

## **Smallholder Agribusiness and Resilience Project - 2023**

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The audit of financial statements of the Smallholder Agribusiness and Resilience Project for the year ended 31 December 2023 was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Section 9.03 of the Loan Agreement No. 2000003227 and Grant No. 2000003226 dated 10 June 2021 entered into between the Democratic Socialist Republic of Sri Lanka and the International Fund for Agriculture Development (IFAD). My comments and observations which I consider should be reported to Parliament appear in this report

### **1.2 Implementation, Objectives, Funding and Duration of the Project**

According to the Loan Agreement, the Ministry of Agriculture is the Executing Agency and the Project Management Unit established for SARP is the Implementing Agency of the Project. The objectives of the Project are to build resilience and market participation of 40,000 rural smallholder households in the project area. The activities of the Project are implemented under three components namely Capacity Building for Climate Resilience and Inclusive value chains, Investment for Climate Resilience and Inclusive value chains and Project management and coordination.

As per the Loan Agreement, the estimated total cost of the Project was US\$ 55.45 million equivalent to Rs 9,966 million and out of that US\$ 42.75 million equivalent to Rs 7,698 million was agreed to be financed by International Fund for Agriculture Development. The balance amount of Rs 2,268 million is expected to be financed by the Government of Sri Lanka.

The Project had commenced its activities on 10 June 2021 and scheduled to be completed by 10 June 2027.

### **1.3 Qualified Opinion**

In my opinion, except for the effects of the matters described in 2.1 section of my report the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2023 and its cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

### **1.4 Basis for Opinion**

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 opinion.

### **1.5 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 Public Sector 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.

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

## 1.6 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 internal control of the Project.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- 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.

I communicate with those charged with governance regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

## 2. Comments on Financial Statements

### 2.1 Accounting Deficiencies

No	Accounting Deficiency/Audit Issue	Response of the Management	Auditor's Recommendations
(a)	The provision for rental expenses amounting to Rs.3 million for the month of December of the year 2023 had not been made. Therefore, current liabilities were underestimated by that amount.	We will have taken corrective actions to the financial statements for the year 2024. To reflect the accrued rental expense of Rs.3,639,102 which was omitted for December 2023. we are implementing measures to prevent similar omissions in the future.	The provision should be made for the accrual expenses.

- (b) According to SLPSAS 02 related to the Cash Flow Statement, the comparative information was not presented using the values of the previous year. We will take the necessary arrangements to correct the issue and prevent similar omissions in the future. Accounts should be prepared according to SLPSASs.
- (c) Although the assets purchases amount of Rs.34 million for the project had been recorded in the Statement of financial position for the year also it was not shown under Investment activities in the Cash Flow Statement. Acquisition of fixed assets for development activities of the project ultimately be transferred to the investment cost of project management and coordination with complying the cost tab allocations. As a result though the additions of PPE during the year under concerned were shown in the SOFP to ensure the existence of such assets, actual movement of cash reflects under the note No 16 “cash flows from operating activities”. Cash Flow Statement should be prepared according to SLPSASs.
- (d) The essential information relating to verify the balance for six payment vouchers aggregating to Rs. 3 million had not been submitted for the audit. The PMU has discussed this issue at the AMC and decided to conduct an investigation. Explanations has already been obtained from the PMU security officer and other related parties. Based on this decision, the PMU will take the necessary actions. Investigate & action should be taken for relevant officers.

## 2.2 Non Compliance with Laws, Rules and Regulations

No	Reference to the Laws Rules and Regulations	Non Compliance	Response of the Management	Auditor's Recommendations
(a)	Financial Regulation of the Democratic Socialist Republic of Sri Lanka			
	i. F.R. 138	The vouchers should be certified by Certifying Officer before making payments. It was observed that some of payment vouches were not certified by certifying Officer.	To prevent recurrence of this type of issues in the future, PMU has taken actions to implement a new internal control system and corrective measures.	Internal control system should be implemented payment certification
	ii. F.R. 139(10) and 261(3)	The Cash Book should be totalled and the balance ascertained daily. No payment should be	To prevent recurrence of this type of issues in the future, PMU has taken actions to implement a new	The Cash Book should be totalled and the balance ascertained daily.

