

BY COURIER

Dr. P.B. Jayasundera
Secretary to the Treasury
The Secretariat
Colombo 1.

**Supreme Court Determination on the Appropriation Bill
Annual Report 2006**

Attention is drawn to the following:

1. Supreme Court in its Determination on the Appropriation Bill 2007 recognising that there is severe criticism *vis-à-vis* absence of transparency and prudential financial management, *inter-alia* observed thus:

"But, considering the severe criticism made, we have to observe that for purposes of ensuring transparency and prudential financial management, the transfers made in terms of Clause 6 that are deemed to be supplementary estimates should be specifically included in the relevant reports submitted in terms of the Fiscal Management (Responsibility) Act. No. 3 of 2003, with reasons for the particular deviation."

"But we note that in the Reports submitted there is no specific reference to the transfers made by the Secretary, in terms of Sections 5(3) or 6 of the previous Appropriation Acts" (Emphasis added)

The foregoing is in reference to the Annual Report 2006 tendered to the Supreme Court by an Officer representing you, who endeavoured to mislead the Supreme Court in such regard.

2. In determining that the Appropriation Bill is not inconsistent with the Constitution, the Supreme Court, however, subjected the same to the following direction:

"We wish to however note the observation stated above that any transfer made from the "Development Activities" Program, in terms of Clause 6 to any other Programme under any other Head by order of the Secretary to the Treasury should be specifically included in the respective Reports submitted in terms of Fiscal Management Responsibility Act No. 3 of 2003 with reasons for such deviation."

Section 22 of the Fiscal Management (Responsibility) Act. No. 3 of 2003 mandates the disclosure of information in the Reports referred to in the said Act, *inter-alia*, **pertaining to public corporations and companies in which the Government own Shares.**

3. Since the Fiscal Management (Responsibility) Act. No. 3 of 2003 mandates reporting of estimated and actual expenditures, revenues, cash-flows and borrowings in terms of Section 15 thereof in the Final Budget Position Report in relation to the Budget Economic & Fiscal Position Report tabled on the day fixed for the Appropriation Bill in Parliament, and since the Appropriation Bill specifically deals with 'Consolidated Fund' and **any other fund**, such reporting should be in comparison of actual data, with the data at the Appropriation Bill stage, and also be in respect of **all other Funds** being operated utilising public monies.

4. Furthermore, in relation to the foregoing, the Supreme Court in its Determination stated thus:

"In any event the expenditure would be subject to audit and the Auditor General would report on the matter to Parliament in terms of Article 154 of the Constitution."

"..... Parliament finally retains full control of public finance not only in the matter of allocation of expenditure but also by supervision of the actual expenditure for which there is adequate legislative provision in Article 154 of the Constitution"

5. Attention is drawn to the following data, as per the respective Documents referred to therewith:

As per the detail Budget estimates presented to Parliament in December 2005 for the Financial Year 1.1.2006 to 31.12.2006, the Total Budget for Head 801- 'Department of National Budget'	Rs. 23,257,026,000/-
As per Appropriation Act No. 39 of 2005 in December 2005, the Total Budget for Head 801- 'Department of National Budget'	Rs. 62,232,026,000/-
As per the Committee Stage Amendments to Appropriation Bill in December 2005, the Total Budget for Head 801- 'Department of National Budget' was increased by Rs. 39,590,000,000/- to a total of	Rs. 77,960,775,000/-
As per the Audited Financial Statements for the Year Ended 31.12.2006, the Total Expenditure incurred for Head 801- 'Department of National Budget' has been reported as <u>only</u>	Rs. 4,587,324,120/-
Therefore difference	Rs. 73,373,450,880/-

6. Attention is also drawn to the following extracts from the Report of the former Auditor General, Mr. S.C. Mayadunne, present Project Director of the Office of the Committee on Public Accounts and the Committee on Public Enterprises, titled – "Proposals for Strengthening of Parliamentary Control over Public Finance", forwarded in September 2007 to the Committee on Public Accounts and Committee on Public Enterprises, for review and action:

"This position has led to an aggravated situation due to the very wide gap between the Budget approved by our Parliament and the budget actually executed and the practice of not obtaining a special approval or authority of Parliament for such variances.

The revision of the Budget approved by the Parliament for the year 2006 by Rs. 220.2 Billion at the discretion of the Officers, as explained in detail in (2) Paragraph of Part II of this report can be cited as an example.

The revision of the budget by Rs.220.2 Billion at the discretion of the officers in terms of provisions in Section 5 of the Appropriation Act, No. 39 of 2005 including Rs.166 Billion in terms of authority granted under Section 6 of the said Act raises the question whether it tantamount to a partial abdication of the powers of full control over the Public Finance vested in the Parliament by Article 148.

As compared with Rs.609 Billion originally approved for expenditure for the year 2006 and Rs.1,072.8 Billion stated as the actual expenditure, that sum of Rs.220.2 Billion represents a very high percentage.

This becomes more serious as this form of version left to the discretion of the Officers has been arranged in such manner, it does not need the approval or sanction of the Parliament as well as that of the Cabinet of Ministries or even the Minister.

