Ceylon Petroleum Corporation – 2016

The audit of financial statements of the Ceylon Petroleum Corporation (CPC) and the consolidated financial statements of the CPC and its Subsidiary (CPSTL) for the year ended 31 December 2016 comprising the statements of financial position as at 31 December 2016 and the statements of comprehensive income, statements of changes in equity and cash flow statements 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 31 of the Ceylon Petroleum Corporation Act, No. 28 of 1961. My comments and observations which I consider should be published with the Annual Report of the CPC in terms of Section 14(2)(c) of the Finance Act appear in this report. I was assisted by a firm of chartered accountants in public practice to carry out the audit of the financial statements of the Subsidiary.

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 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 consistent with International 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 judgments, including the assessment of the risk 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 CPC'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 CPC'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 the 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 extent of the audit.

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

1.4 Basis for Qualified Opinion

My opinion is qualified based on the matters described in paragraph 2.2 of this report.

2 Financial Statements

2.1 Qualified Opinion

(a) Qualified Opinion – CPC

In my opinion, except for the effects of the matters described in paragraph 2.2.2 of this report, the financial statements give a true and fair view of the financial position of the Ceylon Petroleum Corporation as at 31 December 2016 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

(b) Qualified Opinion – Group

In my opinion, except for the effects of the matters described in paragraph 2.2 of this report, the consolidated financial statements give a true and fair view of the financial position of the Ceylon Petroleum Corporation and its Subsidiary as at 31 December 2016 and their 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 Group Financial Statements

The following observations are made.

(a) In consolidation of the financial statements, the intercompany transactions should be eliminated. However, the elimination of a difference of Rs. 39.66 million and Rs.1,104.15 million between the amount receivable from and payable to Ceylon Petroleum Storage Terminals Limited (CPSTL) respectively shown in the financial statements of the CPC and the correspondent amounts shown in the financial statements of CPSTL had not been done. The details are given below.

Item	Amount as per the financial statements of the CPC	Amount as per the financial statements of the CPSTL	Difference
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	Rs. Million	Rs. Million	Rs. Million
Amount Receivable from CPSTL/ Payable to CPC	302.87	263.21	39.66
Amount Payable to CPSTL/ Receivable from CPC	3,589.44	4,693.59	1,104.15

(b) A qualified opinion had been expressed on the financial statements of the CPSTL for the year under review based on the following matters.

i. Ceylon Petroleum Corporation Thrift Society Limited (Thrift Society) pays retirement benefits and medical benefits to the employees of Ceylon Petroleum Storage Terminals Limited (CPSTL) (Members). The Thrift Society pays an additional half months' salary for every year of service to its members at the time of retirement. Accordingly, Thrift Society is an arrangement whereby CPSTL provides post- employment benefits to its employees and qualify as a post-employment benefit plan as per the Sri Lanka Accounting Standard LKAS 19 Employment Benefits. CPSTL has not actuarially valued and accounted for the above retirement benefit plan as per LKAS 19.

ii. Trade and Other Receivables included an amount receivable from Ceylon Petroleum Corporation amounting to Rs. 4,857.2 million. Based on the confirmation received from Ceylon Petroleum Corporation, the above amount includes a disputed amount of Rs.652 million (2015: Rs.336 million) for which only an allowance of Rs.163.5 million (2015: Rs.163.5 million) has been made as impairment. Accordingly the provision for impairment is understated by Rs.489 million (2015:Rs173 million)

iii. As per the Inland Revenue Bill passed by the Parliament on 07 September 2017 the applicable tax rate for the Company with effect from 01 April 2018 would be 28 per cent. The provisions of the bill will become effective once it receives the certification of the Hon. Speaker. Any impact that may arise due to the provisions of this Bill has not been disclosed in these financial statements.

2.2.2 Financial Statements of the CPC

2.2.2.1 Negative Net Assets Position of the CPC

Attention is drawn to the matter that even the operations of the CPC had resulted in an after tax net profit of Rs. 53,027 million and a total comprehensive income of Rs. 53,137 million for the year 2016, had a negative net assets position of Rs. 185,847 million as at the end of the year under review. The negative impact of exchange rate variation for the year under review, and heavy losses incurred by the Corporation due to Hedging transactions taken place during the previous years had also caused to that negative net assets position. Even though the financial performance of the Corporation had improved during the year under review, the heavy losses sustained during the previous years had resulted to retain further negative net assets position of the CPC.

2.2.2.2 Compliance with Sri Lanka Accounting Standards (LKAS)

The following observations are made.

(a) **LKAS 19 – Employee Benefits**

According to the accounting policy No. 1.3 disclosed with the financial statements, the Corporation had computed the expenditure for retirement benefits by applying the Projected Unit Credit Method using the software issued by the Institute of Chartered Accountants of Sri Lanka, which is permitted to use only for Small and Medium-sized Entities. However, the actuarial valuation method should be used for the calculation of retirement benefit obligation. Accordingly, it was observed that the requirements in the Standard had not been followed in the computation of provision for gratuity.

(b) **LKAS 24 – Related Party Disclosures**

Related party involvement between the Corporation and key management personnel had not been properly disclosed in the financial statements.

2.2.2.3 Accounting Deficiencies

The following observations are made.

(a) The validity period of 581 cheques valued at Rs 989.9 million which issued but not presented for payments had been elapsed as at 31 December 2016. Further, a cheque issued in the name of the Director General of Customs on 28 June 2016 for Rs.972.25 million had been included in the above un-presented cheques. However, the CPC had failed to make proper accounting treatments in this regard. Hence, both cash and relevant liability accounts had been understated by similar amount.

(b) In amalgamation, inter Branch transactions should be eliminated. However, a balance in Inter-Branch trade and other receivable of Rs. 1,397,300 was observed in the financial statements as at the end of the year under review. Therefore, balance of trade and other receivable shown in the financial statements had been overstated by similar amount. Hence, the accuracy and completeness of recording and settlement of Inter Branch Accounts is critically doubt in audit.

(c) An amount aggregating Rs. 924,879,000 had been provided in the financial statements of the year 2015 as income tax for the years of assessment from 2011/2012 to 2014/2015. However, according to the information made available for audit, the actual income tax for the said period including penalties totaling Rs.157,439,252 thereon was Rs. 1,409,169,766. Accordingly, the provision made for unpaid income tax in the financial statements of the year 2015 appears to be understated by Rs. 484,290,530.

(d) According to the information made available for audit, an additional assessment of Rs.1,703,895,425 was imposed by the Department of Inland Revenue on unpaid Nation Building Tax (NBT) relating to the years 2015 and 2016. However, only a total sum of Rs. 410,300,842 was provided as NBT in the financial statements for the year under review. Accordingly, provision made for unpaid NBT in the financial statements of the year 2016 appears to be understated by Rs.1,293,594,583.

(e) According to the detailed schedule furnished to audit, the total expenditure on demurrages for the year 2016 was Rs. 353,737,477 which comprised with accrued amount of Rs. 173,504,644 and paid amount of Rs. 180,232,833. However, as per the financial statements for the year under review, only Rs. 173,504,644 had been charged.

(f) CPC had paid Rs. 10,000 million to the General Treasury as special fee on the request of the General Treasury in 2014 and accounted for as receivable instead of being charged against income for the year 2014. Accordingly, Rs. 250 million, Rs. 750 million and Rs. 1,000 million had been charged against income for the years 2014, 2015 and 2016 respectively. As a result, the net operating income of the respective years had been understated by similar amounts. It was further observed that the erroneous accounting treatment had violated the fundamental accounting principles.

