

Tea Research Board – 2016

The audit of financial statements of the Tea Research Board for the year ended 31 December 2016, comprising the statement of financial position as at 31 December 2016 and the statement of financial performance, 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 15 of Tea Research Board Act, No. 52 of 1993. 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 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 Board’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 Board’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. Sub-sections (3) and (4) of Section 13 of the Finance Act, No. 38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

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 Qualified Opinion

My opinion is qualified based on the matters described in paragraph 2:2 of this report.

2. Financial Statements

2.1 Qualified Opinion

In my opinion, except of the matters described in paragraph 2:2 of this report the financial statements give a true and fair view of the financial position of the Tea Research Board as at 31 December 2016 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

2.2 Comments on Financial Statements

2.2.1 Sri Lanka Public Sector Accounting Standards

The following observations are made.

(a) Sri Lanka Public Sector Accounting Standard 03

According to a decision taken in the year 2016 to release the lands with gem deposits that had been accounted, and located in the St. Joachim Estate, Hidellana, Ratnapura belonging to the Board, to the National Gem and Jewellery Authority in order to be auctioned for mining for gemstones, the said lands had been released to the National Gem and Jewellery Authority in the year 2017. However, information in that connection had not been disclosed in the financial statements in terms of Section 12 of the Standard.

(b) Sri Lanka Public Sector Accounting Standard 07

- (i) Assets valued at Rs. 57,209,881 were still in use despite being fully depreciated, due to failure in reviewing the useful life of the non-current assets annually in terms of Section 65 of the Standard. Action had not been taken accordingly to revise the estimated error in terms of Sri Lanka Public Sector Accounting Standard 03
- (ii) Lands and buildings are assets separable from each other, and they should be classified separately in terms of Section 50 of the Standard. Nevertheless, lands and buildings of which the net value amounted to Rs. 226,166,964, shown in the financial statements as at 31 December of the year under review, had not been so classified. Accordingly, the accuracy of the depreciation on the buildings could not be verified.

2.2.2 Accounting Policies

If the accounting system utilized for the preparation of financial statements does not disclose the manner in which any specific accounting affair should be dealt with, the Best Practice should be more appropriately adopted therein and an accounting policy should be formulated, followed and stated. Nevertheless, the Board had not taken action accordingly in connection with the accounting of following assets.

- (i) Amortization and accounting of intangible assets valued at Rs. 2, 404,163 shown in the statement of financial position as at the end of the year under review.
- (ii) Recognition of the tea cultivation costing Rs. 178,385,689 shown in the statement of financial position as at the end of the year under review, separately after being classified as mature and immature cultivation. The said value had been computed without considering the prevailing biological situation by examining the physical existence of the said tea cultivation.

2.2.3 Accounting Deficiencies

The following observations are made.

- (a) The cost of the water purification unit completed in the year under review by spending a sum of Rs. 11,727,594, had been shown under work in progress, instead of being accounted as non-current assets.
- (b) The cost of living allowance should be added to the basic salary, and the contribution to the Provident Fund in respect of the staff and the labourers should be computed thereon. However, due to failure in doing so during the period January 2006 to 30 May 2012, a sum of Rs. 37,316,860 should have been credited to the Employees' Provident Fund as at 31 December 2016, but provisions had not been made therefor in the financial statements of the year under review. The said sum had been settled on 28 February 2017.
- (c) As the final stock of made tea remained unsold in the year at the tea factories, had been accounted as sales on credit in computing the sales income, instead of being disclosed in the accounts, the tea sales income, and the debtor balance of the year, had been overstated by a sum of Rs. 5,216,710.
- (d) The machinery of the Lamilier Estate given to an external party on lease by the Board, had been sold to a lessee in the year 2003 at a value of Rs. 1,010,100. However, the cost of the said machinery had not been eliminated from the accounts even up to the end of the year under review.
- (e) The value of 5654 plants in the lands belonging to the Board, identified as biological assets, had not been evaluated and brought to accounts.

2.2.4 Unexplained Differences

According to the accounts of the St. Coombs Estate for the year ended as at 31 December 2016, a sum of Rs. 256,641 had been shown as being receivable from the Tea Smallholdings Development Authority. However, according to the accounts of the Authority, the sum amounted to Rs. 340,300.

