Northsea Limited – 2020/2021

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Northsea Limited ("Company") for the year ended 31 2021 comprising the statement of financial position as at 31 March 2021 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.My comments and observations which I consider should be report to parliament appear in this report.

In my opinion, except for the effects of the matters described in Paragraph 1.5 of this report the accompanying financial statements give a true and fair view of the financial position of the Company as at 31 March 2021, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Qualified Opinion

My opinion is qualified on the matters described in Paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those Standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

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

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards 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, Managementis 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 intends 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

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 skepticism 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 documentshave been properly and adequately designed from the point of view of the presentationof information to enable a continuous evaluation of the activities of the Company, andwhether such systems, procedures, books, records and other documents are in effectiveoperation;

- Whether the Companyhas complied with applicable written law, or other general or special directions issued by the governing body of the Company.

- Whether the Companyhas 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 Audit Observations on the Preparation of Financial Statements

1.5.1 Internal Control over the Preparation of Financial Statements

Entities are required to "devise and maintain" a system of internal accounting controls sufficient to provide reasonable assurance that , transactions are executed in accordance with Management's general or specific authorization, transactions are recorded as necessary to permit preparation of financial statements in conformity with the applicable reporting Standards, and to maintain accountability for assets, access to assets is permitted only in accordance with Management's general or specific authorization, and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

1.5.2 Non-Compliance with Sri Lanka Accounting Standards

Audit Issue	Management Comments	Recommendation
(a) As per the Paragraph 25 of the Sri Lanka Accounting Standard (LKAS) No.01, when preparing financial statements Management should make and assessment the Company's ability to continue as a going concern. In making its assessments, ifManagement is aware of material uncertainties related to events or conditions that may cast significant doubt upon the entities ability to continue as a going concern, the entity shall disclose those uncertainties. Accordingly, as per the financial statements as at 31 March 2021 of the Company , loss for the year was Rs.79,452,613 and accumulated loss as at the year ended 31 March 2021 was Rs.284,661,904. Further, the Company's net current asset value shows a negative figure of Rs.28,216,315 and total net assets value shows a negative figure of Rs.259,756,538. Even though these uncertainties were cast from the financial statements; it had not been disclosed in the financial statements.	The Company's ability to be a going concern was assessed during the period and it was badly affected by external factors which were common to all concerned island wide. The Government imposed restriction on imports also had a negative consequence on the Company as Company depends heavily on imported raw materials for its production. Since, these factors were common to all and we did not disclose it in the financial statements.	Management should consider the uncertainties at the time of preparing financial statements to comply with the Standard and indicate real situation of the Company to the stakeholders.

(b) As per the Paragraph 51 of LKAS 16 “Property, Plant and Equipment” the residual value and the useful life of an asset shall be reviewed at least at each financial year end and if expectation differ from previous estimate, the change(s) shall be accounted for as a change in an accounting estimate in accordance with LKAS 8 Accounting Policies, Changes in Accounting Estimate and Errors. However, no action had been taken to review the asset as required in respect of fully depreciated assets which were further being used by the Company amounting to Rs. 364,174,483.	The lives of the fully depreciated assets could not be reviewed owing to tight time schedules arising from the Covid 19 pandemic and the resultant intermittent closure of the Company’s three factories and the Head Office. We will endeavour to comply with the Standards in the next year.	If the assets are used even they totally depreciated, they should be revalued considering the useful life time to the entity. As per LKAS, useful life time of every asset should be reviewed annually and depreciable amount should be adjusted accordingly.
(c) As per the Paragraph 69 of LKAS 01, at the time of preparation of financial statements, all the liabilities to be settled during next twelve months, it should be shown as current liability. In contrary to that, the Company had shown the trade and other payables amounting to Rs. 297,454,198 as non-current liabilities in the statement of financial position.	The Creditors amounting to Rs. 50,256,554 relates to the prior years and has been incurred by the previous Management. Hence, these creditors have been stated as non-current liabilities as Company cannot settle them in the next year (within one year). The Cabinet Memorandum is being processed and due for submission to the Cabinet soon as Company cannot afford to pay the VAT and NBT liabilities. Therefore, these have been shown it as non-current liabilities.	As per the Standard,the trade creditors should be shown under current liabilities.
(d) According to Paragraph 39 (a) of LKAS 21 on “assets and liabilities, for each statement of financial position presented shall be translated at the closing rate at the date of that statement of financial position”. However, contrary to that, the Company had not translated the foreign creditor amounting to USD 170,580 at closing rate, hence, financial expenses and total creditors were understated by Rs. 441,802. Further, the Company adjusted the foreign exchange loss to the retained earning	We translated the outstanding to Chidamparam (Pvt) Ltd. of USD 170,580 at the closing rate of USD on the 31st March 2021. The exchange loss will not affect the current cash flow for the period under review and future cash flows as the liability was incurred by the previous Management and hence, the present Management will not be settling it and also is not in a position to do so. Therefore, the exchange loss was charged to	Company should apply standard exchange rate (Published by Central Bank of Sri Lanka) to translate closing balance and all foreignexchange losses to be shown under finance expenses in the statement of comprehensive income to avoid under or overstatement of the bottom line.

instead of showing as finance expenses in the statement ofcomprehensive income. Hence, the total loss for the period was understated by Rs.4,497,350.	retained earnings as per the Paragraph 41 of LKAS 21.

