**Ceylon Ceramics Corporation - 2013**

The audit of financial statements of the Ceylon Ceramics Corporation for the year ended 31 December 2013 comprising the statement of financial position as at 31 December 2013 and the statement of income, statement of comprehensive income and statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information 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 13(1) of the Finance Act, No. 38 of 1971 and Section 29 of the State Industrial Corporations Act, No. 49 of 1957. My comments and observations which I consider should be published with the annual report of the Corporation in terms of Section 14(2)(c) of the Finance Act, appear in this report.

**1:2 Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

**1:3 Auditors' Responsibility**

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards of Supreme Audit Institutions (ISSAI 1000-1810). Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgements, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Corporation's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements. Sub - sections (3) and (4) of Section 13 of the Finance Act, No. 38 of 1971 give discretionary powers to the Auditor General to determine the scope and the extent of the audit

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my adverse audit opinion.

**1:4 Basis for Adverse Opinion**

Had the matters described in paragraph 2.2 of this report been adjusted, many elements in the accompanying financial statements would have been materially affected.

**2. Financial Statements**

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**2:1 Adverse Opinion**

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In my opinion, because of the significance of the matters described in paragraph 2.2 of this report, the financial statements do not give a true and fair view of the financial position of the Ceylon Ceramics Corporation as at 31 December 2013 and its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

**2:2 Comments on Financial Statements**

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**2:2:1 Sri Lanka Accounting Standards (LKAS / IFRS)**

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(a) The financial statements for the year under review had not been prepared based on the newly introduced Sri Lanka Accounting Standards (LKAS/IFRS) which come to effect from 01 January 2012.

(b) Eleven Court cases had been filed against the Corporation in the Labour Tribunals and several other Courts by retired employees of the Corporation in connection with non-extension of their services and non-payment of their retirement benefits. It was observed that an appropriate provision or disclosures for legal obligations as at the end of the year under review had not been made in the financial statements as required by LKAS 37, Provision, Contingent Liabilities and Contingent Assets. The Corporation had been paid a sum of Rs. 173,700 as legal charges during the year under review in this connection.

**2:2:2 Accounting Deficiencies**

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The following observations are made.

a) The equity balance of Rs.250,094,284 shown in the statement of changes in equity was not tallied with the equity balance of Rs.138,494,826 stated in the balance sheet. The Non-inclusion of fund received from the State Resource Management Corporation (SRMC) and the growth received from the several ministries in time to time were the reasons for the difference of Rs.111,599,458.

b) Employee Provident Fund (EPF) payable amounting to Rs.7,088,898 shown in the financial statements had been differ from the actual payable of Rs.236,960 shown in the EPF return. Hence the EPF payable as at 31 December 2013 had been overstated by Rs.6,851,938.

c) Revenue of the Eragama and Mahiyanganaya factories had been understated by Rs.655,662 and Rs.980,165 respectively during the year under review due to recording and clarification errors.

d) Sales revenue in September 2013 amounting to Rs.1,024,825 had been erroneously credited to the miscellaneous income account. Thus the sales revenue and miscellaneous income had been understated and overstated respectively by that amount.

e) Excess stocks and damage stocks as per the physical verification as at 31 December 2013 were amounted to Rs.1,818,753 and Rs.911,658 respectively. However, no adjustments for excess stocks and provision for damage stocks had been made in the financial statements as at 31 December 2013.

f) The Weuda, Elayapattuwa and Yatiyana factories had been closed down in 2009, 2011 and 2013 respectively and the physical stocks valued at Rs.12,731,807 was made available in those factories as at 31 December 2013. However, as per the financial statements the total stocks stated under the above three factories were amounted to Rs. 25,475,412. Therefore the closing stocks and the profit for the year under review had been overstated by Rs.12,743,605.

g) Physical stocks had not been made available at the end of the year under review in two factories of Oddusudan and Bangadeniya which was closed down in 1982 and 2001 respectively. However, stocks amounting to Rs. 1,750,648 had been included in the stocks showing in financial statements under above two factories.

h) General stocks shown under Eragama and Uswewa factories had been overstated by Rs.17,056,366 while Mahiyanganaya and Bingiriya factories had been understated by Rs.27,226,060 in the financial statements as compared with the physical verification of such factories.

i) Gratuity provision relating to Eragama and Mahiyanganaya factories as at 31 December 2013 shown in the financial statements had been understated by Rs.602,428 while Uswewa and Yatiyana factories had been overstated by Rs.600,519 as per the calculation made by audit.

j) Renovating expenses incurred for painting, electrical works, furniture, curtains etc. amounting to Rs. 2,659,209 had been capitalized on an existing building in Eragama which used for Deyeta Kirula Exhibition instead of being recognized as maintenance expenses,

k) Total cash balances shown in the financial statements under Eragama, Mahiyanganaya, Uswewa factories and Head Office were overstated by Rs.1,537,881 as compared with the physical cash verification carried out by the corporation.

