

Custom Officers Reward Fund - 2016

The audit of financial statements of the Customs Officers Reward Fund for the year ended 31 December 2016 comprising the statement of financial position as at 31 December 2016 and the statement of comprehensive income, the statement of changes in equity and cash flow statement and a summary of significant accounting policies and other explanatory information was carried out under my direction in pursuance of provisions in Article 154(3) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

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 the Sri Lanka Public Sector 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 my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000-1810). Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Fund's preparation and fair presentation of the financial statements 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 the Fund's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

1.4 Basis for Adverse Opinion

Had the matters described in paragraph 2.2 of this report been adjusted, many elements in the accompanying financial statements would have been materially affected.

2. Financial Statements

2.1 Adverse Opinion

In my opinion, because of the significance of the matters described in paragraph 2.2 of this report, the financial statements do not give a true and fair view of the financial position of the Custom Officers Reward Fund as at 31 December 2016 and its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards

2.2 Comments on Financial Statements

2.2.1 Sri Lanka Public Sector Accounting Standards

Sri Lanka Public Sector Accounting Standard 01

The following observations are made.

- (a) Even though it had been reported that the financial statements of the Fund has been prepared in terms of Sri Lanka Public Sector Accounting Standards, fines and confiscations imposed by Officers had been brought to account on cash basis contrary to the standard.
- (b) According to the paragraph 21 of this standard, when the entity makes publicity available its approved budget, a comparison of budget and actual amounts either as a separate financial statements or as a budget column in the financial statements should be shown. However, the budgeted information in the financial statements of the Custom Officers Reward Fund had not been disclosed.
- (c) Even though the investigations has completed, no any information relating to the investigation files which had not been received the Rewards files to the Accounts Branch and investigations which are being carried on further more had not been disclosed in financial statements.

2.2.2 Accounting Policies

Even though 50 per cent of the income earned from customs fines and sale of confiscated goods had been identified as the income of the Fund, the Management had not decided whether that income identified at the completion of customs investigation, at the completion of the paying of fines, or at the distribution of fines among Customs Officers. The relevant policy had not been disclosed even in the financial statements.

2.2.3 Accounting Deficiencies

The following observations are made.

- (a) The total income received for the Reward Fund is divided for 05 Sub-Funds and as a result of calculation errors happened in the instance of dividing in this manner ,the “2.5 per cent Reward Fund” which is one of the Sub-Fund had been overstated by Rs.200,000.
- (b) Out of the fine amounted to Rs.1,597,390,932 imposed relating to 81 case files which the investigations completed at the end of the year under review , only a sum of Rs.436,806,066 had been recovered. Out of the fine imposed ,the income of Rs.798,695,466 of 50 per cent of the contribution to the Fund , a sum of Rs.218,403,033 recovered and a sum of Rs.580,292,433 which should have been recovered further had not been accounted.
- (c) Out of the sale income of customs fines and confiscated goods , a contribution of 50 per cent to the Rewards Fund and another 20 per cent to the Management Compensation Fund and the remaining 30 per cent to the Consolidated Fund are credited . Even though it had not been disclosed in financial statements, it was observed at audit that the income of the Fund is identified at the time of payment of rewards by the Accounts Division. Accordingly, the income amounted to Rs.51,198,102 to be identified as the income to the Rewards Fund proportional to the sum of Rs.20,479,241 identified as the income for the Management Compensation Fund ,had not been identified.

2.2.4 Weakness in presentation of Financial Statements

Even though the income over expenditure in the statement of Comprehensive Income had shown as Rs.164,425,880 in the financial statements, it is not a surplus over expenditure. The component of this had been a sum of Rs.67,333,645 allocated for the Fuel Fund which are the Sub Funds of Rewards Fund , a sum of Rs. 33,826,973 allocated for the 2.5 per cent Fund , a sum of Rs.23,558,781 allocated for the Narcotic Drug Fund and a sum of Rs. 39,706,481 allocated for the payments made for the reserved officers.

2.3 Accounts Payable

Even though the rewards totaled Rs.993,492,865 which would have been granted to the Officers by 31 December 2016 were accumulated and brought forwarded over a number of years , action had not been taken to settle those money.

3. **Financial Review**

3.1 **Financial Results**

According to the financial statements presented, the operations of the Fund for the year ended 31 December 2016 had resulted in a surplus of Rs.164,425,880 as compared with the corresponding surplus of Rs. 32,476,907 in the preceding year, thus indicating an increase in the financial results by Rs.131,948,973 or 406 per cent during the year under review as compared with the preceding year. Even though the payment made to the Custom Officers as rewards increased by Rs.538,030,080 ,increase of income of fines by Rs.721,644,255 had mainly attributed to the above growth.

4. **Operating Review**

4.1 **Performance**

An amount of money equivalent to 50 per cent of the penalty imposed for the various customs faults in terms of Section 153(2)(b) of the Customs Ordinance and the money received from the sale of confiscated goods are credited to the Customs Officers Reward Fund and this Fund had been established with the objective of disclosing, controlling and preventing the customs duty frauds.

