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**EMPLOYMENT INVESTMENT AND ENTERPRISE  
DEVELOPMENT DIVISION (EIED)**

**OF THE  
MAHAWELI AUTHORITY OF SRI LANKA**

**FINANCIAL MANAGEMENT SYSTEMS REVIEW**

IQC - D/O # 383-0499-C-01-3452-00

 **ERNST & YOUNG**  
OCTOBER, 1993

A

WRHF/DTR/DdeZ

November 1, 1993

Mr. Mark Anderson  
Executive Officer  
USAID - Mission to Sri Lanka  
P.O. Box 106  
Colombo

Dear Sir

IQC - D/O No. 383-0499-C-01-3452-00

*As requested by you vide the above Delivery Order, we have now completed the financial management systems review of the Employment, Investment and Enterprise Division (EIED) of the Mahaweli Authority of Sri Lanka and have pleasure in forwarding our report in this regard.*

*We trust that the information contained in this report is adequate for your purposes. If however, you require any further information or clarification in this connection, please do not hesitate to contact us.*

*We also wish to place on record our appreciation of the co-operation and assistance provided to us by the management and staff of the EIED and the Controllers Office and project personnel at the USAID Mission.*

Yours faithfully

(Sgd.) Ernst & Young.

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DEVELOPMENT DIVISION (EIED)  
OF THE  
MAHAWELI AUTHORITY OF SRI LANKA

**FINANCIAL MANAGEMENT SYSTEMS REVIEW**  
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## **EXECUTIVE SUMMARY**

### **BACKGROUND**

Ernst & Young was requested by the USAID Mission to Sri Lanka to carry out an assessment of the adequacy of the financial management systems of the Employment, Investment and Enterprise Development (EIED) division of the Mahaweli Authority of Sri Lanka.

The primary responsibility of the EIED is to plan and implement the Mahaweli Enterprises Development (MED) Project. The total cost of this project is estimated at US\$ 24 Mn, of which the planned contribution from USAID amounts to US\$ 15 Mn.

### **OUR APPROACH**

We obtained the existing accounting and internal control systems of the organisation through inquiry and observation and documented same using flow charts. We also walked through a few transactions to confirm our understanding of the documented system.

In addition, we visited a project site to familiarise ourselves with the project and review the transactions at the site.

We also discussed the weaknesses observed in the accounting and internal control systems and the recommendations made thereon with the management of EIED.

### **RESULTS**

The main observations made during the course of our review of the financial management system of EIED, are as follows:

- Key managerial positions such as the Director EIED, and Deputy Director, Enterprise Development have been vacant for a considerable period. However, it is noted that the Deputy Director (Investment Services and Marketing Development) has been seconded to the post of the Director EIED.



- There is no adequate segregation of duties in the finance division, especially with regard to handling cash and maintaining related records.

The above matters along with the other observations and findings are discussed in detail in section 5.0. A summary of our recommendations in order to improve the financial management systems of EIED are as follows:

- Key managerial vacancies such as the Director EIED and Deputy Director - Enterprise Development should be filled. (Page 7)
- The fixed assets register should be completed as to the respective location of the assets. (Page 13)
- The system with regard to assets sent to project sites should be strengthened as recommended in section 5.4.3. (Page 14)
- As regards the inadequate segregation of duties, we recommend that the duties between the two clerks be reallocated as suggested in section 5.4.5. (Page 15)

## **1.0 BACKGROUND OF THE PROJECT**

### **1.1 Objectives.**

The Purpose of the Mahaweli Enterprise Development (MED) project is to accelerate the creation of permanent jobs in private enterprise in the Mahaweli settlement area, by facilitating the development of small enterprise, encouraging the formation of medium and large scale enterprise, and developing a market oriented environment conducive to sustained increase in employment in private enterprises of all sizes.

The project was commissioned in June 1989, with an estimated life span of six years. The activities of the project will focus on systems B,C,G and H of the Mahaweli settlement area, and the Uda Walawe special area.

### **1.2 Components of the MED Project.**

The three major components of the project are described below:

- Special Studies  
This component will comprise a phased review and analysis (with the active participation of the private sector) of the policies, regulations, procedures and decision making criteria which affect enterprises in the Mahaweli regions.
  
- Medium and Large Scale Enterprise Development  
This component will share the high risks and costs associated with pioneer enterprises and meet the investor's needs for information and expertise.
  
- Small Scale Enterprise (SSE) Development  
This component will concentrate on the small investors. The assistance to the SSE will include access to land with transferable title or lease, business advisory services, training for aspiring entrepreneurs and existing entrepreneurs with common technical problems, entrepreneur development, access to administrative services at cost and assistance to access credit.

### 1.3 Project Funding

The estimated cost of the project is US\$ 24 Million, of which 63% amounting to US\$ 15 Million is to be funded by an AID grant. The balance 37% is to be funded by the Government of Sri Lanka through the Mahaweli Authority of Sri Lanka.

The relative contributions from the above funding sources upto September 1993, are as follows:

	Rs. Mn	%
GOSL	170	38
USAID	<u>273</u>	<u>62</u>
	443	100
	===	===

### 1.4 Project Implementation.

The implementing agency for the project is the Employment, Investment and Enterprise Development (EIED) division of the Mahaweli Authority of Sri Lanka (MASL).

## **2.0 SCOPE OF THE ASSIGNMENT**

### **2.1 Objective.**

Ernst & Young was requested by the United States Agency for International Development (USAID) Mission to Sri Lanka to carry out an assessment of the adequacy of the financial management systems of the Employment, Investment and Enterprise Development Division (EIED) of the Mahaweli Authority of Sri Lanka (MASL).

### **2.2 Tasks.**

We were required to carry out the following tasks in achieving the above objective as given in the relevant Delivery Order.

- I. Review and comment on the legal status, goals, organisation structure, structure of the finance division and sources of funding of the organisation being assessed. *(Section 3.0)*
- II. Review and comment on the administrative and management capability of the organisation, the finance division, and in particular the management of the USAID sponsored projects. *(Section 4.0)*
- III. Review, document and comment on the accounting system in place, accounting records maintained, and internal controls etc.

In connection with the above, we were also required to assess the adequacy of the organisation's invoice examination capability, payment procedures and internal controls in connection with approval and payment of invoices. *(Section 5.0)*

- IV. Review and comment on the internal control system to determine:
- (a) The adequacy of segregation of duties and responsibilities in the following functional areas:
- \* Accounting
  - \* Procurement (Contracting)
  - \* Collection
  - \* Voucher Payments
  - \* Reporting
- (b) The effectiveness of the current internal control system with regard to the management of funds. *(Section 5.0)*
- V. Review and comment on the contract management capabilities and procedures to advertise, solicit, negotiate, award and administer contracts both for commodities and services. *(Section 6.0)*
- VI. Review and document the inventory control procedure of the organisation, including the adequacy of maintenance of asset registers. *(Section 7.0)*
- VII. Ensure the compliance with laws and regulations by the agency. *(Section 8.0)*
- VIII. Review the adequacy of the recording and reporting procedures of the counterpart contribution under the AID grant. *(Section 9.0)*

### **2.3 Our Approach**

The following procedures were adopted by us in carrying out the above tasks:

- Reviewed the agreement between the MASL and USAID to obtain an understanding of the terms and conditions of the contract, the background of the project and the implementing agency etc.
- Reviewed the Mahaweli Act to ensure that the Agency is complying with the relevant regulations.
- Obtained the existing accounting system through inquiry of client personnel, and available documentation such as systems manuals etc.
- Documented the existing system through the use of flow charts.
- Performed walk-through tests and observed the client procedures to ensure the proper implementation of the documented system.
- Visited the project site (i.e Embilipitiya) in order to familiarise ourselves with the MED Project and to review the transactions at the site.
- Discussed the main areas of concern/weaknesses in the system and measures of improving the financial management system with the management of the implementing agency.

## **3.0 OPERATING ENVIRONMENT**

### **3.1 Legal Status**

EIED is an agency of the Mahaweli Authority of Sri Lanka, which was incorporated under the Mahaweli Authority Act No. 23 of 1979.