l) The cash balances as at end of the year under review totalling to Rs.856,275 shown under closed down factories of Bangadeniya, Elayapaththuwa, Weuda, Oddusudan and Yatiyana shown in the financial statements for the year under review were not physically made available for audit.

m) A fixed asset register had not been properly maintained by the Corporation and schedules for some fixed assets had been only submitted along with the financial statements. The following observations were made in this connection.

i. Opening balance of Tile Pallets shown under the property plant & equipment had been overstated by Rs.3,364,866 as compared with the previous year audited financial statements.

ii. Thirty one motor vehicles valued at Rs. 2,162,747 shown in the vehicle schedule had not been physically available in the Corporation premises while the value of 9 motor vehicles which physically available had not been included in the vehicle schedule attached to the financial statements.

**2:2:3 Accounts Receivable and Payable**

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The following observations are made.

(a) Although the Lanka Ceramic Limited had been closed down in the year 2002, sums of Rs.48,602,070 and Rs.22,375,918 had been included in the financial statements as receivable and payable respectively as at 31 December 2013 without being taken prompt action to clear those balances.

(b) Water bills of Mahiyanganaya factory amounting to Rs.220,463 which was accrued since 2009 had not been settled even up to end of the year under review.

(c) Even though the Bangadeniya factory had been closed down over 10 years ago, trade debtor balance and accrued expenses amounting to Rs.314,673 and Rs.1,069,613 respectively had not been settled even by the end of the year under review.

(d) Tax payable amounting to Rs.13,363,261 and Rs.15,778,623 relating to closed down factories of Bangadeniya and Elayapaththuwa respectively were remained in the financial statements as at 31 December 2013.

(e) Festival advance of Rs.262,167 recoverable from the Oddusuddan factory had been remained in the accounts for over 26 years.

(f) Reserves amounting to Rs.33,939,592 relating to five closed down factories had been included in the financial statements as at 31 December 2013 under review without making proper adjustments.

(g) A sum of Rs.757,674 had been included in debtors under five closed down factories without being settled or adjusted.

(h) An amount of Rs.854,658 receivable from a private institution to the Elayapattuwa factory since 2008 had not been recovered even by the end of September 2014.

**2:2:4 Lack of Evidence for Audit**

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The following observations are made.

(a) The central administration expenses amounting to Rs.5,778,494 or 82 per cent of the total administration expenses could not be satisfactorily vouched in audit due to unavailability of sufficient information such as vouchers, schedules etc.

(b) According to the statement of the Competent Authority of the Corporation, the Weuda and Elayapattuwa factories had been handed over to the Sri Lanka Army in 2011. However, no evidence had been received to audit in this regard.

(c) The agreement entered in to between Corporation and the Department of Inland Revenue regarding the payment of Rs.30,000 on the installment basis in order to settle the arrears taxes had not been made available for audit.

**2:2:5 Non-compliance with Laws, Rules, Regulations and Management Decisions**

The following instances of non-compliance were observed during the course of audit.

| | Reference to Laws, Rules, Regulations, etc. | Value | Non-compliance |
|---|---|---|---|
| | | Rs. | |
| (a) | Nation Building Tax, Act No. 9 of 2009. | 5,056,579 | Taxes totalling Rs.171,759,557 brought forward over a long period had not been remitted to the Commissioner General of Inland Revenue even by 31 December 2013. |
| | Value Added Tax Act, No. 14 of 2002. | 55,574,968 | |
| | Economic Service Charges Act, No. 13 of 2006 | 11,002,254 | |
| | National Defence Levy Act, No. 36 of 1995 | 38,406,286 | |
| | Goods and Services Tax Act, No. 34 of 1996 | 59,488,624 | |
| | Inland Revenue Act, No. 10 of 2006 | 2,230,846 | |
| (h) | Western Provincial Finance Statute No. 6 of 1990 | 5,583,755 | The Turnover Tax that should be remitted to the Western Provincial Commissioner of Revenue had not been remitted even by 31 December 2013. |

## 3. Financial Review

### 3:1 Financial Results

According to the financial statements presented, the operation of the Corporation for the year under review had resulted a pre tax net profit of Rs.5,287,855 as compared with the corresponding pre tax net profit of Rs.5,149,861 for preceding year. Thus indicating an improvement of Rs.137,994 in the financial results for the year under review. The reasons for the improvement are as summery below.

