Sri Lanka Cement Corporation - 2016

The audit of financial statements of the Sri Lanka Cement Corporation , and its subsidiary - Lanka Cement Company Ltd for the year ended 31 December 2016 comprising the consolidated statement of financial position as at 31 December 2016 and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated 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 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. A detailed report in terms of Section 13(7)(a) of the Finance Act was issued to the Chairman of the Corporation on 11 October 2017.

1.2 Management's Responsibility for the Financial Statements

The 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 Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on the audit conducted in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000-1810).

1.4 Basis for Disclaimer of Opinion

As a result of the matters described in paragraph 2.2 of this report, I am unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded items, and the elements making up the statement of financial position, statement of comprehensive income and statement of changes in equity, and cash flow statement.

2. Financial Statements

2.1 Disclaimer of Opinion – Group

Because of the significance of the matters described in paragraph 2.2.1 of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

Disclaimer of Opinion – Corporation

Because of the significance of the matters described in paragraph 2.2.2 of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

2.2 Comments on Financial Statements of the Group

2.2.1 Going Concern of the Group

The capital of the Cement Corporation was Rs. 967 million, whereas the accumulated loss amounted to Rs. 676 million. Although the going concern of the Corporation had not been affected, an accumulated loss of Rs. 3,045 million had incurred as per the consolidated statement of changes in equity due to continuous losses incurred by the Corporation, whereas the capital amounted to Rs. 2,702 million. Accordingly, it was observed that 112.7 per cent of the share capital had been eroded. It was observed that the going concern of the Lanka Cement Company Ltd was uncertain without the assistance of the Treasury due to that reason.

2.2.2 Comments on the Financial Statements of the Corporation

2.2.2.1 Sri Lanka Accounting Standards

Sri Lanka Accounting Standard 37

Even though sufficient information on contingent liabilities of the Institution should be disclosed through financial statements in terms of Section 86 of the Standard, action had not been taken in terms of the Standard relating to 15 lawsuits that are being tried in the Court as at 31 December 2016 by the Corporation.

2.2.2.2 Accounting Deficiencies

The following observations are made.

(a) The gross loss of the year had been decreased by that value on noting the gross sales values including the Nation Building Tax totalling Rs.600,360 in noting the cement sales value in the year under review in financial statements.

(b) A land located in Puttalam belonging to the Cement Corporation had been rented to the Holcim Lanka Company and, the rent agreement period was from May in the relevant year to June in the next year. As such, the rent income in the year 2016 had been noted a sum of Rs.50,416 less than its value on accounting to cash basis the rent income amounting to Rs.121,000 received for the years 2015/2016 as an income in the year 2015 and, an income receivable amounting to Rs.70,584 from June to December in the year under review had not been brought to account.

(c) A sum of Rs.31,900 of the value amounting to Rs.321,900 receivable from a private institution as entrance fees to the premises for technical studies relating to the limestone deposit in the land in Aruwakkalu, Puttalam are receivables for the Value Added Tax and even the receivables on the Value Added Tax had been brought to account as Miscellaneous Income.

(d) Even though the sum of Rs.1,065,027 that could not be brought forward of the economic service Charges paid in the year 2012 should be debited to the Retained Profit Account, the surplus of the year had been understated by that amount due to debiting it to the statement of comprehensive income by the Corporation.

(e) The oil tanks belonging to the Corporation had been given to the Ceylon Petroleum Storage Terminals Limited on lease basis in the year 2010. As such, the total lease amount recoverable to the Corporation from the year 2010 to the year 2015 had been a sum of Rs.84.6 million. Those income receivables had not been brought to account and, action had not been taken to recover those income even by the end of the year under review.

(f) Even though the ownership of the Oil Tanks Complex and the land in Kankasanthurai belonging to the Corporation had been confirmed in writing, these assets had not been included in the statement of financial position since the year 1989.

(g) Even though only 152 acres in extent of the land 221 acres in extent in Palawi in the Puttalam District belonging to the Corporation had been estimated and brought to the accounts the remaining 69 acres in extent had not been estimated and brought to the accounts.

2.2.2.3 Unexplained Differences

Even though a balance amounting to Rs.2,654,122 remained as at 31 December 2016 according to the Cash Book maintained using computers for a Current Account maintained for the Institution, a difference of Rs.1,548,090 observed on that balance being a sum of Rs.1,106,032 according to the hand- written Cash Book. The financial statements had been prepared based on the balance of the computerized Cash Book without taking action to identify and settle that difference remaining from the year 2008.

2.2.2.4 Lack of Evidence for Audit

The following Items of Accounts shown in the financial statements could not be satisfactorily vouched or accepted due to non- submission of evidence for audit indicated against each Item of Account.