1.5.3 Accounting Deficiencies

Audit Issue	Management Comments	Recommendation
During the year under review the Company had obtained two salary loans aggregating to Rs.28,785,649 and a term loan amounting to Rs. 8,732,989. The Company had not settled these loans on due dates and moratorium was granted by the bank up to 31 March 2021. However, no disclosure had been made in this regard. Further, as per the conditions of the salary loan agreement, monthly interest computed based on Average Weighted Prime Loan Rate (AWPLR) plus one percent rate of interest should be paid and AWPLR plus three percent interest should be paid for Term loan. However, no provision for interest expenses had been made for the year under review. As per the calculation done by the audit, the due interest for salary loan was Rs.1,361,635.	The Company was granted a debt moratorium on the interest and capital payments up to 31st March 2021 for the term loan and the two salary loans obtained by the Company from Bank of Ceylon. They did not provide us with any confirmation or response thereafter. Therefore, the interest and capital payment were not due from September, October 2020 to 31st March 2021. However, the payments were due and will have to be made from April 2021 onwards. We are not accruing interest on the loan of Rs.1,000,000 payable to Paddy Marketing Board since they have not requested the Company to pay interest and capital since inception. The loan was granted to the Jaffna Factory in the year 2006 after its incorporation in June 2001 and is outstanding from the year 2006, but, the Paddy Marketing Board has not demanded the repayment of neither interest on the loan nor the capital. Therefore, we are not accruing for the interest under finance expenses.	Management should point out the correct loan repayment due and the interest expenses at the end of the year to show the correct picture in the financial statements.

1.5.4 Documentary Evidences not made available for Audit

Audit Issue	Management Comments	Recommendation
It was observed that the balance confirmations relating to 13 debtors amounting to Rs. 6,893,156 had not been made available to audit.	The Company has purchased spare parts from Malba (Pvt) Ltd. and they were returned due to incompatible to Company's specifications. But the money which should be received amounting to Rs. 1,234,000 to the Company had not been returned.	Management should introduce a proper internal control over collecting debtor balances and confirming creditor balances. Taking follow up actions and calling annual

	However, we could not obtain balance confirmations from any other debtors mentioned in the Audit Query, even though we have sent the request letters.	confirmations should be included to the internal control system.

1.6 Accounts Receivable

Audit Issue	Management Comments	Recommendation
The total outstanding trade receivables as at the end of the year under review was Rs. 18,582,052. Out of that, debtors aggregating to Rs. 4,257,487 had remained over 3 years without being recovered.	The factories are endeavouring to collect the outstanding debts, except under unavoidable circumstances.	The Management should take immediate steps to collect receivable to avoid any default of payment and becoming bad debt.

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

	Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a)	Company Act No. 7 of 2007, 50(i) Section	Even though the Company had issued shares, share certificates had not been issued to its shareholders until 30June 2022.	As per the decisions taken at the Annual General Meeting, we sent a letter of request to the General Treasury officials to advise on the matter of issuing share certificates, but we did not get any response from them.	Share certificate should be issued to the shareholders
(b)	Company Act No. 7 of 2007, (i) Section 220	Net assets position of the Company as at 31 March 2021 had gone down to negative of Rs.256.76 million and the Management had not taken any step to comply with the requirement of the Act.	The Management was not able to convene an Extra Ordinary General Meeting (EGM) due to the Covid 19 Pandemic and the crisis in the country. We will convene in due course if the country's situation permits.	As per the Section 220 of the Company Act, The Management should callEGM and explain the subject to shareholders with the plan to overcome the problems in the future.
(c)	Chapter 6.5.1 of the Public Enterprises Circular No. PED	The Financial Statement should be rendered to the Auditor General within 60 days after the closure of	The financial statements were compiled and ready to be rendered to the Auditor General within 60	It is responsible of the Management to ensure that financial statement are submitted on due

12 of 02 June 2003	the financial year with copies to the Line Ministry and the Department of Public Enterprises, General Treasury. However, the Company had submitted the financial statements of the year under review on 29 March 2022 by delaying 10 months.	days of the end of the financial year 31st March 2021, but, the Board of Directors did not approve the Accounts until February 2022 due to various problems both internal and external.	date.
(d) National Procurement Agency Circular No.09 dated 01 March 2006.	As per the National Procurement Agency Circular No.09 dated 01 March 2006, a fully owned Government Company should follow the Procurement Guidelines at the time purchasing goods and service to the Company. In contrary to that, the Company had purchased raw material and chemicals amounting to Rs.125,842,484 in 82 occasions without following the Procurement Guidelines.	The Company had purchased the raw materials from the same supplier from the incorporation November 2011 up to January 2017. Current Management also continued to procure from these suppliers in the year 2020/21.	Management should follow the Procurement Guideline at the time of purchasing Goods and Service to the Company.