### **3.2 Responsibilities of the EIED**

EIED will bear primary responsibility for planning and implementation of the MED Project. However, some of the functions have been directly contracted to the International Science & Technology Institute Inc. (ISTI), a private consulting firm based in Washington D.C.

The project inputs in achieving its objectives can be broadly classified as follows;

- Technical Assistance
- Training
- Pre-investment programs
- Investment Promotion
- Information Dissemination
- Equipment Procurement

### **3.3 Organisation Structure**

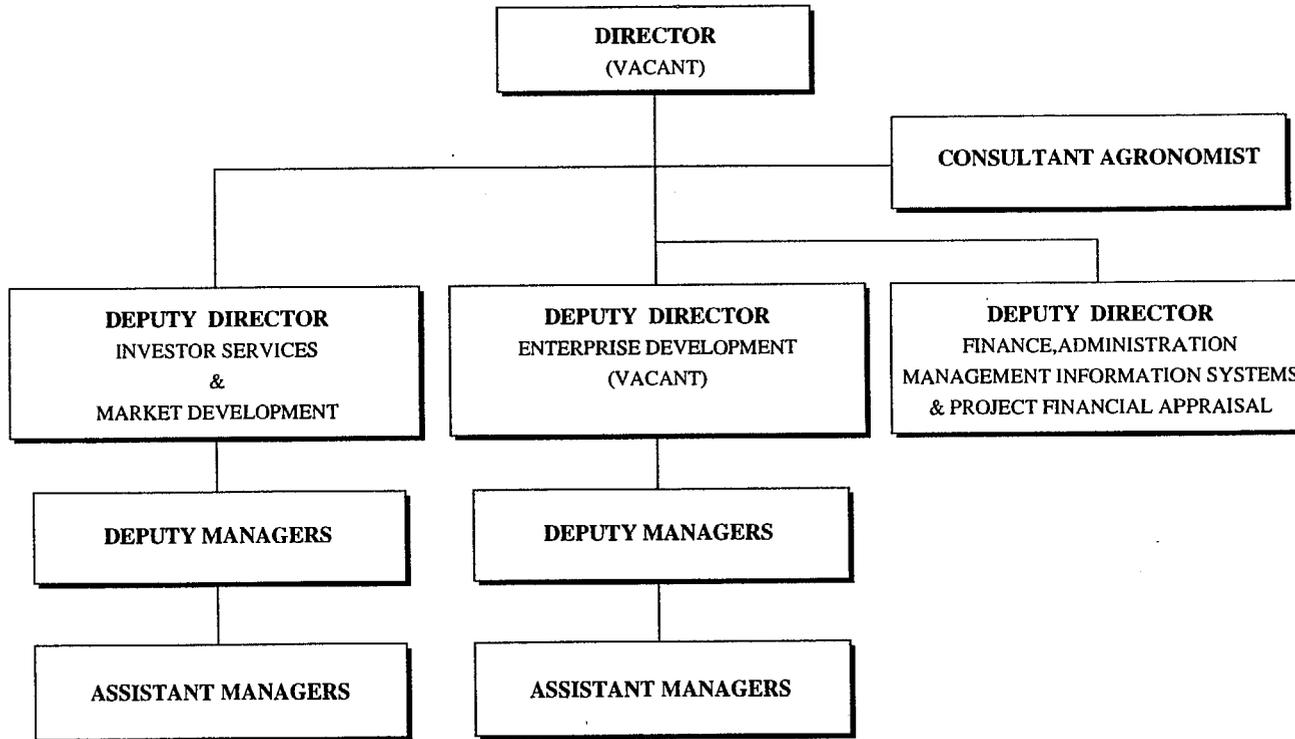
The organisation structure of the Senior Management of EIED is given in Exhibit 3.1, whilst the organisation structure of the Finance and Administration Division is given in Exhibit 3.2.

The present staff strength of EIED is 77 employees, although the approved cadre is 102 employees. This can be attributed to the decreasing trend in activities of the Agency.

Since, EIED is a relatively small organisation in terms of the number of employees, we noted an instance of the lack of segregation of duties. This is discussed later in this report.

We also noted that the key positions of the Director and Deputy Director - Enterprise Development, have been vacant for sometime. Therefore, we recommend that these key vacancies be filled as early as possible or make permanent the persons seconded to those positions to ensure the smooth functioning of the organisation.

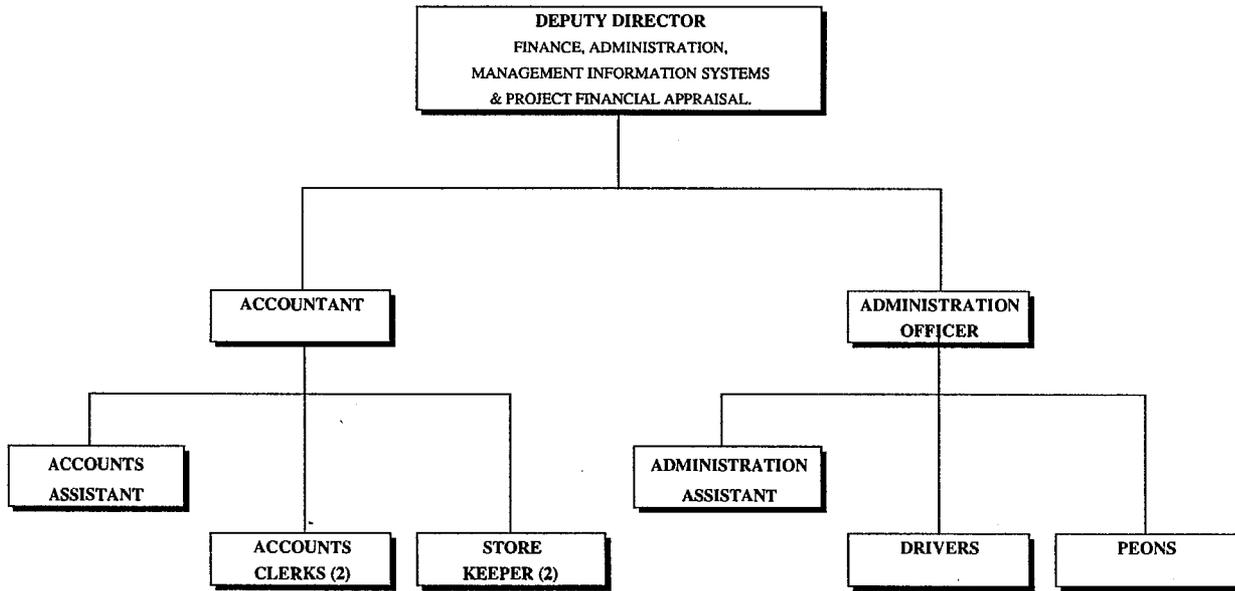
**ORGANISATION CHART**  
**SENIOR MANAGEMENT-EIED**



AV

### ORGANISATION CHART

#### FINANCE & ADMINISTRATION DIVISION



1B

#### 4.0 ADMINISTRATIVE AND MANAGEMENT CAPABILITIES

The experience and qualifications of the senior management of the organisation is given below :-

DESIGNATION	NAME	DATE OF APPT.	QUALIFICATIONS	EXPERIENCE
Actg. Director/ Deputy Director (Inv. Serv. & Mkt. Devlpt.)	W. A. S. Amarasinghe	Nov. 17, 1990	B.Sc. University of Colombo M.Sc (Food & Nutrition) University of Kelaniya	1980 Project Officer, MEA  1984 - 1985 Dec. Project Officer/ Business Development Officer, MEA  1986 - 1988 Deputy Manager, EIED  1988 April - 1993 Manager, EIED
Consultant Agronomist	U. Pethiyagoda	July 1, 1989	B.Sc. (Ceylon), Ph.D (London) DIC, FNASSL, FNIPM	1954 - 1961 Lecturer in Botany, University of Ceylon, Colombo.  1961 - 1975 Head , Divisions of Physiology Prorogation and Breeding, Tea Research Institute, Talawekelle.  1975 - 1981 Director, Coconut Research Institute, Lunuwila  1981 - 1984 Expert in Breeding - FAO Date Palm Project, Baghdad, Iraq.
Senior Deputy Director (Finance and Administration)	Mrs. P. C. Matthias	Aug. 17, 1989	Fellow Member of the Institute of Chartered Accountants of Sri Lanka	1977 - 1980 Accountant, SD&CC  1980 - 1983 Chief Accountant, SD&CC  1983 - 1989 DGM (F), SD&CC  1989 - July 1993 Manager (F&A), EIED

DESIGNATION	NAME	DATE OF APPT.	QUALIFICATIONS	EXPERIENCE
Senior Accountant	Mr. S.G. Somasiri		B. Com. (Spl.) - 1980 University of Sri Jayawardenepura Chartered Licentiate Certificate Higher National Diploma in Accountancy (CTC)	1970 - 1980 G.C.S. Clerk, Govt. Dept.  1980 - 1983 Accountant, C.W.E  1983 - 1988 Internal Auditor, MASL  1988 - 1993 Accountant, MASL

In addition, EIED boasts of nine highly qualified and experienced Deputy Managers and eleven Assistant Managers, responsible for the twelve projects currently in operation.

