

Lanka Ceramic Corporation - 2020

1. Financial Statements

1.1 Adverse Opinion

The audit of the financial statements of the Lanka Ceramic Corporation for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 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 the Financial Act No. 38 of 1971 . My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, because of the significance of the matters discussed in the basis for Adverse Opinion section of my report, the accompanying financial statements do not give a true and fair view of the financial position of the Corporation as at 31 December 2020 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 Adverse Opinion

Based on the matters described in paragraph 1.4 of this report, I do not express a true and fair view.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuS). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of this report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my adverse 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, management is responsible for assessing the Corporation'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 Corporation or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Corporation's financial reporting process.

As per Section 16 (1) of the National Audit Act No. 19 of 2018, the Corporation 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.

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.
- Obtained 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 Corporation's internal control.
- Evaluated the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Concluded 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 Institute'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. However, future events or conditions may cause to cease to continue as a going concern.
- Evaluated the 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 Corporation and whether such systems, procedures, books, records and other documents are in effective operation;

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

1.5 Financial Statement

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

Non-compliance with Reference to the Standard	Comments of the Management	Recommendation
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<p>(a) A total of medical bonuses, audit fees and tax allocations for the year under review amounted to Rs. 2,122,850 had not been adjusted to the cash flow from operational activities during the year in preparation of the cash flow statement as per the indirect method accordingly, in terms of Section 20 (b) of Sri Lanka Accounting Standards 7. Further, although the actual medical bonus and audit fees incurred with regard to the year amounting to Rs. 355,742 and Rs.2,107 respectively should be adjusted to the profit before taxes under the operational activities, it had not been so adjusted.</p>	<p>Actions will be taken accurately account for in future.</p>	<p>The cash flow statement should be prepared in accordance with the Accounting Standards.</p>

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| <p>(b) When re-valuing items of property, plant and equipment, the class of property, plant and equipment to which those assets belong should be fully re-valued in accordance with Section 36 of the Sri Lanka Accounting Standards No. 16 . Nevertheless, out of 7 lands owned by the Corporation totalled to Rs. 172,275,704, only 02 lands had been brought to accounts to a revaluation amount of Rs. 165,422,500 and balanced 5 lands had been accounted for at the cost of Rs. 6,693,204.</p> | <p>Two factories were re-valued for lease to a suitable investor and land re-valuing activities of all the remaining factories owned by the Corporation will be carried out when the financial condition of the institution is good.</p> | <p>The class of property plant and equipment to which the assets belong should be fully re-valued at the revaluation.</p> |
| <p>(c) Although a revaluation is required on changes in the fair value of property plant and equipment items in accordance with Section 34 of the 16 Sri Lanka Accounting Standards, arrangements had not been made to revalue and account for the fair value of lands purchased in 1972 and 1984 respectively in extent of 243 acres 30.1 perches at Eragama and Bingiriya valued at Rs. 191,603 and 11 vehicles currently in use but completely depreciated cost at Rs.6,413,555.</p> | <p>Lands at Eragama and Bingiriya factories will also be re-valued respectively when the financial position improves.</p> | <p>Actions should be taken to revalue the assets and to account for at the fair value.</p> |
| <p>(d) Although the Government Grants should not be identified as the equity and should be identified as profit or loss on a systematic basis in accordance with Sri Lanka Accounting Standards No. 20, the grant received from the Ministry amounted to Rs. 1,000,000 had been accounted for</p> | <p>Actions will be taken to obtain instructions in this regard and to account for accurately.</p> | <p>It should be corrected in the preparation of financial statements 2021 .</p> |

as reserves before 2017.

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| (e) Details of transactions with related parties had not been disclosed in the financial statements in accordance with Sri Lanka Accounting Standards No. 24 . | Actions will be taken to disclose the transactions with related parties in the financial statement in future. | It should be disclosed in the preparation of financial statements 2021 . |
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1.5.3 Accounting Policies

----- Audit Observation -----	----- Comments of the Management -----	----- Recommendation -----
Provisions had not been made for the debtor balance of Rs.9,904,684 for more than 5 years in accordance with Paragraph 32 of Sri Lanka Accounting Standards No. 8 and the Corporation had not introduced an accounting policy for this purpose.	Arrangements will be made to make a provision in the next financial year for the debtor balances for more than 05 years.	It should introduce an accounting policy and make relevant provisions in the financial statements.

