

Custom Officers' Management and Compensation Fund - 2023

1 Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Custom Officers' Management and Compensation Fund of the Sri Lanka Customs for the year ended 31 December 2023 comprising the statement of financial position as at 31 December 2023 and the statement of comprehensive income, statement of changes in equity and fund flow statement for the year then ended, and notes to the financial statements, including material accounting policy information, was carried out under my direction in pursuance of provisions in Article 154(3) of the Constitution of the Democratic Socialist Republic of Sri Lanka 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 of the Fund give a true and fair view of the financial position of the Fund as at 31 December 2023, and of its financial performance and their fund flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

1.2 Qualified Opinion

My opinion on the accompanying financial statements 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 Fund'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 Fund or to cease operations, or has no realistic alternative but to do so.

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

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Fund 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.

1.4 Auditor's Responsibility in Auditing 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.
- Obtained 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 Fund'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 Fund'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 to cease to continue as a going concern.
- Evaluate the structure and content of the financial statements, including disclosures, and the transactions and events on which the content is based are appropriately and fairly included in the financial statements.

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 Fund, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Fund has complied with applicable written law, or other general or special directions issued by the governing body of the Fund ;
- Whether the Fund has performed according to its powers, functions and duties; and whether the resources 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 Public Sector Accounting Standards

Non- Compliance with the reference to particular Standard	Comments of the Management	Recommendation
In accordance with Sri Lanka Public Sector Accounting Standard No.03, (i) An accounting policy should be consistently used and when an accounting policy is changed voluntarily, it should be disclosed. Nevertheless, the statement of fund flow prepared in indirect method in the preceding year had been presented in direct method during the year under review without disclosing in the financial statements.	Agreed with the audit observation. Such policy changes were noted to be disclosed as per the Public Sector Accounting Standards in the future.	Compliance to Sri Lanka Public Sector Accounting Standards is required.
(ii) Although, a change in accounting policy, accounting estimate and error relating to a prior period should be corrected by retrospective restatement, the statement of financial position as at 31 December 2023 had been incorrectly stated as retrospectively restated information relating to the previous year when no such amendment was made.	It is stated that no any amendment was made for the values published in the accounts for the year 2022.	Compliance to Sri Lanka Public Sector Accounting Standards is required.

1.5.2 Accounting Deficiencies

Audit Observation	Comments of the Management	Recommendation
A number of divisions of the Sri Lanka Customs confiscate goods, sell them, impose penalties and collect such money, the details of	All penalties and sale proceeds of forfeited items are credited to the temporary retention account on statutory payments deposit account. After finalizing some investigations,	The payable amount in relation to the divisions of the entire department should be shown in the

the total income due from the sale of confiscated goods and the total penalty income due in respect of the entire year were not provided to the Finance Division. Since, no control system had been prepared in relation to that, the amount of Rs.80,379,402 to be paid from this fund as at 31 December 2023, was calculated only according to the files received by the finance department for payment. Accordingly, it was observed that the value shown in the statement of financial position as the total amount of reward payable as at the end of the year was not accurate.

there are cases where penalties related to the investigation have to be returned to the relevant persons. Further, the expenses related to the investigations have to be born from this deposited money. Therefore, remaining money will be credited to the Custom Officers' Reward Fund (50%), Management and Compensation Fund (20%) and Government Revenue (30%) at the time of payment the rewards after completion of the inquiry file. Therefore, the accounts are maintained on the basis described above, as it is not possible to identify a specific amount for accounting the penalty income receivable until the completion of the relevant investigation. It is noted that this situation to be disclosed under special disclosures in the final accounts in the future.

statement of financial position.

1.5.3 Unreconciled Accounts

Audit Observation

In accordance with the Section 153 (b) 1 of Customs Ordinance No. 17 of 1968, 50 per cent for the Customs Reward Fund and 20 per cent for the Management and Compensation Fund from sale proceeds of forfeited goods and penalties should be credited. Hence, the revenue recognized related to the Reward Fund for the year under review amounting to Rs.5,611,873,320 equivalent to 50 per cent should have been proportionately equivalent to the contribution of 20 per cent recognized in the Management and Compensation Fund which was amounted to Rs.2,244,749,328. Nevertheless, there was a difference of Rs.218,647,862 related to the revenue recognized in the Management and Compensation Fund as the amount shown in the financial statements was Rs.2,463,397,190.

Comments of the Management

Although, the payment was made for the whole file in the year 2023 related to 50% of the proceeds from the sale of forfeited goods and penalties credited to the Customs Reward Fund in the year 2023, even if a partial payment has been made in the previous year, the same amount and an amount not accounted for the reward fund when paying for another file had also been added.