In addition to such revisions made to the provisions at the full discretion of the officers, instances of non-implementation of Budgets approved by Parliament properly abound as follows.

- i. Savings of approved provisions due to non-release of funds for Budget implementation.
- ii. Savings of approved provisions due to various other reasons
- iii. Irregular excess spending over the provisions
- iv. Discretionary expenditure within the approved provision contrary to estimates.
- v. Non-achievement of expected Performance despite expenditure incurred.

Even though provision has been made in Sections 13, 14 and 15 of the Fiscal Management (Responsibility) Act, No. 3 of 2003 for carrying out a statements of the approved Budget and the actual Budget and report thereon to Parliament, the Annual Report for the year 2006 presented by the Ministry of Finance and Planning does not clearly and adequately facilitate a comparison.

Therefore the opportunity afforded to report the actual position to the Parliament had been abandoned." (Emphasis added)

7. Reference is drawn to the Supreme Court 'dicta' at 1. and 2. above and to the fact that the utilization of funds and the deviations giving the reasons therefor, have not been transparently disclosed demonstrating prudential financial management in the Annual Report 2006, as also confirmed by the former Auditor General, as aforesaid.
8. **Hence, in compliance with the direction of the Supreme Court, please have the said data disclosed to Parliament and the public, without delay, inasmuch as such data ought to be readily available in the Department of State Accounts, which would have kept an accounting record thereof.**
9. With reference to the Supreme Court 'dicta' referred to at 4. above, pointing out that in any event the aforesaid data would be subject to audit by the Auditor General in terms of Article 154 of the Constitution, it has to be pointed out in the public interest and in the context of the said 'dicta' of the Supreme Court, that the Government's Financial Statements for the Year 2006 had been certified (presumably) in August 2007 by Auditor General, Mr. P.A. Pematilaka, who had given an 'unqualified' report on the said Government's Financial Statements of 2006.
10. Such 'unqualified' report has been notwithstanding the adverse Special Audit Report submitted to Parliament in July 2006 by former Auditor General, Mr. S.C. Mayadunne, adverting to a loss caused to government tax revenue amounting to about Rs. 389 billion due to failure to collect in accordance with legal provisions therefor, which is very material in comparison to the total revenue of Rs. 477 billion in the Year 2006.

"According to test checks carried out during the course of audit it was observed that the annual loss of the Government Tax Revenue is extraordinarily large. According to audit test checks the computable value of the loss of Government Tax Revenue and the failure to collect in accordance with the legal provisions during the last few years amounts to about Rs.389 billion while the amount that cannot be computed is extremely large."

The said Special Audit Report forwarded to Parliament in terms of the Constitution stands uncontradicted, without any evidence to have controverted the same.

11. It is indeed shocking that Auditor General, Mr. P.A. Pematilaka, who had given an 'unqualified' audit opinion on the Government's Financial Statements for the Year 2006, had in fact been the Director General, State Accounts, General Treasury during the very Year 2006, presumably at least upto 20th October 2006, as disclosed by the Government's Financial Statements for the Year 2005 issued by him on 20th October 2006, as Director General, State Accounts, under your very direction, purview and control, as Secretary to the Treasury.
12. Thus, Auditor General Mr. P.A. Pematilaka had been involved in and responsible for the maintenance, supervision and processing of the Government's Accounts during the Year 2006, as Director General, State Accounts, General Treasury. (*Relevant pages of documents attached*).
13. The aforesaid Special Audit Report to Parliament *inter-alia* in its Executive Summary has stated thus:
- "The institutions dealing with the Tax Revenue had not maintained an adequate tax management co-ordination with their supervisory institutions that is, the General Treasury and the Ministry of Finance."**
- "The responsibilities devolving on the Secretary to the relevant Ministry in terms of the provisions in the Constitution, and on the Secretary to the Treasury and the respective Heads of Departments as the Accounting Officers through the Financial Regulations had not been discharged properly." (*Emphasis added*)**
14. Furthermore, whilst the audit opinion given for the Year 2006, notwithstanding the foregoing adverse Special Audit Report of July 2006 forwarded to Parliament, had been an 'unqualified' opinion, on the other hand, **the audit opinion given on the Government's Financial Statements for the Year 2005 on 13th September 2006 by the Actg. Auditor General, Mr. W.D. Hemaratne had been a 'qualified' audit opinion, with comments and observations pertaining thereto. (*Audit Report attached*).**



Nihal Sri Amersekere

15th November 2007

cc: Mr. P.A. Ratnayake P.C., Addl. Solicitor General *vis-à-vis* the SC Determination
Mr. S.C. Mayadunne, former Auditor General, present Project Director, Office of the Parliamentary Committees on Public Accounts and Public Enterprises *vis-à-vis Reports referred to above*
Mr. M.N. Peiris, Secretary, Parliamentary Committees on Public Accounts and Public Enterprises
- Copies to be given to Hon. Members

