

**1.1 Disclaimer of Opinion**

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The audit of the financial statements of the Maga Neguma Road Construction Equipment Company (Pvt) Limited (“Company”) for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, 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 provisions of the National Audit Act No. 19 of 2018 and. My comments and observations which I consider should be report to Parliament appear in this report.

I do not express an opinion on the accompanying financial statements of the Company. Because of the significance of the matters discussed in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

**1.2 Basis for Disclaimer of Opinion**

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I do not express an opinion based on the matters described in paragraph 1.5 of this report.

**1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements**

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Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standard and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company’s financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Company.

## 1.4 Audit Scope

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My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company ;
- Whether the Company has performed according to its powers, functions and duties; and
- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

## 1.5 Financial Statements

### 1.5.1 Accounting Deficiencies

Audit Issue -----	Management Comment -----	Recommendation -----
(a) Under the trade payable of the company as at 31 December 2019, debit balances had been shown as advance received from RDA, other trade payable and retention payable amounting to Rs. 45.6 million, Rs. 11.4 million and Rs.5 million respectively. As a result, the company's overall payable balance was understated by Rs. 124 million as at 31 December 2019 and further no action had been taken to clear the balances.	The reconciliation with the RDA will be continuing.	Relevant ledger balances should be arranged enabling to show the real picture of the company from accounts.
(b) Credit balances had been shown under the Certified work bills receivable from the RDA, retention receivable from the RDA, work bills on construction RDA submission and trade debtors amounting to Rs.173.8 million, Rs.345.9 million, Rs.37.86 million and Rs. 43.2 million respectively. As a result, the Company's debtor balance had been understated by Rs. 1201.59 million and no action had been taken to clear the above balances.	Majority of minus balances of Rs.173.81Mn included in the debtor balances which represent the advance received as part payment and which should not offset according to Sri Lanka Accounting Standards. Therefore, action will be taken to report such balances as liability in the financial year 2021. Further Rs.130.62Mn has been settled subsequent to the period ended 31st December 2019. Rs.37.86Mn represents reversal entries of submission 75% against certified bills which should not be considered separately.	Relevant ledger balances should be arranged enabling to show the real picture of the company from accounts.

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| (c) | Out of the trade debtors' balance of Rs.43.2 million a sum of Rs.22.95 million are shown as suspense credit balance.  | Subsequence ledger balances have been updated with respective debtor balances and for long outstanding non-moving balances will be submitted to the board for the necessary actions including suspense balances.    | The balance of any Suspense account which is in the general should be zero at the end of the intendant purpose is fulfilled and no longer should be existed such account in the financial statements.  |
| (d) | A Suspense debtor balance amounting to Rs. 95.5 million had been shown under the trade receivables over a significant period of time without being cleared.   | Various long outstanding balances had been transferred to suspense account on 1 <sup>st</sup> May 2018 intention was to write off. Therefore, information will be submitted to the board for the necessary actions. | The balance of any Suspense account which is in the general should be zero at the end of the intendant purpose is fulfilled and no longer should be existed such account in the financial statements.  |
| (e) | According to the information submitted by the project division of the Company, Interim Payment Certificates amounting to Rs. 202.9 million relating to the work done during the year under review and certified by Road Development Authority in the same year, had not been accounted. As a result, the revenue of the Company year under review had been understated by similar amount.                                   | As practice, the company recognized revenue once certified bills received to the company despite bills submission date. Therefore, these balances have been accounted during the year 2020.                         | Revenue for the year should be recognized correctly as stipulated in the relevant accounting standard rather than how the company is being practiced.  |
| (f) | According to the information submitted by the project division of the Company, Interim Payment Certificates amounting to Rs.2,421.7 million relating to the work done on the basis of subcontracts during the year under review, had not been certified even as at the audited date by the RDA. As a result of delayed in the process of certification the Company had been failed to identify its income in the same year. | As practice, the company recognized revenue once certified bills received to the company despite bills submission date. Therefore, these balances have been accounted during the year 2020.                         | <ul style="list-style-type: none"> <li>• Revenue for the year should be recognized correctly as stipulated in the relevant accounting standard rather than how the company is practicing to recognize revenue.</li> <li>• The company should accelerate its authentication process of Interim payment certificates joined with the RDA.</li> </ul> |