Recommendation

When 50 per cent of the revenue from the sale of forfeited goods and penalties is credited to the Customs Reward Fund, 20 per cent should be credited to this fund proportionately.

1.5.4 Lack of Audit Evidences

Subject	Amount Rs.	Audit Evidence Not Submitted	Comments of the Management	Recommendation
Although the property, plant and equipment with a cost of Rs.123,465,297 and accumulated depreciation of Rs.118,179,542 under 02 categories of assets were stated in the statement of financial position as non-current assets, no information such as fixed asset registers, asset verification reports, etc. required to scrutinize the said assets had been submitted to the audit.	123,465,297	Fixed asset registers, stock verification sheets and premises located.	It is noted to prepare the documents in the future so as necessary to verify and scrutinize the assets.	Maintaining the required documents to verify the assets is necessarily essential.

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

Reference to Laws, Rules, Regulations etc.	Non-compliance	Comments of the Management	Recommendation
(a) Gazette No. 792 of 05 November 1993	Although, 5 main rules had been introduced to dispose money of the Management and Compensation Fund of Customs Officers, and if no provisions were made in those rules, it was mentioned that if there is any special program required for the Department's management effectiveness as per the opinion of the Director General of Customs, it could be done so with the	According to Section 153 (a) 1 of the Customs Ordinance, the Director General of Customs may incur expenses for the purpose of improving the effectiveness of customs management. The expenditure mentioned in the audit report has been made subject to the provisions of Gazette No. 792 of 05.11.1993.	Compliance to the provisions of the Gazette should be required.

prior approval of the Minister of Finance. However, a sum of Rs.554,984 had been spent from this fund even though there was no direct relationship to increase managerial effectiveness. Accordingly, there is no need to obtain special approval from the Minister.

- (b) National Budget Circular No 2023/01 of 27 January 2023
- While the Heads of Departments have been advised to take necessary steps to reduce recurring and operational expenses wherever possible, an amount of Rs.975,941 had been spent from this fund for the Customs Day event in the year under review.
- In order to bear the expenses related to the International Customs Day 2023, according to the letter of the Treasury Operations Department No. TO/BE1/02/05/01 and dated 11.01.2023, permission has been obtained through an interim order and the relevant amount has been spent for the official event and the remaining amount has been settled.
- Compliance to the circular should be required.

2. Financial Review

2.1 Financial Results

The operating result of the year under review was a surplus of Rs.2,400,069,243 and the corresponding surplus for the preceding year was Rs.1,499,675,714. Accordingly, an improvement of Rs.900,393,529 was observed in the financial results. The increase in income from penalties by Rs.1,126,202,914 was the main reasons for this improvement.

3. Operational review

3.1 Management Inefficiencies

Audit Observation

An importer had filed a suit against a forfeiture and penalty imposed as a result of a customs investigation and the importer had to pay back Rs.31,000,000 from the amount recovered by the customs. Although, only 20 per cent of the forfeiture and penalty value is credited to this fund,

Comments of the Management

After pointing out that it is practically difficult to collect the said amount due to the fact that during the completion of the full payment of the reward file, nearly 541 officials have been paid from the money

Recommendation

According to the court decisions, when the forfeitures and penalties made by the customs have to be repaid, the recovery should also be done from the officers who received the rewards.

as per the court decision, the 20 per cent value of Rs.12,000,000 credited to this fund and the amount of Rs.18,000,000 credited to the government revenue were fully recovered to pay the compensation due to the importer. While there were approximately 541 officers who received reward money, no money was recovered from them.

allocated for the reward file as well as the pool funds and Rs.2,716,696 have been paid as government taxes, the relevant importer has agreed to get only the amount that can be paid without collecting from the officials.

3.2 Operational Inefficiencies

Audit Observation	Comments of the Management	Recommendation
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An amount equal to 20 per cent of the proceeds from the sale of forfeited goods and penalties imposed for various customs offenses is credited to this fund and according to section 153 (b) 1 of the Customs Ordinance, the functions of the fund were as follows.

- Expenditure to facilitate the Director General of Customs to enhance the effectiveness of Customs management.
- Compensation to any customs officers permanently or totally or partially disabled or temporarily incapacitated.
- Compensation to the legal heirs of a customs officer on death.

In order to achieve the above objectives, the following observations are made.