Hon. Minister Rauf Hakeem, M.P. Chairman, Parliamentary Committee on Public Accounts
Hon. Wijeyadasa Rajapakshe P.C. M.P., Chairman, Parliamentary Committee on Public Enterprises
Hon. Ranil Wickremesinghe M.P., Leader of the Opposition, Parliament of Sri Lanka
Hon. Minister Nimal Siripala de Silva M.P., Leader of the House, Parliament of Sri Lanka
Hon. W.J.M. Lokubandara M.P., Speaker, Parliament of Sri Lanka

N. B. — Sinhala and Tamil versions of this Report will be printed Separately.



**THE GOVERNMENT OF THE DEMOCRATIC
SOCIALIST REPUBLIC OF
SRI LANKA**

**FINANCIAL STATEMENTS FOR THE YEAR
ENDED 31st DECEMBER, 2006**

DEPARTMENT OF STATE ACCOUNTS
GENERAL TREASURY
COLOMBO 01

Printed on the order of the Government

Printed at the Department of Government Printing, Sri Lanka.

To be purchased at the Government Publication Bureau, No. 132, Maya Avenue, Colombo 05

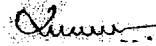
Price : Rs. 56.00

Postage : Rs. 20.00

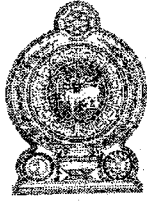
(VIII) AUDIT OPINION

The Balance Sheet of the Democratic Socialist Republic of Sri Lanka as at 31 December, 2006 and the Statement of Financial Performance and Cash Flow Statement, Stated accounting policies set out in Notes and other explanatory notes set out in Notes 1 to 31 for the year then ended were audited under my direction in pursuance of provision in Article 154 (1) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

I am of opinion so far as appears from my examination and to the best of my information and according to the explanations given to me, the said Financial Statements have been prepared and presented in accordance with Generally Accepted Accounting Principles and give a true and fair view of the financial assets and liabilities as at 31 December, 2006 and the results of its operations and its cash flows for the year then ended.



P. A. PEMATILAKA,
Auditor General.



ශ්‍රී ලංකා ප්‍රජාතාන්ත්‍රික සමාජවාදී ජනරජයේ
නියවැනි පාර්ලිමේන්තුවේ
(දෙවැනි සැසිවාරය)

පාර්ලිමේන්තු ප්‍රකාශන මාලා අංක : 02

இலங்கை சனநாயக சோசலிசக் குடியரசினது
ஆறாவது பாராளுமன்றத்தின்
(இரண்டாவது அமர்வு)

பாராளுமன்றத் தொடர் இல : 02

PARLIAMENTARY SERIES No : 02
OF THE SIXTH PARLIAMENT OF THE DEMOCRATIC
SOCIALIST REPUBLIC OF SRI LANKA
(SECOND SESSION)

(ඉංග්‍රීසි මුද්‍රණය/ஆங்கிலப் பதிப்பு / English Print)

ශ්‍රී ලංකා ප්‍රජාතාන්ත්‍රික සමාජවාදී ජනරජයේ
ආණ්ඩුක්‍රම ව්‍යවස්ථාවේ 154 (6) ව්‍යවස්ථාව ප්‍රකාර

රාජ්‍ය බදු ආදායම් කළමනාකරණය ආශ්‍රිත විශේෂ
ව්‍යාපෘති විගණනය පිළිබඳව
විගණකාධිපතිවරයාගේ වාර්තාව

இலங்கை சனநாயக சோசலிசக் குடியரசு அரசியல் யாப்பின் 154(6) ஆம்
உறுப்புரையின் பிரகாரம்

அரசாங்க வரி வருமானத்தின் முகாமைத்துவம் மீதான விசேட செயற்திட்டக்
கணக்காய்வு கணக்காய்வாளர் தலைமை அறிபதியின் அறிக்கை

REPORT OF THE AUDITOR GENERAL ON
SPECIAL PROJECT AUDIT ON THE MANAGEMENT OF
GOVERNMENT TAX REVENUE

IN TERMS OF ARTICLE 154(6) OF THE CONSTITUTION OF THE
DEMOCRATIC SOCIALIST REPUBLIC OF
SRI LANKA



විගණකාධිපති දෙපාර්තමේන්තුව
கணக்காய்வாளர் துறைமுக அறிவுறு திணைக்களம்
AUDITOR GENERAL'S DEPARTMENT



මගේ අංකය
எனது இல
My No.

පරිශීලක-20/වදාල-2004

ඔබේ අංකය
உமது இல
Your No.

දිනය
திகதி
Date

2006 ජූනි ෧෨

ගරු කපාහරායක කුමාර,

පරිශීලකවරයා,

ශ්‍රී සංවර්ධනපුර

කොළඹ.

ගරු කපාහරායකුණේ,

" රාජ්‍ය බදු ආදායම් කළමනාකරණය ආශ්‍රිත විශේෂ ව්‍යාපෘති විගණනය "

පිළිබඳ විගණකාධිපතිවරයාගේ වාර්තාව.

