

## **Kurunegala Plantations Limited - 2022**

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### **1. Financial Statements**

#### **1.1 Qualified Opinion**

The audit of the financial statements of the Kurunegala Plantations Limited (“Company”) for the year ended 31 December 2022 comprising the statement of financial position as at 31 December 2022 and the statement of comprehensive income, statement of changes in equity, and cash flow statement for the year then ended and notes to 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 and Companies Act, No. 07 of 2007. My comments and observations which I consider should be presented in Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the financial statements give a true and fair view of the financial position of the Company as at 31 December 2022, and its financial performance and 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 (SLAuS). 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 determines 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 Sub-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 Audit Scope (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 scepticism 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 Audit Observations on the Preparation of Financial Statements**

### **1.5.1 Non-compliance with Sri Lanka Auditing Standards**

<b>Non-compliance with Reference to the Relevant Standard</b>	<b>Comment of the Management</b>	<b>Recommendation</b>
<p>Due to failure in annually reviewing the useful life of non-current assets contrary to Paragraph 51 of the Sri Lanka Accounting Standard 16, the assets fully depreciated as at 31 December 2022 such as, office equipment valued at Rs. 13,134,390, furniture valued at Rs. 6,969,684, and computers valued at Rs. 3,825,790, had still been in use. Nevertheless, action had not been taken to correct the estimated error in accordance with Sri Lanka Accounting Standard 08 thereby failing to show the accurate carrying amount in the financial statements.</p>	<p>It is stated in Paragraph 51 of the Sri Lanka Accounting Standard 16 that useful life of non-current assets should be annually reviewed, but the useful life of assets mentioned herein has exceeded. However, the reason for such assets to be still in use is that a higher maintenance cost had been incurred thereon.</p> <p>With office equipment and computers being gradually withdrawn from use, new equipment is obtained. Fixed assets will be verified in this year and the assets withdrawn from use at present will be eliminated from books. It is also expected to eliminate the other assets from books in accordance with Sri Lanka Accounting Standard 16 (8).</p> <p>The assets fully depreciated, have been shown under Note 13 to the accounts.</p>	<p>Carrying amount of the fully depreciated assets should be revised, and the correct value should be shown in the financial statements.</p>

## 1.5.2 Accounting Deficiencies

Audit Observation	Comment of the Management	Recommendation
<p>a) Assets such as, the office building, the green house, and the irrigation system used for the ornamental plant cultivation maintained at the Attanagalla estate had been given on lease to a third party on lease for a period of 05 years, and the lease rent income therefrom had been included in other income. As the sum of Rs. 1,093,414 being the value of amortization on assets relating to that project, had been included in the cost of sales, thus observing that the cost of sales had been overestimated whilst the gross profit had been underestimated by the same amount.</p>	<p>The assets relating to the cultivation of ornamental plants being maintained by the Attanagalla Estate have been properly identified. Such assets are depreciated based on the useful life thereof, and recognition of depreciation as cost of sales, is correct. The income earned from this project given on lease, is recognized as lease rent income. The estates recognize the cost of sales. All the expenses on that unit are accounted for under cost of sales. Nevertheless, this project had been fully depreciated by November 2022.</p>	<p>The value of cost of sales should be corrected by correctly accounting for the amortization of assets.</p>
<p>b) The sum of Rs. 546,632 had been shown in the statement of financial position as the value of biological assets acquired. Nevertheless, that value had been shown as Rs. 1,643,921 under investment activities in the cash flow statement.</p>	<p>A sum of Rs. 1,643,921 had been shown as an outflow under the cash flow generated through investment activities. The said value comprised development expenses amounting to Rs. 546,632 and expenses relating to the sale of timber amounting to Rs. 1,097,289. Despite being shown in the accounts correctly, the value had been shown as “addition of consumable biological assets in the description”. Corrective measures will be taken thereon in the ensuing financial year.</p>	<p>Expenditures and assets should be correctly accounted for in the financial statements.</p>

## 1.5.3 Document Evidence not made available for Audit

Item	Amount Rs.	Audit Evidence Not Furnished	Comment of the Management	Recommendation
Property, Plant and Equipment	41.6 million	As the Company did not possess plans for leased lands pertaining to 16 divisions of estates in extent of 1,478 hectares and valued at Rs. 41,600,178 shown under	Although it was mentioned that there were 16 divisions sans plans, the Company has received plans relating to the divisions of Kurakkana and Madhurakanchiya mentioned in the said Annex. Accordingly, there were 14	Agreements and plans for verification of the rights to the leased lands, should be prepared and approved.

