

Smallholder Agribusiness Partnerships Programme - 2023

The audit of financial statements of the Smallholder Agribusiness Partnerships Programme 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. 2000001843 dated 26 June 2017, the Loan Agreement No. 2000001984 dated 21 November 2017 and the Loan Agreement No. 2000002639 dated 16 May 2019 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 SAPP is the Implementing Agency of the Project.

The objectives of the Project are to sustainably increase the income and quality of diet of 57,000 smallholder households involved in commercially-oriented production and marketing system. The activities of the Project are implemented under three components namely Access to Commercial partnership, Access to Rural Finance and Program management and Policy Dialogue.

As per the Loan Agreement, the estimated total cost of the Project was US\$ 105.03 million equivalent to Rs 17,170 million and out of that US\$ 54.4 million equivalent to Rs 8,892 million was agreed to be financed by International Fund for Agriculture Development. The balance amount of Rs 8,278 million is expected to be financed by the Government of Sri Lanka.

The Project had commenced its activities on 26 June 2017 and scheduled to be completed by 30 June 2023. However, the date of completion of the activities of the Project had been extended up to 30 June 2025.

1.3 Opinion

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2023, statement of expenditure 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 Non-Compliance with Laws, Rules and Regulations

Reference to the Laws Rules and Regulations	Non-Compliance	Response of the Management	Auditor's Recommendation
Financial Regulation No 754/756	The program had not properly prepared the inventory book for the year 2023 and it was not balanced as per Financial	Excel work book is being maintained as the Fixed Asset Register. 2021 Board of Survey has been completed and the report is	Action should be taken according to the Financial regulations.

Regulation No 754/756 available.2022 Board of by 28 February 2024. Survey was unable to complete Furthermore, the board of by the BoS committee survey for the years of appointed by SAPP. 2023 2021 and 2022 had not Board of Survey is going on been conducted by 28 and planned to complete by February 2024. 15th June 2024.

2.2 Unsettled Balances

Audit Issue	Response of the Management	Auditor's Recommendations
The amount of Rs.301,950 of staff advance paid on 15 June 2023 had not been settled until 31 December 2023.	Due to some unacceptable bills, justifications have been called for the responsible officer who has taken the advance. Since that has not been received as a proper settlement voucher, the expenditure remains as unsettled for accounting purposes. Action has been taken to rectify this issue.	Advance should be settled immediately.

3. Physical Performance

3.1 Physical and Financial Progress of the Activities of the Project

No	Audit Issue	Response of the Management	Auditor's Recommendations
(a)	The project commenced on 26 June 2017 and scheduled to be completed 88 per cent target progress as at 31 December 2023 however it was reported only 69 per cent physical progress as at 31 December 2023.	As of 30th April 2024, out of 40,686 number of farmers committed to the Matching Grants, 30,779 number of farmers have been physically engaged 76 percent and they have received at least one grant item. Further 40 percent of financial target under the 4P Matching Grants have been met against the commitments.	The target should be completed within project time frame as planned.
(b)	The Moringa cultivation project that was started in Anuradhapura district had failed due to the inefficiency of the officials and the promoter. Apart from the contribution value of the farmers, an expenditure of Rs. 25.52 million was incurred for obtaining water motors for drip irrigation based on the contribution of the project. Due to the failure of the Moringa project, the farming families associated with the project	Until Covid 19 period, Moringa project has been successfully implemented with 116 farmers, demonstrating significant initial progress. Due to market collapse, the Promoter has been suspended purchasing due to challenges in the export market. The primary issue affecting the continuation of the project is the requirement for the product to be 100 percent organic to meet export standards. Due to soil residues detected, the project cannot currently satisfy these stringent	Before providing grants to promoters, supervision of their business should be done. Paid grant should be recovered from the ineffective promoters and relevant officials.

faced economic crises. The agreement entered with the promoters of the Moringa project had expired on 05 December 2021 and the Program Director had spent more than 18 months to notify the promoter.

organic criteria. Given the export constraints, the project has shifted its focus to fulfilling local market demands. However, this shift does not fully compensate for the intended export goals. Discussions were going on for revamping the project but due to the inability of meeting the organic certification requirements, finally SAPP had to suspend the project.