(g) Interest of Rs. 6.7 million computed on the value of unsettled invoices of the Sri Lankan Airlines Ltd totaling Rs. 160.5 million for the year under review had not been brought to accounts and as a result, both accrued interest and interest income for the year under review had been understated by same amount.

2.2.2.4 Un-reconciled Differences

The following observations are made.

(a) As per the books of account of the CPC, the net amount payable to CPCTSL at the end of the year under review was Rs. 7,600,745. However, as per the balance confirmation from CPCTSL, it was Rs. 42,460,782. Therefore, an un-reconciled difference of Rs.34,860,037 was observed between those two records.

(b) Un-reconciled differences of Rs. 177 million and Rs. 400.9 million were observed between the charges for storage and distribution of oil (i.e. terminal charges, transport charges and interest payment etc.) shown in the financial statements of the CPC and CPSL for the year 2016 and 2015 respectively.

(c) According to the financial statements for the year 2016, the medical expenditure for the year under review was Rs 38,579,072 whereas, according to the detail schedule made available to audit it was Rs. 57,951,039. Therefore, an unexplained difference of Rs 19,371,967 was revealed in audit.

(d) According to the confirmation of the year end balances, sums of US$ 22.77 million and US$ 8.65 million had to be paid by the CPC to the People's Bank and the Commercial Bank PLC respectively relating to the Hedging transactions taken place in respect of procurement of oil during the period of 2007 to 2009. However, it had not been brought to the accounts of the CPC.

2.2.2.5 Lack of Evidence for Audit

The following observations are made.

(a) Value Added Tax (VAT)

Value Added Tax (VAT) aggregating Rs.623,573,943 including Rs.326,394,420 Rs.124,733,322 and Rs.172,446,201 had been recorded as VAT recoverable, refundable VAT and VAT on local purchases respectively under other receivable in the statement of financial position at the end of the year under review. However, the reasons for this had not been furnished to audit. Further, the VAT recoverable amounting to Rs.326,394,420 had continuously been recognized as other receivable since 2010 without being cleared. Moreover, the tax invoices and other relevant supporting documents were not made available to verify the refundable VAT of Rs. 124,733,322.

Further, according to the books of accounts of the CPC, the VAT on Local Purchases amounting to Rs. 172,446,201 had been generated during the year under review. However, there was no recorded recoverable VAT or carried forward VAT in the VAT returns submitted to the Department of Inland Revenue by the CPC for the year under review and the tax invoices of the year under review were also not made available for audit.

(b) According to the financial statements of the CPC, the total VAT recoverable and net Nations Building Tax (NBT) payable as at the end of the year under review was Rs.623,573,943 and Rs.1,803,656,120 respectively. However, these were shown as Rs.29,528,455 and Rs. 2,831,220,633 respectively in the records maintained by the Department of Inland Revenue. Hence, an un-reconciled difference of Rs. 594,045,488 and Rs.1,027,564,513 respectively were observed among those figures. Further, the total VAT payable balance shown in the records of the Department of Inland Revenue at the end of the year under review was Rs. 3,336,528,365. However, no payable balance is shown in the financial statements of the year under review. The reasons for these had not been furnished to audit.

(c) As per the statement of financial position there was neither receivable nor payable balance relating to Economic Services Charges (ESC) at the end of the year under review. However, as per the records of Department of Inland Revenue, the total ESC payable balance at the end of the year under review was Rs.55, 800,000. Therefore, the accuracy and completeness of the record of financial statements in relation to the ESC is doubt in audit.

(d) According to the statement of financial position of the Corporation, the net income tax recoverable balance at the end of the year under review was Rs. 3,959,861,589. However, as per the records of Department of Inland Revenue, it was a receivable balance of Rs. 6,443,430,012. Therefore, the total outstanding amount shown in the statement of financial position had been differed by Rs. 10,403,291,601 and therefore, the reliability, accuracy and completeness of the figure in the statement of financial position at the end of the year under review was in doubt.

(e) According to the statement of the financial position of the Corporation, the custom duty payable was Rs. 5,119,928,266 whereas, according to the records of Sri Lanka Customs, it was Rs. 5,707,652,279. Therefore, a difference of Rs. 587,724,013 was observed between those two records as at 31 December 2016.

(f) Income Tax amounting to Rs. 1,511,857,999 had been shown in the statement of financial position at the end of the year under review under other receivables and its composition is as follows.

	Amount Rs.
Other Receivable - Department of Inland Revenue	376,000,065
Other Receivable - Department of Inland Revenue Department of Customs	1,135,857,934
Total	**1,511,857,999**

The following observations are also made in this regard.

(i) Neither overpayment nor carried forwarded tax balance had been appeared in any tax return submitted to the Department of Inland Revenue.

(ii) The reason why those figures classified under other receivable without directly classified as receivable from the Department of Inland Revenue was not clear to the audit.

(iii) It was observed that the amount of Rs. 376,000,065 had continuously been shown as other receivable in the statement of financial position since 1998. The reason for continuation of such a balance for a so longer period without being settled was not clear to the audit.

(iv) The above mentioned other receivable balance of Rs. 1,135,857,934 which had been carried forwarded year by year since 2012 without any review could not be satisfactorily verified due to unavailability of relevant information. Therefore, I am not in a position to satisfactorily verify the reliability, accuracy, valuations and completeness of the above mentioned receivable balances aggregating Rs. 1,511,857,999 in audit due to absence of sufficient evidence.

(g) According to the financial statements, the accrued interest expense as at 31 December 2016 was Rs. 313,820,185. However, according to the ledger, it was a net figure of Rs 12,146,081 which comprises with 04 debit balances aggregating Rs.1,617,112 and 31 credit balances aggregating Rs. 13,763,193. Further, this balance has been accumulating since 2010 and it could not be able to satisfactorily verify the accuracy, existence and completeness of this expense due to lack of supporting information.

2.3 Accounts Receivable and Payable

Total trade receivable as at 31 December 2016 was Rs 33,387 million and it comprised with balances of Rs. 24,136.8 million and Rs. 9,250.2 million due from Government institutions and private institutions respectively. The total dues as at the end of the year under review had increased by 78 per cent with compared to the previous year outstanding balance of Rs.18,787 million. The age analysis thereon is given below.

Type of Customer	Total	Age Analysis					
		Less than one year	1-2 years	2-3 years	3-4 years	4-5 years	Over 5 years
	Rs.	Rs.	Rs.	Rs.	**Rs.**	Rs.	Rs.
Dealers	1,016,605,312	990,626,246	(599,010)	8,971,155	1,282,138	1,138,177	15,186,606
Aviation	9,263,688,816	9,257,815,945	217	38,394	1,803,327	1,617,303	2,413,630
Power Plants	19,996,044,020	19,007,529,142	8,582,378	226,321,671	753,610,829	-	-
Government Customers	2,002,371,035	1,312,981,322	31,856,507	480,596,958	61,454,860	49,270,208	66,211,176
Private Consumers	628,092,693	316,810,086	23,670,804	21,653,010	22,533,993	25,412,079	218,012,717
Agro Chemical	17,001,940	7,782,212	1,997,458		50,322	49,815	7,122,133
Others	462,891,297	458,684,841	-	-	-	106,198	4,100,258
Total	**33,386,695,105**	**31,352,229,794**	**65,508,354**	**737,581,188**	**840,735,469**	**77,593,780**	**313,046,520**

The following observations are also made in this connection.