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| (a) | In the period of 7 years from 2017 to 2023, the amount spent from the Management and Compensation Fund to follow post-graduate courses for 337 with a view of improving Customs managerial effectiveness was Rs.131,978,786. However, only 162 people had completed the course and submitted their certificates and the department did not have | The department did not have the information whether postgraduate courses were successfully completed or abandoned from 2017-2022, this information was started to be computerized in the year 2023. It should be noted that if it is found that some money has been taken from | It should be confirmed that the courses have been completed. |
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information on whether the remaining 175 officers successfully completed the course or abandoned it, and there was no follow-up system.

the above fund for pursuing postgraduate courses and the course has been abandoned midway, the customs department will also work to recover the amount from his/her monthly salary according to the agreement signed with the said officials. Further, the relevant post-graduate institution will also inquire about the progress of completion of degree courses annually.

- (b) Although, it was informed to audit that 13 officers who received money from the fund in the year 2023, to study postgraduate courses had completed the courses and submitted their certificates by 28 March 2024, during an examination of personal files, 08 officers had not completed the courses and submitted the relevant certificates to the institution.
- (c) Hence, the allocation of money to this fund for improving management effectiveness of customs officials and for compensation of officials had been made without a proper plan of the future expected purposeful expenses and specific criteria, a trend of continuous growth of the accumulated balance of the fund was observed annually. Therefore, the accumulated balance of the fund amounting to Rs.10,090 million as at 31 December 2022 had grown to Rs.12,490 million as at 31 December 2023 by Rs.2,400 million or by 24 per cent. Therefore, it was observed that 96 per cent of the income for the year
- The relevant officials have been informed about this and efforts are being made to obtain certificates.
- It should be confirmed that the courses have been completed.

under review was accumulated in the fund. The following reasons were also primarily affected for the continued growth of the fund's accumulated balance.

- (i) Due to insufficient steps being taken to introduce advanced methods linked to artificial intelligence to control customs duty evasion and due to the fact that various customs offenses detected by the officers in the course of their routine duties have to be paid in abundance and a percentage equal to 20 per cent is credited to this fund, this fund had continued to grow.
- It is noted to deal with this after an analytical study.
- The modern technical methods should be introduced to control customs tax frauds.
- (ii) In imposing penalties for customs offences, 20 per cent of the penalty value shall be credited to this fund and 30 per cent to the Government. In some occasions, there were the reasons to increase in amount of the money allocated to this fund such as the imposition of penalties up to treble the value of the goods and tax value of the goods attempted to be defrauded, low reduction in customs offenses, not made amendments for the legal provisions of the Customs Ordinance and the related funds in a formal and timely manner to suit the complexity of imports and exports due to the current free economic policies.
- Customs duty is collected as per the provisions mentioned in sub-schedule (a) under section 10 of the Customs Ordinance. The amounts of duty related to the respective goods are announced by the revenue conservation orders passed by the Parliament. After recovery of taxes due to the government, the money is credited to the consolidated fund of the government. The imposition of customs penalties or confiscation of goods shall be made only in accordance with the provisions of the Customs Ordinance, and shall be made where any importation or exportation has been made or attempted to be imported or exported in contravention of any customs law, and the goods in respect of such contravention shall be
- The revenue received by the government should be secured.

"Illegal goods". Therefore, no tax can be levied on them, and only confiscation of the goods or imposition of penalties can be done in accordance with the relevant sections of the Customs Ordinance. Therefore, taxation can only be levied in respect of legitimate imports made under the normal system. The primary objectives of customs investigations and imposition of customs penalties are to catch the parties violating the customs law, to punish them and to increase the compliance and adherence to the customs law among the concerned parties.

(e) Although one of the basic objectives of this fund is to compensate the customs officials for the disasters in the course of their duties, no such compensation was reported during the last 10 years period under review.

In the above 10 years, no compensation claims have been received for such disasters. Furthermore, since there have been threats to the lives of the honest officers who work hard for customs raids, the presence of a large sum of money in this kind of fund ensures the security of their families like an insurance fund for those officers to dedicate themselves to their duties despite the risk to their lives. It encourages officers to devote themselves to duty regardless of risk to their lives in the performance of their duties. It is further reported that the allocation of money to this fund will

The continuous growth related to the accumulated balance of the fund should be reviewed.

be done according to the provisions of the Customs Ordinance.

(f) The total income of the fund in the year under review and in the last 4 years was Rs.6,138,888,719 and the amount spent from the fund during that period (excluding depreciation) was Rs.364,303,235. Accordingly, due to the fact that a very low percentage of 6 per cent of the total income was spent from the fund and the remaining 94 per cent was added to the fund, a review of the annual allocation to the fund had to be done.

It is noted to deal with this after an analytical study.

The continuous growth related to the accumulated balance of the fund should be reviewed.