ශ්‍රී ලංකා ප්‍රජාතාන්ත්‍රික සමාජවාදී ජනරජයේ ආණ්ඩුක්‍රම ව්‍යවස්ථාවේ 154(6) වගන්තියට ප්‍රකාරව " රාජ්‍ය බදු ආදායම් කළමනාකරණය ආශ්‍රිත විශේෂ ව්‍යාපෘති විගණනය " සම්බන්ධව මාගේ වාර්තාව පරිශීලකවරයාගේ ව්‍යාපෘති කමිටේ සඳහා තෝරා පූර්වකම පුද්ගලයන් සඳහා.

ශ්‍රී - විශ්වාසී

(පැවැත් වෛශාලයන්ගේ)

විගණකාධිපති.

පිදුමස් වතුපොළ,
කොළඹ 17, ශ්‍රී ලංකාව

දුරකථනය
தொலைபேசி
Telephone } 2691111

කොළඹ - පුදුමස් වතුපොළ,
පිදුමස් වතුපොළ, කොළඹ 17

දුරකථනය
தொலைபேசி
Telephone } 2691111

INDEPENDENCE SQUARE,
COLombo 07, SRI LANKA

දුරකථන සංචාරක
தொலைபேசி
Telephone } 2691111
දුරකථන සංචාරක
தொலைபேசி
Telephone } 2691111



**Special Project Audit on the
Management of Government Tax
Revenue**



Contents

	Page
1. Introduction	1
2. Executive Summary	3
3. General Matters	4 - 26
4. Detailed Audit Findings	27 - 175
5. Overall Audit Findings	176 - 179
6. Recommendations	180 - 184

WEAK MANAGEMENT OF THE GOVERNMENT TAX REVENUE

Introduction

Observations relating to the audits of the management of the Government Tax Revenue appear in this report.

- According to test checks carried out during the course of audit it was observed that the annual loss of the Government Tax Revenue is extraordinarily large. According to audit test checks the computable value of the loss of Government Tax Revenue and the failure to collect in accordance with the legal provisions during the last few years amounts to about Rs.389 billion while the amount that cannot be computed is extremely large.
- The detailed observations relating to each audit test check are given in paragraph 4.
- The overall audit observations on these test checks are given in paragraph 5.
- Audit recommendations are given in paragraph 6.
- The audit coverage is very much limited due to limitations of time and resources and as such the possibility of the prevalence of large scale irregularities and weaknesses in the wider areas which were not covered in audit cannot be ruled out.

2. Executive Summary

- Even though the Tax Revenue represents about 90 per cent of the overall Government Revenue, a sound and efficient management had not been maintained for the management of the Tax Revenue.
- Even though the contribution of the Value Added Tax represented about 42 per cent of the Government Tax Revenue, its management is replete with serious deficiencies.
- One of the major reasons for the weak management of the Tax Revenue is the neglect of the responsibility for the introduction of specialised methodology of systems and controls by the authorities concerned.
- The most important weakness is the neglect of the usage of the existing methodology of systems and controls and the exercise of supervision thereon.
- The co-ordination of the flow of information and confirmations which should be in operation among the major Government institutions dealing in matters relating to the Tax Revenue had been at an extremely weak level.
- The inter-division co-ordination within the Government institutions responsible for the management of the Tax Revenue had also not been maintained adequately.
- The institutions dealing with the Tax Revenue had not maintained an adequate tax management co-ordination with their supervisory institutions that is, the General Treasury and the Ministry of Finance.
- The responsibilities devolving on the Secretary to the relevant Ministry in terms of the provisions in the Constitution, and on the Secretary to the Treasury and the respective Heads of Departments as the Accounting Officers through the Financial Regulations had not been discharged properly.
- Even though the timely reconciliation of the estimates and the actuals in relation to the Tax Revenue and the refunds from Tax Revenue, identification of discrepancies, identification of reasons for discrepancies, follow up action and taking appropriate action thereon are essential, any such action taken by the parties concerned could not be established in audit.
- A reliable, complete and up to date information data network essential for the tax management had not been built up and used.
- A methodology capable of preventing the irregular revision or deletion of the computerised data on tax is not in operation.
- Even though the sphere of tax forms the major source of revenue which forms the basis of the budget proposals of the Government, a methodology for estimating the Tax Revenue at an adequately reliable level is not being used.
- The reliability of statistics published as the Government Tax Revenue and Exports are uncertain to a considerable extent.
- The risk of uncertainty over the future economic plans exists due to the inability to utilise accurate data as a basis for planning.
- Questionable responses made instead of taking the immediate steps necessary to be taken even after serious lapses are brought to the notice of the institutions concerned by audit, pose problems.

**THE GOVERNMENT OF THE DEMOCRATIC
SOCIALIST REPUBLIC OF
SRI LANKA**

**CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED
31ST DECEMBER, 2005**

DEPARTMENT OF STATE ACCOUNTS
GENERAL TREASURY
COLOMBO 01.

Foreword

Accompanying Statement of Financial Performance & Statement of Cash Flows for the year, and the Statement of Financial Position as at the end of the year 2005 with relevant explanatory "Notes" and a Statement of Contingent Liabilities have been prepared and presented by the Department of State Accounts of the General Treasury.