## **5.0 ACCOUNTING AND INTERNAL CONTROL SYSTEMS**

### **5.1 Existing Systems**

The existing accounting and internal control systems of EIED except for the petty cash system at the project sites which is noted below, are given by the flow charts annexed to this report.

Our observations and recommendations with regard to these systems are discussed in Section 5.4

#### Audit

The annual statutory audit is carried out by the Auditor General of Sri Lanka. The most recent audit report available is for the year ended December 31, 1991.

In addition to the annual statutory audit, EIED is also subject to review by the Internal Audit Division of MASL. This is carried out twice a year and the audit report is submitted to the MASL for necessary action.

#### Petty Cash at the Project Sites

An imprest of Rs. 2,500/- is available with the respective Deputy Managers (DM) at the 12 project sites for sundry expenses. Reimbursements are done once the DM completes a petty cash voucher at the head office with the relevant supporting documents attached.

### **5.2 Accounting Records**

The main books of account and control registers maintained by the Agency are described below:

- Voucher Register (VR)  
All payment vouchers raised and approved are serially numbered and entered in this Register.

- Votes Ledger (VL)  
This ledger acts as a temporary general ledger. All payments except advances are entered in this ledger under the relevant account code.
- General Ledger (GL)  
At month end, a data entry operator enters all payment vouchers and journal vouchers into a PC based computer system in order to generate the general ledger.
- Advances Register (AR)  
All advance payments are recorded in the Advances Register until final settlement.
- Cash Book  
The agency parallelly maintains two manual as well as a computerised cash book. The computerised cash book is generated at the end of the month and compared with the manual cash books. The two manual cash books maintained by EIED are for the purpose of segregating the funds received and utilized from the Government of Sri Lanka and the USAID.
- Fixed Assets Register (Computerised)  
All fixed assets procured for the MED project are recorded in this register.

### **5.3 Duties of the Accounting Personnel**

The finance division comprises seven persons with the Deputy Director-Finance and Administration as the divisional head.

The various duties and responsibilities of the personnel in this division are summarised below.

### Deputy Director, Finance and Administration

As the head of finance and administration functions of the organisation, the Deputy Director is responsible to the Director, EIED for these two divisions. As such, she is involved in reviewing and approving all finance related activities as given in the annexed systems flow charts.

### Accountant

Certifying of payment vouchers, preparing the final accounts and overall supervision of the accounts department.

### Clerk - 1

Maintains the manual cash books, Voucher Register and Votes Ledger. He is also in charge of the cash, the writing of cheques, and the preparation of the monthly bank reconciliation statement.

### Clerk - 2

Maintains the Advances Register and Prepares the statement of expenditure submitted to USAID and MASL. He is also responsible for the checking of the data keyed in by the data operator (Employee of ISTI) before generating the cash book and general ledger.

### Store Keeper - 1

This store keeper is in charge of the fixed assets. Therefore, his duties include raising purchase orders, GRN's GIN's (goods issue notes) and maintaining the bin cards and the fixed assets register. He is also involved in calling for quotations from the registered suppliers for stationery and other small commodities.

### Store Keeper - 2

Store Keeper -2, is in charge of stationery and other miscellaneous items. He is responsible for raising P.O.'s GRN's, GIN's and maintaining the Bin-cards for such items.

## **5.4 Review of Internal Controls**

From our review of the internal control systems of the organisation, the following weaknesses and instances of non-compliance with the existing systems were observed.

### **5.4.1 Observation:**

The fixed assets register does not indicate the location of the respective assets.

#### **Implication:**

It may be difficult to identify the location of a particular asset at any given time.

#### **Recommendation:**

The Goods Issue Note (GIN) identifying the destination of the asset should be made in triplicate one of which (2nd copy) should be sent to the clerk who maintains the fixed assets register.

Any transfer between locations should also be facilitated by an Asset Transfer Note, a copy of which should be sent to the same clerk.

#### **Management's Comments:**

The asset coding system is so designed as to identify the different locations. However, the recommendation is accepted and the fixed assets register will be updated accordingly, based on a physical verification of assets carried out recently.

### **5.4.2 Observation:**

There are instances where the asset purchased is directly delivered and installed at the required location. Even in such instances, the GRN is raised at the Head Office in Colombo on production of the invoice and delivery order by the supplier, duly signed by the Deputy Manager of the respective location as evidence of receipt of goods.

Implication:

It may be possible for the supplier to produce the invoice for payment at the Head Office without actually delivering the goods by forging the signature of the Deputy Manager or alter the details of the actual invoice in the absence of a proper Goods Received Note (GRN).

Recommendation :

A method should be devised whereby the Deputy Manager is able to communicate directly with the Head Office confirming the receipt of goods. For this purpose, please refer recommendation in 5.4.3.

Management's Comments :

Since the frequency of such commodity purchases are low, there has always been communication between the Deputy Manager and the Head Office through telephone or facsimile.

However the recommendation is accepted.

5.4.3 Observation :

When assets are received at project sites, no check exists to ensure that the goods received conform to the order placed.

Implication :

Assets received at project locations, may not conform to the order specifications.

Recommendation :

We recommend that the second copy of the Purchase Order (PO) be sent to the respective location when assets are to be delivered directly to such locations. The Deputy Manager should check the goods received with the P.O. and sign same as evidence of checking. This P.O. along with the suppliers' Delivery Order duly signed as accepted by the Deputy Manager should then be sent to the Head Office through the Supplier. These documents together with the Invoice may then be produced for payment at the Head Office.

Management's Comments :

Same as 5.4.2

5.4.4 Observation :

When performing a walk - through of the tendering system, we noted an instance where a particular asset was purchased based on a previous tender decision which had already been satisfied.

i.e. December 15, 1992 - Purchase of Furniture for Rs. 81,510/- based on a decision dated October 16, 1992.

Implication :

In addition to being an instance of non-compliance with the stipulated procedures, the Agency may not get the best prices when procuring assets.

Recommendation

We recommend that the Agency adhere strictly to the tender procedures stipulated by the Mahaweli Authority.

Management's Comments

Normally, internal decisions are permitted for purchases less than Rs. 500,000/-. The above instance may have been due to an urgency. Also, there was no change from the original quotation price.

5.4.5 Observation :

The segregation of duties among the accounting personnel is not adequate. It was noted that the clerk responsible for the handling of cash was also responsible for maintaining the relevant records such as the cash book etc. He is also responsible for preparing the bank reconciliation statement.

Implication :

Any errors or defalcations may not be discovered, at least for a very long time.

Recommendation

We recommend that the duties between the two clerks be re-allocated so that the clerk responsible for handling cash will not be responsible for maintaining the pertinent records.

Management's Comments

The above recommendation is accepted and the reallocation of staff will be considered.

