

Kurunegala Plantations Limited - 2018

1.1 Qualified Opinion

The audit of the financial statements of the Kurunegala Plantations Limited for the year ended 31 December 2018 comprising the statement of financial position as at 31 December 2018 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, 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 provisions of the National Audit Act No. 19 of 2018. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the accompanying financial statements give a true and fair view of the financial position of the Company as at 31 December 2018, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Qualified Opinion

My opinion is qualified based on the matters described in Paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Company.

1.4 Scope of Audit (Auditor's Responsibilities for the Audit of the Financial statements)

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.
- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to

enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company;
- Whether the Company has performed according to its powers, functions and duties; and
- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Comments on Financial Statements

1.5.1 Non- compliance with Sri Lanka Accounting Standards

The following observations are made.

Non- compliance	Comments of the Management	Recommendation
<p>(a) Although the assets should be depreciated from the time when they are ready for use in accordance with Sri Lanka Accounting Standard No. 16, due to the asset was not depreciated in the year it was purchased in contrary to that and totally depreciated in the year of sale, depreciation expense for the year under review had been understated by a sum of Rs. 1,450,603 .</p>	<p>Action will be taken to correct it by 2019 accounts.</p>	<p>Fixed Assets should be depreciated in case of ready for use as per the Standard.</p>
<p>(b) According to Paragraph 51 of the Sri Lanka Accounting Standard No.16, vehicles cost at Rs. 107,775,018 which were completely depreciated but currently used and buildings cost at Rs. 17,693,752 had not been re-assess and taken into accounts.</p>	<p>Actions will be taken to re-assess the vehicles and since the buildings have been received on lease there is no need to assess.</p>	<p>Actions should be taken to re-assess the assets which were fully depreciated and to re-assess the currently used assets and taken into accounts as per the Standard.</p>
<p>(c) Even though the Biological Assets should be valued at fair value as</p>	<p>Actions will be taken to correct it by 2019</p>	<p>According to the Standard, the</p>

per Sri Lanka Accounting Standard accounts. No. 41, because of the lack of assessment accordingly, those assets had been understated by a sum of Rs. 994,790.

livestock should be assessed at fair value and shown in the accounts.

1.5.2 Accounting Policies

Audit Observation

According to the accounting policy of the Company, although the cost of development of the land acquired on lease should be amortized over 30 years, the amortization has not been adjusted for that expenditure of Rs. 4,019,754 incurred after the year 1992 .

Comments of the Management

Actions will be taken to correct it by 2019 accounts.

Recommendation

According to the accounting policy of the Company, the costs incurred for the development of the land should be amortized during the relevant time period.

1.5.3 Accounting Deficiencies

Audit Observation

Instead of being written off as an expense , the expenditure of Rs. 8,123,564 made to the Divisional Secretary of Kurunegala on 11 November 2015 for the acquisition of tenure of 1.416 hectares of land in extent by the Company during the intended period to use the relevant land, it had been shown as an asset in the Financial Statements.

Comments of the Management

As there are no timelines are provided, in relation to the return of the property to the value of Rs 8,123,564 as specified by the Court, the terms and conditions only for use are included, this land has been registered as freehold property .

Recommendation

Actions should be taken to obtain legal ownership to the Company and arrangement should be made to take in to accounts as a deferred asset if that right is not received.

1.5.4 Lack of Evidence for Audit

Audit Observation	Comments of the Management	Recommendation
<p>Out of the 1,751 hectares of land in extent allotted to the Company at the time of established, had again been released for various purposes of the government and the register of parties the lands released regarding 550.88 hectares of land in extent included in that valued at Rs. 16,214,000 had not been submitted for audit.</p>	<p>This observation was continuously made and the land surveying activities is being carried out by the Ministry of Plantation Industries. Although the Ministry has carried out 78 surveys of the 87 Divisions of the Company, the Company has not received the reports and decisions relating to changes in land surveying should be made by the competent authorities.</p>	<p>The lands allotted to the Company and the lands not currently occupied, identify the released parties and should submit them for audit.</p>

1.6 Non-compliance with Laws, Rules, Regulations and Management Decisions

The following observations are made.

References to Laws, Rules, Regulations, etc.	Non-compliance	Comments of the Management	Recommendation
<p>(a) Financial Regulations of the Democratic Socialist Republic of Sri Lanka 108 (3)</p>	<p>Although whenever a Chief Accounting Officer is not authorized to deal with damages he should seek the approval of the Treasury, the cost of damaged rubber and other plantations amounting to Rs. 11,110,806 had been written off from the accounts of the year 2017 without obtaining</p>	<p>Although the cost incurred for these projects which were commenced as pilot projects should be taken in to accounts under research and development expenses, had been capitalized and that cost was brought to accounts in the year 2017 as expenses. This is being investigated by a Committee appointed</p>	<p>Writing off of damages should be made after obtaining approval in accordance with Financial Regulations.</p>