These Statements have been prepared in full compliance with Generally Accepted Accounting Principles and practices and required guidance has been obtained from Sri Lanka Accounting Standards and International Public Sector Accounting Standards. This is the first time that these Financial Statements are presented in these formats. This is indeed the first step in the transitional stage of preparing and presenting the Government Financial Statements on the Basis of Accrual Accounting as against the present practice of Cash Based Accounting. In designing these formats for presenting these reports, different types of formats adopted by different countries for making advanced Public Sector financial reporting had been considered and ideas were taken from them to have an advanced presentation in consistent with the classification and presentation of the Annual Budget of the Government to enable to provide the reader with a clear view on the Financial Performance of the Government in compared with main targets of the Annual Budget as approved by Parliament.

These financial statements encompass the financial operations of forty four Government Ministries, one hundred and six Government Departments and twenty five District Secretariats/ Kachcheries performed in the process of making use of the financial resources allocated to them during the year 2005 in terms of the Annual Budget for implementing the intended work programs and projects for achieving the set goals and objectives. Basic information pertaining to the financial resources allocated by the Government in 2005 to eight Provincial Councils and Public Enterprises comprised of main two categories, i.e. Commercial Public Corporations, thirty three in number and the other Public Corporations and Statutory Boards getting involved in activities in regulatory, manpower development, infrastructure development etc., has also been furnished.

In compiling these reporting statements, the relevant data is collected in a specially designed system taken place in the form of a network involving above mentioned Public Institutions, by making use of electronic data transmission methodologies. Through this network all the financial data generated in the system gets transmitted to the central data base of the Department of State Accounts, being the Central Agency of the Government for financial information processing. In full conformity with the vision of the Department to be the Centre for Excellence in Government Financial Information, all the necessary internal controls, checks and balances and required level of supervision is maintained to maintain the integrity, accuracy and completeness of the data collected, stored and processed in order to assure the quality of information generated and furnished, as it is the main Government Department which is responsible for presenting the Annual Financial Statements of the Government in Parliament to discharge the responsibility for the public accountability on Financial resources utilized by the Government.

Any comments and suggestions to be considered for effecting further improvements to these Financial Statements are very much appreciated and such comments and suggestions in written form may be referred to the "Department of State Accounts, General Treasury, Colombo 01, Sri Lanka".

P.A. Pematilaka
Director General of State Accounts

Department of State Accounts
General Treasury
Colombo 01.
20th October, 2006.

N. B. — Sinhala and Tamil versions of this Report will be printed Separately.



**THE GOVERNMENT OF THE DEMOCRATIC
SOCIALIST REPUBLIC OF
SRI LANKA**

**FINANCIAL STATEMENTS FOR THE YEAR
ENDED 31ST DECEMBER, 2005**

DEPARTMENT OF STATE ACCOUNTS
GENERAL TREASURY
COLOMBO 01

Printed on the order of the Government

Printed at the Department of Government Printing, Sri Lanka.

To be purchased at the Government Publication Bureau, Colombo 01

Price : Rs. 61.00

Postage : Rs. 20.00

AUDIT OPINION

Audit of accounts of the Democratic Socialist Republic of Sri Lanka for the year ended 31 December, 2005 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.

Except for the effect on the financial statements of the matters referred to in paragraph 2.3 of my report, I am of opinion so far as appears from my examination and to the best of my information and according to the explanations given to me, the Statements of Financial Performance for the year ended 31 December, 2005 had been prepared and presented in accordance with the generally accepted accounting principles and the stated accounting policies as set out in notes (from Note Nos. 1 to 35) to the financial statements and give a true and fair view of the receipts and payments of the Government of Sri Lanka for the year ended 31 December, 2005.

Comments and observations arising out of the audit are contained in my report of even date addressed to the Deputy Secretary to the Treasury.



W. D. HEMARATNE,
Acting Auditor General.

13 September 2006
Auditor General's Department
Colombo 07.

Deputy Secretary to the Treasury

REPORT OF THE AUDITOR GENERAL ON THE ACCOUNTS OF THE DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA FOR THE YEAR ENDED 31 DECEMBER 2005

The audit of the accounts of the Democratic Socialist Republic of Sri Lanka for the year ended 31 December 2005 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. My observations on the accounts are given below.

1:2. Scope of Audit

Audit opinion, comments and findings in this report are based on a review of the financial statements presented to audit and substantive tests of samples of transactions. The scope and the extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitations of staff, other resources and time available to me.

2. Accounts**2:1. Audit Opinion**

Except for the effects on the financial statements of the matters referred to in paragraph 2.3 of this report, I am opinion so far as appears from my examination and to the best of my information and according to the explanations given to me, the Statement of Financial Performance for the year ended 31 December 2005 has been prepared and presented in accordance with the generally accepted accounting principles and the stated accounting policies set out in notes (Nos.1 to 35) to the financial statement and give a true and fair view of the receipts and payments of the Government of Sri Lanka for the year then ended.