1.8 Non- compliance with Tax Regulations

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) Value Added Tax (VAT) Act No.14 of 2002	As at the end of the year under review, Value Added Tax amounting Rs.182,799,880 had not been paid by the Company. Further, due to non-payment of VAT on timely basis, the Company have to pay a penalty of Rs.27,963,374.	The company has not paid any penalty for the non-payment of VAT. The Inland Revenue has agreed to waive the penalty on discussion with it in the year 2021/22.	Management should comply with relevant tax law to avoid any unnecessary penalty payments.

(b)	National Building Tax (NBT) Act No.9 of 2009	As at the end of the year under review, National Building Tax amounting Rs. 28,580,611 had not been paid by the Company. Further, due to non-payment of NBT on timely basis, the Company have to pay a penalty of Rs.4,713,899.	The Company has not paid any penalty for the non-payment of NBT. The Inland Revenue has agreed to waive penalty on discussion with it in the year 2021/22.	Management should comply with relevant tax law to avoid any unnecessary penalty payments.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a loss of Rs. 75,334,392 and the corresponding loss in the preceding year amounted to Rs. 101,028,366. Therefore, an improvement amounting to Rs. 25,693,974of the financial result was observed. Being the earning of other income was Rs. 7,308,562, decrease of selling and distribution expenses by 27 per cent, decrease of staff cost such as salaries and wages, other allowance, overtime payments and staff welfare by 5, 36, 20 and 13 per cents as compared to previous year respectively had mainly attributed to this improvement.

2.2 Trend Analysis of major Income and Expenditure items

Item	2020/2021	2019/2020	Increase/(Decrease)	Percentage increase (decrease)
		Rs.	Rs.	%
Revenue				
Gross Turnover	243,062,940	260,508,899	(17,445,959)	(6.70)
Job Work Income / Sundry sales	2,274,495	332,607	1,941,888	583.84
Livelihood Project	-	4,453,409	(4,453,409)	(100.00)
Other Sales	167,246	1,951,905	(1,784,659)	(91.43)
Legal fees	699,000	289,800	409,200	141.20
Directors' Allowances	2,238,000	1,811,456	426,544	23.55
Rent	2,000,000	600,000	1,400,000	233.33

Below mentioned observations are made.

2.2.1 The Gross turnover of the Company for the year under review had decreased by Rs.17,445,959 that is 6.70 per cent as compared with preceding year. Meanwhile, job work income / sundry sales increased by 583 per cent and other sales decreased by 91 per cent during the year under review.

2.2.2 The Company incurred legal fees for cases filed against it by the Inland Revenue Department for the non-payment of VAT liability, pertaining to the years 2011-2015, hence it was increased by 141 per cent.

2.3 Ratio Analysis

The key ratios for the year under review as compared with preceding year are given below.

	31-Mar-21	31-Mar-20
Profitability Ratios		
Gross Profit Ratio	(19.80)	(28.93)
Net Profit Ratio	(30.77)	(42.69)
Return on Capital Employed	(33.92)	(1840.59)
Activity Ratio		
Inventory Day	80	75
Trade Receivable Days	24	21
Trade Payables Day	73	53
Liquidity Ratios		
Current Ratio	0.76:1	0.23 :1
Quick Ratio	0.21:1	0.06:1

Following observations are made.

2.3.1 Profitability Ratio

2.3.1.1 Improvement in the gross profit was observed mainly due to gross revenue increased by 4 percent and the cost of sales decreased by 4 per cent compare to previous year.

2.3.1.2 The net profit ratio also had decreased by 28 per cent due to the same reason mentioned above and gratuity charges, custom duty and travelling & subsistence had been decreased by 26, 60 and 30 per cents respectively.

2.3.1.3 The ratio of return on capital employed shows the earnings which can be distributed between both debt holders and equity holders and the return on capital employed had decreased by 33.92 per cent.

2.3.2 Activity Ratio

2.3.2.1 Trade receivable days had increased in the year 2020/21 from 21 to 24, due the decrease in sales revenue in the year 2020/21.

2.3.2.2 Trade payables days had increased in the year 2020/21to 73 from 53 of 2019/20

2.3.3 Liquidity Ratio

Even though there are improvements in the current and quick assets ratio during the year under review, this is less than the generally accepted ratio of 2:1 and 1:1 respectively.

3. Operational Review

3.1 Management Inefficiencies

Audit Issue	Management Comments	Recommendation
The Company had incurred a sum of Rs.11,247,881 to construct buildings in the land at Weerawila and Jaffna Factories. However, ownership of those lands had not transferred to the name of the Company.	The Weerawila factory building does not belong to Northsea Ltd. Moreover, the Management is in the process of negotiating to secure the ownership of the Jaffna factory land.	Management should take actions to transfer the ownership of the land to the name of Company to avoid any legal issue arise in the future and protect the investment on building and to continue the business in the same premises.