## 6.0 CONTRACT MANAGEMENT CAPABILITY

### 6.1 Contracting Procedure

EIED being an agency of MASL is required to adhere to the procedures stipulated by MASL in contracting for projects and purchase of capital assets. These procedures are as follows:

Value Limits (V)	Procedure before authorisation	Approval
V > Rs. 2,000,000	Ministry Tender Board	Secretary General
Rs.2,000,000 > V > 500,000	MASL Tender Board	Secretary General
500,000 > V > 50,000	MASL/Divisional Tender Board	Secretary General/ Director Personnel and Admn.
50,000 > V > 25,000	Sealed Quotations	Head Of Division
25,000 > V	Sealed Quotations	Manager Finance/ Accountant/Administration Officer

### 6.2 Management Capabilities and Personnel Involved

The ministry tender board and The MASL tender board consist of competent personnel with adequate capabilities. The Secretary General of the ministry has a list of the suitable personnel in various divisions and their relevant qualifications and experience. Depending on the situation, the Secretary General will appoint the appropriate persons to the tender board.

Even in instances where internal decisions are permitted, if necessary, the Agency can forward the tenders/quotations received to the MASL for a decision.

The Mahaweli Engineering and Construction Agency (MECA), which specialises in construction is also an agency of MASL. This could be considered a strength to EIED where construction management is concerned.

### **6.3 Types of Contracts**

The EIED follows tender procedures for the purchase of fixed assets and to obtain the services of professional institutions for the purpose of training entrepreneurs.

For advertising, quotations are called from approximately 3-4 advertising firms and the decision is made by the Director and Manager of the marketing division.

For stationery items, quotations are called from registered suppliers each time a requisition is made. The decision is taken by the Administration Officer and the Accountant which is approved by the Senior Deputy Director.

## **7.0 INVENTORY CONTROL PROCEDURE**

The only consumable stock items purchased by EIED are stationery and tyres. The systems pertaining to these items are given in the annexure to this report.

Due to the insignificance of the items involved and the relative size of the organisation, we accept the existing systems as adequate with regard to inventory control.

The internal controls relating to capital assets were dealt in Section 5.0.

During the course of our review, we also followed up on the recommendations made by Coopers and Lybrand in their report on the *Commodity Tracking System* dated March 1993. In this regard, whilst the procedure of cancelling supporting documents is satisfactory, the recommendation regarding the purchase orders has not been implemented due to the low volume of activity.

## **8.0 COMPLIANCE WITH LAWS AND REGULATIONS**

EIED being an agency of the MASL, is governed by the Mahaweli Authority of Sri Lanka Act No. 23 of 1979.

From our limited review, we did not encounter any instance of non compliance with the above Act nor of the general laws applicable to such an agency.

Our review was also extended to ensure the compliance of the terms and conditions stipulated in the project grant agreement between USAID and the Government of Sri Lanka.

## **9.0 REPORTING PROCEDURES**

EIED maintains two separate cash books in order to segregate the funds received from USAID from the funds received from the MASL. Also the Agency operates two bank accounts; ANZ Grindlays Bank for USAID funds and the Bank of Ceylon for MASL funds.

A statement of recurrent expenditure which represents the total counterpart contribution is sent monthly to the financial controller of MASL. This expenditure is reported under the following categories;

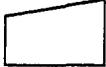
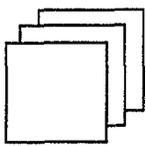
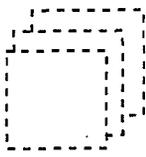
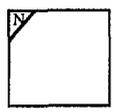
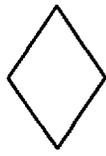
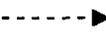
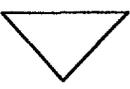
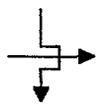
- Personnel Emoluments
- Travelling Expenses
- Supplies and Requisites
- Repairs and Maintenance
- Grants, Contributions and Subsidies
- Pensions/Retirement Benefits
- Others

The report format is well structured and identifies clearly the following :

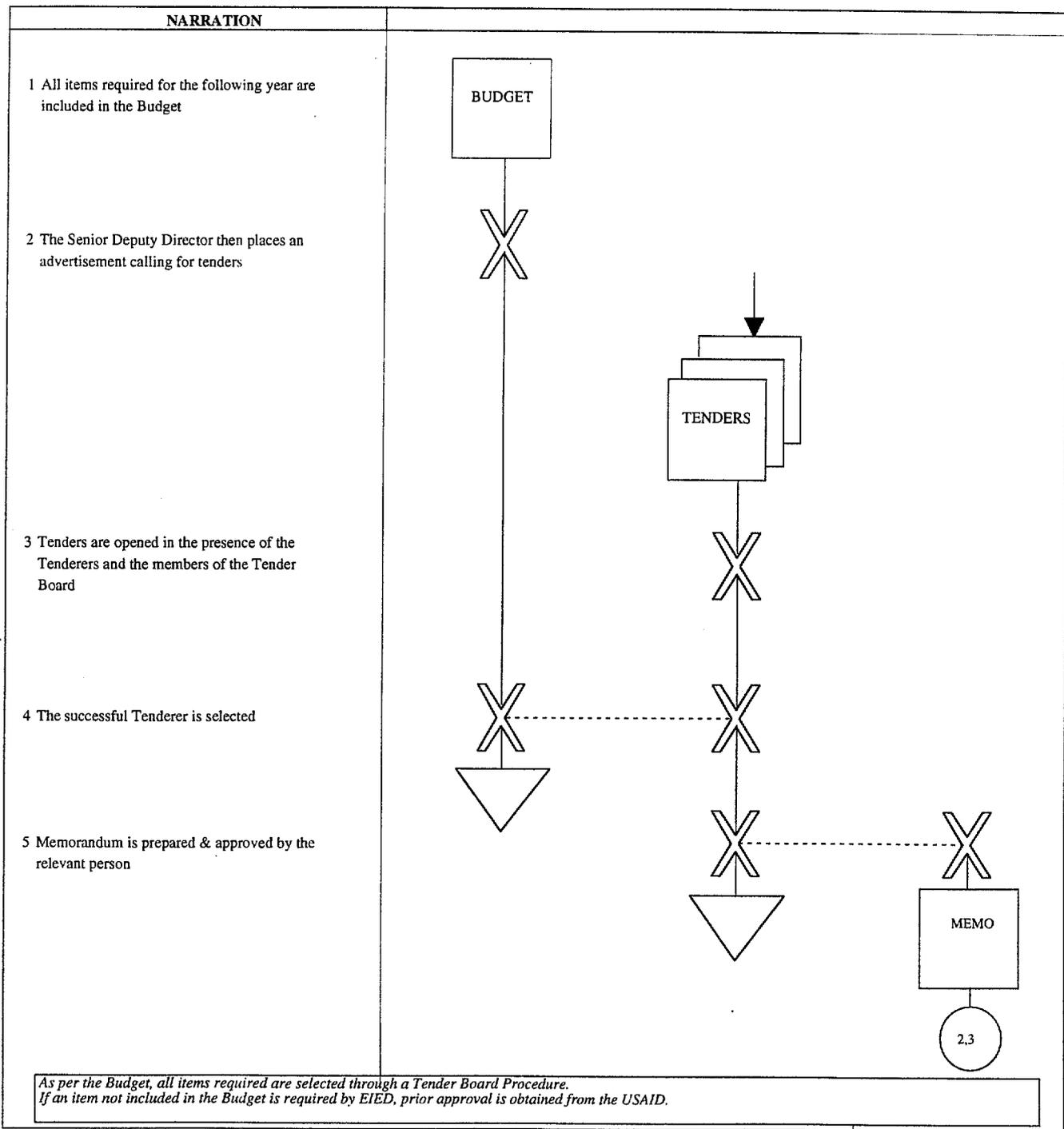
- Total expenditure for the month
- Total cumulative expenditure from beginning of period to date
- Budgetary allocation for the corresponding month
- Budgetary allocation for the corresponding period and remarks thereon

