Lanka Phosphate Limited (State Company) – 2016/17.

The audit of the financial statements of the Lanka Phosphate Limited 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 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 comments and observations on the operations of the Company of the year under review which I consider should be presented to Parliament in terms Article 154 (6) of the Constitution of the Democratic Socialist Republic of Sri Lanka appear in this report.

1.2 Board'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 judgement, 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 management, 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 audit opinion.

2. Financial Statements

2.1 Opinion

In my opinion, the financial statements give a true and fair view of the financial position of the Lanka Phosphate 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.

2.2 Comments on Financial Statements

2.2.1 Sri Lanka Accounting Standards

Sri Lanka Accounting Standard 16

The following observations are made

(a) As property, plant and equipment of the Company had not been revalued in terms of Section 34 of the Standard, the fair value of the assets with carrying amount totalling Rs.328,289,853 as at 31 March 2017 had not been shown in the financial statements.

(b) Although the assets of a similar nature and function in an entity's operation should be recognized under a same class in terms of Standard 37, contrary to that, assets of different nature with different economic life costing Rs.11,283,522 had been recognized as different assets and shown under non-current assets. As such, the computed annual depreciation value had been incorrect.

2.2.2 Accounting Deficiencies

An expenditure amounting to Rs.3,055,620 incurred for the purchase of machinery and equipment relating to the preceding year had been brought to account as an expenditure of the year under review.

2.2.3 Unexplained Differences

The following observations are made

(a) There were differences totalling Rs.1,192,594 as mentioned below between the direct balances confirmations obtained by the audit and the debtors balance indicated in the financial statements.

Debtor Institution	Balance as per the financial statements of the Company	Balance as per the balance confirmations	Difference
	Rs.	Rs.	Rs.
State Plantation Corporation	1,237,280	1,684,528	447,248
Tea Shakthi Fund	79,200	--	79,200
Lanka Fertilizer Ltd.	666,146	--	666,146
			1,192,594

(b) There was a difference of Rs.240,397 between the balances of the Debtors Control Account and the balances indicated in the Debtors Sub-ledger continued to exist over a long period of time.

2.3 Accounts Receivable

The debtors balance amounting to Rs.43,903,244 as at 31 March 2017 had included the balances totalling Rs.8,414,141 older than 05 years and action had not been taken either to recover or settle those balances.

2.4 Transactions not Supported by Adequately Authority

The concurrence of the Ministry in charge of the subject of finance should be obtained on the recommendations of the Line Ministry with regard to the other allowances apart from the additional allowances indicated in the Section 2.8 of the Public Enterprises Circular No.PED 3/2015 dated 17 June 2015. Nevertheless, without obtaining approval, a sum of Rs.352,000 had been paid as attendance allowance at Rs.2000 per day during the year under review in respect of the arrival of the Chairman and the Executive Director of the Company to the site.

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

The following non-compliance with Laws, Rules, Regulations and Management Decisions were observed.

Reference to Laws, Rules, Regulation etc.	**Non-Compliance**
(a) Public Enterprises Circular No. PED 01/2015 dated 25 May 2015	Transport allowance of Rs.138,000 had been paid during the year under review for 09 officers who were not covered by the Circular.

(b)	The 19 Supplementary issued by the Department of Public Finance for the Government Procurement Guidelines 2006	In case the expenditure for the repairs of motor vehicles and equipment exceeds Rs.200,000, the personal approval of the Secretary to the Ministry should be obtained. Nevertheless, contrary to that, repairs amounting to Rs.3,502,931 had been done in 03 instances.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the financial results of the Company for the year under review was a loss of Rs.10,533,931 as against the profit of Rs.26,586,534 for the preceding year thus indicating a deterioration of Rs.37,120,465 in the financial results during the year under review as compared with the preceding year. Even though the administrative overhead cost and the income tax had decreased by Rs.23,098,023 and Rs.55,780,952 respectively, the decrease in the gross profit by Rs.125,627,433 had mainly attributed to the above deterioration.

In analyzing the financial results of the year under review and the 3 preceding years, the surplus of Rs.134,385,026 in the financial year 2013/2014 had deteriorated up to Rs.26,586,834 in the year 2015/2016 and it had turned out to be a loss of Rs.10,533,931 by the end of the year under review. However, when re-adjusting the Government tax, employees remuneration and depreciation for non-current assets to the financial results, the contribution of the Company amounting to Rs.338,932,189 in the year 2013/2014 reflected a continuous downwards trend up to Rs.293,879,067 in the year 2015/2016 and Rs.255,409,411 in the year under review.

3.2 Analytical Financial Review

The following observations are made

(a) The contribution of the main productions of the Company as compared with the two preceding years is given below.

Production	Contribution 2016/2017 Rs.	Contribution 2015/2016 Rs.
ERP	263,439,441	424,242,325
HERP	78,840,900	92,069,620
Coconut Fertilizer	23,813,360	46,424,398

The contribution made by the ERP and HERP productions had decreased by Rs.174,031,604 or 34 per cent in the year under review as compared with the preceding year and the contributions made by the Coconut Fertilizer had decreased by Rs.22,611,038 or 49 per cent in the year under review as compared with the preceding year.

(b) As the sales income had drastically decreased in the year under review as compared with the preceding year, earning of an ordinary share of the Company had decreased from 3.67 to minors 1.45.