(a) Interest Charges on Overdue Balances

(i) The Corporation is charging interest from customers who are having outstanding balances exceeding the credit periods. However, a proper system had not been designed, implemented and maintained by the Corporation to calculate the interest due to ineffective decision taken by the Board to control the unnecessary dragging of the payment for an unforeseen period.

(ii) It has been reiterated in previous audit reports that there were errors due to manual calculation of interest and therefore suggested to use the introduced SAP system. However, favorable actions had not been taken by the Corporation to rectify such control weaknesses and such errors had been observed in the year under review too.

(iii) Interest had not been charged on balance of Rs. 31,207,680 outstanding from Provincial Road Development Authority of Western Province since 2015.

(b) Agreements of Fuel Supply

(i) The CPC had not entered into formal agreements, especially, with 17 major customers whose outstanding balance represent Rs. 27,636 million or 82 per cent of the total debtor balance as at 31 December 2016. Therefore, the default risk is very high due to lack of legal right to the Corporation, if any, complication arisen at the settlement.

(ii) A sum of Rs.7.9 billion had been paid by the Sri Lankan Air Lines Ltd on 30 September 2015 in local currency as settlement of the outstanding balance prevailed at that date ignoring the billing currency i.e. US$. Thereafter, the Corporation had converted that amount into US$ at the rate prevailed on that date and necessary adjustments had been made in its books of accounts, accordingly. Subsequently, the Sri Lankan Air Lines Ltd. had made a request to the CPC not to treat the exchange gain of Rs. 307,063,541 on that transaction as an income and consider the entire amount (including the exchange gain) as the final settlement. Accordingly, it was revealed that non-availability of firm conditions on such issues in the credit agreement entered into between two parties had critically impacted to the settlements.

Further, the Corporation had agreed to share the previously recognized exchange gain approximately Rs. 154 million, equally. However, no adjustments had been made in the financial statements in this regard.

(iii) It was observed that the petroleum products had continuously been supplied to the customers despite their long outstanding balances. Selling petroleum products to Sri Lanka Transport Board – Jaffna, Road Development Authority and Ministry of petroleum development having long outstanding balances of Rs.3,964,634, Rs. 90,002,930 and Rs. 6,243,570 respectively can be cited as examples.

(c) Short Term Loans

The following observations are made in relation to the Short Term Foreign Currency Loans (STFCL) obtained by the CPC.

(i) According to the age analysis, the credit period granted on behalf of loans amounting to Rs 76,488.442 million (USD 504.062 million) or 39 per cent of such total loans had been expired at the end of the year under review. Of that, 52 per cent was in arrears over a period nearly one year as at 31 December 2016. Those short term foreign currency loans had been granted by the Peoples Bank during the period from 01 October 2015 to 31 December 2015.

(ii) The Corporation had to incur an additional cost approximately Rs. 3,416 million as interest due to non-settlement of such loans within the agreed period. That additional cost was only for the short term foreign currency loans where the credit period exceeded over 01 year as at 31 December 2016. However, the total cost of the late settlement of such loans would further increase if calculation is done for the entire period of delay. Further, it was observed that there were short term investments of Rs. 63,763 million available as at the beginning of the year under review which generated lesser return than the above mentioned loan interest rate.

The Managing Director of the Corporation status as follows in this regard. "*The Bank was not in a position to purchase sufficient quantity of USD to settle foreign currency loans granted by them*".

Accordingly, existing a proper evaluation for selection of borrowing source and availability of proper settlement plan to honor the conditions of the loan, especially to mitigate the impact of higher interest cost and loss due to depreciation of currency was in doubt.

2.4 Non-compliance with Laws, Rules, Regulations and Management Decisions, etc.

The following instances of non-compliance with Laws, Rules, Regulations and Management Decisions, etc. were observed in audit.

Reference to Laws, Rules, Regulations and Management Decisions	Non-compliance
(a) Public Enterprises Circular No. PED/12 of 2 June 2003 - Guidelines for Good Governance.	
(i) Guideline 3.2	At least one industry expert had not been included in the Board of Directors of the CPC.
(ii) Guideline 7.4.4	It is essential that a Training Committee, a Subcommittee of the Senior Management Committee, should evaluate the training needs of the enterprise, to enable the human resources of the enterprise to keep abreast of changes, both locally and abroad to improve employee productivity. Further, such Committee should formulate procedures relating to selection of individuals for local/ foreign training. However, no such mechanism had been in operation.
(iii) Guideline 9.14	The Scheme of Recruitments and Promotions (SOR) of the CPC other than A Grade officials had not been approved by the Department of Management Services (MSD).
(iv) Guideline 9.3.1	The CPC had not maintained proper succession plan to mitigate the risk of filling vacancies in the posts of senior management level.
(v) Guideline 9.5.1	A training budget should have been prepared and the amount allocated for training should be determined in consultation with the Training Committee. However, no such

		training budget had been prepared by the CPC up to date.
(vi)	Guideline 9.5.4	Internally generated funds of a commercial corporation or Government grants should not be utilized for foreign training, unless specific approval is obtained from the Secretary to the Treasury. However, it was not observed in audit that the specific approvals had been obtained by the CPC in accordance with the Guideline.
(b)	Finance Circular No. 124 of 24 October 1997 of the Ministry of Finance and Planning.	Covering up duties of a vacant post should be limited to a period of 03 months. However, 14 officers had been assumed for cover up duties of the vacant posts including 08 posts in Grade A such as Manager (Investigation), Manager Marketing (Retails), Management Assistance Regional Manager (Central) etc. for the period ranging 07 months to 3 years as at 31 December 2016.
(c)	Department of Public Enterprises Circular No. FP/06/35/02/01 of 04 November 2013 and No. PED 03/2016 of 29 April 2016.	The CPC had borne the Pay As You Earn (PAYE) tax of its employees amounting to Rs. 152,690,099 without deducting it from their personal emoluments for the year under review.
(d)	Financial Regulations of the Government of the Democratic Socialist Republic of Sri Lanka. Financial Regulation 396	According to the sample selected, 1,619 cheques to the total value of Rs. 3,652.74 million had been issued but not presented to the Banks as at 31 December 2016 for a longer period. However, actions had not been taken to clear those outstanding cheques even up to 27 July 2017.

3 Financial Review

3.1 Financial Results

According to the financial statements presented, the operation of the CPC for the year under review had resulted in a pre-tax net profit of Rs. 69,553.681 million as against the pre-tax net loss of Rs. 19,885.780 million for the preceding year, thus indicating an accretion of Rs.89,439.461 million in the financial results. The stable of import cost due to untiring of oil prices in the international market, the growth of sales in the domestic market as a result of increase of demand, decline the depreciation trend of Lanka Rupee against the United States Dollar in the year 2016 and the decrease of financial expenditure as compared with the previous year had been caused to this surplus. In addition to the pre-tax profit of Rs.69,553.681 million, the contribution of the CPC to the Country during the year under review was Rs. 153,184 million and it was Rs. 100,175 million in the previous year.

3.2 Analytical Financial Review

3.2.1 Profitability

The operations of the CPC had resulted in a markup of 29.6 per cent for the year under review thus indicating an improvement of 17.85 per cent as compared with the markup of 11.75 per cent in the preceding year. Similarly, the gross profit for the year under review had increased by Rs. 57,004 million or 144 per cent as compared with the corresponding gross profit of Rs. 39,616 million in the preceding year. These improvements are summarized and shown below.