**ANNEXURE**  
SYSTEMS FLOW CHARTS

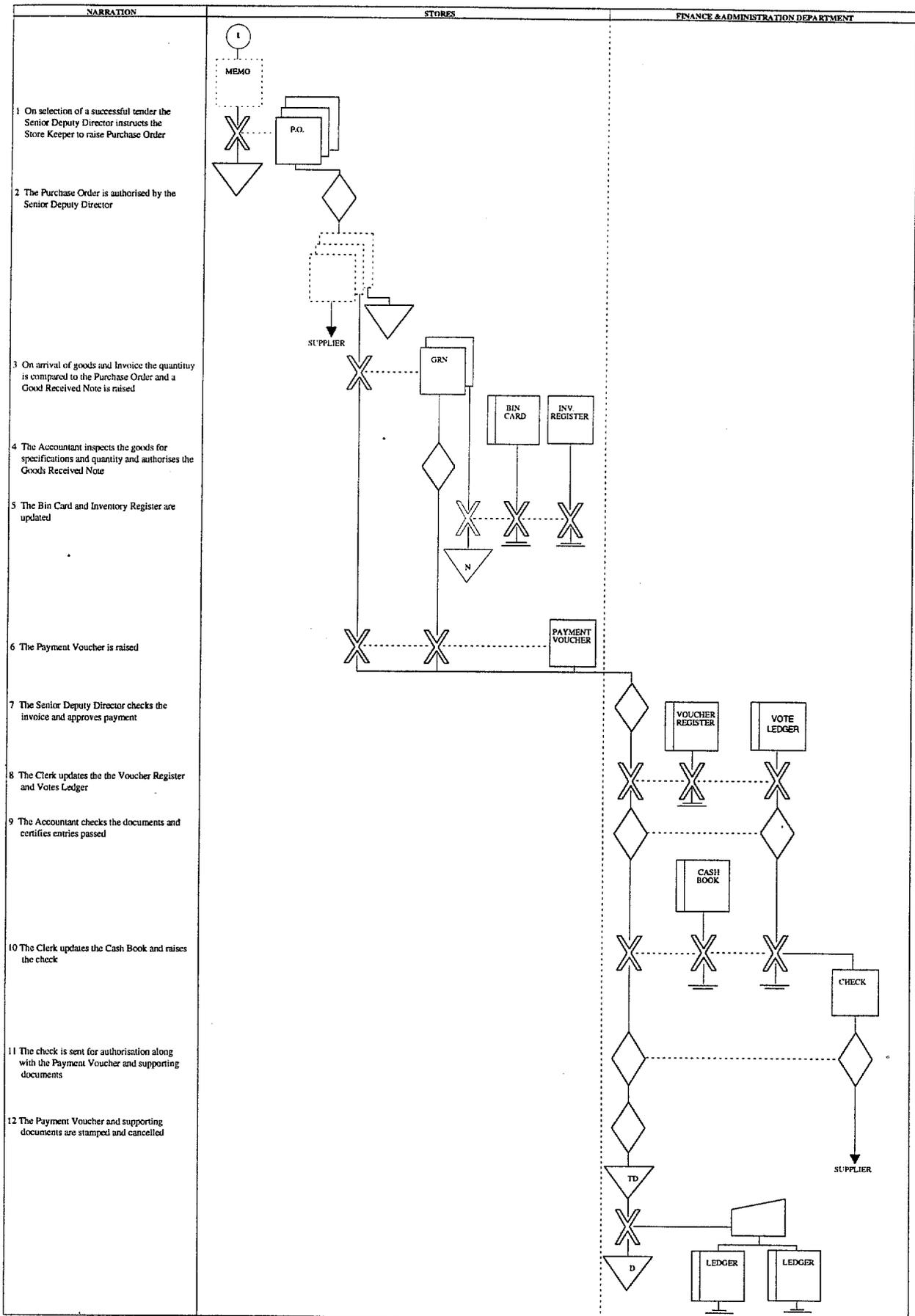
## FLOW CHART SYMBOLS

	DOCUMENT		COMPUTER OPERATION
	ACCOUNT BOOK		CONNECTOR
	3 PARTS/COPIES		OPERATION
	'GHOSTING' OF DOCUMENTS		ALTERNATIVE ROUTINE
	PRENUMBERED SET		DOCUMENT FLOW
	CHECK/INSPECTION		INFORMATION FLOW
	FILE		TIME FLOW OF DOCUMENT
			DOCUMENT CROSSING