(c) The Company had withdrawn fixed deposits of Rs.25 million during the year under review and obtained a bank loan amounting to Rs.25 million by keeping fixed deposits as security. Out of this amount a sum of Rs.24,979,533 was payable even by the end of the year under review. The gradual decrease in the viability of earning income through the main business activities had mostly attributed to this situation. Accordingly, the company had faced to a risk of failure in maintaining an income level sufficient to maintain at least its operational activities.

4. Operating Review

4.1 Performance

The Lanka Phosphate Limited established in the year 1992 with the objective of excavating, processing and selling of Rock Phosphate, which is used as a fertilizer for perennial crops produces only 02 basic from productions (ERP/HERP) and another basic from product, Coconut Fertilizer at present. The ERP Fertilizer is applied for the long term crops such as Tea, Rubber and Coconut while HERP Fertilizer is applied for the minor export crops such as Cinnamon and Pepper.

The following matters were observed in the examination carried out on the performance of the Company.

(a) Even though the above fertilizers cannot be applied for the paddy cultivation which is the main agricultural crop in Sri Lanka, this mineral can be used for the production of the chemical fertilizers such as Triple Phosphate used for the paddy cultivation. Nevertheless, attention had not been focused on that matter and it was observed in audit that despite the availability of natural resources within Sri Lanka, outflow of foreign exchange to the foreign countries is extensively taking place annually for the import of Triple Super Phosphate.

(b) Although the other products that can be manufactured with the use of Apatite and the instances where that mineral can be used are as follows, the Company had not taken steps to make use of those instances.

(i) Production of Animal Foods
(ii) Production of Water Softeners
(iii) Electroplating
(iv) Production of Ceramics
(v) Production of Paints
(vi) Possibility of using them in the Rubber Industry.

(c) The production and the sales of the Company in the year under review and the preceding year had been as follows.

Item	2015/2016		2016/2017	
	Production (M.T)	Sales (M.T)	Production (M.T)	Sales (M.T)
ERP	45,216	47,144	28,318	27,736
HERP	8,446	7,961	6,497	6,784
Total Production Sales (M.T.)	53,662	55,105	34,815	34,520
Total Production Cost and Sales Value (Rs.)	214,697,465	515,851,225	253,160,119	341,510,811

Although the ERP and HERP production had decreased by 18,847 Metric Tons or 35 per cent as compared with the preceding year, total production had decreased by 15 per cent only. Even though the total production cost had decreased, unit production cost had increased and it had been mainly attributed by the increase in the absorption production cost of a metric tons unit of raw material by Rs.439 as compared with the preceding year due to the increase in the other fixed expenditure including the employees salary, expensive maintenance expenses and the tax recovered in respect of excavations carried out by the various Government institutions. As a result of the above situation, the Company had already sustained a financial loss and this position may further aggravate in the future, thus resulting difficulties in the payment of dividends to the Treasury. Accordingly, it was observed in audit that action should be taken to step towards a value added production expeditiously in a manner able to face the weather and Government policy changers under the patronage of the Government without depending solely on the production of basic form.

(d) Although the Action plan had been prepared with the objective of increasing the production and sales, providing new market opportunities, savings of foreign exchange, conduct of new researches and providing high quality service, the progress of any activities included therein had not been furnished to audit.

4.2 Management Activities

The rates of the Special Daily Allowance approved by the Board of Directors based on the monthly sales and the production had been in higher value for the higher ranking officers while it had been in lower value for the lower ranking officers. Accordingly, rates from Rs.1,115 to Rs.2,387 had been paid for the higher ranking officers and lower rates from Rs.333 to Rs.462 had been paid for the group that make direct contribution for the production. Accordingly, it was observed in audit that the above situation may directly affect the efficiency of the labourers.

4.3 Idle and Underutilized Assets

The following observations are made.

(a) The Wheel Loader machines valued at Rs.7,901,000 purchased by the Company in the year 2008 had become inoperative after the utilization of the machine for excavation activities for 14,349 hours. Although a sum of Rs.4,243,799 had been spent for the repairs of this machine during the years 2015 and 2016, it had remained idle without being utilized from the year 2015 up to June 2017, the date of audit. As such, Wheel Loaders had to be obtained on rent and a sum of Rs.3,467,893 had been paid therefor to the external parties during the years 2015 and 2016.

(b) A sum of Rs.43,453,115 had been spent for the purchase of spare parts for the installation of New Mill machines at the Eppawala premises in the year 2014. Out of those spare parts, spare parts valued at Rs.17,234,953 had been used for another machines and the remaining spare parts valued at Rs.26,218,162 had been kept at the stores from the date of purchased even up to the date of this report. Accordingly, it was observed in audit that the spare part, *TGM 160 main mill* valued at Rs.11,513,434 could not be used for any machine.

5. Accountability and Good Governance

Internal Audit

Although an officer had been appointed as the Internal Auditor, an adequate internal audit had not been conducted in terms of the Internal Audit Plan.

6. Systems and Control

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

Areas of System and Control	Non-compliance
(a) Stock Control	Failure to introduce a specific method for the computation of stock value of the raw materials.
(b) Financial Control	Failure to get an examination done by the Internal Audit Division prior to make payments relating to the transactions with high value.
(c) Debtors Control	Failure to recover, without delay, the money receivable from the debtors and not correctly posting them in accounts.
(d) Accounting	Failure to delegate authority properly to mark journal entries.