(c) A grant of Rs.4.5 million was given to the Parabowa Environmental Farmers Organization and the beneficiary farmers, which aimed to increase the production of small-scale traditional rice farmers in Puttalam district, increase the income and economic status of the farmers. Although the Parabowa Environmental Farmers Organization has contracted with the farmers to purchase the produce of the farmers, the paddy was purchased by Parabowa Exports Private Limited, which is owned by the Chairman of Parabowa Environmental Farmers Organization.

At first, Parabowa Farmer Organization purchases paddy from the member farmers and then sells to Parabowa Export Pvt. Ltd. Further Farmer Organization has employed a Field Officer to organize the farmer fields and purchasing.

Farmers Organization that benefited from the project should purchase paddy and if the organization does not purchase the paddy, the grants given to them should be recovered.

(d) Grants of Rs.9 million were received from the Agriculture Sector Modernization Project Part 01 under the Ministry of Plantation Industry at that time and grants of Rs.2.7 million were received for the construction of paddy warehouses (sailo) through the SAP program under the Ministry of Agriculture at that time by the owner of Parabowa Export Company who is the promoter of Parabowa Environmental Farmers Organization. The expected tasks of Rs.9 million grants received from the Agriculture Sector Modernization Project Part 01 were not fulfilled.

Parabowa Project is a value chain programme under the 4P concept signed with the Farmer Organization. Storage facilities are included in the traditional paddy cultivation proposal and the signed agreement. Therefore, SAPP has taken steps to implement the agreement by providing Rs.2.7 million as a grant for establishing that facility which is utilized for storing the paddy collected from farmers until exportation.

During the implementation of the projects through the SAP program, the government officials of the area where the project is implemented should be coordinated.

We are informed by the promoter (FO) that Rs. 9 Mn has been granted to the Exporting Company for a constructing a noodles factory.

- (e) SAPP has spent only Rs.89 million from expected contribution for the pepper cultivation project which was carried out in Matale district by expecting to spend Rs.292 million and targeting 2500 beneficiaries. According to the implementation plan of the project, the work of setting up the harvest collection centers and high-quality processing centers to be done in the year 2020 had not been done.
- The construction of the processing center was started and executed under the initially approved budget of Rs. 2,635,351. However, due to price inflation following the pandemic and economic crisis, it was found that this amount was insufficient.
- When selecting a project, it should be designed and implemented efficiently in such a way that its benefits can be returned to the society.

3.2 Contract Administration

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	The procurement of server software for the program had been done without obtaining a performance bond or bid bond contrary to paragraphs 5.3.10 and 5.3.11 of the Procurement Guidelines. Paragraph 6.3.1 of the Code of Procurement Guidelines had been contravened during the opening of bid documents. A committee was not appointed to open the bids and the server software was procured at a cost of Rs.974,600 on the technical recommendations of the IT Officer.	Considering the estimated value, this procurement was conducted by applying the shopping procedure where Bid Bond and Performance Bonds are not compulsory in terms of procurement manual 2006.	Procurement guidelines should be followed.
(b)	A Technical Evaluation Committee was not appointed during the procurement of office equipment (a printer, photocopier, toner, wood, camera, 04 projectors) worth Rs.5,654,726 under the contract number SAPP/PRQ/GDS/2022/10.	Few procurements in different values have been done under the procurement file "Office Equipment and Maintenance" for the value of Rs.5,654,726. There are four procurements which comes under the delegated authority of Programme Director.	Procurement guidelines should be followed.