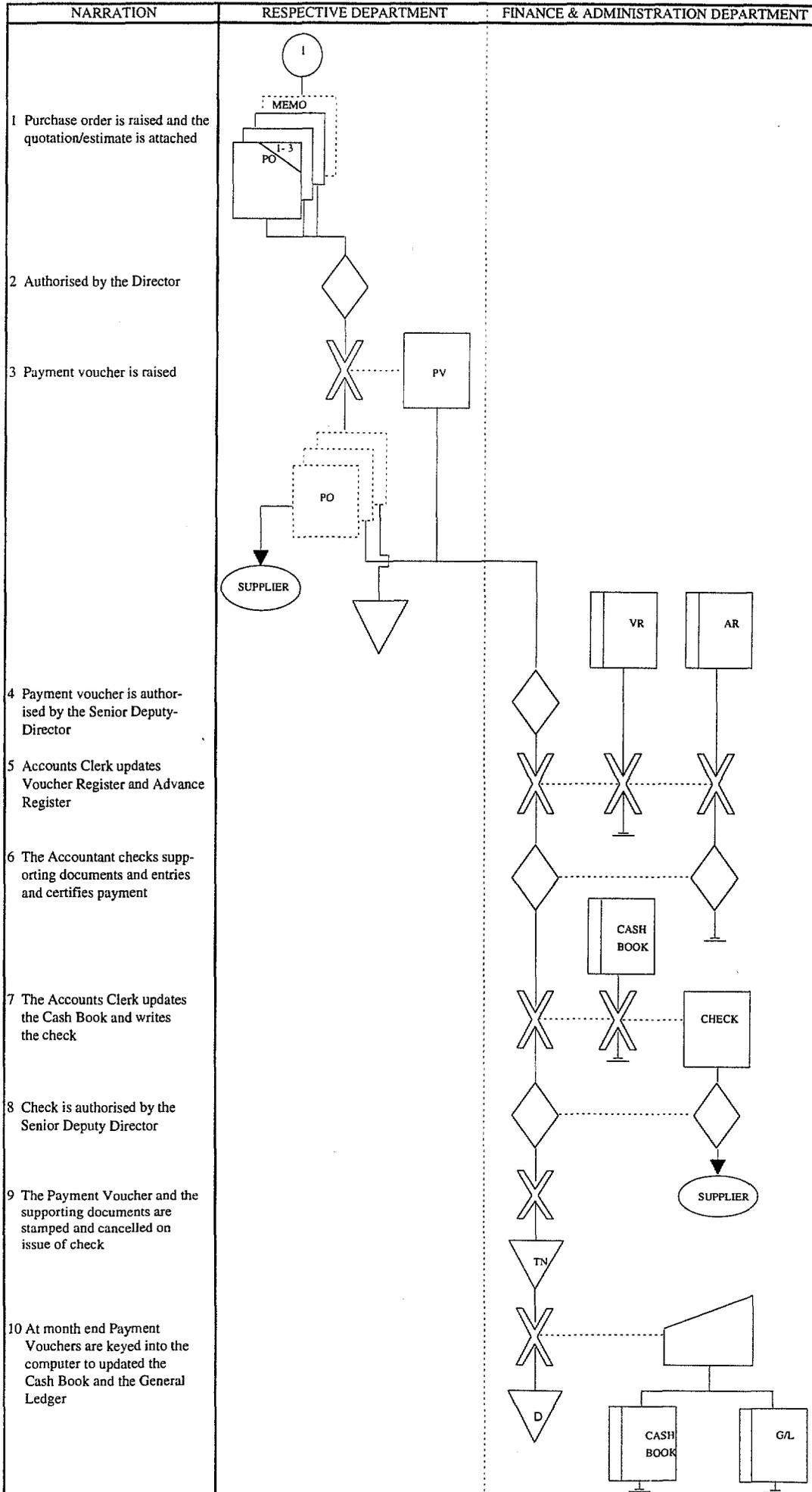
### TENDER PROCEDURE



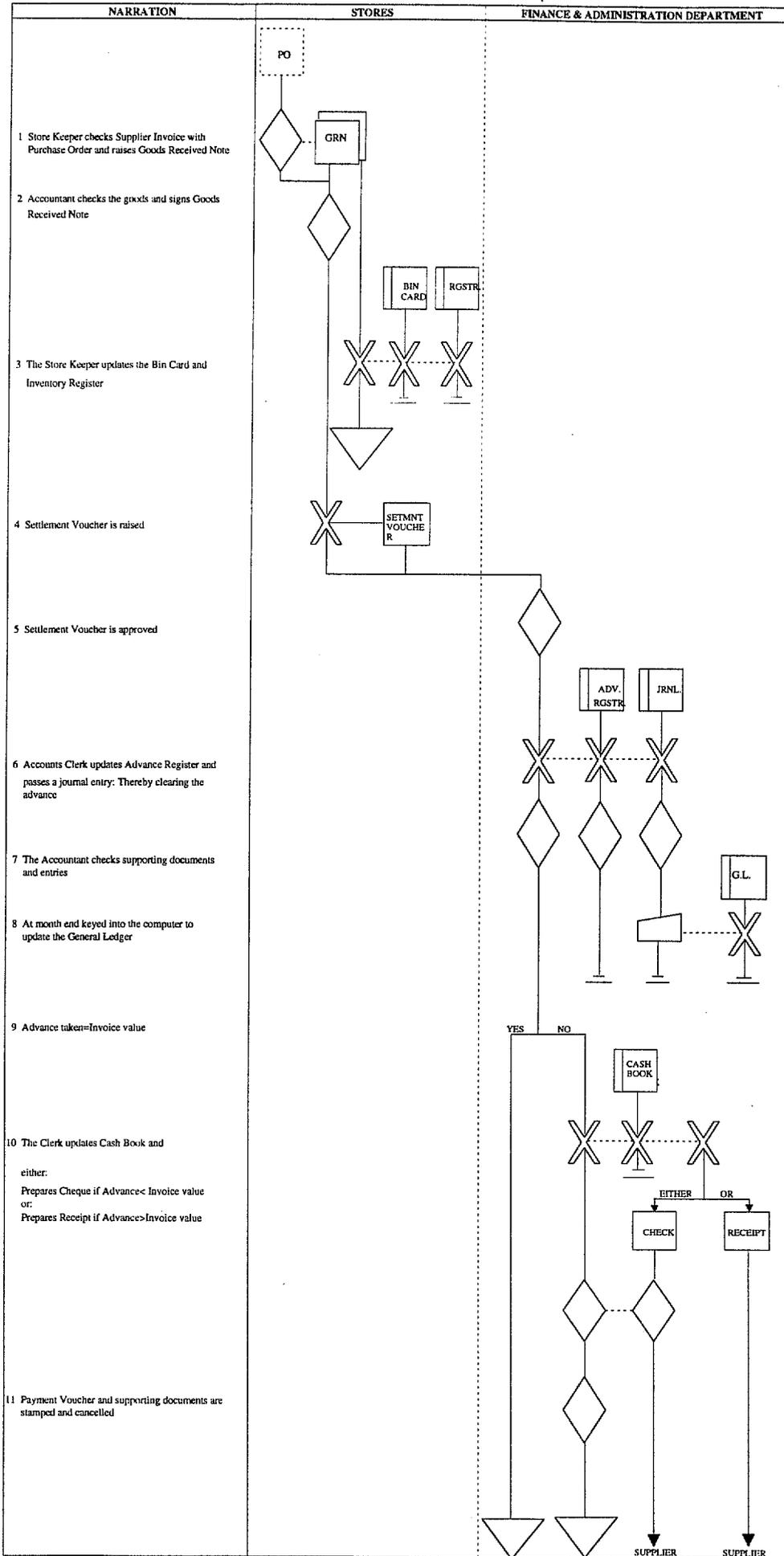
CAPITAL ASSETS PURCHASES SYSTEM



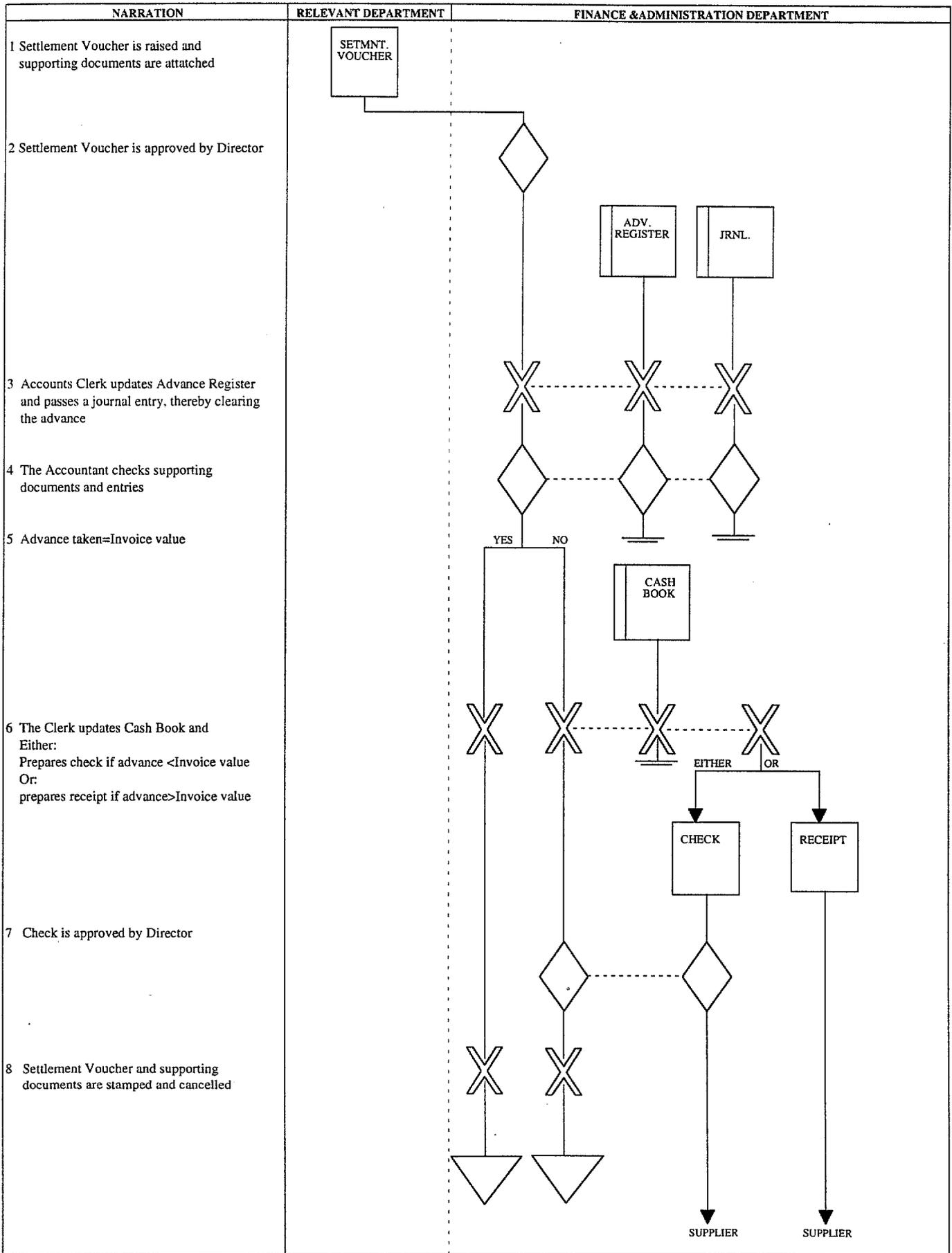