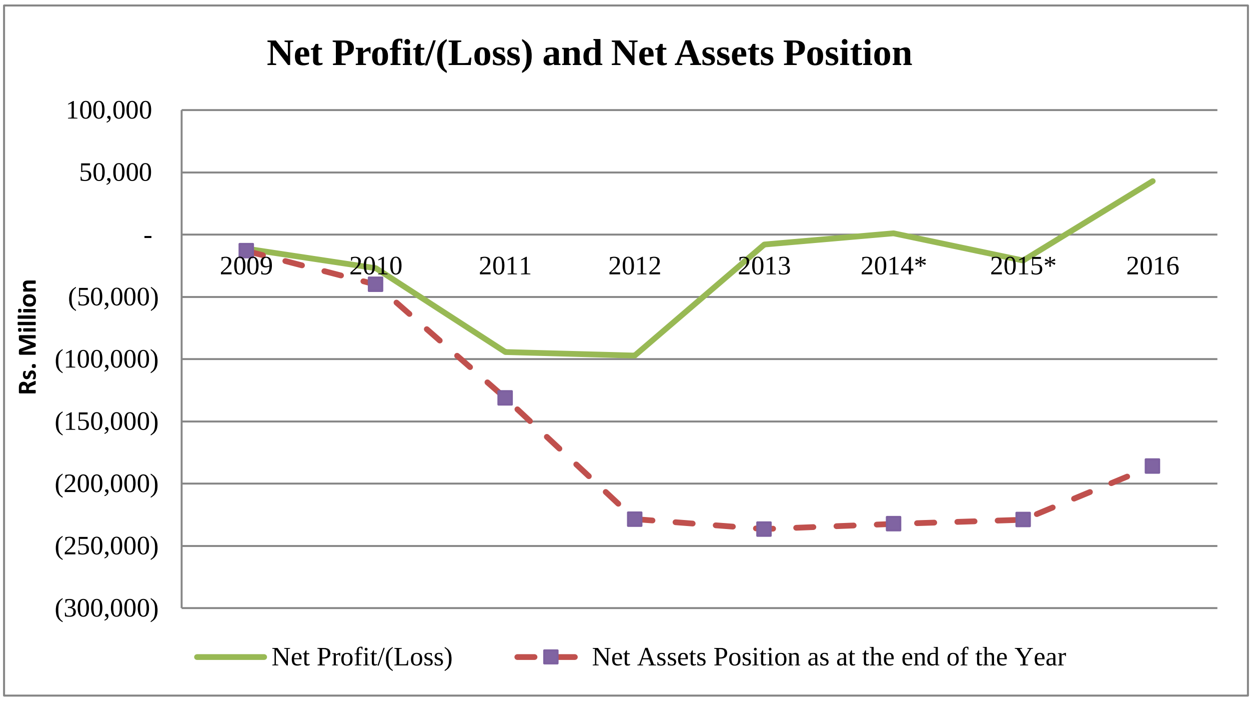
Description	**For the year ended 31 December**		**Variance {Favorable/ (Adverse)}**	
	2016	**2015 Restated**		
	Rs. million	**Rs. million**	**Rs. million**	**Percentage**
Revenue	423,061	376,734	46,327	12
Cost of Sales	(326,441)	(337,118)	10,677	3
Gross Profit	**96,620**	**39,616**	57,004	144
Other Income	3,589	4,234	(645)	(15)
Selling and Distribution Expenses	(14,412)	(13,401)	(1,011)	(7.5)
Administration Expenses	(4,384)	(3,592)	(792)	(22)
Operating Profit	**81,413**	**26,857**	54,556	203
Exchange Rate Variation	(8,829)	(32,841)	24,012	73
Finance Expenses	(11,404)	(15,049)	3,645	24
Finance Income	8,374	5,011	3,363	67
Hedging Expenses	-	(3,864)	3,864	100
Profit/(Loss) Before Income Tax	**69,554**	**(19,886)**	**89,440**	**450**

3.2.2 Net Profit/(Loss) Vs. Net Assets

The net profit/ (loss) and the net assets position of the CPC for the year 2016 and previous seven years are depicted in the table and the chart given below.

Year	Net Profit/(Loss)	Net Assets Position as at the end of the Year
	Rs. million	Rs. million
2011	(94,357)	(131,236)
2012	(97,181)	(228,545)
2013	(7,889)	(236,467)
2014*	1,129	(232,257)
2015*	(20,681)	(228,985)
2016	53,027	(185,847)

* Restated



3.2.3 Significant Accounting Ratios

According to the information made available, some important accounting ratios of the CPC for the year under review and the preceding year are given below.

Ratios	2016	2015 (Restated)
Profitability Ratios		
Gross Profit Ratio (GP) (%)	22.84	10.52
Operating Profit Ratio (%)	19.24	7.13
Net Profit/(Loss) Ratio (NP) (%)	12.53	(5.45)
Liquidity Ratios		
Current Assets Ratio (Number of times)	0.34:1	0.31:1
Quick Assets Ratio (Number of times)	0.24:1	0.21:1
Working Capital (Rs. million)	(249,297)	(295,098)
Investment Ratios		
Return on Assets (ROA) (%)	27.82	(10.4)

The following observations are made in this regard.

(a) The gross profit ratio and the net profit ratio had improved by 12.33 per cent and 17.98 per cent respectively during the year under review as compared with the previous year.

(b) The negative working capital position of the CPC in 2016 had improved by 6 per cent as compared with the previous year. The main contributory factors for this positive condition were increase of trade and other receivables, short term investments and decrease in borrowings.

4 Operating Review

4.1 Performance

(a) The domestic retail prices of petroleum products had been revised upward continuously up to September 2014 in order to address the financial difficulties of the CPC. In the meantime, the domestic retail prices of petroleum products had been reduced twice during 2014 and 2015 as international oil prices had continued to be on a declining trend. However, the above price revisions had not reflected the actual reductions in international market prices in full as no price revision had been taken place since then. Moreover, the CPC had continuously sustained losses from following petroleum products during the year under review and previous four years.

Sector	**Net Losses Sustained for the Year**				
	2016	**2015**	**2014**	**2013**	**2012**
	Rs. Million	**Rs. Million**	**Rs. Million**	**Rs. Million**	**Rs. Million**
Power Generation					
Fuel Oil 1500	-	252	299	1,240	34,959
Industrial & Domestic					
Fuel Oil 1500	-	262	69	350	2,003
Domestic Kerosene	2,982	3,860	2,715	2,449	3,525
Export					
Naphtha	1,580	827	1,799	-	-
Fuel Oil	727	5,346	1,627	-	-
Bunkering					
Fuel Oil	68	-	-	-	-

Further, the CPC had incurred losses of Rs. 8,251 million and Rs. 1,291 million from petrol 92 Octane and 95 Octane respectively in the year under review as shown below.

Profitability on Petroleum Products (per liter) for the year 2016

Product	**Selling Price per Liter**	**Sales Price Net of Dealer Margin per Liter**	**Cost of Sales per Liter**	**Gross Profit per Liter**	**All Taxes Included in the Total Cost per Liter**	**Total Cost per Liter**	**Net Profit/ (Loss) per Liter**	**Total Net Profit/ (Loss) for the year**
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.	Rs. Mn.
Petrol 95	128.00	124.15	95.29	28.86	67.87	133.06	**(8.91)**	(1,291)
Petrol 92	117.00	113.49	84.29	29.20	57.89	120.84	**(7.35)**	(8,251)
Auto Diesel	95.00	92.83	60.37	32.46	17.22	76.02	**16.81**	31,128
Super Diesel	110.00	107.20	66.46	40.74	24.93	83.62	**23.58**	1,761
Kerosene	49.00	47.77	56.38	(8.61)	-	65.59	**(17.82)**	(2,982)*

* Kerosene loss of Rs. 2,982 million has been accounted in the financial statements as a subsidy receivable from the General Treasury.

