 5,965,656, and Rs. 5,540,196 had been deducted as retention money in the years 2013 and 2014 respectively. However, those sums had not been adjusted in the accounts.
- (d.) The value of the stock of paddy had not been physically verified as at 31 December of the year under review; instead, the book balance of Rs. 2,365,549,763 had been shown in the statement of financial position.
- (e.) The stock in transit valued at Rs. 54,385,222, the stock of soyabean valued at Rs. 3,302,853, and the stock of rice valued at Rs. 84,972 being brought forward in the statement of financial position since the year 2012, had not existed physically. Hence, the stock balance had been overstated by a total of Rs. 57,773,047.

2.2.5 Lack of Evidence for Audit

As the evidence shown against the following Items of Accounts had not been made available, they could not be satisfactorily vouched or accepted in audit.

<u>Item of Account</u>	<u>Value</u> Rs.	<u>Evidence not Made</u> <u>Available</u>
Unidentified Purchase of Paddy	73,829,883	Detailed Information, Confirmations.
Purchase Control Account	49,743,530	
Sale of Rice Millers on Credit	68,993,349	

2.2.6 Accounts Receivable and Payable

The following observations are made.

- (a.) The debtor balance of Rs. 2,271,997,405 as at 31 December 2014 included a sum of Rs. 60,335,368 relating to a period of over 05 years, a sum of Rs. 540,850,201 relating to a period of 2-4 years, a sum of Rs. 1,454,547,464 relating to a period of 1-2 years and a sum of Rs. 216,264,372 relating to a period of less than 6 months. Action had not been taken even up to 30 June 2017 to settle those balances.
- (b.) Following instructions of the Ministry of Co-operatives and Internal Trade, the Board had issued 12,019,045 Kg of Nadu paddy worth Rs. 469.34 million in the year under review and the preceding year to the paddy mills for exporting. Invoices on sales had not been prepared under the name of the Ministry relating to the said issuance, and only a sum of Rs. 169.46 million had been received from the Ministry in respect of the said paddy. As such, a sum of Rs. 299.88 million had remained receivable to the Board from the Ministry for the supply of paddy for export.
- (c.) In terms of the letter No. DFD/Agri/RiceExp, of the Department of Development Finance, dated 06 February 2014, the Board had issued 5,028,063 Kg of Nadu paddy and 468,726 Kg of Samba paddy worth Rs. 216.26 million to the District Secretaries of Ampara and Hambanthota in the year under review for donating rice under the World Food Programme. The said sum had not been obtained from the Department of Development Finance even up to 31 July 2017.

2.3 Non-compliances with Laws, Rules, Regulations, and Management Decisions

The following non-compliance were observed.

<u>Reference to Laws, Rules, and Regulations, etc.</u>	<u>Non-compliance</u>
(a.) Financial Regulation of the Democratic Socialist Republic of Sri Lanka	
(i) Financial Regulation 188 (2)	Action had not been taken in terms of Financial Regulations on non-realized deposits valued at Rs. 233,300 that had continued to exist since the year 2012.

- (ii) Financial Regulation 395 (c) The delay in preparing the bank reconciliations for 08 bank accounts of the Board for December 2016, had been 06 months. Bank reconciliation statements for one bank account, had not been prepared since March 2015.
- (b.) Procurement Guidelines-2006
 - (i) Section 5.4.4 Mobilization advances subject to a maximum of 20 per cent of the contract value can be provided by obtaining an advance payment guarantee. However, the Board had given advances totalling Rs. 49,754,113 or up to 30 per cent of the contract value without obtaining any advance payment guarantee in respect of 14 construction contracts executed in the year under review.
 - (ii) Section 5.4.8 The relevant contractors must furnish a performance bond equivalent to 5 per cent of the contract value. However, the Board had not taken action to obtain performance bonds in respect of the contracts mentioned under (i) above.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the operating loss of the Board for the year under review amounted to Rs. 1,126,931,765 as compared with the corresponding loss of Rs. 1,036,227,966 for the preceding year, thus indicating an increase of Rs. 90,703,799 in the loss for the year under review. The increase in the net loss by a sum of Rs. 115,040,103 as compared with the preceding year, had mainly attributed to the said increase in the loss.

An analysis on the financial results for the year under review and 03 preceding years revealed that the financial result for the year 2012 had deteriorated by 857 per cent as compared with that for the year 2011. The financial result for the year 2013 had improved by 48 per cent as compared with the year 2012, whereas the financial result had deteriorated by 9 per cent in the year 2014 as compared with the year 2013. However, when the employee remuneration and depreciation on non-current assets had been adjusted to the financial result, the minus contribution of the Board in the year 2013 amounting to Rs. 1,003,710,494, had increased by 07 per cent in the year 2014 up to a minus contribution of Rs. 1,078,742,573.