Property, Plant and divisions for which plans Equipment in the surveyed by the Department of statement of financial Survey, had not been provided. position, the legal rights to the lands vested in the Company in the year 1992, could not be verified.

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

Reference to Laws, Rules, and Regulation, etc.	Non-compliance	Comment of the Management	Recommendation
a) Sub-section (5)(1) of Part 02 of the Payment of Gratuity Act, No. 12 of 1983, and Payment of Gratuity (Amendment) Act No. 62 of 1992.	Gratuity should be paid to the relevant person or his heirs within a period of 30 days since his date of retirement or death. However, there existed a balance of gratuity totalling Rs.2,066,450 payable with respect to Head Office and 05 estates in more than 180 days. That balance comprised sums payable since 2016. That balance had not been settled even by 20 March 2023, and surcharges totalling Rs. 18,754,389 remained payable by the end of the year 2022 due to failure of the Company in paying gratuity on time.	It was mentioned in the audit query sent by you in the year 2016 that the scheme for paying gratuity based on monthly salary, was against the laws and rules, but the payable gratuity balance had not been based on half-month salary. It was informed by the Department of Labour that such a payment being enjoyed by the employees, could not be discontinued unilaterally. The Company had to release the outstanding gratuity along with surcharges in accordance with cases filed at the appellate court and supreme court.	An audit query is sent during the auditing process only to summon information. Rather than discontinuing the payment of gratuity based thereon, decisions should be taken with emphasis on the relevant legal background.

- b) Section 38 (1) of the Inland Revenue Act, No. 45 of 2022. The income tax payable by a person for the year of assessment beginning from 01 April 2022, should have been computed for the first half year and second half year separately. But, the Company had done so by dividing the year into two periods being the first nine months and the last three months. Furthermore, as per Section 33 (3) (ii) of the said Act, tax should have been computed at 24 per cent for the first six months whilst the rate for the second half was 30 per cent with respect to the year of assessment beginning from 01 January 2022. However, the Company had failed to comply with that requirement, and hence, expenditure on tax and payable tax balance had been understated by Rs. 2,303,821.
- Given the fact that the new amendments to the Act relating to Companies had become effective from 01 October 2022, the income tax payable by a Company should be computed separately for the first half year period and the second half year period. However, the investment income under the taxable income, should be computed on actual basis as per the Guideline. Accordingly, the income tax payable on investments for the said assessment year had been taken into consideration based on the period of maturity; and, hence, income tax had been recovered at the rates of 24 per cent or 30 per cent.
- The first and second half years should be correctly identified thereby computing tax at the relevant rates in accordance with provisions of the Inland Revenue Act.
- c) Section 90 of the Inland Revenue Act No. 24 of 2017. Tax should be paid in installments on or before the fifteenth day after each three-month period commencing at the beginning of each year of assessment and a final instalment on or before the fifteenth day after the end of each year of assessment, unless it coincides with the end of one of the three-month periods. Nevertheless, the Company had not complied with that requirement.
- The balance of taxable income is the interest which varies based on the period of maturity (tax based on investment income under cash basis). As such, the Company had not tax quarterly as mentioned in provisions of the Department of Inland Revenue. The Company shall comply with such regulations in due course.
- Installments of tax should be paid in accordance with provisions of the Inland Revenue Act.

- d) Section 6 (1) of the Inland Revenue Act No. 24 of 2017. As a sum of Rs. 5,756,571 included in other revenue had not been taken into consideration in computing the taxes, liability of the Company for tax had been undervalued by Rs. 1,554,274. As for the tax objectives of the Company, it is considered by the Company that the income earned through firewood and soil is productively related to the business. As such, the said revenue is a constituent of the business activities of the Company. When computing the income tax, all the sources of revenue should be taken into consideration.

## 2. Financial Review

### 2.1 Financial Results

Operating result of the year under review was a profit of Rs. 472,374,439 as compared to the profit of Rs. 447,954,706 for the preceding year, thus observing an improvement of Rs. 24,419,733 in the financial result. This improvement had mainly been attributed by the increase in sales revenue of other crops including coconut and rubber by Rs. 110,922,328 and increase in other revenue by Rs. 21,761,703 as compared to the preceding year.

### 2.2 Ratio Analysis

- By the end of the year under review, the current ratio and quick ratio of assets indicated 4:1 whereas that ratio stood at 6:1 in the preceding year.
- The gross profit ratio of the year under review was 48 per cent, and comparison of that percentage to the preceding year being 56 per cent, indicated a decline in gross profit ratio by 8 per cent.
- The net profit ratio of the year under review was 44 per cent, and comparison of that percentage to the preceding year being 48 per cent, indicated a decline in net profit ratio by 4 per cent.