(b) The agreement entered into between a private Gas Company and CPC in respect of selling liquid petroleum gas had been expired on 20 October 2006. As reported in the previous audit reports, the CPC has been supplying liquid petroleum gas to that Company continuously without entering into a fresh agreement or renewing the earlier agreement. In addition to that, the CPC supplies liquid petroleum gas to the other private Company without entering into an agreement.

4.2 Management Weaknesses

The following observations are made.

(a) **Enterprise Resource Planning (ERP) System -** It was observed that there was no any agreement or a Memorandum of Understanding among the CPC, CPSTL and Lanka Indian Oil Company (LIOC) with regard to their individual responsibilities in respect of the involvement of the Enterprise Resource Planning (ERP) System introduced by the CPSTL, and as such this system is not adequately utilized, especially, for the fuel stock reviewing purposes.

(b) **Collection of Monthly Utilized Fee (MUF)**

According to the Board Decision number 38/1140 dated 29 October 2013, the Board has approved to charge a Monthly Utilized Fee (MUF) from all Corporation Owned Dealer Operated (CODO) Filling Stations and Treasury Owned Dealer Operated (TODO) Filling Stations with effect from 01 January 2014. However, MUF shall be charged from the dealers who are paying Monthly Occupational Rental (MOR) with immediate effect. Accordingly, MUF shall be calculated as 35 per cent of the average monthly commission out of average monthly commission earned during the previous year (12 months period). Further, a rebate had been granted to small scale dealers to sustain them as per the following basis.

Monthly Commission Category	Rebate percentage
Less than Rs. 500,000	70
Rs. 500,001 - Rs. 1,000,000	50
Rs. 1,000,001 - Rs. 1,500,000	25
Above Rs. 1,500,001	0

After considerable delay, over 13 months, the Marketing Manager (Retail) had notified to the Board, by Board Paper No. 16/1154 dated 11 December 2014 that *"the implementation of this scheme with effect from 01 January 2014 was not possible due to the delay caused in preparing the agreements. The finalization of the CODO agreement is on the verge of completion and once it is finalized, the marketing function is expected to implement this scheme with all CODO/TODO dealers"*.

However, the Board had granted their approval to amend those agreements on 16 February 2016 wide the Decision No. 11/1179 but actions had not been taken to charge MUF from the dealers in both categories as mentioned above (MUF had been charged only 11 out of 248 dealers in 2016) up to 31 October 2017. As a result, over Rs 300 million per annum had been lost to the CPC since the year 2014 due to non-implementation of the said Board Decision.

(c) Medical Assistant Scheme (MAS)

According to the information available with audit, Ceylon Petroleum Corporation Thrift Society Limited (CPCTSL) had been registered on 31 December 1981 under the Section 123(3) (a) of the Society Ordinance and has been operating as a Not-for-Profit Organization (Non-Governmental Organization) as per the definition provided in the Sri Lanka Statement of Recommended Practice for Not-for-Profit Organization. All permanent employees of both CPC and CPSTL are the members of CPCTSL. The principal objectives of CPCTSL are to provide retiring benefits, financial assistance to the next of kin in the event of death of members, financial assistance to the members in the event of death of eligible family members, financial assistance to the members under the medical benefit scheme and loans provide to the members.

The following major benefits had been provided to the employees of the CPC and CPSTL by the CPCTSL as its members.

1. Payment of retirement benefits (half month salary for each completed year of service)
2. Conduct of MAS on behalf of CPC and CPSTL.

It was stated in the meeting minute of the CPCTSL dated 23 February 2016, the inability to continue the MAS due to a net deficit of CPCTSL which contribute to a negative accumulated reserves amounting to Rs. 1,473,714,266 at the end of the year 2015. Then, according to the Board Decision No. 08/1186 dated 11 August 2016, the approval was granted to continue the management of MAS by the CPC with effect from 01 July 2016 and to bear the cost for providing basic entitlement by the CPC for a period of six months or until a suitable medical insurance provider is selected.

The following observations are made in relation to the MAS.

(i) Requested information was not provided to audit by the CPC even two reminders had been issued after the information called on 19 July 2017 regarding the CPCTSL. The reasons for not giving requested information about the relationship and transactions with the CPCTSL are questionable to audit.

(ii) According to the Board Decision No. 08/1186 dated 11 August 2016, even the management of Medical Assistant Scheme should be continued by the CPC with effect from 01 July 2016, audit was not observed any policy or procedure to manage Medical Assistant Scheme up to date. Further, medical bills amounting to Rs 41,237,505 had been claimed by the CPCTSL from the CPC relating to the period after the 01 July 2016 which is contrary to such Board Decision.

(d) Pipeline Network for Oil Transportation

The pipelines installed several decades back to transport of finished petroleum products such as petrol, diesel, kerosene and furnace oil from the Colombo Port to the Kolonnawa Petroleum Installation are in a state of repair and it was revealed that some of them have already been abandoned due to the deteriorated condition beyond repairs. Renovation and modernization of these pipelines have been a very urgent need, as a large quantity of the national requirement of the petroleum products is being carried into Kolonnawa fuel Storage Terminal through those deteriorated pipelines. The possibility of paralyzing the whole country with a severe fuel crisis due to transporting the imported finished petroleum products through those deteriorated pipelines cannot be ruled out in audit.

The Chairman of the CPC stated in this regard as follows.

"Action has been taken to call tenders to construct two new transfer lines having diameters of 18" and 14" respectively. These lines will be starting from Dolpin Tanker Birth (DTB) (with two new loading arms) and end up at Kolonnawa oil installation of CPSTL. In addition, the 12" line which is currently under repairs will also be completed, once the segment where horizontal drillings are needed to be done is carried out."

The Muthurajawela installation is fed through a Single Point Buoy Mooring (SPBM) facility located in the mid sea about 6 km from the shore and 7.2 km from Muthurajawela Terminal and there was no alternative supply source in case of rough sea conditions or when the SPBM facility is under maintenance. At the same time, there was no linkage between the Muthurajawela Terminal and Kolonnawa Installation for inter-terminal product transfers, which had also hampered the optimum utilization of those Terminals due to those constraints.

Even though, the approval of the Cabinet of Ministers for the implementation of "Cross Country Pipeline Project" had been granted on 13 September 2012, it had not been implemented even in the year under review. The current position of the Cross country pipelines – Fuel lines from Colombo Port to Kolonnawa Depot is shown below.

Diameters of the Line (Inches)	Product	Current Position
10	Gas Oil	Working condition
10	Other White Oil	Not Working
10	Naphtha Oil	Not Working
12	Naphtha Oil	Not Working. The CPSTL is replacing the line
14	Fuel Oil	Working condition

According to the records of the CPC, total cost incurred by the CPC due to Pipe Line Transferring (PLT) Leakages and Demurrage Chargers was amounting to Rs.1,096,304,695 which comprise PLT variation loss of Rs. 922,800,051 and Demurrage Chargers loss of Rs. 173,504,644 respectively for the year under review too and, both losses have been arisen mainly due to the issues in the Pipelines. Even these matters have continuously been pointed out in my previous audit reports; favorable actions had not been taken by the management of the CPC to mitigate the loss due to issues in the Pipelines.