- the relevant by the Board of approval. Directors.
- (b) Management Services Circular No. 39 of 26 May 2009
- Although the recommendation of the National Salaries and Cadre Commission and approval of the Department of Management Services should be obtained when determining the payment of allowances to officers, without doing so, 31 officers of JM and the salary categories in above that were paid a total of Rs. 10,835,213 as “Labor Allowance” in the year under review.
- This allowance is an allowance relevant to the plantation sector and it is eligible to Executives Officers from the inception of the Company and even though the enough employees were available in the past, since there is a shortage of employees at present, this is paid as an allowance. This for-profit Company competes with the private sector without obtaining money from the Treasury and submission of these impractical audit queries has led to an increase of the leaving of employees from service and to reduce the employee attraction.
- When making payment of allowances for officers, the allowance should be paid as per the approval of the Circular.
- (c) Public Enterprises Circular No. 01/2015 dated 25 May 2015
- A sum of Rs. 1,140,506 for 10,435 liters of fuel had been paid during the year under review for the 05 officers in MM salary category who were not entitled to fuel allowance as per the Circular.
- It is not accurate to mention the officers in the MM wage category were not entitled to receive fuel allowance as per your audit query because they are Senior Officers of the Company. It is problematic to manage without providing fuel to Senior Executives of the Company and if
- Whenever a fuel allowance is paid, it should be paid only to the relevant authorities as per this Circular.

the such audit queries are provided for fueling the officials of this profit making organization, it is problematic how such a Company operates and it is not fair to mention 05 officers in the MM salary category when there are 12 officers available.

2. Financial Review

2.1 Financial results

The operating results for the year under review was a profit of Rs. 188,994,219 and the corresponding profit for the preceding year was Rs. 161,797,211 . Accordingly, a growth of Rs. 27,197,008 in financial results was observed. The increase in coconut sales in the year under review had mainly attributed to this growth.

2.2 Trend Analysis on Major Income and Expenditure Items

- (a) The Coconut production and coconut sales by 19 per cent, plant sales income by 17 per cent and costs of coconut production had been increased by 20 per cent whilst copra income declined by 56 per cent in the year under review as compared to 2017.
- (b) As result of he selling price of a kilogram of rubber reduced by Rs. 65 per, decrease in production of Latex by 6,401 kg and the increase in the cost of production of one kilogram of rubber by Rs. 16, the income of rubber declined by 23 per cent in the year under review as compared to the preceding year.

3. Operating Review

3.1 Uneconomic Transactions

Audit Observation

Comments of the Recommendation Management

Although the cost of living allowance should be considered in calculating contributions under the Employees' Provident Fund Act, due to the fact that the Company had not considered the

The payment has been made after obtaining the approval of the Board of Directors with the surcharge whilst the

Contributions should be calculated and paid according to the total earnings in accordance with the Employees

allowance for the period 2006-2015 when make payment for relevant contribution, in addition to that allowance a sum of Rs. 5,729,125 had been paid as surcharges when payment of the allowance relevant for that period in the year under review.

disclosure made by the relevant institution that the Cost of Living Allowance was not applicable in the payment of Employees Provident Fund during 2006-2015.

Provident Fund Act.

3.2 Management Inefficiencies

The following observations are made.

Audit Observation -----	Comments of the Management -----	Recommendation -----
<p>(a) As a result of lack of required raw materials to maintain maximum production capacity and due to inadequate sales revenue the rubber factory which was started incurring a sum of Rs. 12,078,708 without conducting a feasibility study in the year 2016 production activities had been stopped by the end of the year. Accordingly, the cost of Rs. 12,078,708 incurred for the factory had become a futile expense.</p>	<p>In the construction of the rubber factory, even though it has been decided to use the production of Latex in Attanagalla and Mahayaya Estates for the manufacture of smoked rubber in the rubber factory, due to the gradual decline in the price of smoked rubber sheets, the company has decided to close down the factory as it would benefit the Company from selling Latex to outsiders rather than the productions of the factory.</p>	<p>Arrangements should be made to carry out a feasibility study for such projects and to make study on availability of raw materials, the production methods and the prospective markets and to sell by formulating the productions as it suits.</p>
<p>(b) The leases relating to land acquired by the Company on lease payments should be made to the Ministry of Plantation Industries and as a result of not obtaining concurrence of the Ministry for the decision taken not to pay the lease for 1,751 hectares releasing the leased lands for various purposes of the government and the Company had informed the Ministry to pay the lease amounting to</p>	<p>The Company has accounted for only the amount of leases pertaining to the extent to which the Company is entitled from the assets acquired on a lease basis, the Ministry of Plantation Industries calculates the total asset</p>	<p>Once the concurrence was taken from the parties agreed, actions should be taken to terminate the payment.</p>

Rs. 197,581,091 by the end of the year under review. value of the lease at the time of the launching of the company. However, the company has made requests that the issue be resolved jointly with the Ministry of Plantation and the Treasury.

3.3 Operating inefficiencies

The following observations are made.