ADVANCE PAYMENT SYSTEM



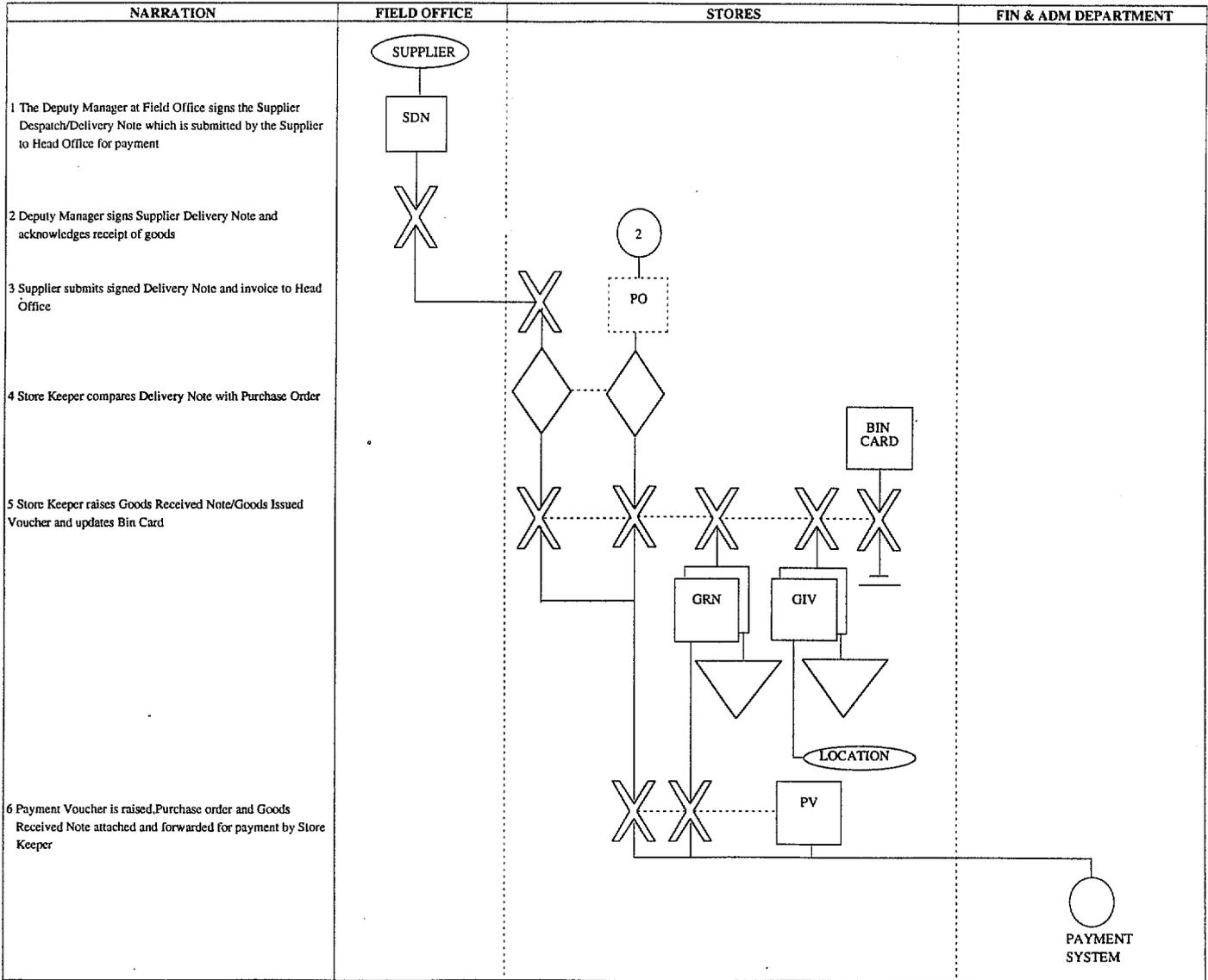
SETTLEMENT OF ADVANCE PAYMENTS SYSTEM - GOODS



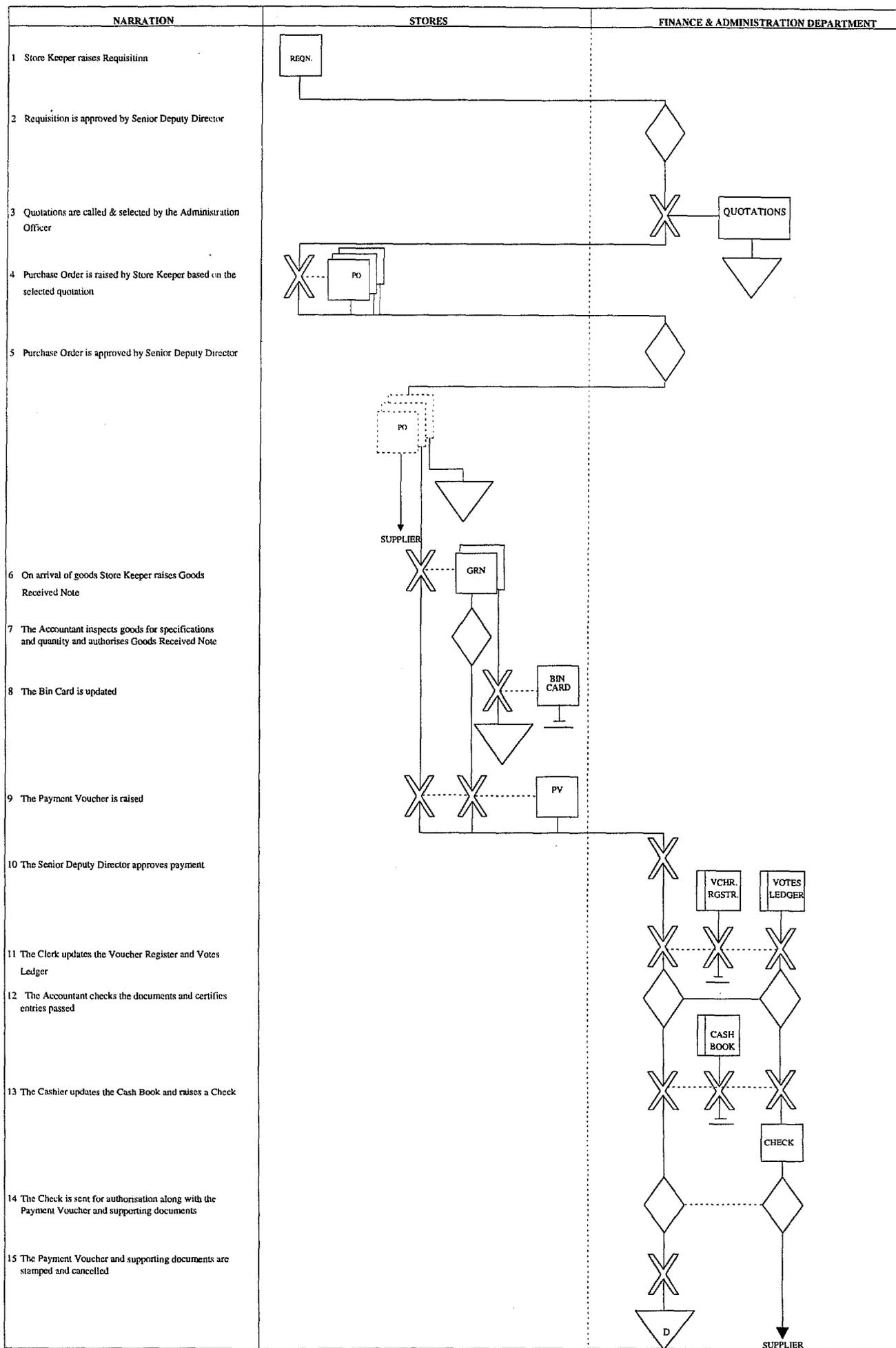
SETTLEMENT OF ADVANCE PAYMENTS (SERVICES)