- (g) As per the information submitted by the project division of the Company, interim Payment Certificates amounting to Rs.135.3 million in respect of the year 2018 and the works certified by the Road Development Authority in the same year, had been accounted as income of the year under review.
- This is due to timing difference of bills certified date and bills received date to the company and all 12 certified bills were certified during the month of December 2018 and the company has recognized revenue during the month of January 2019 and similarly this has occurred for the year 2017/2018.
- Revenue for the year should be recognized correctly as stipulated in the relevant accounting standard rather than how the company is being practiced.
- (h) Interim Payment Certificates aggregating to Rs.590.8 million in respect of bills submitted to the RDA in 2016, 2017 and 2018 had been accounted as income of the year under review.
- In practical point of view there is a significant delay in receiving certified bills from the PD offices around the country. Company recognizes revenue from construction works on the date in which certified bills received to the company.
- Revenue for the year should be recognized correctly as stipulated in the relevant accounting standard rather than how the company is practicing to recognize revenue.
  - The company should accelerate its authentication process of Interim payment certificates joined with the RDA.
- (i) Income relating to the bills submitted to the RDA for the year 2017 and 2018 in respect of direct contracts amounting to Rs. 158.7 million, only 75 percent had recognized as an income in respective years and subsequently balance income had been adjusted to current year financial statements without adjusting to the retained earnings.
- Income relating to the direct contract bills amounting to Rs.158,663,672 represents reversal of submission during the year 2019. When submission bill is certified, reversal entry of submission is passed to the system while recognition of certified income in the same year.
- In recognizing 75 percent income out of the amount bills submitted in respect of direct contracts to the respective years and then subsequently balance income should compulsorily be adjusted to the retained earnings.

- (j) According to the financial statements of the Company, the total tax liability was Rs.54.9 million as at 31 December 2019. However, according to the records of Inland Revenue Department it was Rs.49.2 million. Hence, a difference of Rs.5.7 million was observed as at 31 December 2019.
- Differences appearing between the amounts recorded as tax payments in the books of accounts of our company and the amounts provided by IRD as per their records. Since, the breakup of the tax payments from IRD is currently not available, we herewith provide you with an explanation for the balance amounts recorded in the tax payable accounts and the amounts recorded as paid in the company books.
- A mechanism should be established for monitoring closely and continuously for payments in statutory nature like income tax, EPF, ETF and gratuity payments.
- (k) As per paragraph 51 of the Sri Lanka Accounting Standard Property, Plant & equipment (LKAS 16), the useful life of the asset shall be reviewed at least at each financial year end and if expectations differ from previous estimates, the changes shall be accounted in accordance with LKAS 08. However, useful life of the fully depreciated Property, Plant & equipment amounting to Rs.562.3 million still in use had not been reviewed and accounted accordingly.
- According to the relevant accounting standard, management has disclosed the value of fully depreciated assets which are being used in operating activities.
- In case of fully depreciated assets, the company should be reviewed its useful life of such assets as per LKAS 16 or should be accounted as per the LKAS 08 considering its estimate changes.

### 1.5.2 Un reconciled Control Accounts or Records

Item	As per Financial Statements	As per corresponding Record	Difference	Management Comment	Recommendation
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	(Rs. Million)	(Rs. Million)	(Rs. Million)		
(i) Receivable from the Road Development Authority in respect of certified work bills.	1,772.52	751.29	1,021.23	We also noted that intercompany balances are not agreeing each other due to various reasons. Therefore, the management has decided to conduct reconciliation.	Reconciliation should carry out periodically and progress should be reviewed jointly with RDA and measures should be taken accordingly.

(ii) Receivable from the Road Development Authority in respect of certified work bills	1622.6	1712.4	89.8	the reconciliation with the RDA will be continuing	Reconciliation should carry out periodically and progress should be reviewed jointly with RDA and measures should be taken accordingly.
(iii) The balance payable to the Road Development Authority	1,888.32	467.72	1,420.6	the reconciliation with the RDA will be continuing	Reconciliation should carry out periodically and progress should be reviewed jointly with RDA and measures should be taken accordingly.
(iv) Other trade payable to the Ceylon Petroleum Corporation	444.46	120.7	323.76	The process of correcting the relevant values has already begun.	Reconciliation should carry out periodically and progress should be reviewed jointly with Ceylon Petroleum Corporation and measures should be taken accordingly.
(v) Other trade payable to the Provincial Road Development Authority (PRDA) of Western Province	128.9	143	14.1	A comparison of accounts with the Road Development Authority has already begun.	Reconciliation should carry out periodically and progress should be reviewed jointly with Provincial Road Development Authority (PRDA) of Western Province and measures should be taken accordingly.

## 1.6 Accounts Receivable and Payable

### 1.6.1 Receivables

#### Audit Issue

Debtors' balance amounting to Rs.1053.9 million shown in the financial statements of the year under review had remained over 04 years without being recovered.

#### Management Comment

According to the letter Ministry of Finance, Economy and Policy Development Rs. 589,863,423 was agreed to settle through Road Development Authority which were overdue more than five years (already received for 502Mn and deposited on 13th October 2021) and also, we would like to pay your attention to which mention actions which was taken to recover those overdue balances to our Company.

#### Recommendation

Debtor balances which are being over more than 04 years should be recovered without further delay.