1.5.4 Accounting Deficiencies

----- Audit Observation -----	----- Comments of the Management -----	----- Recommendation -----
(a) In valuing the finished stock as at 31 December 2020, it had been calculated based on the unit cost for the year 2018. As a result, it was observed that the finished stock in hand amounted to Rs. 27,270,948 was not accurate.	The computation of stock of finished goods produced has been carried out at the cost and that price was given by the Production and Marketing Division.	Stock in hand of the relevant year should be calculated at the production cost of that year.
(b) Due to non-provision of depreciation in the year under review for buildings and machinery which were re-valued in the year 2019 at a Rs.8,300,000, the depreciation expenses had been understated	Actions will be taken to correct the depreciation which was calculated in less as shown by the audit.	The relevant corrections should be made in the financial statements 2021 .

by Rs. 329,500 and the balance of assets had been overstated by that amount.

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| <p>(c) Although the gratuity amounting to Rs. 180,753 allocated during the year with regard to the Head Office should be credited to the gratuity provision account, the balance of provision had been understated by Rs.361,406 as a result of being recorded as a debit balance and the gratuity expenditure for the year had been taken into accounts as a revenue of Rs. 108,254 .</p> | <p>The accounts have been mistakenly changed and accounted for .</p> | <p>The relevant debit or credit note should be applied accurately when accounting for expenses.</p> |
| <p>(d) The expenditures totalled to Rs.299,838 had been understated in accounts as at 31 December 2020 .</p> | <p>The accounts have been mistakenly changed in accounting for. It is ensured that, this will not happen in future.</p> | <p>The relevant debit or credit note should be accurately applied when accounting for expenses.</p> |
| <p>(e) Even though the electricity expenditure payable with regard to the Eragama Factory for the month of December in the year under review amounting to Rs. 233,634 should be debited to the electricity expenditure account and credited to the provision account, as a result of debited and credited to the electricity expenditure account, the expenditure and the provision had been understated by the same amount.</p> | <p>The accounts have been mistakenly changed in accounting for and it is ensured that, this will not happen in future.</p> | <p>The relevant debit or credit note should be accurately applied when accounting for expenses.</p> |
| <p>(f) Due to the record of factory maintenance costs and excavator rental costs that contribute to production, as institutional and administrative costs, the gross profit of the Corporation had decreased by Rs. 1,979,157.</p> | <p>Actions will be taken in future as per the observation in the audit query .</p> | <p>The expenditure classifications should be accurately stated in the financial statements .</p> |

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| <p>(g) Non-manufacturing administrative expenses of 5 factories where no production or sale took place during the year amounting to Rs. 1,267,927 had been reduced as a cost of sales when calculating gross profit. Accordingly, the cost of goods had been overstated and the institutional and administrative costs had been understated in the financial statements by 31 December 2020 .</p> | <p>Actions will be taken as per the observation in the audit query in future.</p> | <p>Non-productive administrative costs in factories should have been noted as institutional and administrative expenses in the revenue statement .</p> |
| <p>(h) As a result of failure to indicate the unit cost of 3,748 units and the total cost related to it pertaining to 521 items of stationery and machine parts according to the Board of Survey Reports of Bingiriya, Bangadeniya, Alayapattuwa, Eragama, Weuda and Yatiyana factories in the year 2020, the aforesaid stock value had not been accounted for in the final account.</p> | <p>Since these goods were the goods sent under internally exchange system to the each factories from the factories where they were used and closed, the unit prices of them were not specified.</p> | <p>The value should be assessed and included in the stock.</p> |
| <p>(i) Although the total value of the audit fees payable to the National Audit Office for the period from 2004 to 2019 should be Rs. 3,623,172, due to the total allocation made for the audit fees payable in the financial statements for the year under review was Rs. 3,046,003, the provision for audit fees totalled to Rs. 577,169 had been made in less.</p> | <p>Actions should be taken to check and take action to correct the cash account payable to the audit office.</p> | <p>The amount to be paid should be properly accounted for.</p> |
| <p>(j) Increase in advances mentioned under working capital changes under operational activities of the cash flow statement, deposits and prepaids amounting to</p> | <p>Actions will be taken to make accurate adjustments in future.</p> | <p>The cash flow statement should be prepared according to the standard.</p> |

Rs. 373,257 and the decline in payments for trade and other creditors amounting to Rs. 169,994 had not been shown.

