Head 248 - Report of the Auditor General on the Excise Department – Year 2017

The Appropriation Account, Reconciliation Statement and two revenue accounts relating to revenue codes included in the tables - 3.1.1, 3.1.2, and 3.1.3 of the annual budget under Head and Item Number stated in the First Schedule and Third Schedule of the Appropriation Act, No. 24 of 2016 as amended by the Appropriation (Amendment) Act, No.32 of 2017 were presented to Audit by the Excise Department. The financial and physical performance reflected by those accounts and reconciliation statements were audited in terms of Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

1.2 Responsibility of the Chief Accounting Officer and the Accounting Officer for the Financial Management and Accountability

The Minister of Finance is charged with the raising of Revenue and the collection of other Government monies as well as with the general oversight of all the financial operations of Government in terms of Financial Regulation 124 of the Democratic Socialist Republic of Sri Lanka. The Chief Accounting Officers have been appointed by the Minister of Finance to discharge the above responsibility in terms of Financial Regulation 124(2). The Head of the Department will be the Accounting Officer in respect of all the financial transactions of his Department in terms of Financial Regulation 125(1)(a) and the Revenue Accounting Officer has been appointed by the Treasury. This responsibility includes designing, implementing and maintaining internal controls relevant to the maintenance, preparation and fair presentation of Accounts and Reconciliation Statements presented within the limitations imposed by Parliament in accordance with the provisions in Articles 148, 149, 150 and 152 of the Constitution of the Democratic Socialist Republic of Sri Lanka, other Statutory Provisions, Government Financial Regulations and Administrative Regulations.

1.3 Scope of Audit

The audit of the Excise Department – Head 248 for the year ended 31 December 2017 was carried out in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka in respect of designing of financial and physical performance, Government expenditure, Government revenue, management of human and physical resources, apply of internal control systems, compliance with laws, rules and regulations and maintenance of books, registers, records and reconciliation statements in an updated manner, preparation and presentation of accounts in timely manner, issuance of performance reports to respective parties based on the performance indicators. The Management Audit Report for the year under review was issued to the Commissioner General of the Department on 12 July 2018. The audit observations, comments and findings on the accounts and the reconciliation statements were based on a review of the plans, accounts, reconciliation statements and performance reports presented to Audit and 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.

1.4 **Audit Observation**

The audit observations of the Excise Department for the year ended 31 December 2017 revealed in audit, appear in the Management Audit Report in detail, mentioned in paragraph 1.3 above. The material and significant audit observations out of the audit observations included in the Management Audit Report appear in paragraph 2.1 to 2.15 of this report. It was observed that the accountability as the Chief Accounting Officer had been satisfactorily executed, to ensure the adequacy of the financial administration subjected to the following summarized audit observations revealed in the execution of the provisions of the Financial Regulation 128 of the Financial Regulations of the Democratic Socialist Republic of Sri Lanka.

General responsibilities of Accounting Officers in terms of Financial Regulation 128		Non-compliance of the Accounting Officer to the Provision	Reference to the Paragraph of the Report Containing Observations
Financial Regulations			
128 (1) (a)	The work of his Department is planned and carried out with due despatch, having regard to the policy laid down by the Government and the intentions of Parliament in granting him financial provision for the activities authorized, and that an endeavour is made to complete the programme of work laid down for the year and / or to attain the targets specified.	1. Failure in planning procurements sufficiently. 2. Over-provisions 3. Deficiencies in the preparation of Action Plan. 4. Failure to achieve the expected level of output. 5. Delays in the implementation of projects. 6. Deficiencies in the execution of procurement process.	2.2 2.7 2.1.1 2.1.2 (a) (b) 2.1.2 (c) 2.2 2.1.2 (d) 2.14

		7. Achievement of Sustainable Development Goals and targets. 8. Deficiencies in internal audit.	
128 (1) (c)	The Financial Regulations and other supplementary instructions of the Government are adhered to in his department, and that they are supplemented by departmental instructions, where necessary.	1. Failure to maintain Books and Registers 2. Non-compliances	2.12 2.13
128 (1) (d)	An adequate system of internal check for receipts, payments and issues is maintained and tested from time to time.	Deficiencies shown in the Advances to Government Officers Account.	2.9
128 (1) (e)	Adequate and proper arrangements are made for the safe custody and preservation of money, stores, equipment, and other assets belonging to the Government, or is in its custody, and that these are verified from time to time; and where they are disposed of, such disposal is according to prescribed Regulations and instructions.	1. Deficiencies in assets management. 2. Losses and Damages.	2.3 2.4
128 (1) (i)	The activities of his department are undertaken with due regard to economy, efficiency, property and integrity expected in the transaction of public business.	1. Management inefficiencies. 2. Transactions of Contentious nature.	2.5 2.6

