Ceylon Shipping Corporation Limited – 2016/2017
--

The audit of financial statements of the Ceylon Shipping Corporation Limited ("the Company") for the year ended 31 March 2017, comprising of the statement of financial position as at 31 March 2017 and the comprehensive income statement, the statement of changes in equity and the 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. My observations on the performance of the Company for the year under review, which I consider should be presented to Parliament in terms of Article 154(6) of the Democratic Socialist Republic of Sri Lanka, appear in this report.

1.2 Responsibility of the Board of Directors for the Financial Statements
---

Board of Directors ("Board") 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 Board of Directors determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

1.3 Auditor's 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. 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 judgment, 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 Company'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 Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Board, as well as evaluating the overall presentation of financial statements.
I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

1.4 Qualified Opinion

In my opinion, except for the effects of the matters described in paragraph 1.4.1 of this report, the financial statements give a true and fair view of the financial position of the Ceylon Shipping Corporation Limited as at 31 March 2017, and its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.4.1 Basis for Qualified Opinion

(a) The company had erroneously debited a sum of Rs 91,338,313 of freight charges to the Comprehensive Income statement instead of entered to the Coal Transport Control Account. As a result, loss and trade payable for the year under review had been overstated by the similar amount. Further, it was revealed that an un reconciled balance of Rs 144,405,551 in the Coal Transport Control account as at 31 March 2017.

(b) Interest income on treasury bills had been accounted after deducting the notional tax. As a result Interest income of the year under review had been understated by Rs 2,892,483.

(c) The Company had considered the provision for current tax liability of Rs.7,281,062 after deducting notional tax of Rs. 2,892,548. Whereas Company should make a provision for the gross tax payable before setting off the tax credits. As a result, the current tax expense had been understated by Rs. 2, 892,548.

(d) As per the paragraph 32 of the Sri Lanka Accounting Standards on Presentation of Financial Statements (LKAs 01), offsetting of assets and liabilities or income and expenses is not permitted unless required by other SLFRS, However contrary to that the Company had set off credit balances against the debit balances of trade and other receivables. As a result, total trade and other receivable and trade and other payables as at the end of the year under review had been understated by Rs.176,067,313.

(e) Due to non-posting of Journal entries relating to freight clearance and exchange conversion accounts the loss had been understated and debtor had been overstated by Rs. 3,274,697.

(f) The Company had calculated differed tax asset without considering the correct current and previous year tax losses and omission of collective impairment. As a result, the differed tax assets as at 31 March 2017 and the provision for the year under review had been understated by Rs.51,065,156.

(g) Income earned from crude oil transport activities in the previous year, had been recognized as revenue of the year under review. As a result, revenue of the year under review had been overstated by Rs.1, 885,152.

1.5 Report on other Legal and Regulatory Requirements

As required by Section 163 (2) of the Companies Act, No.07 of 2007, I state the followings:

(a) The basis of qualified opinion and the scope and limitations of the audit are as mentioned above.

(b) In my opinion,

- Except for the effect of the matters described in basis for qualified opinion paragraph, I have obtained all the information and explanations that were required for the audit and as far as appears from my examination, proper accounting records have been kept by the Company,
- The financial statements of the Company comply with the requirements of Section 151 of the Companies Act, No. 07 of 2007.

2. Financial Statements

2.2 Comments on Financial Statements

2.2.1 Non-Compliance with Sri Lanka Accounting Standards.

According to section 54 (n) of Sri Lanka Accounting Standard on Presentation of Financial Statements (LKAS 01), it is required to disclose the assets and liabilities for current tax, as defined in LKAS 12 (Income tax) as a line item in the statement of financial position. However, Company has aggregated the income tax payable with other tax payable and disclosed as statutory payable in statement of financial position.

2.2.2 Lack of Evidence for Audit

The following observations are made.

(a) A sum of Rs. 4, 058,232 which had been spent in previous years to built five houses in a land not belongs to the Company, had shown in the financial statement as land and housing project under the line item Property, Plant & Equipment**.** The Company had not provided sufficient appropriate evidence, except a deed of declaration to prove the ownership of the property. Futher, it was noted that the Company uses only two houses and other 3 houses are used by another party.

(b) The evidences mentioned corresponding to the following account balances shown in the statement of financial position had not been submitted for Audit.