- recorded in the Cash Book, or a cheque drawn out for payment, unless there is sufficient money available. It was observed that it is not considered whether sufficient balance available in the bank account while drawing out cheque for payment. internal control system and corrective measures.
- iii. F.R. 371 & Para 09 of Public Finance Circular No PFD/RED/01/01/2020/01 dated 28 August 2020 Advance should be limited to Rs. 100,000. However, 27 advances exceeding Rs.100,000 amounting Rs.6,590,385 were released during the year under reviewed. To prevent recurrence of this type of issues in the future, PMU has taken actions to implement a new internal control system and corrective measures. Advance should be limited according to the Circular
- iv. F.R. 372 Advance should be checked by relevant officers frequently. It was observed that some advances which expenses beyond the approved estimates were not approved. To prevent recurrence of this type of issues in the future, PMU has taken actions to implement a new internal control system and corrective measures. Advance settlement should be checked by relevant officers frequently.
- v. F.R. 454 Every department and sub-office of a department should keep an Inventory Book in Form General 44. It was observed that inventory books were not maintained by the Project. To prevent recurrence of this type of issues in the future, PMU has taken actions to implement a new internal control system and corrective measures. Inventory books should be maintained by the Project.
- vi. F.R. 756 and 757 The appointment of the Annual Commodity Survey Board should be done on or around 15 December of every year. Annual Commodity Survey Board had not been appointed due date. Project had not Nominated members for BOS on the project side has been sent to the MOAPI for necessary arrangements on time. Waiting for further arrangements at the Ministry end. Annual Commodity Survey Board should be appointed due date.

conducted an annual commodity survey for the year of 2023. The project had purchased Rs.34.24 million computers and office equipment during the year. Furthermore, Reports of Board of survey have not been submitted to the audit as at 31 May 2024.

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| (b) | Circular No 01/2022 dated 07 February 2022 issued by the Department of Management Audit        | Project Internal Audit Committee meeting should be held first and third quarter. However, none of meeting had been held during the year under review.  | At present we have aligned ourselves with the guidance outlined in Circular.  | Audit Committee meeting should be held according to the circular.          |
| (c) | Circular No 01/2019 dated 15 March 2019 issued by the Department of Management Services        | Project Steering Committee (PSC) meeting should be held once in two month. However, only four PSC meetings had been held during the year under review. | We have aligned ourselves with the guidance provided in Circular No. 01/2019 dated 15 March 2019 issued by the Department of Management Service, and all steering committee meetings have been scheduled accordingly. | Steering Committee (PSC) meeting should be held according to the circular. |
| (d) | Public administration Circular No.09/2009 and 09/2009 (1) dated 16 April 2009 and 17 June 2009 | As per the Circular, Finger Print Machine had not been used to record the attendance in the Project Management Unit.                                   | The PMU has taken actions to procure the fingerprint machine, and the procurement process is underway.  | Finger Print Machine should be used according to the circular.             |

### 3. Physical Performance

#### 3.1 Physical progress of the activities of the Project

<b>Audit Issue</b>	<b>Response of the Management</b>	<b>Auditor's Recommendation</b>
According to the Project Design Report issued on 04 November 2019, it was planned to start the project in 2020, however the financial agreement was signed on 10 June 2021, and the duration of this project is 06 years. It was observed that the project has started financial and operational activities from August 2022. Accordingly, it was further observed that the project reported only 05 per cent physical progress as at 31 December 2023.	As at 31.12.2023 project mobilization, PRA and other initiatives only started	Tasks should be completed within the pre-determined time frame.