Financial Regulation 128 (2) Duties and responsibilities of Revenue Accounting Officer Financial Regulations ------------------			
128 (2) (k)	Rates and charges or taxes, fees, etc. are reviewed and that due action is taken to revise them from time to time, where necessary, having regard to changes in economic and other circumstances.	Failure to analyse the factors contributed to the fluctuations in the revenue.	2.8 (a) (b)

2. Material and Significant Audit Observations

2.1 Performance

2.1.1 Planning

The following matters were observed.

a) The Action Plan for the year 2017 had not been prepared accurately in terms of Public Finance Circular, No. 01/2014, dated 17 February 2.14
b) An Action Plan had not been prepared in order to achieve the expected objectives of the Excise Rewards Fund established under the Department.
c) The Plan contained the results expected only from the five main functions of the Department. Although there had been 16 main tasks relating to the implementation of the National Authority on Tobacco and Alcohol Act, the activities for the execution of those tasks had not been included in the Plan.
d) Plan on the requirement of imprests for the annual activities had not been prepared.

2.1.2 Failure to Carry Out the Activities

The following observations are made.

a) Failure to carry out the activities shown in the Action Plan

The Department had carried out only 5 out of 8 activities shown in the Annual Action Plan. Due to failure in executing procurements s planned in the Action Plan, provision amounting to Rs. 111 million made on 3 main activities had been saved.

b) Failure to Obtain the Expected Benefits

Examination on the net revenue generated in the year under review and 03 financial years relating to excise (liquor), revealed that the revenue had increased by 52 per cent and 14 per cent in the years 2015 and 2016 respectively whilst the revenue had decreased by 6 per cent in the year 2017.

c) Delays in the Implementation of Projects

The Department had awarded the contract with an estimated value of Rs. 191.83 million for the construction of divisional offices in Chilaw, Ampara, and Kandy expecting the completion of the constructions in March 2018. A sum of Rs. 81.66 million had been spent by 31 December 2017, and the construction works had come to a halt as payments had not been made for the bills furnished by the contractors to the value of Rs. 42.81 million.

d) Achievement of Sustainable Development Goals and Targets

The Department had not become aware of the goals and targets to be achieved in terms of Year 2030 Agenda of Sustainable Development adopted by the UN, and no action had been taken to make provisions thereon by including in the Action Plan.

2.1.3 Annual Performance Report

In terms of Public Finance Circular, No. 402, dated 12 September 2002, the performance report for the year under review should have been tabled in Parliament by the Department within 150 days since the closure of the financial year. However, the report had not been tabled even up to 30 June 2018.

2.2 Procurement Planning

Observations on the procurement plans prepared on the provision of Rs. 282 million made for the supplies and services, are given below.

a) Procurements had been planned without preparing the specifications, and timeframes, etc.
b) According to the Procurement Plan for the year 2017, the procurement of uniform materials and shoes worth Rs. 6,350,000 should have been completed by March – May , 2017. However, only the quotations had been called even up to 10 October 2017.
c) A sum of Rs. 228,203,000 had been estimated in the Procurement Plan of the year 2017 for supplying the safety sticker. However, the procurement value thereof had been estimated to be Rs. 1,782,624,000 by the Ministry of Finance indicating an increase of 681 per cent.

2.3 Assets Management

The following deficiencies were observed in the audit test checks carried out on the assets of the Department.

a) Disposal of assets sans cost and efficiency

Despite being recommended by the reports of the Board of Survey, 09 vehicles withdrawn from use, had not been disposed of even up to June 2018.

b) Annual Boards of Survey

Reports of the Board of Survey should have been furnished to the Auditor General before 15 June 2018 in terms of Section 3.2.6 of the Public Finance Circular, No. 05/2016, dated 31 March 2016. However, such reports pertaining to 22 offices including regional offices and several divisions of the Head Office, had not been furnished to the Auditor General even up to 15 August 2018.