2.2.1 Financial Performance

Financial Performance of the Government of the Democratic Socialist Republic of Sri Lanka for the year ended 31 December 2005 as compared with that for the preceding year is given below :

	2005	2004
	Rs. (Million)	Rs.(Million)
Receipts		
Tax Revenue	345,864	274,895
Non Tax Revenue and Others	55,414	36,220
Foreign Borrowings	73,370	73,465
Foreign Grants	14,451	3,803
Domestic Non Banking Borrowings	328,196	262,188
Recoveries from On Lent Loans	10,364	15,920
Divestiture Proceeds & Others	1,100	2,330
Donations Received Locally –Tsunami	154	-
Total Receipts	828,913	668,821
Payments		
Recurrent Expenditure	415,863	361,250
Public Investments	163,675	122,214
Foreign Debt Repayments	18,172	29,959
Domestic Debt Repayments	215,673	152,343
Net changes in Deposits and Miscellaneous	20,567	(2959)
Total Payments	833,950	662,807
Increase/(Decrease) in cash	(5,037)	6,014
Cash at the beginning of the year	2,272	(3,742)
Cash at the end of the year	(2,765)	2,272

2:2.2 Financial Position

A comparison of the assets and liabilities according to the new format of accounts of the Democratic Socialist Republic of Sri Lanka as at end of the year under review and the preceding year is given below:

	2005	2004
	Rs. (Million)	Rs. (Million)
Assets:		
Cash and Bank Balance	-	2,272
Loans to Public Officers	18,965	19,197
Advances to Government Departments	9,010	6,857
Foreign Aid Counterpart Funds	2,726	4,361
Membership Fees Paid	1,885	1,885
On lent loans	192,596	180,840
Capital Contribution in State Owned Enterprises	67,605	63,254
Total Assets	292,787	278,666
Liabilities		
Bank Overdrafts	2,765	-
Advance from the Central Bank	39,746	34,791
Foreign Loan Revolving Funds	13,904	13,465
Miscellaneous Funds	1,166	530
Government Borrowings	2,101,663	2,027,634
Deposits and Other Liabilities	14,363	38,653
Operating Accounts with Government Departments	2,171	3,661
Sundry Accounts	2,589	46
Total Liabilities	2,178,367	2,118,780

2.3. Comments on Accounts

2:3:1 Rendition of Accounts

The draft Annual Financial Statements of the Government of the Democratic Socialist Republic of Sri Lanka for the year 2005 had been furnished for audit on 24 April 2006. However, the Deputy Secretary to the Treasury by his letter number SA/AS/FA/03/97 dated 5 September 2006 informed that the above draft Annual Financial Statements to be considered as certified Financial Statements for the year 2005. The "Statement of Financial Performance" with the latest revised estimated figures for the year 2005 had also been submitted with the above letter.

2.3.2 Introduction of New Accounting Format

The Department of State Accounts had presented the accounts of the Government of Sri Lanka in a new format for the year 2005 in accordance with the Sri Lanka Accounting Standards and the International Public Sector Accounting Standards. These new type of Financial Statements reflects classification and presentation of the annual accounts in accordance with the budget as approved by the Parliament.

2:3:3 Accounting Deficiencies

Following accounting deficiencies are observed.

- Overdraft balance included unrealized cheques for which the validity period had elapsed for amounting to Rs.125,338,073 and unidentified debits and credits amounting to Rs.274,116,421 and Rs.37,827,386 respectively in respect of 36 Heads.

- (b) Following accounts balances had not been brought to accounts.

<i>Details of Accounts</i>	<i>Value</i>
Building Department Stores Account	769,765
Stock Certificates (Received from Inland Revenue)	88,589
Loan Account (Allocated from Votes)	9,150,920,188
Bank of Ceylon Share Capital	3,000,000
Peoples Bank Share Capital	3,000,000
	9,157,778,542

- (c) The Revenue and Expenditure Accounts had not been agreed with the corresponding balances of the relevant schedules. The following differences were observed.

	<i>Balance shown as per account</i>	<i>Balance shown as per schedule</i>	<i>Difference</i>
	<i>Rs.</i>	<i>Rs.</i>	<i>Rs.</i>
Total Revenue	401,277,998,780	401,431,988,334	153,989,554
Total Expenditure	833,949,986,253	803,545,990,884	30,403,995,369

- (d) According to the accounts, the revenue received on Social Responsibility Tax was Rs.255,306,098 whereas according to the Revenue Account submitted by the Department of Fiscal Policy and Economic Affairs, it was Rs.295,915,668. The reason for the difference of Rs.40,609,570 had not been explained.
- (e) Differences between the interest on Treasury Bonds and Interest on Overdrafts for the years 2000 and 2001 amounting to Rs.117,312,004 had been carried forward in the Bank Reconciliation Statement as unidentified debits without being cleared.
- (f) Balances of Rs. 188,235,925 in the Lloyd Merchant Dollar Accounts continued to be carried forward and shown in the accounts for several years whereas Central Bank of Sri Lanka had reported a nil balance on this account.
- (g) Seven deposit accounts showing debit balances totaling Rs.112,578,726 had not been investigated by the respective Departments.