2.3 Accounts Receivable and Payable

Of the miscellaneous debtors of the Board totalling Rs. 2,853,977 by the end of the year under review, 26 per cent of the debtors equivalent to a sum of Rs. 730,905 had been older than 05 years, but no productive measures had been taken by the management to recover those balances.

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

The instances of non-compliances with Laws, Rules, and Regulations, etc. observed during the course of audit, are as follows.

Reference to Laws, Rules, Regulations, and Management Decisions.

Non-compliance

- | | |
|--|---|
| (a.) Section 13.3 of Chapter II of the Establishments Code of the Democratic Socialist Republic of Sri Lanka | An acting appointment should be made as a temporary measure only and until a substantive appointment is made. Nevertheless, acting appointments had been made with respect to the posts of residential engineer of the Board, senior accountant, and 08 posts of divisional head, for a period of 01-07 years. A sum of Rs. 2,648,179 had been paid during the 07 preceding years as acting allowances. |
| | |
| (b.) Financial Regulations of the Democratic Socialist Republic of Sri Lanka. | |
| (i) Financial Regulation 104 (2) | Although 05 vehicles belonging to the Institute had met with accidents in the year under review in 06 instances, reports on losses and damages had not been presented to the Auditor General in terms of Financial Regulations. |
| (ii) Financial Regulation 316 (2) | Records of the articles lodged in, or withdrawn from safe custody, should be maintained by the officer responsible. However, such records had not been maintained with respect to the cash lodged in the vault of the Institute. |
| (iii) Financial Regulation 396 | Action had not been taken in terms of the Financial Regulation on 14 cheques issued but not presented and valued at Rs. 117,940 that had exceeded the period of validity despite being issued with respect to 03 bank accounts. |

- (c.) Paragraph 9.14 of the Public Enterprises Circular, No. PED/12, dated 02 June 2003. A Manual of Procedures providing rules and regulations on Human Resource Management should be prepared, and approval of the Secretary to the Treasury should be obtained thereon. However, the Board had not done so.

2.5 Transactions Not Supported by Adequate Authority

Approval of the Board of Directors had been received on 17 March 1995 on the procedure for making payments at the retirement over the vacation leave unavailed by the officers. However, approval of the Treasury had not been obtained thereon. A sum of Rs. 213,634 had been paid in the year under review to 06 retired officers in respect of unavailed vacation leave.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the financial result of the Board for the year under review had been a deficit of Rs. 6,599,148 as compared with the corresponding deficit of Rs. 13,302,192 for the preceding year, thus indicating an improvement of Rs. 6,703,044 in the financial result as compared with the preceding year. The increase in the profit of the St. Coombs Estate by a sum of Rs. 5,266,067 and the decrease in the loss by a sum of Rs. 10,648,682 sustained by the St. Joachim Estate in the year under review, had mainly attributed to the said improvement.

The analysis of the financial result of the year under review and 04 preceding years revealed that a financial deficit had resulted in from the year 2012 to 2016. However, when the employee remuneration and the depreciation for non-current assets had been adjusted to the financial result, the contribution of the Board in the year 2012 amounting to Rs. 142,812,049, had continuously improved in the year 2016, and reached Rs. 227,982,026.

3.2 Analytical Financial Review

The ratio of profits of the ADB Project relating to the St. Coombs Estate and St. Joachim Estate had been unfavourable in the year under review, and the said ratio had been (415) per cent and (48) per cent respectively, whereas those ratios had been (139) per cent and (13) per cent respectively in the preceding year. The annual decrease in the quantity of clonal cuttings sold by the said Project, had caused the deterioration of the ratio.

3.3 Legal Cases Instituted by or against the Board

The following observations are made.

- a) As 05 officers who had proceeded abroad by obtaining full-pay study leave and never returned, had not acted as per the agreement entered into with the Board, cases had been filed in Courts even before 6 years to recover the bonds amounting to Rs. 18,552,991.

- b) A case had been filed by an external party in the year 2012 to acquire a plot of land by naming the Board as the third defendant, and an employee of the Board had filed another case in the year 2015 against the Board requesting reinstatement in the position that he had held previously.

4. Operating Review

4.1 Performance

The objectives of the Tea Research Board established under the Tea Research Board Act, No.52 of 1993, as amended by the Act, No. 30 of 2003 with emphasis on conducting researches in order to uplift the productivity and quality of tea production in a profitable manner, are as follows.