(e) Trincomalee Tank Farm

The Tank Farm contained of 100 Oil Tanks, each having a capacity of 12,500 cubic meters (m^3) (10,000 MT) and other associated facilities, had been constructed in 1930. The land with an extent of 358,553 hectares belonged to the Tank Farm had been given on lease basis by the Government of Sri Lanka to the Commissioners of the Lord High Admiralty of the British Government for a period of 999 years before gaining independence to Sri Lanka. In 1961 at the request of the Government of Sri Lanka, the CPC had paid Sterling Pounds 250,000 in three installments and taken over the possession of Land, Tank Farm, Buildings and other equipment with effect from 01 April 1964. Nevertheless, no legal documents had been obtained from the Government for the above land.

In 2003, the Government of Sri Lanka had signed a MOU with Lanka Indian Oil Company (LIOC) to lease out the storage facilities and the land for a period of 35 years and lease agreement should be executed within 6 months from the date of the agreement. However, the CPC had not yet entered into any lease agreement.

In 1942 one oil tank had been totally destroyed by the war. Out of remained 99 oil tanks, 14 tanks are currently used by the LIOC and balance 85 tanks had been abandoned. During the Visit of Prime Minister of India to Sri Lanka in March 2015, it had been agreed that Lanka IOC and Ceylon Petroleum Corporation would jointly develop the China Bay upper tank farm. The Cabinet approval was granted to hand over the operation of the tank farm to the joint venture formed by the CPC and LIOC on 13 July 2016 and the Cabinet Committee on Economic Management (CCEM) held on 13 July2016 had granted the approval to appoint a consultant to development mechanism for a joint venture.

The Chairman of the CPC states in this regard as follows.

"This issue on how to utilize the Trincomalee tank farm had been discussed with a view to provide a solution to the storage constrains faced by CPC at Kollonawa installation. However, it has been brought to the notice of CPC that the ownership of these tanks at Trincomalee is yet to be decided as per the bi-lateral agreement between India and Sri Lanka. CPC has planned to modify 16 tanks and to deliver fuel from Trincomalee to the nearby areas which will directly help to reduce the risk of product shortage in the country and a reduction of distribution cost. Once the approval is given CPC to own and operate few tanks, CPC is ready to go ahead with the commencement of the project of pipeline laying and related modifications within few months".

(f) Service Agreement between the CPC and CPSTL

A service agreement between the CPC and CPSTL was not made available, and therefore, a proper understanding of the services provide by each organization has not clearly been defined. Further, the CPC had not properly designed and implemented monitoring policies and procedures, including performance indicators, to ensure the provision of petroleum products in required quality and quantity by the CPSTL.

(g) Stock Review Committee

The Stock Review Committee consisted of members from the CPC, CPSTL, JCT Oil Bank and Lanka Indian Oil Company, Ceylon Electricity Board (CEB) and an officer from the line Ministry and its meetings are held in every week. However, The CPC had not maintained proper records relating to the stock levels, i.e. re-order level, maximum level, minimum level, and re-order quantity etc. in each petroleum product. The order quantity of petroleum products was decided solely based on the Stock Quantity Maintenance Report submitted by the CPSTL and no other document with regard to the maintenance of stocks of petroleum products had been submitted to the Stock Review Committee. However, it was revealed that, since the introduction of SAP system in 2010, the CPC was unable to extract data to produce required stock related reports.

(h) Utilization of Muthurajawela Terminal

Even it had continuously been reported in the previous audit reports, the Muthurajawela Terminal still had not been optimally used in issuing petroleum products. Accordingly, the following benefits had not accrued to the CPC from the investment made.

- Savings port charges
- Shortening lay time of vessels
- Reducing demurrage charges
- Savings delivery costs
- Reducing human resource costs
- Savings delivery loss at the point of discharging of fuel through pipelines
- Reducing traffic congestions in delivering fuel by bowsers.

4.3 Fisheries Coupon System

With the intention of reducing the negative consequences on fisheries industry resulted by revising the fuel prices, the CPC with the collaboration of the Department of Fisheries and Aquatic Resources had initiated a programme to give a fuel subsidy to the owners of the fisheries boats with effect from March 2012. The subsidy coupons had been distributed among the owners of the fisheries boats by the Department of Fisheries and Aquatic Resources, and it had been stopped from September 2013. The CPC had selected dealers to distribute fuel for fisheries coupons and accordingly, the fisheries boat owners had obtained fuel by producing the coupons from that selected regional dealers. The CPC had settled the due amounts to dealers when they submitted such fisheries coupons to the CPC. Accordingly, the amount incurred by the CPC had been reimbursed from the General Treasury through the Department of Fisheries and Aquatic Resources. The following observations are made.

(a) According to the information made available, the amount paid by the CPC up to 31 December 2016, to the dealers with regard to the fisheries coupon programme was Rs. 4,367,320,839 (As at 31 December 2015 was Rs.4, 371,312,889). However, the CPC had reimbursed a sum of Rs.4, 549,775,000 from the General Treasury in three installments.

(b) Although a sum of Rs. 182,454,161 had been excessively reimbursed by the CPC, it was not settled to the General Treasury even to date.

(c) The following deficiencies were observed with regard to the fisheries subsidy distribution process of the CPC.

 (i) Allowable amount of fuel for the fisheries coupons had not been obtained by the fisheries boats owners and instead, they had obtained only the amount of fuel equivalent to the face value of the coupons (subsidy) from dealers.

 (ii) There were instances that the fisheries boats owners had obtained cash from dealers by discounting fuel coupons instead of purchasing fuel, and the dealers had submitted those coupons to the CPC and got reimbursed the total amount of the value of the coupons.

 (iii) There were instances that the amounts over the reimbursable had been credited to the distributors' accounts. According to the test check a sum of Rs. 9,759,350 had been credited to the distributors' accounts over the amount reimbursable as at 31 December 2015. However, a part of such over reimbursements had been settled later.

 (iv) In some instances that the money had been credited to dealers' accounts without obtaining the fisheries coupons and later they had provided coupons to set off such amounts. In one of such instance, a sum of Rs. 24,310,000 had been credited to the distributors' accounts and within a period ranging from 01 to 12 months, the CPC had settled that amount by journal entries using coupons received subsequently.

(d) Instances of selection of unsuitable dealers for distribution of fuel for fisheries coupons had been observed. For instance, a filling station located in Hakmana area, which was 24 km away from the coastal area in Matara, had been selected for distribution of fuel for fisheries coupons.

(e) There was a difference of Rs. 85,878,751 between the actual value of the fisheries coupons issued to the fisheries boats owners and the value of coupons submitted by the dealers to the CPC for settlement.

(f) According to the test check carried out on the amount of fuel bills settled to a dealer, the following deficiencies were observed.

(i) According to the fisheries coupons procedure of the Department of Fisheries and Aquatic Resources, the dealers were not allowed to issue fuel to the fisheries boat owners of other districts. Even though the filling station of the above mentioned dealer had been located in Trincomalee District, he had obtained fisheries coupons from the fisheries boat owners of Mullaitivu and Jaffna Districts at discounted prices (without issuing fuel), and submitted to the CPC for the settlement of fuel bills. Accordingly, fisheries coupons amounting to Rs. 17,508,875 had been submitted to the CPC for settlement but, it had not been settled by the CPC. Further, some other fisheries coupons amounting to Rs. 6,281,250 had been retained by him as at 30 June 2016 because the Corporation had rejected to accept them.