2.3.4 Suspense Accounts

The following observations are made :-

- (a) Suspense Accounts Ledger had not been maintained properly for the year 2005.
- (b) Two debit balances amounting to Rs. 7,895,049 and five credit balances amounting to Rs.8,659,198 had been carried forward from 2003 and 2004 under the suspense account without being investigated and cleared.
- (c) Subsidy granted to the Ceylon Petroleum Corporation and Ceylon Electricity Board amounting to Rs.29,258,470,000 and Rs.11,305,692,442 respectively had been credited to suspense account – subsidy. No budgetary provision or supplementary allocation had been approved yet for those subsidies.

2.3.5 Non- Operating Control Accounts

Non-operating control account shows a debit balance of Rs.20.7 million as at end of the year under review as compared with Rs.260.5 million in the year 2004. Fourteen account balances, which had been transferred in 1998, had remained in the accounts without being cleared.

2.3.6 Un-reconciled Control Accounts

The Following observations are made.

- (a) The following differences were observed between the amounts shown in the accounts and in the ledger accounts maintained in the respective Departments.

<i>Details of Accounts</i>	<i>Balance as per account</i>	<i>Balance as per ledger</i>	<i>Difference</i>
	<i>(Rs.Mn) Cr/(Dr)</i>	<i>(Rs.Mn) Cr/(Dr)</i>	<i>(Rs.Mn)</i>
Asian Development Bank Loan(ADB), Central Bank of Sri Lanka (CBSL) Special Dollar Account	6,323	3,812	2,511
General Manager Railway	(39)	906	(945)

(b) Additional information regarding Fixed Assets, Advances, Deposits, Imprest and Bank Reconciliation had to be shown as notes to the Appropriation Accounts as per Director General of State Accounts. The following differences were observed between the aggregated amounts shown in the Appropriation Accounts and in the accounts maintained by the Department of State Accounts.

<i>Description</i>	<i>No. of sub Accounts</i>	<i>Amount as per Account</i>	<i>Amount as per notes of the appropriation accounts</i>	<i>Difference</i>
		<i>(Rs. Million)</i>	<i>(Rs. Million)</i>	<i>(Rs. Million)</i>
Advance Accounts	14	1,229.601	1,254.071	(24.470)
Deposit Accounts	10	302.128	438.917	(136.789)

As per Deputy Secretary to the Treasury's comments it was stated that under a completely correct situation even differences could be seen between Treasury figures and departmental figures, when taken them separately. The important requirement in such a situation is the reconciliation of the Departmental account balances with that of the Treasury books of Account at the end of the month or at the end of the year by identifying the reasons for the differences, for corrective measures, at their earliest.

It is observed that in a complex system involving a large number of accounts, existence of a difference between centrally maintained Treasury Book balances and Individual balances of few Departments as pointed out in the draft audit para would not necessarily give a correct picture and if a correct picture to be given in totally, a complete and overall assessment needed by taking all differences of debits and credits separately to ascertain the overall net difference, if any.

2.3.7 Foreign Loans

The following observations are made.

(a) According to the accounts, the total foreign debt outstanding as at 31 December 2005 was Rs.924,454 million whereas according to the Central Bank Bulletin for the month of December 2005 it was shown as Rs.944,478 million. The difference of Rs.20,024 million had not been reconciled or explained.

(b) A sum of Rs. 43,401,047 in the Temporary Loan Account had been inappropriately treated as Loan Borrowings in the final accounts.

(d) Debit Loan balances amounting to Rs.988,705,353 were included in the Loan Account.

2.3.8 Foreign Grants

According to the accounts, Grant Received in the form of cash was Rs. 3,145,012,189 whereas according to the individual balances, it was shown as Rs.3,145,192,731. The difference of Rs.180,542 had not been explained.

2.3.9 Foreign Aid Counterpart Funds

The following observations are made.

- (a) Debit balances of three Counterpart Fund Accounts aggregating to Rs. 1,027,195,239 had not been operated for several years and had been continuously brought forward without being investigated and adjusted in the accounts.
- (b) A sum of Rs. 299,824,617 had been carried forward for several years in the accounts without being settled.

2.3.10 On Lent Loans

According to the confirmation letters received from the National Water Supply and Drainage Board, lent loans granted by the Treasury was Rs. 521,734,016. But according to the Treasury books it was shown as Rs. 569,810,317. The difference of Rs. 40,076,301 had not been explained.

2.3.11 Capital contribution in State Owned Enterprises

The following observations are made in this connection.

- (a) Balance of the capital contributions in State Owned Enterprises as at 31 December 2005 were Rs. 67,604,832,106 whereas according to the ledger accounts it was shown as Rs. 138,627,750,664. The difference of Rs. 71,022,918,558 had not been explained.
- (b) Documentary evidence for additions to the shares during the year 2005 had not been made available for audit.
- (c) Investment in 955 Million shares in respect of sixteen institutions had not been agreed with the records held by Public Enterprises Reform Commission, which aggregating the Number of shares as 956 million only.
- (d) Investment in 691 Million shares in respect of eleven institutions had not been agreed with the related evidence and records, which aggregating the Number of shares as 280 million only.

2.3.12 Lack of Documentary Evidence

A credit entry made to the suspense account amounting to Rs.1,083,396,777 could not be satisfactorily vouched or accepted in audit due to non availability of documentary evidence.

2.3.13 Items of Contentious Nature

The following observations are made.