#### 3.2 Idle/ Unutilized/ Underutilized Resources

<b>No</b>	<b>Audit Issue</b>	<b>Response of the Management</b>	<b>Auditor's Recommendation</b>
(a)	When considering the progress of utilization of funds as at 31 December 2023, it was observed that the project utilized only USD 367,590 funds from USD 41.70 million of total allocation by the IFAD Loan. As a percentage, it was 1 per cent. Therefore, the utilization of funds is ineffective when considering the rest of three and half year time period with balance funds.	Comments have not been made by the Management.	Funds should be utilized efficiently.
(b)	Furthermore, total agreed contribution of government of Sri Lanka for SARP is USD 12.70 million, the cumulative use of government fund as at the year under review is only USD 0.08 million and it is equivalent to 0.62 percent of agreed amount. This project is to be ended on 10 June 2027 and use of remaining 99 percent of agreed government fund in next three and half years is uncertain.	The management has accepted the observation. Further explanation has not been provided.	The activities should be properly planned and used effectively and efficiently.
(c)	It was observed that the year under review, the project has utilized only Rs120.29 million from allocation for the reimbursable foreign loan of Rs.300 million. Therefore, allocation of Rs.179.71 million representing 59 per cent of the total allocation had not been utilized by the project.	The management has accepted the observation. Further explanation has not been provided.	Funds should be utilized efficiently.

- (d) Out of GOSL allocation of Rs.30 million under the Project had utilized only Rs.20 million and allocation of Rs.10 million representing 33 per cent had not been utilized due to slow progress of the Project during the year under review. Balance imprest of Rs. 10 million return to the line ministry as unutilized as at 31.12.2023. Funds should be used effectively and efficiently.

### 3.3 Issues Related to Human Resources Management

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	According to the Management Audit Circular 1/2022 dated 07 February 2022 issued by Department of Management Audit, although an internal auditor should appoint for projects which project period of more than one year and a total cost of more than USD 05 million, it was observed that internal auditor was not appointed until 01 December 2023. Further, the person who recruited were appointed for cover up duties. That person also left from the job and new internal auditor was appointed for cover up duties on 21 March 2024.	Initial request for recruiting an Internal Auditor for the SARP PMU was forwarded to the Department of Management Services on July 24, 2023.	Internal auditor should be appointed according to the Circular.
(b)	38 officers and employees had been recruited by Smallholder Agribusiness and Resilience Project as at 31 December 2023. The basic eligibility documents for recruitment that should be contained in the personal files of those officers and employees were informal. Further, the correctness/authenticity of the certificates submitted in respect of the posts had not been verified from the institutions which submitted the certificates.	Actions were taken to formally align the documents according to the guidelines stated in Project Management Circular 01/2019. Further actions are in progress to verify the correctness and authenticity of the certificates submitted for these positions.	Qualifications of employees verified and personal files should be maintained up-to-date.

### 3.4 System and Controls

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	The project is maintaining a Petty Cash Imprest amount of Rs.25,000. As per Generally Accepted Accounting Principles, Petty Cash Imprest should be settled at the end of reporting year. But the project had not settled Petty Cash Imprest account until 31 December 2023.	To prevent recurrence of this type of issues in the future, PMU has taken actions to implement a new internal control system and corrective measures.	All Petty Cash Imprest must be settled at the end of the accounting year.

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| (b) | According to the information given to the audit staff advance amount of Rs.1 million has not been settled until 31 December 2023.  | To prevent recurrence of this type of issues in the future, PMU has taken actions to implement a new internal control system and corrective measures. | Staff advance must be settled at the end of the accounting year. Action should be taken against employees who have not settled advances. |
| (c) | It was observed that weakness of the internal control related to maintain general ledger in the areas of maintaining general ledgers without ledger codes, erroneous ledger posting since the entries are made batch wise and are not checked by any other officer the accuracy and the completeness of the entries, not maintaining of cash book etc. | To prevent recurrence of this type of issue in the future, PMU has taken actions to implement a new internal control system and corrective measures.  | Formal Internal controls should be maintained and an accurate accounting software system should be used.                                 |