Sums totalling Rs.6,261,990,253 comprising Rs.822,569,372, Rs.1,268,050,168, Rs.1,142,901,944 , Rs.1,214,323,918 and Rs.1,814,144,851 had been distributed among the officers and the informants during the years 2012,2013,2014, 2015 and 2016 respectively. Out of that, a sum of Rs.5,586,704,859 or 89.21 per cent had been paid to the officers.

The following observations are made in this connection.

- (a) Even though the sum paid to the Officers and the informants in the year 2012 amounted to Rs.822.5 million only, it had been increased by Rs.1,814.1 million or 120 per cent by the year 2016. As such, this money paid only for the several customs faults which the investigations completed in each year, it was observed that the number of incidents which the investigation had not been completed had become very high value. Accordingly, it was problematic at audit that whether the Rewards Scheme had fulfilled the considerable control or decrease on the customs duty frauds.

- (b) The particulars of fines charged relating to several investigations carried out by the Sri Lanka Customs and the amount credited to the Revenue are given below.

Customs Number	Investigation	Amount charged as Fines	The value credited to the Revenue from fines	Tax income should have been recovered under normal condition	Different between the tax received on fines and the tax value lost.
		Rs.	Rs.	Rs.	Rs.
	INDS/BIU/39/2015	17,000,000	5,100,000	32,006,279	26,906,279
	INDS/BIU/032/2015	250,000	75,000	1,527,040	1,452,040
	INDS/BIU/043/2015	2,900,000	870,000	1,473,692	603,692
	INDS/BIU/31/2014	1,754,458	526,337	827,228	300,891
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Total		21,904,458	6,571,337	35,834,239	29,262,902
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The following observations are made in respect of the above matters.

- (i) Decrease in the income occurred which should have been received to the Government through the imports which were under the fines due to imposing fines relating to customs faults despite the minimum quantity of tax income received to the Government on normal imports method in the investigations carried out in respect of customs faults and increase of rewards distributed to the officers was observed.
- (ii) A sum of Rs.67,333,645 had been credited in the year under review to the Fuel Fund which a percentage of 1.485 per cent allocated from the income collected to the Custom Officers Rewards Fund. Even though, it had been stated that the objective of the establishment of that Fund is to settle the fuel expenses required for the customs investigations, as a result of the fuel expense incurred for the investigations had been a burden of expenditure to the General Expenditure Head of the Department, no any expense had been incurred from that Fund during the year under review.
- (iii) Even though balances of Rs.110,838,866 and Rs.79,739,956 remained as at 31 December 2016 in the Sub-Funds under the Fund named 2.5 Per cent Rewards Fund and Narcotic Drugs Fund respectively, no any expense had been incurred from several years from that Funds. However, it was observed that a colossal amount of money kept in this Fund which is the money collected continuously despite the reasonable requirements.
- (iv) It was observed at audit that the necessity of the revision of Customs Ordinance as well as the legal provisions of this Funds properly and timely as suitable for the complexity arisen in the imports and exports due to the free economic policies existed at present.

4.2 Transactions of Contentious Nature

Legal provisions had been made by Section 8 of the Customs Ordinance to the Preliminary Investigation Officer for act on behalf of the Director General of Customs at a customs investigation. According to this legal provisions, a fine amounted to Rs.10 million had been imposed by the Customs Investigation Officer for the customs investigation activity No.PREV/FPO/1725/2015 . However, the said fine had been reduced up to Rs.3 million by the relevant Investigation Officer on an appeal received afterwards. Accordingly, mitigation of fines is a matter of contentious nature and a written information made by the Attorney General to the Director General of Customs that such a legal provisions had not been entitled to the Director General of Customs.

5. Accountability and Good Governance

5.1 Presentation of Financial Statements

In terms of Section 4.3 of the Public Finance Circular No.PF/423 dated 22 December 2006, the annual performance reports and the financial statements of the Funds should be furnished to audit within 02 months from the close of the year of accounts. Nevertheless, the financial statements of the year under review had been furnished only on 06 June 2017 .

5.2 Budgetary Control

Variances in 06 items of income and expenditure ranging from 20 per cent to 230 per cent were observed between the budgeted and the actuals, thus indicating that the budget had not been made use of as an effective instrument of management control.

6. Systems and Controls

Deficiencies observed during the course of audit were brought to the notice of the Director General of Customs from time to time. Special attention is needed in respect of the following areas of control.

Areas of Systems and Controls	Observations
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(a) Accounting	Failure in taking action to maintain a Leger Account system properly and failure in preparing accounts on accrual basis.
(b) Calculating Rewards	Failure to follow a practical calculating procedure to secure the Government tax income, make control in customs duty frauds and receive a maximum draw back to the parties who engaged in customs frauds in the calculation of rewards.
(c) Payments of Rewards	When the rewards files received to the Accounts Branch ,failure to register the files and made payments according to the order.
(d) Underutilization of Funds	Failure to utilize the Sub-Funds such as “2.5 Per cent Rewards Fund “,Narcotic Drugs Fund and Fuel Fund during the year under review.