2.4 Losses and Damages

Observations on losses and damages revealed in audit test checks are as follows.

a) A sum of Rs. 128,000 (advertisement fees, and entertainment expenses) had been incurred in the year 2017 on the procurements relating to a computer software for managing the license issuing process, liquor manufacturing process, and tax computation of the Department. Having been observed as a consultancy service procurement by the Procurement Committee once the activities relating to the procurement had been carried out, it had been decided to call for quotations again, and hence, the sum spent was observed to have been a futile expense.

b) The approval of the Cabinet had been given for the lowest bidder for the procurement of the Department to supply the safety stickers for the bottles of liquor and the products relating to the liquor bottles, and supply, installation and maintenance of a management system for the safety stickers. However, as the bidder selected in terms of the Cabinet Decision, No. 16/2556/719/153/TBR, dated 08 November 2016, had not fulfilled the legal requirements for being considered as a reputed joint venture, approval had been granted to call for quotations once again by rejecting the said bidder. Accordingly, the Ministry had called for quotations again, and selected the same bidder himself. The price submitted by the said bidder in the first instance for 1000 stickers amounted to US $ 3.19, but in the second instance, the bid he submitted amounted to US $ 5.99. As such, a sum of US $ 2.80 had to be overpaid for 1000 stickers. Hence, it was observed that the loss likely to be incurred on 384 million stickers in the first year amounted to approximately US $ 1,075,200 (about Rs. 166.65 million)

2.5 Management Inefficiencies

The following inefficiencies were observed in the audit test checks.

a) It had been recommended at the meeting of the Committee on Public Accounts (COPA) held on 26 January 2016 to implement a new computerized information system for the Department with the expectation of linking the Department of Excise, Sri Lanka Customs, and the Department of Inland Revenue. But, the Department had failed to implement the above information system even up to the year under review.

b) A sum of Rs. 1,597,559 had been spent in the year under review on the project for the procurement of supplying the safety stickers, and supply, installation and maintenance of safety sticker management system for the bottles of liquor, and the products relating to the liquor bottles so as to increase the Government revenue. Nevertheless, the Department had failed to implement the budget proposal even up to 12 July 2018.

c) The Commissioner of Excise had sent a notice to a distillery company informing that a tax amounting to Rs. 50,620,739 be paid before 31 December 2015 relating to the offences revealed in the excise investigation carried out on 21 May 2015 on the said company. The Department had appointed committees of investigation with respect to the objections raised by the company against the said notice. Although those committees had recommended that the relevant amount be charged, the Department had failed to recover the amount even by June, 2018.

d) The Department had conducted an investigation on a company that had imported spirits illegally, in addition to the investigation carried out by the Customs. It had been decided through the committee report, dated 13 January 2016 that a tax amounting to Rs. 588,900,344 should be recovered from the company, but that sum had not been recovered even by January 2017. The Minister had granted approval to recover that sum in 30 instalments at Rs. 15,391,208.75 per month. However, whether that decision had complied to the Sections 22 and 32 (2) of the Excise Ordinance (Amendment) was questionable.

2.6 Transactions of Contentious Nature

Some of the transactions performed by the Department were of contentious nature. Particulars relating to several such transactions revealed in the test checks are as follows.

a) It had been emphasized that any type of liquor should not be imported sans an import license in terms of Directive 04 of the Excise Notice, No. 995 published in the Gazette, No. 2009/45, dated 10 March 2017. However, in case liquor was imported sans a license, the Directive, No. 05 of that Notice stated that the Commissioner General had the authority either to charge a surcharge of 3 per cent on the CIF Value in addition to the tax, or confiscate the stock of liquor being imported. Accordingly, the condition allowing to clear the liquor imported illegally by paying a surcharge of 3 per cent was too lax, and hence, it was questionable in audit as to whether the illegal imports would be controlled in that backdrop. According to the test check conducted, a surcharge of 3 per cent had been charged on a volume of 35,815.3 litres of liquor imported illegally by 4 companies in 07 instances during the period from 22 March to 22 June 2017.

b) According to the survey plan, a school had been located within a distance of 169.98 meters. However, action had been taken to grant a license on strong foreign liquor and arrack for a film hall in Thissamaharama without fulfilling the condition relating the specified distance for spot consumption.

2.7 Utilization of Provision Made by the Department for the Execution of Activities.

Information relating to the utilization and saving of the provision made for the Department during the period of 05 years ended as at 31 December 2017 along with the audit observations thereon, are shown below.