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| (k) | Instead of the allocation for the year amounted to Rs.448,018 with regard to gratuity allocations, the total allocation of Rs.14,474,881 had been adjusted to the operational activities of the cash flow statement . | Actions will be taken to adjust accurately in future and to check the relevant difference and adjust accordingly. | Accurate numbers should be used in preparing financial statements. |
| (l) | Although the cash balance as at 31 December 2019 was Rs. 4,954,894, the figure had been noted as Rs. 5,043,834 as at 01 January 2020, in preparing the cash flow statement. | Arrangements will be made obtaining instructions to prepare the cash flow statement accurately. | Accurate numbers should be used in preparing financial statements. |

1.6 Payables

Audit Observation	Comments of the Management	Recommendation
(a) Actions had not been taken to settle the balance of Rs.33,805,882 remaining prior to the year 2015 and there were unidentified balances of Rs. 1,435,955 within this balance.	Answers have not been given.	Actions should be taken to settle the loan balances and to identify the undisclosed values and correct the accounts.
(b) Retained amount of Rs. 507,091 with regard to Head Office and Mahiyanganaya Factories had not been settled until the date of the audit.	Answers have not been given.	Actions should be taken to settle the balance payable.
(c) The advance received on sale of products in the year 2011 from the State Resources Management Corporation of Sri Lanka had been Rs. 13,254,533. Although this institution is not currently in operational level,	This is an amount that has been bringing forward for years and arrangements will be made in future to correct it obtaining approval by referring	Actions should be taken as per the answer given.

actions had not been taken so far to settle this balance. to the Board of Directors.

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

Reference to Laws, Rules and Regulations	Non-compliance	Comments of the Management	Recommendation
(a) Financial Regulation 571	Tender deposits remaining before the year 2015 was Rs. 510,324 and actions had not been taken to collect the revenue by making inquiries regarding those deposits. An unidentified balance of Rs. 235,224 had also included within this balance.	Answers have not been given.	Actions should be taken in terms of Financial Regulation.
(b) Section 13.2 of the Public Finance Circular No. 01/2020 dated 28 August 2020	Actions had not been taken in respect of 11 vehicles of the Corporation which were removed from use and to be disposed in terms of the Circular.	Arrangements are being made on vehicles that should be disposed of.	Disposals should be carried out and the work should be completed.
(c) Paragraph 9, Part II of the Ministry of Finance Circular No. 2020/1 dated 28 August 2020	Actions had not been taken by the officers who were responsible to keep securities on the custody of the cash of the Corporation.	Securities had not been kept because the staff has not been properly appointed after the voluntary compensation scheme 2012.	Actions should be taken in terms of Circular.
(d) Financial Regulation 756(6) and Paragraph 11.3 of Ministry of Finance Circular No. 2020/1 of 28 August 2020	A Board of Survey for the year 2020 had not been conducted with relevance to 9 factories owned by the Corporation.	Actions will be taken in the future to conduct a Board of Survey.	An Annual Board of Survey should be conducted in accordance with the Circular.

- (e) Sections 9.2 (a), 9.2 (b) and (d) of Public Enterprises Circular No. PED 12 dated 02 June 2003. The activities such as identifying staff requirements, obtaining approval for the staff, and prepare an organizational plan had not been carried out even by the year under review. This institution was run after 03 March 2012 under a competent authority and that the institution is run with a view to providing one factory or all factories with a suitable investor as per the Cabinet Decision. Actions should be taken in accordance with the provisions of this Circular.
- (f) Management Services Circular No. 2016/02 dated 25 April 2016. Due to the inability to obtain the approval of the Department of Management Services for the staff of the Corporation, although the salary codes have been issued for each post as per the Circular, a sum of Rs. 16,173,408 had been paid to 34 of permanent staff annually as the gross salary in contrary to the Circular based on the salary before the salary conversion 2016 without doing a salary revision whatsoever. Necessary steps are being taken at the required level to obtain the approval of the Department of Management Services. Salaries should be revised as per the Circular of the Department of Management Services

1.8 Non-compliance with Tax Regulations

Audit Observation	Comments of the Management	Recommendation
Even though the balances of 8 types of taxes to be paid to the Inland Revenue Department as Business Tax, Defence Tax, Nations Building Tax, Value Added Tax, Goods and Services Tax, Retention Tax, Economic Service Tax and Income Tax was Rs. 173,769,640 as per the financial statements as at 31 December 2020, since the balance receivable from the Corporation as per the records of that Department was	A letter has been sent on 05.02.2021 as to inform us of the actual balances from this tax balance as per the documents of the Inland Revenue Department. Nevertheless, there was no answer to that letter until today and we will go to that institution in future to check and correct it.	The balances with changes should be discussed and settled with the Inland Revenue Department.