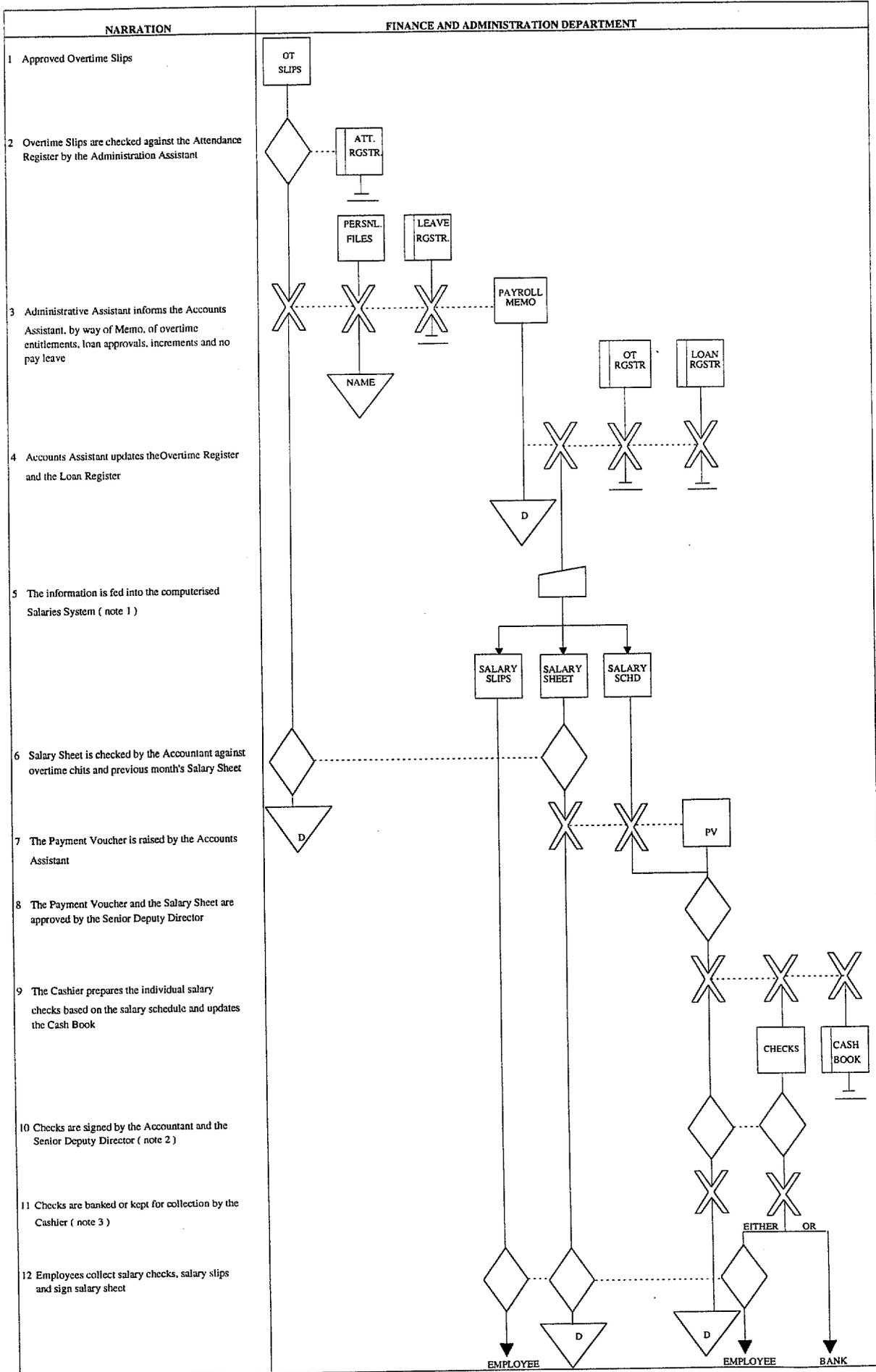
**DESPATCH OF GOODS TO FIELD OFFICES**



PURCHASE OF OTHER COMMODITIES



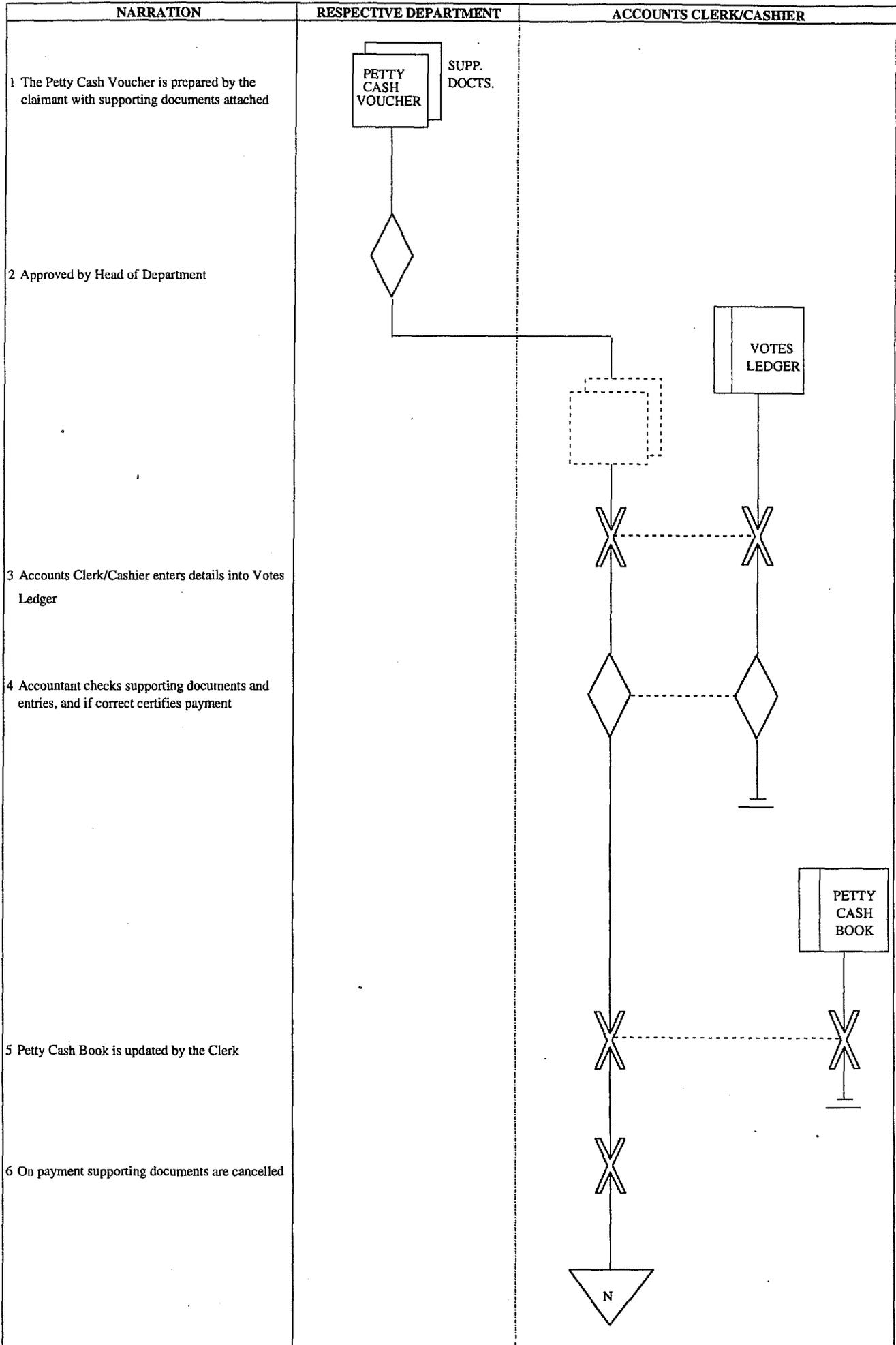
SALARIES SYSTEM



NOTES :

- 1 The computer system generates hard copies of the Salary Slip, Salary Sheet (Payroll) and Salary Schedule (gives the net salary and the payment instructions i.e. direct credit to bank or not).
- 2 Salary checks are prepared according to payment instructions i.e. crossed 'account payee' for direct banking and cash checks for others.
- 3 Salary checks are sent to the bank with credit instructions. Field Officers' salary checks are sent by registered post to individuals or their respective banks by the Accounts Assistant.

### PETTY CASH SYSTEM



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DESPATCH OF STATIONERY & SUNDRY ITEMS