Year	Type of Expenditure	Net Provision Rs. Million	Utilization Rs. Million	Saving Rs. Million	Saving as a Percentage of the Net Provision
2013	Recurrent	493.96	492.52	1.44	0.29
	Capital	174.50	172.22	2.28	1.30
	Total	668.46	664.74	3.72	0.55
2014	Recurrent	547.95	547.86	0.09	0.01
	Capital	182.50	150.42	32.08	17.57
	Total	730.45	698.28	32.17	4.40
2015	Recurrent	666.62	665.08	1.54	0.23
	Capital	387.91	147.46	240.45	61.98
	Total	1054.53	812.54	241.99	22.94
2016	Recurrent	745.66	743.09	2.57	0.34
	Capital	326.77	240.88	85.89	26.28
	Total	1072.43	983.97	88.46	8.24
2017	Recurrent	1039.50	806.51	232.99	22.41
	Capital	272.52	160.36	112.16	41.15
	Total	1312.02	966.87	345.15	26.3

The following observations are made relating to the year under review.

Failure in the Utilization of Provision Allocated

(i) Although provision amounting to Rs. 18.6 million had been approved through supplementary estimates in the year under review for the project of implementing the system relating to production regulation and automated tax computation, that provision had saved entirely.

(ii) As overprovision totalling Rs. 452 million had been made on 06 Items of Expenditure, the saving after utilization amounted to Rs. 307 million. Accordingly, 40 per cent to 94 per cent of the provision made for the Items of Expenditure, had been saved.

2.8 Estimated and Actual Revenue

The Department had estimated revenue totalling Rs. 115,035 million under 02 Revenue Codes for the year 2017 whereas a revenue totalling Rs. 113,259 had been collected in the year under review representing 98 per cent of the estimated revenue. Particulars are as follows.

Revenue Code	As at 31 December 2017			Collected Revenue as a percentage of the Estimated Revenue
	Estimated Revenue	Actual Revenue	Excess/(Deficit)	
	Rs. Million	Rs. Million	Rs. Million	
10.02.04.01	115,000.00	113,214.00	(1786.00)	98
10.02.06.00	35.00	45.75	10.75	130

The following observations were made in the audit carried out on the aforesaid Revenue Accounts.

a) Revenue Code - 10.02.04.01 - Excise Duty (Liquor)

(i) Due to decline in the production of strong liquor in the year under review, the revenue estimates prepared at the beginning of the year had been revised. But, despite the increase in the taxes levied on liquor from November 2017, action had not been taken to revise the revenue estimates by considering the increased revenue.

(ii) According to the Revenue Account made available to Audit, revenue totalling Rs. 1,233.16 million had remained due, and the said revenue in arrears had continued to exist over a period of 01 – 05 years. The follow-up action on the recovery of revenue in arrears remained poor.

(iii) The decrease in the actual income of the year under review as compared with that of the preceding year, amounted to Rs. 7,024 million. The following observations are made in that connection.

- The policy of levying a tax of Rs. 1,850 per litre of liquor with standard strength that had been issued after being manufactured, was revised to be Rs. 3,300 per litre with effect from November 2017 as per the budget proposals for the year 2017. Accordingly, the production of the year under review had decreased by 8.6 million litres.

- It was decided in accordance with budget proposals for the year 2017 that the policy of levying a tax of Rs. 315 per litre of malt liquor produced of which the absolute strength was 5 per cent or more, or

Rs. 190 per litre otherwise, should be revised in a manner that a tax of Rs. 2,400 be levied per litre of malt liquor produced and issued since November 2017. Accordingly, the tax revenue on the malt liquor was increased by Rs. 2,795 million in the year under review, but the production thereof was decreased by 3.7 million litres.

b) Revenue Code – 10.02.06.00 – Tobacco Tax

The following deficiencies were observed.

(i) The initial revenue estimate on the tobacco tax for the year under review amounted to Rs. 35 million whereas the actual revenue amounted to Rs. 45.74 million. The increase in the tax revenue on imported cigarette and tobacco by a sum of Rs. 6 million in the year under review as compared with the preceding year, mainly attributed thereto.

(ii) The Department issues licenses for exporting cigarettes. The Department had not prepared a methodology to verify that the quantity reported to have been exported had actually been exported.

(iii) In terms of Section 02 of the Tobacco Tax Act, No. 08 of 1999, there shall be charged, levied, and paid on every cigarette, cigar, beedi, cigarette substitute and every kilogram of pipe tobacco manufactured in Sri Lanka, a tax at such respective rates as may be fixed by the Minister by Order published in the Gazette. However, the Department charged the tobacco tax only on cigarettes. As such, it was observed in audit that the Department did not comply with the Tobacco Tax Act.