Rs.151,431.418 , a difference of Rs.22,338,222 had remained. The Corporation had not taken action to settle these balances and the tax balance payable amounted to Rs. 22,338,222 had been overstated in the financial statements.

2. Financial Review

2.1 Financial Results

The operational result for the year under review was a surplus of Rs. 1,606,181 and the deficit as against the preceding year was Rs. 5,122,202 . Accordingly, a growth of Rs. 6,728,383 was observed in the financial result. The decrease in administrative expenses and the increase in other revenue had mainly caused to this growth.

3. Operating Review

3.1 Management Inefficiencies

	Audit Observation -----	Comments of the Management -----	Recommendation -----
(a)	The ownership of 134 acres Rood 15 perches 217.2 acres relevant to 07 factories owned by the Corporation had not yet been taken over by the Corporation at the time of the audit.	The land in Eragama Factory is a land transferred to the Corporation by a gazette notification.	Arrangements should be made to take possession of the lands in writing.
(b)	Six cases had been filed for and against the Corporation on the reasons such as the use of lands belonging to the Corporation by external parties, make retirement of employees and supply of damaged tiles. The information in this regard had not been disclosed in the financial statements and even though the time of the case filed had ranged from 2007 to 2019, the Corporation had failed to settle so far.	The Attorney General's Department attends this and the reasons such as the change of lawyers from time to time and the inability to hand over the summons to the respondent, this affects the long period of hearing of cases.	The information about the case should be disclosed in the financial statements and it should try to settle cases that have been remaining for a long time.

3.2 Operational Activities

Audit Observation	Comments of the Management	Recommendation
<p>(a) The approval had been given by the Decision of the Cabinet of Ministers No. 20/0989 / 224 / 002-1 dated 09 July 2020 to resume operations of Oddusudan Factory under the control of Corporation. Although a sum of Rs. 3,275,129 had been spent to commence this factory during the year 2020, the Corporation had not been able to start production in the factory until May 2021. An assessment in respect of the fixed assets including land owned by the factory had also not been obtained by now.</p>	<p>The Oddusudan factory has been completed about 60 per cent of the maintenance required to commence production and has also obtained electricity and the money spent has been used for that and spent on employee salaries and it is stipulated to begin further maintenance after the covid situation in the country quelling down and actions will be taken to complete these activities and to obtain assessments regarding the lands and fixed assets in future.</p>	<p>The productions of Oddusudan Factory should be commenced without delay.</p>
<p>(b) Although the production activities whatsoever was not done at Bangadeniya, Weuda, Illeyapattu and Bingiriya factories, a sum of Rs. 2,650,837 had been spent on administrative and overhead expenses . Even though the land, buildings and machinery of the Weuda, Bangadeniya factories had been valued at Rs. 173,722,500 in 2019, the Corporation had not taken steps to make an effective investment.</p>	<p>The Investors had joined to inspect the factories to launch new projects at Weuda, Alayapattuwa and Bangadeniya factories and there has been a delay due to the situation in the country and the necessary steps will be taken to provide new projects for the new investors and when the situation improves and until then, administrative and overhead expenses has to be borne for the safety of the factories.</p>	<p>Measures should be taken as minimized the cost of functioning of factories.</p>

4. Accountability and Good Governance

4.1 Tabling of Annual Reports in Parliament

Audit Observation	Comments of the Management	Recommendation
<p>Even though the annual reports with the audited accounts should be tabled in Parliament in trilingual within 150 days of the end of the financial year in terms of Section 6.5.3 of the Public Enterprise Circular No. PED 12 of 02 June 2003, actions had not been taken to table the Annual Reports in Parliament from the year 2010 to 2018.</p>	<p>Annual reports from the year 2010 to 2015 have been submitted to the Ministry and the reports from 2016 to 2019 are being prepared.</p>	<p>The reports should be tabled in Parliament as per this circular.</p>