Particulars	Ammount	Evidence not made Available
----------------	---------------	-----------------------
	Rs.	
Debtors (16 Balances)	938,145,101	Balance confirmation
Foreign Trade Payables (09 Balance)	23,742,998	Balance confirmation

2.3 Receivable and Payable Accounts

2.3.1 Receivable

Total outstanding balances of trade debtors as at 31 March 2017 was amounting to Rs. 1,360,274,152 and impairment provision of 30 per cent which equalant to Rs. 408,868,624 had been made as at the end of he year under review. According to the age analysis of the debtors some balances were remained unpaid for more than 37 years and the Company had not taken proper action to recover those balances.

The following observations are made regarding the unsettled balances.

(i) Sample of 17 debtors amounting to Rs. 938,793,849, were selected and called for conformation. However, only one debtor had confirmed his balance as zero which is shown in the accounts as Rs.648,748. Therefore, the existence and reliability of these receivables had not confirmed to the audit.

(ii) A sum of Rs.128.86 million due from 04 private companies had remained unchanged over a period of 3 years as at the end of the year under review. Out of that Rs.87.4 million had referred to arbitration process. Satisfactory actions had not been taken to recover the Rs. 41.4 million due from other 03 Companies and made 100 per cent provisions for impairment.

(iii) A sum of Rs. 20.59 million receivable from 06 overseas shipping agents had remained unchanged over a period of 03 years under the Freight Clearance Account. However, the Company had not taken effective action to recover those receivables and made 100 per cent provisions for impairment.

(iv) Goods and Services Taxes and National Security Taxes amounting to Rs. 21.54 million had been excessively remitted to the Department of Inland Revenue by the Company had been shown in the financial statements over 17 years period as statutory receivables.

(v) Security deposits amounting to Rs. 6,722,762 had remained over a period of years without being recovered at the end of the year under review. However, the company had not taken action to recover those deposits in timely manner.

(vi) Sufficient and appropriate audit evidences relating to guarantee repair receivable and prepayments amounting to Rs.28,052,356 were not provided to ensure the accuracy and existence of the balances.

2.4 Non-compliances with Laws, Rules, Regulations and Management Decisions

The following instances of non-compliances with laws, rules and regulations were observed.

	References to Laws, Rules and Regulations	Non-compliance
(a)	Public Enterprises Circulars	
(i)	Paragraph 03 of the Circular No. PED 1/2015 of 25 May 2015.	Contrary to the paragraph 3 of the Circular, fuel allowances amounting to Rs. 648,414 had been provided for 12 Officers under the approval of the Board of Directors during the year under review by exceeding the fixed monthly fuel limit for each category of officers. As per the answer of the Chairman, the Company had rectified the matter.However, overpaid amounts had not been recovered.
(ii)	Circular No. PED 12 of 02 June 2003.	The draft budget should be placed before the Board of Directors for approval, three months before the commencement of financial year and the copies of approved budget should be forwarded to Line Ministry, the Department of Public Enterprises, General Treasury and Auditor General not later than 15 days before the commencement of the ensuring year. However, the Board approvals for the budgets for financial year 2015/16 and 2016/17 had been granted on 19 May 2015 and 07 April 2016 respectively.
(iii)	Section 9.3.1(viii) of the Circular No.PED 12 of 2 June 2003 and Circular No.52 of 25 November 2008,	Every enterprise should have a succession plan, with an understudy designated to take over in the event of such post falling vacant, particularly at management levels. However, the Company had not been made arrangements to design and implement a plan so that a suitable successors could be appointed. As a result, the Company had appointed retired officers in contrary to the Circular requirements.
(iv)	Circular No. PED 3/2015 of 17 June 2015,	The monthly allowances entitle to the Chairman and the Executive Director of the Company were Rs.

80,000 and Rs. 65,000 respectively. However, Contrary to that the Company had been paid monthly allowances to the Chairman and the Executive Director Rs. 85,000 and Rs.75,000 respectively as per the decision taken by the Board of Directors in the year 2007, without obtaining any recommendation from Secretary to the Line Ministry and with the concurrence of the Minister of Finance. As per the answer of the Chairman, the Company had rectified the matter in 2019. However, overpaid amounts had not been charged.

3. Financial Review

3.1 Financial Result

According to the financial statements presented, the loss of the Company for the year ended 31 March 2017 amounted to Rs. 237,010,652 as compared with the surplus of Rs. 74,317,129 for the preceding year thus indicating a deterioration of Rs. 311,327,781 or 418.9 per cent in the financial result as compared with the preceding year. The increase in financial expenses by Rs. 1,075,542,832 or by 1,373 per cent had mainly attributed to this deterioration.