Item of Account	Value	Evidence not made Available
	Rs.	
Bank Loans	56,293,352	Loan Documents and Schedules
Receivable Deposits	859,437	Letters of Confirmation of Balance

2.3 Accounts Receivable and Payable

The following observations are made.

(a) Trade and other receivable balances as at 31 December 2016 had been a sum of Rs.89,212,053 and, there were balances amounting to Rs.11,010,343 ranging from 1 to 3 years and amounting to Rs.57,988,878 which had lapsed over 3 years in those balances. Action had not been taken to recover those arrears balances.

(b) Payable trade balances as at 31 December 2016 had been a sum of Rs.46,502,068 and, there were balances amounting to Rs.13,180,262 ranging from 1 year to 3 years and amounting to Rs.30,086,483 which had lapsed over 3 years in those balances. Action had not been taken to settle those balances.

(c) A short- term loan had been obtained from a State Bank by putting a land belonging to the Corporation under security on the basis of making payments within 02 months in 13 instances in the years 2014 and 2015 by the Corporation. Even though the payments of this loan should be completed by 15 September 2015, a total sum of Rs.56,293,352 remained payable as at 31 December 2016.

(d) The Corporation had to pay interests for interest as well on not properly making the payment of installments and interests for the bank loans obtained by the Corporation. As such, bank loans obtained in the prior year and the total of the interest relating thereto amounting to Rs.42,000,000 had been transferred to a short- term Loan Account on the decisions of the Board of Directors and the unsettled balance of that Loan Account as at 31 December 2016 had been a sum of Rs.17,500,000.

(e) A loan amounting to Rs.40,000,000 had been obtained in the year 2012 from a State Bank for settling a loan payable to an international company as per a decision of the Cabinet of Ministers. Even though the payment of that loan should be completed in similar 5 installments within 5 years from the year 2013, the total loan value payable out of the total loan amount had been a sum of Rs.24,000,000 on not properly making the installment payments.

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

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

Reference to Laws, Rules and Regulations	Non- compliance
(a) Financial Regulations of the Democratic Socialist Republic of Sri Lanka	
Financial Regulation 396	Action had not been taken in terms of Financial Regulations relating to 09 cheques of which the total value being a sum of Rs.1,116,485 which had been issued but not presented for payment relating to 02 Bank Current Accounts and those cheques had been cancelled.
(b) Public Finance Circular No.PED/12 of 02 June 2003	
Section 4.2..6	The Performance Reports should be reviewed by the Board of Directors every three months and even though that report should be furnished to the Department of Public Enterprises and to the Treasury 30 days before the end of the quarter, action had not been taken accordingly.
(c) Public Finance Circular No.03/2015 dated 14 July 2015	The Advances totalling Rs.1,388,569 which had been provided for miscellaneous functions had been further brought to account as advances in the financial statements without taking action to identify and settle them.
(d) Public Finance Circular No.5/2016 dated 31 March 2016	A Board of Survey had not been carried out relating to the year under review relating to the lands, buildings, furnitures and equipmenst valued at Rs.2,624,338 in the Oil Tanks Complex in Kankasanthurai, belonging to the Corporation.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the financial result of the year under review had resulted in a surplus of Rs.31,700,843 as compared with the corresponding surplus of Rs.2,583,617 for the preceding year, thus indicating an improvement of Rs.29,117,226 in the year under review as compared with the preceding year. The decrease of the gross loss by a sum of Rs.7,906,665 or by 77.4 per cent and the increase of other income by a sum of Rs.31,498,348 or by 52.46 per cent had been the main reason for this improvement.

In analyzing financial results in the year under review and of 04 preceding years, it had indicated gross losses continuously from the year 2012 to the year 2014 and again, had indicated a position of net profit amounting to Rs.2,583,617 and amounting to Rs.31,700,843 respectively in the years 2015 and 2016. However, the contribution of the Corporation had taken a plus value of Rs.26,165,135 in the year 2012 after adjusting personnel emoluments, taxes paid to the government and depreciation for non- current assets again to the financial result and it had taken a minus value of Rs.338,370,664 in the year 2013. It remained a plus value in the years 2014 and 2015 and it had remained a plus value of Rs.70,978,162 in the year 2016.

4. Operating Review

4.1 Performance

Manufacturing, importing and selling cement, selling goods made of cement or manufacturing telephone and electricity cable poles, telephone boxes, water transporting equipment, Hume Pipes and tiles which include cement concrete and supplying electric energy as stocks had been the main objectives of the Corporation in terms of the Gazette Extraordinary No.11634 dated 2 January 1959.

The following observations are made on the achievement of the above objectives.

(a) Even though manufacturing cement and selling and manufacturing cement related products had been the main objectives of the Corporation, the key functions of the Institution had been restricted to importing and selling cement bags and to selling concrete products by the current period with defaulting of manufacturing cement in Kankasanthurai with the condition of war remained in the past years.

