Gal-Oya Plantations Private Limited – 2016/2017

The audit of the financial statements of the Gal-Oya Plantations Private Limited ("the Company") for the year ended 31 March 2017 comprising the statement of financial position as at 31 March 2017 and the statement of comprehensive income, 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. This report is issued in terms of provisions in Article 154(6) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

1.2 Management's Responsibility for the Financial Statements

The 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 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 misstatement 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 Board, as well as evaluating the overall presentation of the financial statements.

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

1.4 Establishment and Ownership of the Company

The Gal Oya plantations Private Limited is a limited liability Company incorporated under the Companies Act, No. 07 of 2007 on 19 September 2008. 51 per cent of the ownership of the Company is owned by the Government.

2. Financial statements

2.1 Opinion

In my opinion, the financial statements give a true and fair view of the financial position of the Gal-Oya Plantations Private Limited as at 31 March 2017 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.1.1 Report on Other Legal and Regulatory Requirements

(a) As required by section 163(2) of the Companies Act No 07 of 2007, I state the following:The basis of opinion and scope and limitations of the audit are as stated above.

(b) - 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, and

- the financial statements of the Company comply with the requirements in Section 151 of the Companies Act, No. 07 of 2007.

2.2 Comments on Financial Statements

2.2.1 Going concern of the Company

The Company had been earning continuous losses from 2006/2007 and in the year 2006/2007 that loss was Rs.219 million and it had been significantly increased up to Rs.949 million after 10 years as at the year under review. Due to this unfavourable financial situation, Company had obtained loans and borrowings at higher interest rates. These conditions may indicate uncertainty about the Company's ability to continue as a going concern. The Treasury which hold 51 per cent of the ownership of the Company on behalf the government had not been taken any action to review this unfavourable situation and present their necessary recommendations to carry on profitable business.

2.2.2. Non-disclosure of the transactions between related parties.

The Company had obtained loans and borrowings amounting to Rs.477,056,722 during the period starting from the year 2007 to 28 August 2009 , But it had not been disclosed in the financial statements and not obtain the approval of the Treasury for this borrowings.

2.2.3 Accounts Receivable and Payable

The following observations are made.

(a) Actions had not been taken to recover the long outstanding balance of Rs. 795,795 due from National Water Supply and Drainage Board shown under trade and other receivable in the financial statements.

(b) Actions had not been taken to settle the long outstanding balance of fines and surcharges amounting to Rs.2,088,899 shown under the administration expenses and balance of unclaimed wages amounting to Rs.144,607 shown under trade and other payables in the financial statements for the year under review.

2.2.4 Non-compliance with Laws, Rules, Regulations and Management Decisions

The following instances of non-compliance with laws, rules, regulations and management decisions were observed in audit.

Reference to Laws, Rules, Regulations etc.,	Non-compliance
(a) Section 220 of Companies Act No:7 of 2007	When company's net assets are less than half of its stated capital, an extra ordinary general meeting should be held within 40 days. But Company had not held such a meeting from Company's starting year 2006/2007 to 2011/2012. That meeting was held from the year 2012/2013, but it was not within 40 days. In 2015/2016, Even though the net assets of the Company were negative value of Rs.2,108,168,227, Extra Ordinary General meeting was held on 23 February 2017.
(b) Section 16(1) of the Employees' Trust Fund Act, No.46 of 1980	Even though Employer should contribute their monthly contribution on or before 30 date of the following month, Company has not paid the monthly contribution for the months of June, August and September 2016 on due time and surcharge of Rs.95,965 has been paid.
(c) Extra Ordinary Gazette Notification No.1533/16 dated 25 January 2008	Environmental protection license had not been obtained by the Company for the production of Sugar and Ethanol in terms of National Environment Act

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the financial result of the Company for the year under review amounted to a deficit of Rs.966,946,320 as compared with the Corresponding deficit of Rs.905,767,924 for the preceding year, thus indicating a deterioration of Rs.61,178,396 in the year under review as compared with the preceding year. Even though the gross profit has been increased by Rs.206,411,005 the increase of the net financial cost by a sum of Rs.210,884,819 that is the increase of 39 per cent had been the main reason for the above deterioration.

3.2 Analytical Financial Review

The following matters were observed.

(a) Current ratio and quick ratio for the year under review is shown unfavourably as 0.28:1 and 0.14:1 respectively and it is observed that no enough liquid and current assets are there in the Company to settle current liabilities of the Company.

(b) Even Gross profit ratio of the company is represent 19.6 per cent but net loss ratio is 95.9 per cent

(c) It is observed that the gearing ratio of the Company 1.86 is shown unfavourably and Company's total assets are not enough to cover total liabilities.

(d) The excess of total assets over total liabilities of the Company as at the end of the year under review was Rs.3,064,962,691 and as compared with the previous year it has been increased by 45 per cent . Even though the Company has obtained loan facilities to support for the working capital requirements, Company has not earned sufficient income from the factory in order to settle those borrowings.

(e) The Company's Bank overdraft as at the financial statements of the year under review was Rs.250,576,425 and the interest paid on that was Rs.16,702,149. Therefore working capital management was not in a favourable position.