- ❖ To conduct, assist and encourage, scientific and technological research into, and investigations of, all problems and matters affecting the production and manufacture of tea, including the prevention and control of pests affecting tea, the prevention and control of diseases affecting tea and the improvement of the quality of tea; as well as the diversification of products manufactured from tea ;
- ❖ To conduct, assist and encourage, research, into the economic viability of the tea industry in Sri Lanka including future economic trends in such industry;
- ❖ To maintain and administer the Tea Research Institute situated at Talawakale, and its substations, in accordance with the rules of the Board ;
- ❖ To establish and maintain, relationships with research institutions, in Sri Lanka and abroad;
- ❖ To conduct, in the discharge of its functions, joint study programmes, seminars or symposia, with foreign research institutions and research institutions in Sri Lanka; to promote investment in tea research ; to advise the Minister on appropriate policies in relation to the tea industry.

The progress of the performance in respect of the researches and other activities conducted by the Board in achieving the said objectives, are as follows.

- a) According to the Corporate Plan for the period 2013-2017, it was expected to conduct 185 researches. Due to various limiting factors, 38 researches equivalent to 20 per cent, had either been abandoned halfway, or postponed.
- b) Seven researches commenced by incurring a sum of Rs. 14,629,986 from the research and development grants received annually from the Treasury, had not yielded the expected objectives, and been halted halfway. It was revealed in the audit examination that the scarcity of human resources had mainly affected thereto.

- c) In the wake of the resignation of the officer in charge of the Biometry Unit established for providing statistics required for researches, the said Unit had remained closed since the year 2013. Due to failure in recruiting an officer with expertise in that field, the Unit could not be restart to the end of the year under review.
- d) According to the Corporate Plan for 2013-2017, it had been planned to implement 04 projects by the Biochemistry Division to study the health benefits and antioxidant benefits of tea, but only one project had been implemented whilst 03 projects had been postponed. Three projects planned on the value added manufacture of tea, had not been implemented, whilst 2 projects had been abandoned. The scarcity of human resources in this field had also attributed to the non-implementation of the projects.
- e) Of the amount of Clonal Cuttings estimated to distribute during the 3 preceding years through the mother bush programme conducted by the Advisory and Extension Division for distribution of newly released tea cultivars, the amount of Clonal Cuttings distributed had only been 67 per cent, 58 per cent, and 59 per cent respectively; hence, the progress of this programme had not reached the expected target.
- f) Of the provision amounting to Rs. 100,000,000 made by the Treasury for the Mechanization Project implemented in the year 2013 to address the dire scarcity of labour, a main issue in the tea industry, a sum of Rs. 48,000,000 had been received by the year 2014, and a sum of Rs. 44,848,107 had been spent therefrom by the end of the year under review. As the harvest had been damaged due to the machines distributed under the said project, and those machines could not be used on slopes, the objectives expected from the project had not been achieved productively. Hence, it is observed that utilization of the funds of the Board on a procedure relating to mechanization and changing of attitudes in order to find solutions for the increasing scarcity of labour, is more productive. Furthermore, 2 researches planned to be conducted in different areas by the Agri Economics Division for the identification of socio-economic measurements in order to avert the scarcity of labour, had not been implemented in the year under review as well.
- g) The following observations are made on the St. Coombs and St. Joachim Estates, and the factory managed by the Board.
 - (i) According to the information made available to the audit, the quantity of sale of tea and the production costs in respect of each estate as compared with the preceding year, are as follows.

Description -----	St. Coombs Estate			
	St. Estate 2016 -----	Joachim 2015 -----	(Including Estate) 2016 -----	the Lamilier 2015 -----
Input of Green Tea Leave (Kg)	955,943	955,206	1,596,530	1,780,384
Production of Tea (Kg)	202,301	203,273	358,752	393,378
Sales of Tea (Kg)	202,266	201,727	348,896	388,417
Cost of Production (Rs. per Kg)	487.42	436.15	508.67	481.10
Average Net Sales (Rs. per Kg.)	483.23	393.09	541.91	475.93
Made Tea Outturn Ratio (per cent)	21.16	21.2	22.47	22.09

- Standard Made Tea Outturn Ratio 21.5

The following observations are made in this connection.