Audit Observation	Comments of the Management	Recommendation
<p>(a) Although the annual average yield of a coconut palm should be about 72 nuts according to the standards of the Coconut Research Institute, and that amount of 07 estates controlled by the Company were in the range of 31-54 and steps have not been taken to set up to achieve that goal by the Company to conduct soil testing and apply fertilizer and chemicals accordingly and establish necessary irrigation systems and obtain new yield.</p>	<p>According to the recommendation of the Coconut Research Institute, 72 nuts can be obtained from the tree under only optimum conditions. But this value varies depending on soil type and weather conditions. As per the recommendations of the Coconut Research Institute, under normal conditions, nearly 50 nuts can be obtained from a coconut palm. It is informed that we are planning to increase the coconut yield from a tree by improving the supervision furthermore introducing water conservation and water supply schemes.</p>	<p>The Company should maintain a coconut plantation with a minimum gain of 72 nuts per tree.</p>
<p>(b) Although according to the industry norms, there should be 158 coconut trees per hectare of land, , the Company had not taken steps to increase it to a standard number of 92-141 in the remaining 06 Estates except for Narammala and</p>	<p>Even though the availability of number of trees should be 158 trees theoretically, due to unsuitable lands for cultivation , that extent cannot be practically cultivated. Actions are</p>	<p>Arrangements should be made to maintain 158 trees which were the minimum number of coconut trees existed in a hectare .</p>

Katugampola Estates.

being taken by now to carry out survey and identify all cultivated areas accurately using GPS Technology.

- (c) Due to inauguration of 2000 vines of pepper cultivation in the Imbulgoda Section of Dodamgaslanda Estate without doing a soil test by the Company in the year 2009, about 1000 plants were destroyed by the end of the year and the amount of Rs. 1,690,314 incurred thereon had become a futile expense. Further, there were 615 vines out of the remaining 1000 vines and according to the data of the Department of Minor Export Crops, the minimum yield required by the vines was 1107 kilograms of dry pepper, the Company had harvested 36.5 kilograms.
- It is accepted that some of the pepper vines of this division were destroyed by the incompatibility with the soil and have not been planted in the spaces again. Although the gravel sites were irrigated in previous years during severe droughts, plants were destroyed by severe temperatures. But it is being harvested from the existing vines.
- Actions should be taken carrying out technical studies on suitability of the land used for cultivation before the commencement of cultivation and in respect of irrigation systems accordingly.
- (d) Although every tree should be fertilized annually for mature cultivation according to the recommendations of the Coconut Research Institute, out of the 222,118 mature trees in the four Estates Company, only 95,037 trees were used to be applied chemical or organic fertilizer and the management had not taken steps to increase the yield by using fertilizer for the remaining trees.
- The policy of the Company is that the 50 per cent of mature coconut palms were manure in the previous year and the remaining 50 per cent in the following year and apply the fertilizer to all trees nearly a period of one year. Since the Company has a large number of mature coconut palms, as the ongoing labor shortage it was not possible to apply fertilizer during rainy season.
- According to the recommendations of the Research Institute, fertilizer should be applied to each coconut tree within a year.
- (e) According to the recommendation of the Coconut Research Institute, 1 kilogram of dolomite should be applied to
- The Company considered about the lack of magnesium exists in the coconut cultivation and Dolomite fertilizer should be used in the recommended quantities of the

every mature coconut palm whereas the chemical fertilizers apply, the company had used 2.4 kilograms of dolomite per tree for 80,844 trees. As a result, the Company had incurred an futile expense for 110,586 kg of dolomite.

decline in P.H due to washing of soil, it has been decided to apply 2 kg of dolomite to all nuts bearing coconut palms.

Research Institute.

3.4 Procurement Management

Audit Observation

When obtaining a consultancy for bid evaluation in accordance with Paragraph 7.3.1 of the Procurement Guidelines, although those advisors should not be the members of the Technical Evaluation Committee, a Consultancy firm conducting bid evaluation on 03 construction works valued at Rs. 6,529,930 had also acted as a Chairman and as well as Member of the Technical Evaluation Committees appointed for the construction.

Comments of the Recommendation Management

In terms of Section 2.8.4 of the Procurement Guidelines, there should be a member who has expertise in the subject and although the expertise had been obtained by the Technical Evaluation Committee when necessary, those members have not influenced the independence of the Committee Decisions. The parties who provide advisory services were not appointed as members of the Technical Evaluation Committee after the year 2018 .

When obtaining a consultancy for bid evaluation in accordance with Paragraph 7.3.1 of the Procurement Guidelines, those consultants should not be appointed as members of the Technical Evaluation Committee

3.5 Deficiencies in Contract Administration

Audit Observation

Comments of the Management

Recommendation

As per the agreement signed between the Company and the Buyer on 19 September 2017 relating to the removal of 2077 rubber trees from the Dodamgaslanda Panagamuwa Division and the Company had failed to do the related activity within 90 days and the contractor had spent an additional 210 days to complete the work. Accordingly, the planting of 17,780 cinnamon plants that had been planned to be set in the land had been delayed.

As a result of the matters such as weather conditions and the additional time taken to call for tenders, the absence of employees the contract period has been extended and the cinnamon plants have been planted in the year 2018 as per the relevant estimates.

Arrangements should be made to complete in accordance with the Contract Agreement and if there are not enough reasons furnished for requests made for unusual time extensions actions should be taken to recover damages.