## 3. Operational Review

### 3.1 Idle or Underutilized Property, Plant and Equipment

Audit Observation	Comment of the Management	Recommendation
An area of 72.4 acres out of 129 acres of paddy lands owned by the Company had been given on lease and to tenant farmers for the Yala Season of 2022 whereas an extent of 78.08 hectares had been so given for the Maha Season. It was observed that 56 hectares and 50.92 hectares of paddy	The extent of 129 hectares of paddy lands mentioned herein, had existed as per the reports of the Company though, the Company does not possess such an extent of paddy lands. The reasons in that connection included, lands had been vested in the Company without properly surveying, and lack of accurate data on	Underutilized paddy lands should be identified thereby taking action to cultivate such lands without delay.

lands had remained idle during the Yala Season and Maha Season respectively. the number of paddy lands given to the tenant farmers due to lack of interest of the farmers in obtaining paddy lands on lease following difficulties faced by them.

### 3.2 Management Inefficiencies

Audit Observation	Comment of the Management	Recommendation
a) The activity “sending value added products of the Company to the export market” had been mentioned as a target in the Action Plan for the period 2021-2025 and business plan of the Company. However, no action whatsoever had been taken in that connection in the year 2022.	Due to reasons such as, the economic crisis in the country and inability to reach the export market, the value added products of the Company could not be sent to the export market.	Action should be taken to achieve the targets mentioned in the business plan and the Action Plan.
b) Twenty two teak trees had been included in the survey book as biological assets of Nadungolla division of the Attanagalla estate in the year 2022. However, it was observed as per the survey register presented by the Estate Superintendent after a subsequent survey that there were 67 teak trees suitable to be assessed . Accordingly, it was observed that the value of biological assets of the Kurunegala Plantations Ltd amounting to Rs. 288,423,832 in the year 2022, had been undervalued by 45 teak trees equivalent to Rs. 2,970,000.	Survey books relating to biological assets, should be updated by the relevant estate companies yearly. Trees with a girth of over 45 centimeters should be recorded in survey books.	Reports on survey of assets should be accurately maintained, and values of biological assets should be correctly accounted for.
c) An initial estimate had not been prepared for construction of the watchman’s hut at the Halgahapitiya Division of Attanagalla Estate. A Bill of quantities had not been prepared as well by adjusting the necessary materials and the approved rates. As purchases had been made without an estimate and a Bill of quantities, the quantities required and the quality could not be verified in audit.	The watchmen’s hut for provincial estates of the Kurunegala Plantations Ltd are constructed according to the same plan. Copies of the Bill of quantities and the plan prepared by the Company in the year 2021, had been provided for the Estates in accordance with Circular 2021/35 dated 23.12.2021. The relevant estimate could not be annexed to the file by mistake; and, the management of the Estate and the Technical Officer	When constructions are made, the BOQs should be prepared based on accurate plans. A Technical Officer should verify the applications, standard, and quality of materials being purchased by following the rates effective at the province.



are responsible for following the procurement procedure, selection of a suitable contractor, purchasing the materials as per the Bill of quantities under instructions of the Technical Officer and supplying to the contractor, and ensuring quality; thus, payments are made.

- d) When constructing the watchman's hut, a standard BOQ had not been forwarded to the Technical Evaluation Committee of the Committee in order to prepare the technical specifications thus failing to call for quotations from a qualified contractor. Furthermore, quotations had been called for materials and labor separately, and suppliers had been selected based solely on their prices.
- Due to reasons such as, those constructions were small-scale ones, scarcity of materials in that year, and other reasons, prices of the materials became higher. As such, the suppliers were reluctant to give quotations.
- Contractors should be selected by following the Procurement Guidelines properly.
- e) It was observed that decisions on the amounts of materials and prices for construction of the watchman's hut, had been taken by inquiring the same contractors who had come up with bids. Furthermore, the specifications required by the relevant company for constructions, had not been taken into consideration when calling for quotations, thus losing the opportunity to purchase building materials of higher quality at minimum cost. Furthermore, purchases of building materials had been done in excess.
- When items were purchased by the Estate, quality of the materials were taken into consideration by following the Procurement Guidelines. As the constructions progressed, the 85 bags of cement already purchased had become insufficient, 15 more bags of cement were also purchased.
- When purchasing building materials, items of higher quality should be purchased at minimum costs by considering the rates of the Commissioner of Local Authorities.
- f) Surveying of 71 divisions out of 87 divisions pertaining to 6,722 hectares of land as at the date of acquisition by the Company, had been completed. A shortage of 533.58 hectares in 53 divisions and an excess of 77.66 hectares in 18 divisions had been identified.
- Once surveying of all divisions are completed, it is informed that the difference between the extent of lands given by the Janatha Estate Development Board and the extent of lands identified in surveys, will be calculated.
- Extent of lands should be correctly identified by completing the surveys. Thus, the values should be mentioned in the financial statements.