- Although the tea sales income of the St. Coombs Estate for the year under review had increased as compared with the preceding year, the amount of sales had decreased by 09 per cent. Furthermore, the decrease in the productivity of the tea estates belonging to the St. Coombs Tea Factory by 17 per cent as compared with the preceding year, had attributed to the decrease in the tea production thereof.
 - As the productivity of labour, usage of firewood, and electric units of both factories, had not reached the expected level, the production cost per kilogram of tea had increased as compared with the preceding year. Moreover, the production cost per unit of the St. Joachim Estate, had exceeded the average net sales price.
- (ii) According to the Action Plan of the St. Coombs Estate, and the St. Joachim Estate, the usage of green leaf had been 2,120,306 Kg and 1,836,826 Kg respectively, whereas the actual usage had been 1,596,530 Kg and 955,943 Kg respectively, thus indicating a variance of 24 per cent and 52 per cent. As such, the amount of made tea had also varied in a manner proportional thereto.
- h) The following matters are observed on the nurseries being maintained at the St. Coombs Estate, and the St. Joachim Estate with the objective of providing standard tea plants.
- (i) About 34 per cent of the number of plants nursed at the tea plants nursery maintained at the St. Joachim Estate during the 2 preceding years, had been unsuccessful. Failure to follow the instructions given to maintain the nurseries had mainly attributed thereto.

- (ii) Due to failure in properly maintaining the nursery at the St. Coombs Estate, 23,495 plants had been disposed of in the year under review causing a loss of Rs. 659,687.

4.2 Management Activities

The following observations are made.

- a) The books of the library at the head office of the Board had not been physically verified since the year 1978. As for the books not returned out of the books borrowed during the 20 preceding years (1985-2016), action had not been taken either to get those books back or settle the value.
- b) Prior to releasing an advance to an external institution for a certain activity, it is necessary to verify that it is feasible for the relevant activity to be carried out. Contrary to that, a private institution had been granted an advance of Rs. 110,124 in the year 2011 for the purchase of a Water Still Unit to be used at the regional office in Mathugama. However, the said institution had been closed, but no action had been taken to settle that value.
- c) Action had not been taken up to 30 June 2017 to take over the ownership of 08 vehicles used by the Board and the lands where the regional offices of Deniyaya, and Kottawa had been built.
- d) Lands in extent of 05 hectares belonging to the St. Joachim Estate, had been encroached by external parties over a period of 26 years. Action had not been taken to acquire those lands back to the Board.
- e) Paddy lands in extent of 8.74 hectares belonging to the St. Joachim Estate had been cultivated by tenant farmers, and action had not been taken to recover the portion of income receivable to the Board therefrom. Furthermore, action had not been taken to count and record the number of trees in the rubber and coconut estates.
- f) Action had not been taken by the management to calculate and account the value of the stock balance of the chemicals that had been kept in the stores at each research division after being purchased for research activities.

4.3 Underutilization of funds

Sums of Rs. 8,151,671 and Rs. 9,500,000 received from the Treasury for the Uplifting the Living Standards Project and the Mechanization Project in the years 2013 and 2014 respectively, had not been utilized even in the year under review.

4.4 Idle and Underutilized Assets

The following observations are made.

- a) As the stock of medicines valued at Rs. 201,408 kept in the custody of the Medical Assistant of the St. Coombs Estate had remained unused for a period of 04 years, that stock had been disposed of from being used.
- b) A quarters of category “A”, 11 quarters of category “D”, and 07 quarters of category “E” belonging to the Board had remained idle without being occupied.
- c) The plant capacity of the St. Coombs, and St. Joachim estates had been 8,000 and 15,000 Kilograms of Green Leaf per day respectively. However, it was observed that the average actual utilization of those plants had been 5,000, and 6,253 Kilograms per day representing 62 per cent and 17 per cent respectively.
- d) Of the 04 roller machines installed at the inception of the factory, only 02 machines are utilized in the production process at a time whilst the other 02 machines are observed to often remain underutilized. Moreover, the Savage Cutter machine had also been disposed of from being used, whilst the E.C.P. 4 Drier machine had remained unused over a period of 16 years.
- e) As the drier machines using firewood had been utilized at the St. Joachim Factory, the drier machine that used fuel had remained idle. Due to the decrease in the quantity of green tea leave received by the factory, the Stake Extractor, had not been used for a period of 03 years.

4.5 Staff Administration

The approved cadre and the actual cadre of the Board as at 31 December 2016 stood at 443 and 253 respectively. Accordingly, 190 posts had fallen vacant. The following observations are made in this connection.