(b) The Performance Report had not been prepared in a manner that the actual operation could be compared, in comparing the Performance Report with the Corporate Plan and the Action Plan relating to the year under review.

(c) Even though it had been planned to sell cement valued at Rs.107,858,978 in the year under review according to the Action Plan, only cement valued at Rs.63,030,000 had been sold according to the Performance Report on the Institution facing financial difficulties. As such, the performance achieved had been 41.56 per cent of the intended target.

(d) Even though an income amounting to Rs.2,408,000 had been earned by manufacturing and selling concrete poles and cement blocks as at 31 December of the year under review, the relevant targets had not been noted in the Action Plan.

(e) Even though the main objective of the Corporation being manufacturing and selling cement, activities such as determining the lease rent, renting for the remaining lands including Kankasanthurai and updating lease agreements had been carried out by deploying the remaining 14 employees of the Corporation and the function of paying the personnel emoluments out of that income and remitting the remaining money to the Government afterwards had been handed over to the Corporation on entrusting the custody of the clinker deposits of the country to the Corporation after restructuring in terms of the Letter No.PE/RES/VRS-1-2016 of the Additional Director General of the Department of Public Enterprises dated 20 October 2016.

4.2 Management Activities

The following observations are made.

(a) A gross loss totalling Rs.2,304,013 had been obtained in the year 2016 by selling cement and cement products of the Corporation.

(b) The land, 89.9 perches in extent located in Kollupitiya had been vested by the Corporation by the Gazette Extraordinary No.14756/7 dated 12 July 1967 and the Deed No.288. This land had been mortgaged to the Bank for obtaining loans under a maximum loan limit of Rs.172,000,000 from the Bank of Ceylon in the year 2008 and a loan amounting to Rs.97,793,352 had been obtained as at 31 December 2016. The interest payable relating thereto had been a sum of Rs.21,767,910 and, the total loan and interest payable to the Bank had been a sum of Rs.119,561,262. As such, there was a risk of settling the land by the Corporation on financial difficulties.

(c) The land, 06 acres in extent located in Kesbepana, Unawatuna in Galle purchased for a sum of Rs.1,200,000 by the Corporation had been used for the resettlement of persons affected by the Tsunami by the Divisional Secretary, Galle without the permission of the Institution. A lawsuit remained being tried in the District Court, Galle for obtaining compensation for that land.

(d) Even though it had been stated that the Oil Tanks Complex located in Kankasanthurai belonging to the Corporation had been leased to the Ceylon Petroleum Storage Terminals Limited, the Corporation had not been entered into any written agreement whatsoever either with that Company or with the Ceylon Petroleum Corporation for the year 2016 and for future years.

4.3 Idle and Underutilized Assets

The following observations are made.

(a) The land in which the Cement Factory and the Buildings Complex are located, located in Kankasanthurai had been 741 acres in extent and, 297 acres in extent out of that land had been conveyed to the Corporation by a Gazette Notification. The remaining land, 444 acres in extent and the buildings had not been estimated and, written evidence on the ownership had not been furnished to audit and, this factory, buildings and the lands remained as an idle asset under the custody of the Army in the High Security Zone from a long period of time.

(b) Steps had not been taken by the Management to utilize the land, 209 acres in extent out of the land, 221 acres in extent remaining being vested under the Corporation in Palawi, in the Puttalam District, in an effective function.

4.4 Uneconomic Transactions

Even though a sum of Rs.1,083,618,910 had been invested in the shares of the Lanka Cement Company Limited from the year 1981 by the Corporation, any benefit whatsoever had not been given by the Company by the Corporation up to the year 2016.

4.5 Identified Losses

A bond is being made for economic service charges only in the instance that the turnover is a sum of Rs.50 million or more per quarter in terms of the Economic Service Charges (Amendment) Act, No.16 of 2009. Economic service charges amounting to Rs.163,388 had been paid based on that income despite only a sum of Rs.54,191,154 had been received in the year 2015 for the two years of the year 2013 and the year 2014. Action had not been taken to recover that amount from the relevant officers. Moreover, a sum of Rs.129,211 had been allocated as economic service charges based on the rent amounting to Rs.27,399,370 relating to the year 2016.

4.6 Personnel Administration

The actual cadre of the Corporation as at 01 January 2016 had been 76. Thirty- six employees had been retired by a Voluntary Retirement Compensation Scheme on 31 July 2016 and, the actual cadre had been restricted to 14 as at 31 December 2016. The approval had not been obtained for the staff of the Department of Management Services for the Corporation after the implementation of the Voluntary Compensation Scheme.