(ii) As per the internal audit investigation conducted in this regard, it was revealed that the CPC had paid a sum of Rs. 2,658,015 to the above dealer on fraudulent coupons presented by him. However, the CPC had not initiated any investigation against the responsible officers in this regard.

4.4 Hedging Transactions

As per the audit examination carried out pertaining to the hedging transactions taken place in respect of procurement of oil during the period of 2007 to 2009, the total loss incurred to the country on those transactions as at 31 December 2016 was Rs. 14,028 million.

The following observations are also made in this regard.

(a) The CPC was cited as a party in the arbitration proceeding pertaining to hedging contracts entered into with several Commercial Banks and a sum of US$ 60 million (Rs. 7,713 million) had been paid to the Standard Chartered Bank (SCB) on 3 June 2013 and a sum of US$ 27 million (Rs.3,881 million) had been paid to the Deutsch Bank AG on 04 August 2016 under the Deed of Settlement entered into between the parties. According to the information made available, the total loss incurred by the CPC as at 31 December 2016 was Rs. 13,641 million.

(b) The Central Bank of Sri Lanka had incurred legal expenses amounting to Rs. 941.2 million on the Hedging Transactions of the CPC and out of that a sum of Rs. 370.6 million had been incurred by the Central Bank of Sri Lanka and a sum of Rs. 567.5 million had been reimbursed to the Central Bank of Sri Lanka by the CPC from the year 2011 to the year 2014. However, an amount of Rs 3.1 million had not been reimbursed as at 31 December 2016**.**

(c) Moreover, the Commercial Bank had filed a case at the Commercial High Court, Colombo against the CPC claiming US$ 8,648,300.

(d) A formal investigation had been initiated against the then DGM (Finance) of the CPC who had sent on compulsory leave since 2008, and his service has been terminated on 04 August 2016. However, no any other investigation had been initiated by the CPC against the persons who were responsible for those transactions.

4.5 Payment of Penalty

As reported in my previous year's audit report, the CPC had paid a sum of Rs. 57,736,913 to the Department of Customs on 20 June 2014 to settle the amount outstanding since 2002 for the purpose of commencing of bunkering operations and on the basis of reimburse that amount from the General Treasury. However, the Department of Customs had identified that this payment was made as a penalty. The following observations are made in this regard.

(a) The amount paid by the CPC had not been reimbursed by the General Treasury or the bunker business even up to the date of this report.

(b) According to the information made available, it was observed that 50 per cent of the above payment or a sum of Rs. 28,868,456 had been shared among the custom officers, and other 20 per cent or a sum of Rs. 11,547,383 had been allocated to the Custom Officers' Welfare Fund.

(c) Even though there was an opportunity to set off that amount since these two institutions are Government institutions, the CPC had not made an appeal in accordance with the provisions in Sections 154 and 165 of the Customs Ordinance.

4.6 Operating Inefficiencies

4.5.1 Refinery Operations

The existing 47 years old refinery, which was commissioned in 1969, is a basic refinery and is not able to cater the increasing demand of petroleum products in the country and this refinery is operating with low margin when compared with refineries operating with advanced technologies including facilities to produce petroleum products at lower cost and capabilities to upgrade bottom products to high value products such as petrol and diesel, whereby maximizing the refinery operating efficiency. However, the CPC was unable to implement the proposed Sapugaskanda Oil Refinery Expansion and Modernization (SOREM) Project in order to ensure the petroleum products are supplied to the market in a cost effective manner. Even though preliminary feasibility study had been completed and the required land (35 acres) had been acquired for this purpose, the CPC was unable to initiate the project yet due to insufficient financial strength to invest for this project. Total cost of the project was estimated at US$ 2.1 billion with a payback period of less than 8 years, and the Net Present Value (NPV) of the project would be US$ 1,535 million. Further, the expenditure incurred by the CPC amounting to Rs. 837 million, which had been included in the assets and capital projects in progress under the property, plant and equipment as at 31 December 2016, was observed as an uneconomic transaction.

4.5.2 Supervision of Filling Stations

Even though the Department of Measurement Units, Standards and Services (MUSSD) and the CPC should take action to seal the dispensing pumps after checking the accuracy of calibration, it had revealed that this task had not been carried out in regular manner. As a result, it was observed in audit that in most of the instances the fuel had been issued to less than required limit of 0.25 through the dispensing pumps.

It was further observed that the supervision of filling stations had not sufficiently been done by the area supervisors i.e. no regular visit to the filling stations by area supervisor for a longer period of time, not taken action to adjust the broken air pump for a longer period of time, not properly monitored the daily sales records and not properly completed the Retail Outlet Inspection Report etc.

4.6 Assets Management

The following assets had been lying idle since the acquisition.

(a) **Halgaha Kumbura Land at Wanathamulla:** This land had been acquired for Rs.10.6 million for the purpose of establishing a LP Gas Project and a Playground. However, this land had not been utilized for the intendant purpose and it had been occupied by more than 700 squatters.

(b) **Mahena Land:** Aaccording to the correspondence made available, the CPC had acquired that land for a sum of Rs. 0.625 million, and it had not been accounted for. However, that land had been utilized by the previous owner even after the acquisition in 1986.

(c) **Investments:** The caring value of the investments made in quoted and unquoted shares of four companies as at 31 December 2016 was Rs. 35.125 million. However, no dividend since longer period had been received to the CPC by the companies. Further the evidence was not available to assure the existence of the International Cooperative Petroleum Association having investment value of Rs. 5 million.

4.7 Resources Released to other Institutions

In contrary to the instructions of the Circulars, particularly, the Public Enterprises Circular No. PED/12 of 02 June 2003 on Public Enterprise Guidelines for Good Governance and the Public Enterprises Circular No.21 of 08 January 2004, and the Letters No. CSA/PI/40 of 04 January 2006 and No. CS/1/17/1 of May 2010 issued by His Excellency the President, the CPC had released the following resources to other institutions and incurred a considerable amount of money for payment of remuneration and other allowances on behalf of released employees and payment of fuel and maintenance expenses for released vehicles. Details are shown below.

	Amount spent by the CPC			Number of Resources Released		
	2016	2015	2014	2016	2015	2014
	Rs.	Rs.	Rs.			
Human Resources	8,531,754	3,452,737	46,261,907	9	11	56
Vehicles	20,613	641,375	3,695,910	2	3	7
Total	**8,552,367**	**4,094,112**	**49,957,817**	**11**	**14**	**63**

4.8 Human Resources Management

The following observations are made.

(a) Filling the Vacancies

Although the approved cadre of the CPC as at 31 December 2016 was 3,284, the vacancies as at that date was 722 or 22 per cent of the approved cadre. Out of those vacancies, 135 posts or 30 per cent was in senior staff level including Deputy General Manager (Technical Services & Corporate Affairs), Deputy Refinery Manger (Maintenance & Projects), Chief Internal Auditor etc. Accordingly, the key positions of Top Management of the CPC were vacant for the period ranging between 7 to 46 months. In addition, the post of the Manager (Secretariat/Secretary to Board) has been vacant since 2012. Therefore, the reason to not taken favorable actions to fill the vacancies in key positions of the top management for longer period is questionable in audit.