- a) Of the 87 approved posts of the executive grade, 38 posts remained vacant. Twenty three posts of the employees had been internal promotions, and due to the lack of qualified officers in accordance with the Scheme of Recruitment for those posts, recruitments could not be made for a period of 05 years.
- b) Ninety seven non-executive posts remained vacant, and the number of approved posts of the Research and Development Technology Officer, and the Extension Officer included therein had been 50 and 24 respectively. Of that, 33 and 17 posts representing 68 per cent had remained vacant. Hence, the research and Extension activities of the Board could not be completed within the targeted period as planned.
- c) The post of Officer in Charge (OIC) is not included in the approved cadre of the Board, but 08 officers had discharged the duties belonging to that post, and acting appointments had been made in respect of the said posts, thereby paying a sum of Rs. 1,278,320 as allowances from the year 2010 up to the year under review.

- d) One hundred and twelve employees already in service after being recruited on temporary or casual basis in accordance with the Public Administration Circular, No. 25/2014, dated 12 November 2014, had been granted permanent appointments with effect from 24 October 2014 (105 posts of primary grade, and 07 posts of Management Assistant). Nevertheless, the number of posts of Labourer approved under PL-1, had been 65 as at 31 December 2016, but the actual cadre had been 104, thus the excess number of employees had been 39.

4.6 Control of Vehicles

The following observations are made.

- a) The engine of a vehicle that had been removed from being used, was fixed to another vehicle. However, action was not taken on the registration certificates of those vehicles in accordance with the directives of the Commissioner of Motor Traffic.
- b) A Pajero Jeep remained idle for a period of 05 years without being repaired completely.

5. Accountability and Good Governance

5.1 Internal Audit

An Internal Audit Unit had been established in the Board, but no examination relating to the financial or physical performance had been conducted on the main function of the Board being research activities.

5.2 Budgetary Control

As variations ranging from 13 per cent to 100 per cent had been observed between the budgeted income and expenditure, and the actuals, it was observed that the budget had not been made use of as an effective instrument of management control.

5.3 Unresolved Audit Paragraphs

The following observations are made.

- a) In order to reimburse a monthly labour allowance for the maintenance of quarters of the Director, Deputy Director and officers in charge of the Regional offices, the approval of the Board of Directors had been granted on 24 May 2007. This Labour allowance had been computed by adding production bonus, overtime, attendance allowance etc. to the daily labour salary and the Board had reimbursed Rs. 1,790,177 for 10 officers in the first 09 months of the year 2016. However, approval of the Line Ministry and the Treasury had not been obtained for this purpose, and instructions had been issued to obtain the approval at the meeting of the Committee on Public Enterprises held on 19 November 2014 as well.

- b) Action had not been taken to obtain the approval of the Treasury in connection with the privileges such as leave, quarters and non-recovery of charges for water and electricity consumption which had been granted by the Board to the staff superseding the relevant circulars and the other similar institutions.
- c) As the machines imported by the Institute in the year 1982 by incurring a sum of Rs. 4,142,173 for processing tea, had not been suitable for the relevant project, the machines remained idle. Despite being informed that action would be taken to write off this value from the books on the approval of the Treasury, the said value had not so far been removed from the accounts, and shown as work in progress instead.

6. **Systems and Controls**

Deficiencies 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.

<u>Areas of Systems and Controls</u>	<u>Observation</u>
(a) Accounting	Failure to revalue and account the assets fully depreciated.
(b) Control of Assets	Failure to take over the ownership of the vehicles and regulate the repairs properly.
(c) Maintenance of Books and Registers	Failure to maintain the Register of Fixed Assets in an up-to-date manner, non-inclusion of the assets belonging to the Board into the Register of Fixed Assets. Although a register should have been maintained on the receipt books in accordance with G.A. N-20, the regional office in Ratnapura had not done so.
(d) Budgetary Control	Observation of significant variances between the budgeted and actual expenditures.
(e) Research Activities	Poor regulation of research activities.
(f) Stores Control	Instead of storing the chemicals purchased for researches at a centralized store, thereby issuing in required quantities, those chemicals had been kept in the stores of the research divisions. Hence, the same chemical had been stored at several places in various quantities, and certain chemicals had become expired whilst redundant stocks had been maintained.