3.3 Idle/ Unutilized/ Underutilized Resources

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	Although the project should be completed as at 30 June 2023, the project had been approved to continue till 30 December 2025 by IFAD. When considering the progress of utilization of funds as at 31 December 2023, it was observed that the project utilized only USD 28.16 million funds from allocated funds of the IFAD Loan of USD 54.4 million. As a percentage, it was 51.76 percent Therefore, it was observed the utilization of funds were ineffective when considering the rest of two-year period with balance funds.	As of the end of May 2024, IFAD Fund utilization is 63 percent and SAPP planned to reach 80 percent progress during this year.	The target should be completed within time frame.
(b)	Total agreed contribution of government of Sri Lanka for the SAPP is USD 19.30 million, the cumulative use of government fund as at the end of year under review was only USD 10.25 million and it was equivalent to 53 percent of agreed amount. This project is to be ended on 31 December 2025 and use of remaining 47 percent of agreed government fund in next two years is uncertain.	As of the end of May 2024 Government Fund utilization is 72 percent and SAPP planned to reach 87 percent progress during this year.	The target should be completed within time frame.
(c)	It was observed that the year under review, the project has utilized only Rs.2,278 million from allocation for the reimbursable foreign loan of Rs. 4,340 million. Therefore, allocation of Rs. 2,062 million representing 48 percent of the total allocation had not been utilized by the project.	This savings was arisen due to tax on equipment purchasing for MILCo Project as planed has been not utilized due to delay in procurement procedure, Unable to proceed Maize seed and fertilizer vouchers due to delay in receiving supporting documents such as recommended farmer lists from Line Agencies. Vouchers worth of Rs. 2,000 million worth of payments were committed. However, 90 percent of these payments for Maize seed, fertilizer and land preparation have been paid in 2024.	The identified target of the project should be completed within a specific time frame.

- | | | | |
|-----|--|---|--|
| (d) | It was observed that Rs.466.48 million out of GOSL allocation of Rs.1,876 million received from two votes which was representing 25 percent of total allocation has not been utilized due to slow progress of the Project. | Though the funds have been requested from Treasury in November 2023, the Imprest has not been released to transfer to CBSL. | The identified target should be completed within a specific time frame. |
| (e) | Under the development of off-farm facilities in relation to the pepper cultivation project, a pepper collection center was constructed at the cost of Rs.1.7 million in the Ambanganga Korale Kumbaloluva area and a pepper collection center at a cost of Rs.1.7 million in Raththota, Bandarapola area by the Programme. As at 31 December 2023, however those centres had not been used for the entire project. | However, due various factors, the initially expected quantity of pepper was not collected. The District Secretary of Matale, who coordinates the construction of these centers, has also highlighted these issues. Facilities are not currently idle due to lack of utility but rather due to external circumstances affecting harvest volumes. | Funds should be used efficiently and effectively. |
| (f) | Although 350 beneficiaries were targeted, the number of beneficiaries actually identified was 85. Seven cinnamon processing centers were supposed to be built, however, there had not been built cinnamon centers until 31 December 2023. | Discussions have been going on with the Director General of newly established Department of Cinnamon Development for evaluating the alternatives to construct processing centers and increase the number of farmers as planned. | Planned the respective objectives should be achieved efficiently. |
| (g) | For the Cavendish Banana Plantation Project, 28 beneficiaries had been given loans of Rs.15.6 million by the banks and it was observed that the loan defaulted due to the failure of the banana plantations on the date of the audit. And it was observed that the Cavendish banana cultivation project had failed, and the expenditure incurred was an idle expenditure. | This project successfully implemented from July 2021 and continued up to the end of the first cropping cycle. But after that, it was subjected to an adverse effect due to inorganic fertilizer crisis. During that period inorganic fertilizer scarcity had been occurred due to import banning, affected the project badly. | Strategies should be planned and implemented to reach the objectives of the project. |

3.4 Matters in Contentious Nature

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	Under Goonagala Agri.Productivity Village Co-Op Society project, Rs.15 million had deducted from the farmers' contribution in the current year due to reports of over contribution in the	An amount of Rs. 15,234,648 which should be accounted under Turmeric Cluster Project- Ruhunu Foods had been shown under the Gonagala Turmeric Project by mistake in 2022	Farmer contribution should be disclosed accurately.