| Reason | 2013<br>Rs. | 2012<br>Rs. | Difference Favourable (Adverse)<br>Rs. |
|---|---|---|---|
| Revenue | 77,920,760 | 112,655,859 | (34,735,099) |
| Cost of Sales | (68,764,795) | (105,380,353) | 36,615,558 |
| Gross Profit | 9,155,965 | 7,275,506 | 1,880,459 |
| Other Income | 3,415,969 | 12,107,644 | (8,691,675) |
| Operating Expenses | (7,284,079) | (14,233,289) | 6,949,210 |
| Pre Tax Net Profit | 5,287,855 | 5,149,861 | 137,994 |

**3:2 Significant Accounting Ratios**

According to the financial statements and information made available, some of the important ratios of the Corporation for the year under review as compared with the preceding year are given below.

| Ratios | 2013 | 2012 | Observations |
|---|---|---|---|
| Stock Turnover Ratio | 1:0.96 | 1:1.70 | It shown that a long period had been taken for converting the stocks to sales. |
| Stock Turnover (in days) | 380 Days | 214 | |

**4. Operating Review**

**4:1 Performance**

The following observations are made.

(a)Out of nine factories belonging to the Corporation, only five factories in Eragama Mahiyanganaya, Bingiriya, Yatiyana and Uswewa were being functioned during the year under review. The profitability of those factories in the year under review and three preceding years are shown below.

| Factory | Profit/(Loss) for the year | | | |
|---|---|---|---|---|
| | 2013 | 2012 | 2011 | 2010 |
| | Rs. | Rs. | Rs. | Rs. |
| Bingiriya | 934,690 | (1,711,014) | (6,837,118) | (7,468,051) |
| Mahiyanganaya | 1,512,804 | 3,978,017 | (20,981,620) | (15,457,782) |
| Yatiyana | (3,155,256) | (4,751,744) | (14,382,036) | (12,071,994) |
| Uswewa | (5,303,273) | (8,985,412) | (17,127,924) | (13,800,090) |
| Eragama | 11,651,721 | 22,720,384 | (4,148,425) | 3,825,335 |

(i) Yatiyana and Uswewa factories were incurred a huge loss of Rs.8,458,529 during the year under review while Yatiyana factory had been closed down in the year under review due to lack of raw materials.

(ii) Profits of Eragama and Mahiyanganaya factories had been significantly decreased by Rs.11,068,663 and Rs.2,465,213 respectively as compared with the previous year.

(b) Even though the estimated production of tiles, bricks and other materials of five factories functioned in the year under review were 6,519,688 units, the actual production was 3,970,921 units or 61 per cent of the estimated quantity.

**4:2 Management Inefficiencies**

The Corporation had to pay a surcharge of Rs.1,700,000 due to failure of remitting the contributions to the Employees Provident Fund on due date.

**4.3 Human Resource Management**

According to the Public Enterprises Circular No. PED/12 of 02 June 2003 on Public Enterprises Guidelines for Good Governance, the Corporation had not approved its cadre after the reform undertaken. The actual cadre of the Corporation as at 31 December 2013 comprising 43 permanent staff and 179 staff recruited on contract basis.

**4:4 Going Concern of the Corporation**

The ability of the Corporation to continue as a going concern due to the following reasons is doubtful.

(a) A negative net assets position of Rs. 247,380,646 and Rs.138,494,826 as at end of the year 2012 and 2013 respectively had been indicated in the financial statements.

(b) The total assets to liability ratio of the Corporation for the year under review and the preceding year were 1: 1.9 and 1: 2.6 respectively.

(c) Out of the total number of 540 employees, 497 staff had been voluntarily retired on payment of compensation in the year 2012 and 43 employees were remained in the year under review as permanent staff.

(d) Out of 09 factories owned by the Corporation, only 04 factories are functioning at present and balance 05 factories had been closed down due to war situation and lack of raw materials.

**5. Accountability and Good Governance**

**5:1 Action Plan**

The Corporation had not prepared an Action Plan for the year under review.

**5:2 Audit Committees**

According to paragraph 2 of the Treasury Circular No. PF/PS/04)XII) of 28 August 2006, the Audit Committee of the Corporation is not in operation. Such Committee should be established and ensure that the Committee meets regularly and take follow up action on the recommendation made by the previous Committee meetings. Nevertheless, the management of the Corporation had not paid attention to appoint the Committee even up to the end of the year under review.

**5:3 Procurement Plan**

The Corporation had not prepared a Procurement Plan for the year under review.

**5:4 Budgetary Control**

A budget for the year under review had not been prepared. As such, the attention of the Corporation had not been paid to making use of a budget as an instrument of management control.

**6. Systems and Controls**

Deficiencies in systems and controls observed during the course of audit were brought to the notice of the Competent Authority from time to time. Special attention is needed in respect of the following areas of control.

(a) Accounting
(b) Utilization of Assets
(c) Control over Debtors and Creditors
(d) Staff Management