5. Accountability and Good Governance

5.1 Presentation of Financial Statements

Even though the financial statements and the Draft Annual Report should be furnished to the Auditor General within 60 days after the end of the Financial Year in terms of Section 6.5.1 of the Public Enterprises Circular No.PED.12 of 02 June 2003, the consolidated financial statements and the Draft Annual Report for the year 2016 of the Corporation had been furnished to audit on 20 June 2017.

5.2 Corporate Plan

The following observations are made.

(a) Key factors such as the Organizational Plan of the Institution that should be included into the Corporate Plan, Human Resources and Management Competencies and the Review of the Operating Results of 03 preceding years had not been included in terms of Section 5.1.2 of the Public Enterprises Circular No.PED/12 of 02 June 2003.

(b) Even though the updated copies of the Corporate Plan approved by the Board of Directors should be furnished to the Line Ministry, Department of Public Enterprises, Treasury and to the Auditor General with the Budget at least 15 days before the commencement of each Financial Year in terms of Section 5.1.3 of the above Circular, action had not been taken in compliance with that Circular.

5.3 Action Plan

The following observations are made.

(a) The responsibility of the Managers on the objectives and targets that should be achieved within the planned period had not been clearly stated in the Action Plan in terms of Section 5.1.2 of the Public Enterprises Circular No.PED/12 of 02 June 2003.

(b) Even though it had been stated that the main objective of the Institution by the end of the year under review as importing and the distribution of 50kg Portland Cement Bags, there was a difference of Rs.2,858,978 between the targeted values mentioned in the Corporate Plan and the Action Plan.

5.4 Internal Audit

Even though an Internal Audit Unit had been established in the first half- year of the year 2016, only one female Officer had been attached to it. Audit queries had not been issued within the first half- year and, even that female Officer had retired by the Voluntary Retirement Compensation Scheme from July 2016. The Internal Audit Unit remained completely inoperative by 31 December 2016 due to this reason.

5.5 Audit Committees

Even though 04 audit committees should be held within a year as an audit committee for at least 03 months with the Chief Internal Auditor as the convenor in terms of Section 7.4.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003, only 02 audit committees had been held in the year 2016 by the Corporation.

5.6 Procurement Plan

A Procurement Plan had not been prepared for the year 2016 in terms of Section 4.2 of the Government Procurement Guidelines.

5.7 Budgetary Control

As variances ranging from 43 per cent to 971 per cent remained between the budgeted expenditure and the actual expenditure in 08 Objects in the year under review and, expenditure totalling Rs.18,925,523 for 11 Recurrent Objects without obtaining the approval for the Budget Estimates. As such, it was observed that the budget had not been made use of as an effective instrument of management control.

5.8 Tabling of Annual Reports

Even though the Final Audited Accounts with the Audit Reports should be tabled in Parliament in all three languages within 150 days after the close of the Financial Year in terms of Section 6.5.3 of the Public Enterprises Circular No.PED/12 of 02 June 2003, action had not been taken to send the Annual Report of the year 2015 to the ministry for tabling in Parliament up to July 2017.

5.9 Unresolved Audit Paragraphs

The following observations are made.

(a) Loan balances totalling Rs.52,506,824 had not been recovered even by the end of the year under review on not obtaining a bond of security which complies with the value received on loan basis in awarding the post of the Sales Agent for selling cement on loan basis and not following a proper and efficient procedure by the management in providing and collecting loans.

(b) The limestone deposit, 5352 acres in extent located in Aruwakkalu in the Puttalam District had been leased for 50 years to a private company to mine limestone for manufacturing cement in the year 1995. The annual lease rent recoverable in the year under review in terms of the lease agreement had been valued at Rs.26,851,358, that is equal to a sum of US$ 202,804. However, even though it had been instructed to revise this lease agreement in the Meeting of the Committee on Public Enterprises held on 16 August 2011 due to a Section on revising the annual lease rent not being included in the lease agreement which had been entered into, action had not been taken accordingly by the Management even to estimate this land and bring it to the financial statements.

6. Systems and Controls

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

Areas of Systems and Controls	Observations
(a) Accounting	(i) Not maintaining and updating the Ledger Accounts, Books and Registers of the Institution. (ii) Not maintaining a Main Journal by the Institution.
(b) Control of Fixed Assets	(i) Not properly maintaining the Registers of Assets. (ii) The delay in the appointment of the Board of Survey and carrying out Boards of Survey.
(c) Stores Control	Not paying proper attention on maintaining stocks of cement, storing and maintaining Stocks Reports.
(d) Internal Control	(i) Not taking action to introduce methods of Internal Control and to maintain control by properly implementing them. (ii) Not having an Internal Audit Unit.
(e) Control of Debtors and Creditors	(i) Not recovering the outstanding loan balances. (ii) Not taking action to settle the payable balances.