In reviewing the financial results for the year under review and past 04 years, the financial result had continuously deteriorated from Rs. 250,477,672 which was the highest obtain in 2013/2014 for the period, to a loss amounting to Rs. 237,010,652 for the year under review. In considering the contribution to the economy, it has been decreased from Rs. 485,942,361 in the year 2014/2015 to Rs. 396,573,669 during the year under review.

3.2 Analytical Financial Review

The following observations are made.

(a) Although the total revenue of the Company had been increased during the year under review by Rs 1,924 Million or 312 per cent as compared with preceding year direct expenses had been increased by Rs.1,339 Million or 513 per cent. Procured two new vessels to the Company deploying in commercial operations was the reason to increase the income & expenditure in considerable amount during the year under review.

(b) Interest expense on vessel loan had been increased by Rs. 611 Million or 1500 per cent and exchange loss on vessel loan had been increased by Rs. 464 Million or1236 per cent during the year under review as compared with preceding year. Accordingly total finance expense had increased by Rs.1075.5 Million which was directly attributable to the net loss for the year under review.

Even though the company’s revenue and gross profit had been increased by 312 percent and 164 percent respectively, net Profit after tax had been decreased by 419 percent. The reasons for the deterioration was increasing of interest expense on vessel loan and increasing of exchange loss as mentioned above.

3.3 Analysis of Ratios

The following observations are made.

(a) Gross profit Margin of the year under review had decreased from 58 per cent to 37 per cent as compared with the preceding year. This was mainly due to the increase in operational expenses, which was substantially higher than the revenue increase. Further the net profit margin for the year ended 31 march 2017 had been dropped to negative 11 percent from 12 percent in proceeding year. The main reason for this reduction was increase in finance expenses up to Rs. 1,075.5 million.

(b) The Company had recorded a low rate of Return on Capital employed as 3 percent, during the year under review.

(c) Current ratio of the Company had been reduced from 1.07 turns to 0.91 turns during the year under review as compared with the preceding year and the quick ratio had been decreased from 1.02 turns to 0.83 turns from 2015/16 to 2016/17

(d) The gearing ratio of the Company for the year under review was 991 per cent which was a 57 per cent increase when comparing preceding year. It shows a very high proportion due to the increase in short term and long term borrowing.

4. Operational Review

4.1 Management Inefficiencies

The Following observations are made.

(a) The Company had awarded a contract without following the procedures prescribed in Government Procurement Guidelines in 2006 to develop a new finance package for Rs. 5,500,000. After being made an initial payment of Rs. 1,375,000 on September 2016, the management had decided to terminate the Contract due to the inability of the service provider to rectify certain errors found in the system. However, the company had not been taken action to recover overpayment if any or to complete the work.

(b) The company had performed cured oil transportation activities without entering into a formal agreement with Ceylon Petroleum Corporation. Therefore, receivable balances relating to crude oil transport amounting to Rs. 175,671,681 which was not confirmed by sufficient, appropriate evidences had remained without being recovered over a period of four years.

4.2 Performance

According to the corporate plan for the five years beginning from the financial year 2016/17 and the action plan for the year 2016/2017, the Company had planned to implement following 05 new activities. However, the Company had failed to achieve the targets as planned and they were remaining in initial stages.

(i) Unaccompanied Baggage Clearance and Construction of Customs Bonded warehouse

(ii) Starting cotainer feeder service between Colombo/Chittagong.
(iii) Purchasing 05 No.s of Self Propelled barges (SPBs)
(iv) Resumption of passenger Ferry Service between Colombo and Tuticorin
(v) Promote Sri Lanka Flag Registry (Flag of convenience)

5. Systems and Controls

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

	Areas of Systems and Controls		Observations
(i)	Accounting	(i)	Accuracy and completeness of the financial information.
		(ii)	Non Compliance with Sri Lanka Accounting Standards.
		(iii)	Weaknesses in approval of journal entries and ledger postings.
(iii)	Technological information Systems	(i)	Non-performance of maintenance activities and controls in the Information System.
		(ii)	Non-compliance with the requirements of the Company
(iv)	Creditors and Debtors		Delays in recoveries and payments.