### 3.3 Delays in Projects or Capital Works.

<b>Audit Observation</b>	<b>Comment of the Management</b>	<b>Recommendation</b>
Although it was scheduled in the business plan of the year under review to install a computerized accounting system, no action required in that connection had been taken even in the year 2022 as well.	Installation of the said system is in progress at present.	Success of projects should be ensured by complying with the business plan and by obtaining approval for amendments.

### 3.4 Operational Inefficiencies

<b>Audit Observation</b>	<b>Comment of the Management</b>	<b>Recommendation</b>
a) A plan relating to the construction of sales center at the Dansalwatta Division of Attanagalla Estate had not been prepared, and a BOQ had not been prepared accurately as well. The provincial officer in charge of estates had been informed by the Manager (Human Resources and Sales) on 26 May 2022 that a BOQ in that connection be prepared. However, without doing so, only a sketch of the sales center had been prepared. As such, information on the cost likely to incur on that construction, was not disclosed to the Audit.	Construction of the sales center, Dansalwata and laying stones at the nearby area had been completed by the year 2023, and an expenditure of Rs. 2,968,227 had been incurred thereon. However, the value of engineering estimate prepared in that connection amounted to Rs. 4,206,725 (excluding the laying of stones), but a sum of Rs. 2,968,227 had been incurred to complete the works (including the laying of stones). As the service of a contractor had been obtained with materials provided by the Estate rather than awarding the tender to a contractor with the materials, the Company reaped economic benefits.	Plans and Bill of quantities for constructions should be prepared accurately. Survey certificates should be certified by a Technical Officer.
b) Construction of the sales center had been commenced by the Company without a plan and a BOQ. The construction had been done in phases such as, laying foundation and construction of walls, roof construction, plastering and titanium flooring, painting, covering the doors, windows and glasses, landscaping the front garden, and wiring. The Company had not prepared any estimate on the costs incurred on each of those activities;	As the construction should have been done without delay in the context that the traders were reluctant to furnish prices due to scarcity of goods in the market and prices changed daily, the Head Office gave instructions to the Estate that the construction be done in phases.	Plans and BOQs for the construction should be prepared accurately, and approval should be obtained thereon.

instead, the construction works had been done based on prices obtained from contractors relating to building materials and labor. No survey certificates whatsoever had been furnished with respect to the works done, and there was no verification on the quality of those materials as well.

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| c) | Although a revenue of Rs. 2,419,200 had been expected from the pepper processing project, Dodamgaslanda for the year 2022, the actual revenue earned by the Company amounted to Rs. 1,315,338. As such, only 54 per cent of the expected revenue had been earned.                        | The production had been reduced considering the low demand due to crisis in the country.   | Action should be taken to achieve the expected targets. |
| d) | Only 14 per cent of the expected target had been achieved by the coconut treacle processing project in Hiriyala Estate. Less than 05 per cent of the targets expected from both of the projects in Attanagalle Estate for processing coconut and jiggery palm treacle had been achieved. | Treacle can not be produced throughout the year due to reasons such as, scarcity of laborers producing palm nectar and the weather prevailing in the area. However, the process is continued successfully in the year 2023 despite the low production of palm nectar.<br>Production of treacle at the estate in Attanagalla had been considerably affected by excessive rain and damages caused by monkeys to the flowers and pots.<br>Production of coconut treacle at the estate in Attanagalla had decreased as the laborers who produced coconut treacle had left the service from time to time. | Action should be taken to fulfil the expected goals.    |
| e) | Despite being scheduled to implement the projects to produce virgin coconut oil and cinnamon oil in the year 2022, those projects had not been implemented even up to the date of audit.   | Initial works for construction of the factory had been commenced in the year 2022, but the construction process could not be completed due to reasons such as, unusual increase in prices of goods and scarcity of items during the  | Action should be taken to fulfil the expected goals.    |

year 2022. Hence, the construction is continued in the year 2023 as well. Furthermore, construction works of the factory relating to the project for extracting oil from cinnamon leaves, could not be completed even in the year 2022. but those constructions continued in the year 2023 and the production process has been commenced after completing the constructions.