3.3 Legal Action Instituted by or against the Company

By the end of the current year 14 cases have been filed by external parties against the Company.

4. Operating Review

4.1 Management activities

The following observations are made.

(a) Company had obtained loans from related parties and financial institutions at higher interest rates of 15 per cent to 28 per cent. With that, the Company’s loans and borrowings as at the end of the year under review was Rs.5,452,164,390 and interest expense on that amount was Rs.747,416,480.

(b) As per the shareholder agreement, 277 hectares of land which was owned by Hingurana Sugar Industries had been leased in the year 2006 for a period of 30 years . But Lease deed had not been given for that Lease lands.

(c) Outside Persons who do not related to the Company had residence in the houses which are received at the transfer of assets of Hingurana Sugar Industries 74 employees out of 94 employees who received those houses had sold their houses to outsiders and 13 transferors had rented out their houses.

(d) 5202 hectares of cultivable lands of 4441 cane growers are there with Hingurana factory and new cultivated lands and ratoon crop as at 31 December 2016 was 1401 and 1378 hectares respectively from total cultivated land of 2779 hectares . Therefore Action had not been taken by the Company to utilize those lands effectively in order to operate the sugar factory under the maximum capacity; even Company has had sufficient cultivable land to obtain required sugar supply.

(e) As per the Business plan 2010 - 2020 Expected financial cost for the year under review should be Rs.58 Million but actual cost was Rs.748 million. Hence it was increased by 1,190 per cent.

(f) The amount of Rs.357.12 million out of the total loan amount of Rs.2, 715 million which was obtained to build up the sugar factory had been used to settle other loan repayments and interests without using that loan for the real purpose.

(g) Excess molasses which is a byproduct of sugar manufacturing process had been stored in an external uncovered pit in the factory premises by the Company due to existing storage tanks are not sufficient to store and that pit has been overflowed. The quality of these molasses is at a risk due to rainy water is adding with that molasses stored in the pit.

(h) Even though the management of the Company had been granted via management agreement signed on 26 April 2010 to the Gal-Oya Holdings Company which is operated under Lanka Orix leasing Company and Browns and Company those who hold the 49 per cent of shareholding of the Company,that management Company had not been taken any action to overcome the Company’s financial crisis and to improve the company performance during the past 7 years period.

(i) The Distillery license has not been obtained to operate the new distillery which is constructed by spending Rs.798 million. Therefore the estimated loss calculated for a day was Rs.7.5 million (Estimated ethanol sale of 21,500 liters per day × Selling price of Rs.350). Even though it was unable to start manufacturing operations; the Company incurred the additional maintenance cost of Rs.14, 172,500 per month.

4.2 Operating activities

Following observations are made.

(a) Cost of 1 kilo gram of sugar production for the previous year and for the year under review was Rs.133 and Rs.165 respectively. This includes borrowing cost of Rs.37 and Rs.60. But the average selling price was Rs.69 and Rs.100 per one kilo gram of sugar .Therefore short term , medium term and long term procedures had not been taken by the management of the company in order to reduce the production cost which is excess of selling price.

(b) The sugar factory was not operating at maximum capacity from 2012/2013 period even though the maximum crushing capacity per day was 400,000 metric tons of cane (2000 MT per day × 200 operational days).The total crushed cane for the year under review was 146,740 metric tons which was 37 per cent of the total capacity.

(c) When it is compared with last 5 years the sugar recovery rate has been decreased and it was 8.1 Percent and 6.7 Percent during the period of 2014/2015 and for the year under review respectively. Action had not been taken by the management to overcome this issue even though the company has recorded a lower sugar recovery rate when it is compared with the other competitive factories in the industry

(d) When it is compared with last 5 years the sugar content of cane has been decreased and in 2012/2013 it was 10.9 Percent but it has been decreased to 9.1 Percent for the year under review. When it is compared with other competitive factories in the industry, sugar content of Company's sugar cane was lower.

4.3 Transactions of contentious nature

Following observations are made.

(a) The company has paid a penalty amounting to Rs.3, 850,000 on 08 June 2017 as per the decision given by the Ampara district court for the court case against the Company due to distill and storage of 513,000 liters of ethanol without obtaining the license from the department of Excise.

(b) Even though the ownership of all the non-movable property of Hingurana Sugar industries is with government, The Company had not obtained proper approval from the Treasury to remove the old distillery building in order to construct the new distillery building.

4.4 Staff Administration

There were 831 employees including 182 permanent employees and 649 contract basis employees as at the end of the year under review. Cadre and the scheme of recruitment of the Company had not been prepared or approved by the Department of Management Services.

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 areas of control.

Areas of Systems and Controls	Observations
(a) Long term loans and borrowings	Action had not been taken to settle long term loan balances.
(b) Working capital management	Increase of short term borrowings and payment of huge interest.
(c) Debtors control	Provisions had not been made for bad debts and doubtful debts base on the debtor age analysis.
(d) Operational control	(i) Action had not been taken to increase the sugar recovery percentage and reducing in sugar content of sugar cane. (ii) Action had not been taken to operate the factory at maximum capacity. (iii) Action had not been taken to obtain the license for distillery in a proper manner.