- previous years. As a percentage, it was 59.91 percent of the opening balance of the current year's farmers' contribution.
- financial statements. This error has been rectified in 2023 Financial Statements.
- (b) The project had signed an agreement with the contractor on 01 January 2022 for a contract amount of Rs. 4.88 million to design, development and implement the Management Information System. The contract agreement has been extended five times for a period of one year and two months and it has been agreed to end on 31 May 2023, however the contractor had published MIS on the web on 28 November 2023.
- MIS agreement has been extended five times due to the delays in system analysis, and testing of the MIS caused by various reasons such as unavailability of fuel, instability in the employment of the positions in the Monitoring and Evaluation division, that were beyond the control of SAPP. However the system is in use since Nov 2023 and the data that were not in the system since 2019 is being entered.
- Project targets should be achieved efficiently and within target time.
- (c) It was observed that the project has entered only 30 per cent information (Overall) into the Management Information System by 04 April 2024. Apart from this, the information of 4P project status, Status of grant disbursement and status of loan disbursement was not entered into the Management Information System.
- Currently 38 percent of the total target has been completed. Balance of about 18,000 farmer information would be entered in 2-3 weeks' time. Feeding of other information such as off farm activities, Institutional Strengthening activities will also be completed by the end of June 2024.
- Project targets should be achieved efficiently and within target time.
- (d) A grant of the total amount of Rs.16 million was proposed to 150 dairy farmers in Weeragama area of the Milk Producers' Cooperative Society Association in the Coconut Triangle of Kuliypitiya, for the construction of cow sheds, obtaining the necessary equipment to supply water to the cows and obtaining milk collection containers. Rs.11 million had been released in 12 occasions.
- i. Although 150 dairy farmers were registered, 26 of them had left the dairy farming activities. Rs.635,216 that had been given as grant and Rs.1,820,000 that had been given as concessional loans for the farmers who left the dairy farming activities had been idle expenses.
- 26 farmers had left due to various reasons. However, these farmers have not defaulted the credit obtained from banks
- Proper planning and identification of the right beneficiaries should be done.

- ii. Out of the allocation for dairy farming project, Rs.7 million had been spent on concreting roads and Rs.372,000 was allocated for the repair of the Diyadora anicate. It was observed that the fund was used for a purpose outside the purpose of the project.
- A budget of Rs. 10 Mn was allocated for off-farm activities, benefiting 150 direct and 262 indirect dairy farm families. Given the number of direct and indirect beneficiaries, these infrastructure developments are aligned with the project's purpose of facilitating the transport of farm inputs and outputs, thereby supporting the dairy farming activities.
- Expenses which are outside the purpose of the project should be avoided.
- (e) The organizations of Pelwatte Dairies and Colombage Distributors Lanka had been signed agreements with Smallholder Agribusiness Partnership Program (SAPP) for Dairy Development and Seed Potato respectively for three-year time period. However, these companies were not engaged in any promoter contribution at the date of 31 December 2023. And also, the agreed time period of those organizations will be ended at the month of July 2023. It was observed that the progress of the project is stage of weak.
- Pelawatta dairy project agreement of the project was signed in 2021 and until 2023 August the project is moving very slowly due to the promoter's weak involvement and coordination.
- The officers of the program should work to fulfill the objectives of the program.
- (f) The value of the contribution to be given by Lanka Eco Product Guarantee Limited, which is acting as the project producer, is Rs.34.6 million. As at 31 December 2020, the contribution made by this company is only close to Rs.9 million and it was observed that the expenses indicated by Lanka Eco Product Guarantee Limited are baseless false values as any payment vouchers or other relevant documents related to the expenses reported by the project were not in the institution.
- SAPP has not agreed with the above observation since all the reported promoter contributions are certified by the Internal Auditor by his physical verification or by the M&E division by their monitoring mechanism.
- Before payments expenses should be certified by the Internal Auditor and M & E division.