(b) Recruitments in 2016

According to the information provided to the Committee on Public Enterprises (COPE) by letter No MPRD/IA/2/6 (i) dated 04 April 2017 with a copy to the Auditor General, it had been mentioned that 98 persons had had been recruited during the year 2016 by CPC even the total recruitments were only 94. Accordingly, seventeen (17) recruitments were not mentioned while twenty one (21) recruitments had been overstated relating to all three Grades in the report submitted to the COPE. Therefore, the accuracy of the information provided to the COPE is doubt to the audit.

(c) Advertising the Notice for Recruitments.

According to the Revision 3 of Criteria and Marking Scheme for Recruitments and Promotions (the Board approved as 01/1163 of 26/05/2015), all internal and external advertisements should be released under functions of Human Resourses Management with the signature of Chairman or Managing Director for Grade A-1 or higher grade vacancies and under the signature of DGM (HR & Admin) or HR Manager for all the other grades of A -2 and below.

The following observations are also made in this regard.

(i) Several vacancies had been advertised in the official website of the CPC contrary to the above Scheme. Further, most of the advertisements published in the website had been uploaded and removed on verbal instructions made directly by then Chairman of the CPC to the Data Analysist (IT Division) without any reference even to the Manager (IT).

(ii) Even though the vacancies were uploaded in the website, those advertisements had not been displayed in the website for reasonable period as enable to seem and applied. It was observed in audit that some advertisements had been displayed in the website for less than three or five hours. Therefore, it had prevented the equal opportunities to apply for suitable citizen of the country to the above posts.

(iii) According to the Newspaper advertisement published on 29 February 2016 in a Sinhala Newspaper, the CPC had made an announcement by stating that all future vacancies of the CPC will be published in the official website of the CPC. However, advertisements for recruitment had been removed from the website before closing date of applications. For example, the advertisement for recruitment of General Labour had been removed on 04 July 2016 although the closing date was 13 July 2016.

(d) Recruitment of Management Assistants (Accounts & Audit)

The CPC had recruited 19 Management Assistants (Accounts & Audit) on 01 January 2017. The following observations are made in this regard.

(i) Those management assistants had been recruited without prior approval of the Department of Management Services (MSD).

(ii) The written examination had not been held as mentioned in the Scheme of Recruitments and Promotions (SORAP) for B 3 Grades.

(iii) Then Chairman of the CPC had informed the Human Resource Manager through Deputy General Manager (HRM & Admin) by his letter dated 02 October 2016, to recruit the candidates to the above post only by holding an interview. However, according to the Gazette Notification No. 1840/34 of 11 December 2013 and SORAP of the CPC, a written examination should be held for the external recruitment to the post of Management Assistants.

(iv) The documentary evidence was not made available for audit in order to ascertain whether five year experience in relevant field of an organization have been obtained or not by the selected candidates as requested by the SORAP of the CPC.

(v) It was observed that, two service certificates from different organizations had been given by an applicant for a particular period. Further, it was not sure that the service letters provided by the candidates had been verified by the CPC.

(vi) According to SORAP, the academic and professional qualifications should be verified from the relevant institutes within first six months after the recruitment. However, it has not been done even up to the date of audit on 30 October 2017.

(e) Recruitment of General Labours

According to the information provided, 6,853 applicants had been applied for the above post and only 156 had been selected to call for interview. However, the basis followed for short listing the candidates was not made available to audit. Further, a written examination had not been held even it had been stated in the advertisement published for recruitment. The Managing Director of the CPC had stated in this regard as follows.

"The CPC had received 6853 applications as at 13.07.2016, the closing date. Since it is not practical to consider such huge applications to fill 18 Nos. of vacancies, as instructed by the former Chairman/ MD, the applications received during the first 4 days which was 156 were considered for the interview since there was no other practical solution."

(f) Training

An approved Foreign Training Policy and Guidelines had not been introduced by the CPC even up to the date of this report. Therefore, it was observed that, the CPC had followed an irregular basis for selection of officers for both local and foreign training programs. According to the letter No. MPRD/ADM/15/02/40(com) dated 29 March 2017 from Ministry of Petroleum Recourses Development (MPRD), there were several issues relating to the foreign training and advised the management of the CPC to rectify those issues.

4.9 Transactions of Contentious Nature

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4.9.1 Fund Transfer to the General Treasury

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As per the request made by the Ministry of Finance, a total sum of Rs. 20,000 million had been paid by the CPC to the General Treasury in 2014 and 2016 by Rs. 10,000 million in each year.

The CPC had been instructed by the Director General of the Department of Public Enterprises by his letter dated 30 December 2014 to charge the above mentioned Rs. 10,000 million paid in 2014 as an expenditure of Rs. 250 million for the year 2014, Rs. 750 million for the year 2015 and Rs. 1,000 million per annum for the period 2016 to 2024. However, without considering the financial impact of the above mentioned accounting treatment, the CPC had fully adhered to the instructions given by the General Treasury.

The secretary to the MPRD had been informed by the Director General of the Department of Public Enterprises by his letter number PE/RE/SP/2016 dated 16 December 2016 to instruct the CPC to remit Rs. 10,000 million to the Consolidated Fund very early to enable the General Treasury to issue Bonds to strengthening the balance sheet of the CPC in 2017 by a similar amount. The way of strengthening the financial position of the CPC as per the proposal of the Treasury by taking off of its cash in a situation of running the business at negative net assets position of Rs. 186 billion would be further deteriorated instead of strengthening the financial position.

After several communications between the CPC and Department of Public Enterprises about the accounting treatment of the above transactions, finally, the CPC had been instructed in October 2017 to treat it as dividend paid to the government from the profit of the year 2016 and also instructed to pay the remaining taxes if any based on the profit of the year 2016 in three years in equal monthly installments.

5 Accountability and Good Governance

5.1 Internal Audit

Internal audits provide important services to the management of any organization. These include detecting and preventing fraud, testing internal controls, and monitoring compliance with organization policy and government regulations. Therefore, internal audit functions provide a vital role in the development of the organization. The following observations are made in this connection.

(a) Out of 42 approved cadres, 09 posts or 21 per cent of the approved cadre were in vacant as at 31 December 2016. Of them 07 posts or 54 per cent was in senior staff level.

(b) Although the Chief Internal Auditor is directly responsible to the Board of the CPC, according to the organization chart available for audit, the Chief Internal Auditor is directly responsible to the Managing Director of the CPC.

(c) Due to above, it was observed that the internal audit functions of the CPC had gradually inactivated since mid of the year 2011.

5.2 Budgetary Control

Significant variances were observed between the budgeted and the actual income and expenditure for the year under review, thus indicating that the budget had not been made use of as an effective instrument of management control.

6. Systems and Controls

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

Major Areas	Observations
(a) Personnel Administration	Failure to get the approval for the Scheme of Recruitment (SOR).
(b) Financial Control	Utilisation of funds for the execution of the main objectives of the Corporation. Utilization of funds for the execution of the main objectives of the Corporation had not been carried out adequately.
(c) Trade and Other Receivables	There were weaknesses in controls over the collection of dues in time and mitigation of the default risk.
(d) Procurement	Complying with the provisions of the National Procurement Guidelines
(d) Utilization of Resources	Complying with the Circular instructions in deploying the resources.
(e) Control over Information Systems	Prevailing opportunities to the officers to access and pass journal entries for previous years in the SAP system in the current year. Hence, the ability to amend other modules too in the SAP systems could not be ruled out in audit. Further, the duplicate customers' accounts had been created in the SAP system. Hence, there is a possibility to damage the internal control mechanism of the CPC and allow to misuse the credit limits, credit period and related controls over the debtors