4. Operating Review

4.1 Management Activities

Action had not been taken to identify and settle a sum of Rs. 49,177,485 continued to exist since the year 2012 with respect to 04 bank accounts of the Board.

4.2 Operating Activities

In terms of the Paddy Marketing Board Circular, No. PMB/MAHA/SARF/2008-09, dated 02 October 2009, it is necessary to verify that monies have been credited to the bank account before issuing the receipts and publishing the notices on selling paddy. However, due to failure in doing so, an instance was observed in which paddy worth Rs. 9,600,000 had been issued twice by taking into account the original and the copy of the same cash deposit slip.

4.3 Contract Procedure

The following observations are made.

- a) Seventeen contracts valued at Rs. 258.19 million had been awarded to a private institution affiliated to the Co-operative Wholesale Establishment in the year under review in contrast with the provisions of the Procurement Guidelines, based on a letter issued by the Minister of Co-operatives and Internal Trade on 06 September 2010 requesting that renovations and new constructions of the buildings belonging to the Ministry and the institutions thereunder, be assigned to the construction division affiliated to the Co-operative Wholesale Establishment functioning under a chief engineer.

The following observations are made in this connection.

- (i) This company had been established on 18 May 2012 by appointing the Chairman of the Board, the Chairman of the Co-operative Wholesale Establishment, and an Additional Secretary to the Ministry of Co-operatives and Internal Trade as the directors of the said affiliated company.
- (ii) As the said affiliated company lacked the officers with expertise in construction technology, the company had awarded subcontracts for the said constructions to the parties selected without transparency.
- (iii) The following matters were observed in the audit examination conducted on the said constructions.
 - The cost estimate valued at Rs. 24,184,502 relating to the contract for renovating the paddy store in Akkarapattu had been prepared with the consent of the contractor. Furthermore, a sum of Rs. 1,345,328 had been paid in respect of the variations of quantities ranging from 150 per cent to 276 per cent as per the Bill of Quantity, whilst a sum of Rs. 559,880 had been paid in 05 instances for additional works.
 - The consultancy fee of Rs. 600,479 relating to the contract for renovating the paddy store in Kaduruwela costing Rs. 23,074,094 had been paid to the CWE Construction and Engineering Private Limited Company. That sum had been paid for the preparation of estimates, Bills of quantity and structural plans of the contract, and supervising the contract, but the estimates and the Bills of Quantity prepared, had not been certified by any Civil Engineer. Furthermore, a sum of Rs. 1,337,400 had been paid for the variances ranging between 100 – 159 per cent as per the estimate.

- b) In addition to the 17 construction contracts mentioned in paragraph (a) above, the contract for the construction of paddy store in Kilinochchi, valued at Rs. 41,140,418 had been awarded to the private company affiliated to the Co-operative Wholesale Establishment by deviating from the Procurement Procedure. The following matters were observed in this connection.
- (i) The activities such as, construction of an office building, construction of roads, erecting chain link fences, construction of water tanks, and landscaping could have been identified during the preparation of estimates for the contract of constructing the store. However, those activities had been identified to be additional activities of the contract worth Rs. 8,252,330, and an overprice had been paid thereon.
 - (ii) The Board had employed an Engineering Consultant on part time basis for supervising the constructions and other related activities. Despite that, the CWE Construction and Engineering Private Limited Company had also been paid a sum of Rs. 2,088,486 for providing consultancy services for this contract. Furthermore, the initial estimates and BOQs of this contract had been prepared by the company that executed the contract. Although a sum of Rs. 5,000 had been paid to the consultant appointed by the Paddy Marketing Board to inspect that estimate, no one had certified those estimates.
 - (iii) No agreement had been entered into with the contractor to make payments in respect of the remaining stocks at the construction site, but without examining the stock register provided by the contractor, at the construction site, and without inspecting the bills relating to the purchase of those items by the contractor, a sum of Rs. 12,904,400 had been paid for the materials remaining at the construction site in 02 instances where the contractor had not requested for monies.

5. Accountability and Good Governance

5.1 Presentation of Financial Statements

In terms of Section 6.5.1 of the Public Enterprises Circular, No. PED/12, dated 02 June 2003, the financial statements should be furnished for audit within a period of 60 days since the lapse of the financial year. However, financial statements for the year 2014 had been furnished on 02 March 2017.

6. Systems and Controls

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

<u>Area of Systems and Controls</u>	<u>Observation</u>
(a.) Control of Vehicles	Failure to maintain the running charts, and log books in an updated manner.
(b.) Awarding and Execution of Contracts	Deviation from the Procurement procedure.
(c.) Stores Administration	(i) Failure to store paddy following proper standards and rectify the deficiencies of the stores. (ii) Failure to issue instructions on stores control to the officers in charge of the stores.
(d.) Bank Reconciliations	Delays in preparing bank reconciliation statements.
(e.) Process of Selling Paddy	Failure to prepare the sales invoices.