## 1.6.2 Payables

Audit Issue -----	Management Comment -----	Recommendation -----
Payable balance amounting to Rs.54.6 million shown under the other payable balance of the financial statement as at 31 December 2019 had remained over five years without being settled.	The same audit query was raised for the audit of 2018 which mentioned that projects had been completed however relevant documents had not been maintained and not presented to the audit purpose by project division. Therefore, information will be submitted to the board for the necessary actions.	Payable balances which are being over more than 05 years should be settled or written back without further delay after getting confirmation of the balances

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

Reference to Laws, Rules Regulations etc. -----	Non-compliance -----	Management Comment -----	Recommendation -----
(i) Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 and the Extraordinary Gazette No. 1074/7 dated 07 April 1999 of the Democratic Socialist Republic of Sri Lanka.	Even though 04 out of the 05 conditions stated in the Gazette, had been satisfied by the Company, the financial statements had been prepared in accordance with Sri Lanka Accounting Standard for Small and Medium Sized-Entities (SLFRS for SMEs) as stated in the note No. 1.2.1 - Statement of Compliance in the financial statements.	An answer was not given by the company.	The company should comply with Sri Lanka accounting standards since four conditions are fulfilled out of five (05) conditions stated in the Gazette No 1074/7 dated 07 April 1999 of the Democratic Socialist Republic of Sri Lanka.
(ii) Section 9.2 of the Public Enterprises Circular No PED 12 dated 02 June 2003.	Action had not been taken to prepare and obtain the approval for the cadre in accordance with the Circular.	An answer was not given by the company.	Action must be taken to follow Public enterprises circular with the consultation of Line ministry and the parent entity or any other administrative framework should be introduced.



## 2. Financial Review

### 2.1 Financial Result

The operating result of the year under review amounted to a profit after tax Rs.46,086,098 million and the corresponding profit after tax in the preceding year amounted to Rs.36,877,319 million. Therefore, an increment amounting to Rs.9, 208,779 million of the financial result was observed. The reasons for the increment were decreasing of finance cost by Rs.6, 676,207 and decreasing of taxation by Rs.50, 666,187 when comparing with the preceding year.

### 2.2 Ratio Analysis

	2019	2018
<b>Current Assets Ratio</b>	<b>1.69</b>	<b>1.81</b>
<b>Quick Ratio</b>	<b>1.32</b>	<b>1.72</b>
<b>Gross profit ratio-percentage</b>	<b>8.06</b>	<b>6.84</b>
<b>Net profit ratio-percentage</b>	<b>1.38</b>	<b>.87</b>

As per the Current Assets Ratio and Quick Assets ratio calculated, it was observed that the company had been maintained within the acceptable range for the year under review and the preceding year.

Gross profit ratio had been increased by 17.84 percent and Net profit ratio also had increased by almost 58.62 Percent. It was observed that the main reason for such increment of the annual profitability was decreasing the finance cost by 39.57 percent and decreasing taxation by Rs.50.67 million compared with the preceding year.

## 3. Operational Review

### 3.1 Idle or underutilized Property, Plant and Equipment

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
(a) The company had not taken actions to dispose or any other suitable arrangement in respect of machineries with a cost of Rs. 46.8 million that are not in usable condition.	As per the guidelines given by the government auditors, management placed a board paper and got the approval for obtaining the service from the recognized private professional valuation firm to revalue company owned plants, motor vehicles and construction machines on 05th March 2021.	The company should take an action without further delay as mentioned in the audit issue.

### 3.2 Defects in Contract Administration

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
(a) A sum of Rs. 662.5 million of mobilization advances received from the RDA had remained without being settled through IPC's over 05 years period as at 31 December 2019.	The reconciliation with the RDA will be continuing and progress report of the reconciliation is attached for your reference.	Mobilization advances received from the RDA should be settled without further delay.
(b) Retention money receivable from the RDA amounting to Rs. 883.9 million had remained over 04 years without being recovered.	As a policy we have made a general provision for long outstanding retention receivable from the RDA.	Retention money receivable from the RDA should be recovered without further delay.
(c) Retention money receivable from the RDA aggregating to Rs. 119.2 million had remained from 02 to 04 years without being recovered.	Accounted for the retention but the company has not recognized retention deduction which should be recorded as retention receivable.	Retention money receivable from the RDA should be recovered without further delay.

## 4. Accountability and Good Governance

### 4.1 Submission of Financial Statements

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
Submission of financial statement of the company had been delayed in nine months from the due date.	No comments	The company should submit its financial statements on due date as prescribe by the national Audit act No.19 of 2018.

### 4.2 Annual Action Plan

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
The Company had not been prepared an Action Plan.	No comments	Annual Action Plan should be prepared and review its progress periodically by the management of the Company.

#### 4.3 Audit Committee

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##### Audit Issue

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Audit and management committee had not been established with correct composition by the company with the concurrent of the line Ministry and the Road Development Authority.

##### Management Comment

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No comments

##### Recommendation

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Audit Committee and management committee should be established with correct composition with the concurrent of the line Ministry and the Road Development Authority.

#### 4.4 Budgetary Control

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##### Audit Issue

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An annual budget had not been prepared by the Company

##### Management Comment

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No comments

##### Recommendation

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Annual Budget should be prepared as a tool of control and reviewed periodically to achieve the objectives of the company.