2.9 Advances to Public Officers Account

Limits Authorized by Parliament

The limits and actual values authorized by Parliament on the Advances to Public Officers Account under Item Code 24801 of the Department, are as follows.

Expenditure		Receipts		Debit Balance	
Maximum Limit	Actual	Minimum Limit	Actual	Maximum Limit	Actual
Rs. Million	Rs. Million	Rs. Million	Rs. Million	Rs. Million	Rs. Million
45.00	44.57	34.00	34.43	177.00	140.08

The following observation is made in this connection.

According to the reconciliation statement made available to Audit, the total of the outstanding balances amounted to Rs. 2,783,872 as at 31 December 2017. A sum of Rs. 1,047,185 included in the said balances had continued to exist over a period of 1-5 years whereas a sum of Rs. 543,714 had remained unrecovered for a period of more than 05 years. The Department had failed to recover those balances in arrears.

2.10 General Deposit Account

Action had not been taken in terms of Financial Regulation 571 on 45 deposits totalling Rs. 2.34 million and older than 02 years.

2.11 Deficiencies in Operating Bank Accounts

Action had not been taken in terms of Financial Regulation 396 (d) on 10 cheques valued at Rs. 16,866 and older than 06 months that had not been presented to the bank despite being issued.

2.12 Failure to Maintain Books and Registers

It was observed in audit test checks that certain registers had not been maintained properly and in an up-to-date manner whilst the following registers had not been maintained by the Department.

	Type of Register	Relevant Regulation	Observation
(i)	Register of Fixed Assets relating to computer accessories and software.	Treasury Circular No. IAI/2002/02, dated 28 November 2002	Not maintained.
(ii)	Register of Fixed Assets	Treasury Circular No. 842, dated 19 December 1978.	Not updated.

2.13 Non-compliances

Non-compliances with Laws, Rules, and Regulations, etc.

Action had not been taken even up to 15 August 2018 to furnish reports that should have been furnished in terms of Financial Regulation 104 (3) relating to 02 vehicle accidents taken place in the year under review.

2.14 Internal Audit

It is required as per Financial Regulation 133 that the Accounting Officers should establish Internal Audit Units in their Departments in order to carry out duties and functions mentioned in Financial Regulation 128. The following observations are made in that connection.

(a) The activities mentioned in the internal audit program prepared with respect to financial affairs, such as collection of excise duties, inspection of imprest account, inspection of Reward Fund, and assets management, had not been carried out.

(b) As per Financial Regulation 133, the Internal Audit Unit should continuously carry out internal audits so as to determine the reliability of accounts and reports, and prepare accurate financial statements in accordance with the accounting policy being followed. Nonetheless, it had not been so done.

2.15 Human Resources Management

2.15.1 Expenditure on the Staff Attached, Actual Cadre, and Personnel Emoluments

Particulars on the actual, vacant, and excess cadre as at 31 December 2017 are as follows. The Department had spent a sum of Rs. 656.786 million on personnel emoluments in the year under review. As such, the expenditure per employee amounted to Rs. 491,974.

Category of Employee	Approved Cadre	Actual Cadre	No. of Vacancies	No. in Excess
(i) Senior Level	66	40	26	-
(ii) Tertiary Level	380	342	38	-
(iii) Secondary Level	868	790	106	28
(iv) Primary Level	172	163	09	-
Total	1,486	1,335	179	28

The following observations are made in this connection.

(a) Sixty four posts in the senior and tertiary levels that could directly affect the mission of the Department had remained vacant since the years 2015 and 2016. It was also observed that the future performance of the Department would be negatively affected as a majority of the officers were on the verge of retirement.

(b) Action had not been taken to obtain approval for 28 officers in excess of the number of posts of Inspector .

(c) Although 100 posts of Sergeant had been approved for the Department, 85 posts that had fallen vacant owing to miscellaneous reasons from the year 2013 up to the year 2016 had remained so even as at 31 December 2017.

2.15.2 Training the Staff

The following observations are made.

(a) It was observed that at least a training of 08 hours per year had not been provided for over 47 per cent of the 1335 employees of the Department.

(b) It was observed that the Department had not adequately brought its attention to acquire a high level of performance by providing subject-oriented knowledge and training for the employees of the Department in view of accomplishing the mission.