- (a) *Indian Line of Credit*
Interest received from 01 June 2002 to 01 December 2005 on Sub Loan Grants under the 12 Participatory Credit Institutions amounting to Rs.301,901,806 had been accounted under the Revenue Heads of 4000-2000-20-01. Out of interest received a sum of Rs. 172,186,875 received for the period of 2002 to 2004 had also been accounted during the year under review. Therefore, Revenue had been overstated by that amount.
- (b) *Purchase of Paddy*
Advance totalling Rs.2,324 million had been released to eighteen Divisional Secretaries for purchase of paddy during the year under review. Out of this amount, only a sum of Rs. 408.4 million had been settled as at 31 December 2005 and the unsettled amount was Rs.1915.6 million or 82%.

2.3.14 Budgetary Control

(a) Government Revenue

Although the estimated revenue for the year 2005 amounted to Rs.422,792 million, the actual revenue collected amounted to Rs.427,347 million or 101% of the total budgeted revenue. And also Government revenue had increased by 29% when compared with the previous year.

Instances of significant variances of Revenue Heads when compared with the Revised Estimates are given below.

<i>Revenue Heads</i>	<i>Category of Revenue</i>	<i>Revised Estimate</i>	<i>Actual</i>	<i>Variance</i>
		(Rs.Mn)	(Rs.Mn)	%
1001.20.0	Export Duties	1	21	2000
1001.30.0	Other Import and Export Charges	425	723	70
1002.10.0	Value Added Tax	138	9	93
1002.50.0	Excise (Special Provision) Duty	57,398	65,385	14
1003.20.0	Transfer Tax	21	38	81
1003.40.0	Social Responsibility Tax	405	255	(37)
1003.90	License Taxes and Others	225	336	49
1004.10.1	Dividend Tax	16,224	1,993	(88)
1004.10.2	Economic Service Charge	8,000	1,683	(79)
1004.10.9	Other	-	17,719	17,719
2002.20.1	On Lending Interest	6,864	15,642	128
2003.10.0	Departmental Sales	38	116	205
2003.90.0	Other Receipts	3,390	6,001	77
2004.10.0	Social Security Contribution to Central Government	5,314	2,971	(44)

As per Deputy Secretary to the Treasury's comments it is emphasized that the percentage as calculated in the draft audit para is mainly due to certain errors made in the classification of actual revenue collected against the applicable Revenue codes, as done by the staff in the revenue collection departments. While admitting that this type of human errors are possible under any circumstances in such a large and complex system, it is also emphasized that this observation has no any material impact on the true and fair view needed to be in built in to the financial statement provided.

(b) Government Expenditure

The following observations are made.

- (i) Expenditure of the Government had increased by 13%. Further, it was observed that out of the total expenditure, a sum of Rs.233,845 million or 28% represented repayment of public debt.
- (ii) The entire estimated provision in the annual budget amounting to Rs.145,747 million in relation to 183 Heads of respective Ministries and Departments had not been fully utilized. Further the expenditure incurred in three instances during the year 2005 exceeded the provision made in the annual estimates by Rs.33,922,535.
- (iii) Instances of significant variances in actual expenditure when compared with the revised estimates are given below.

<i>Revenue Heads</i>	<i>Ministry/Department</i>	<i>Revised Estimate</i>	<i>Actual</i>	<i>Variance</i>
		(Rs.Mn)	(Rs.Mn)	%
102	Office of the Prime Minister	765	452	41
224	Ministry of Industries and Investment Promotion	815	478	41
234	Ministry of Small and Medium Enterprise Development	3,125	1,616	48
244	Ministry of Constitutional Affairs and National Integration	208	135	35
314	Ministry of Fisheries and Aquatic Resources	5,609	3,680	34
334	Ministry of Justice and Judicial Reforms	945	597	37
424	Ministry of Post, Telecommunications and Udarata Development	1642	339	79

Revenue Heads	Ministry/Department	Revised Estimate	Actual	Variance
		(Rs.Mn)	(Rs.Mn)	%
434	Ministry of Small and Rural Industries	1437	837	42
474	Ministry of Skills Development, Vocational and Technical Education	2,506	1,700	32
544	Ministry of Agriculture , Marketing Development and Co-operative Development and Hindu Affairs and Ministers Assisting Education and Vocational Training	712	312	56
584	Ministry of Medium and Small Scale Plantation Industries and Rural Human Resources Development	603	353	41
846	Department of Economic Policy Research	25	0.96	96
861	Department of Animal Production and Health	412	282	32

This indicate the necessity of efficient budgetary control over public expenditure of the Government.

3. Systems and Controls

Special attention is needed in respect of the following areas to control :—

- (a) Accounting for Public Debt, Grants, On Lent Loans and Counterpart Funds
- (b) Capital Contribution in State Owned Enterprises
- (c) Advances made to Other Institutions and Ministries
- (d) Cash and Bank Balances
- (e) Reconciliation of Control Accounts
- (f) Non-operating Accounts
- (g) Revenue Collection
- (h) Maintenance of Expenditure Records
- (i) Deposit Accounts


W. D. HEMARATNE,
 Acting Auditor General.