Kahatagaha Graphite Lanka Limited - 2023/2024

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1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Kahatagaha Graphite Lanka Limited for the year ended 31 March 2024 comprising the statement of financial position as at 31 March 2024 and the statement of financial performance, statement of changes in equity and cash flow statement for the year then ended and notes to the financial statements, including information about the 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 reported 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 2024 and its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards for Small and Medium Enterprises.

1.2 Basis for Qualified Opinion

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

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibility for the financial statements is further described in the Auditor's Responsibilities Section. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my 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 Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern of the Company 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 sub 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 Auditor's Responsibility on the Audit of Financial Statements

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 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 has performed according to its powers, functions and duties,

- 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 Comments on the Preparation of Financial Statements

1.5.1 Non-compliance with Sri Lanka Accounting Standards for Small and Medium Enterprises

	Audit Observation	Comments of the Management	Recommendation
(a)	Two cases pending against the company at the Kurunegala Labor Tribunal and one case pending at the Colombo Labor Tribunal Authority as at the end of the year under review had not been disclosed in the financial statements in accordance with Sri Lanka Accounting Standards for Small and Medium Enterprises 21.15.	The two cases pending against the company in the Kurunegala Labor Tribunal by the end of the year under review have been disclosed under Accounting Note No. 8. The management has decided to submit the information regarding the case pending before the Colombo Labor Tribunal in the further accounting reports.	According to the standard, information related to cases should be disclosed in the financial statements.
(b)	According to accounting policy No. 3:1:2 of the company, interest income was recognized on a cash basis, but that income was recognized on an accrual basis.	Interest income has been accounted on an accrual basis on the advice of the Auditors in previous year. But it has not been possible to revise the accounting notes due to an omission.	The followed accounting policy should be accurately disclosed in the financial statements.
(c)	According to section 73 of Sri Lanka Accounting Standard No. 16, it had not revealed by the financial statements that the opening balance of the year, additions during the year, removals during the year and the balance at the end of the year of the mature coconut crop which has been carried out over an area of 27 acres belonging to the Kahatagaha mine, which is taken under the property processing equipment.	The mature coconut crop that has been carried out over an area of 27 acres belonging to the Kahatagaha mine has been accounted in accordance with Sri Lanka Accounting Standard No. 41. Removals during the year and additions during the year were not recorded. This information is given Accounting Note No. 20.	According to the accounting standard, a reconciliation statement should be submitted with mentioning the opening balance of the year of cultivation, additions during the year, removals during the year and the balance at the end of the year should be submitted.

(d)	As per paragraph 45 of Sri Lanka Accounting Standard No. 41, the coconut crop of the company, which was been carried out even an area of 27 acres belonging to the Kahatagaha mine, was not recognized separately as mature and immature in the financial statement. Accordingly, the cost incurred for the immature coconut crop was capitalized according to the standard and the value of the mature coconut trees in the coconut crop was assessed at cost or fair value and it was not accounted according to Sri Lanka Accounting Standard No. 41.	The coconut crop accounted under above (e) is currently a mature coconut crop and as the coconut cracking has started, the capital cost has been cut off (depreciated) over the period of expected economic benefits.	According to the accounting standard, mature and immature crops should be capitalized and valued at cost or fair value and accounted.
(e)	According to Note No. 3.6 of the financial statements, the Weighted Average Price method was used in valuation the graphite stock and the Weighted Average Price of one metric ton of graphite was Rs.231,675. Although due to absorption of the Value of normal waste into the stock, the final stock of graphite was valued at Rs.256,916 per metric ton. Due to this, as the value of the graphite stock which was 1,195.67 metric ton was overvalued by Rs.30,179,906, the profit and current assets of the year were overstated by that value.	Normal waste identified from physical stock survey work is absorbed by good one and abnormal waste is deducted from the accounts as stated by the Auditors. Accordingly, as stated by the accounts, the stock and profit have not been overstated.	The cost of normal waste should not be included in to the closing stock, but it should be absorbed into the cost related to the sold units.

1.5.2 Accounting Deficiencies

	Audit Observation	Comments of the Management	Recommendation
(a)	Due to that the repair expenditure of machinery and equipment of Rs.454,250 incurred in the year under review has been capitalized as a capital expenditure, the profit of the year under review was overstated by Rs.454,250.	The expenditure of Rs.135,000 spent on completely wrapping and repairing the 22 KW water motor and Rs.319,250 spent on repairing two other water motors with completely new motors have been accounted as capital expenditure according to Sri Lanka Accounting Standard No. 16.	Repair expenditures should be accounted as expenses.
(b)	The net loss of Rs.748,547 generated in the year under review from the cultivation of coconut, banana and other crops maintained on the land owned by the company was set off from other income and mentioned in the financial statements instead of being mentioned in separate financial statements.	The basic function of the company is the mining industry and the mining site should be maintained for the needs of mining and other activities. The various income generated by this are classified under other income and when preparing the financial statements, the balances of the various income accounts are indicated separately and finally indicated as only a total.	Income and expenses should be identified separately without set off.

(c)	Since the information required to confirm the balance of Rs. 6,408,798 stated as tax on the value added receivable was not submitted to the audit, it was not possible to verify the correctness of that balance.	The tax value is Rs.6,408,798 in the accounts as at 31 March 2024 and it has been requested through the monthly tax returns from the Inland Revenue Department. Only verified debit VAT payments can be set off against the tax payable and any VAT rejected during the VAT audit from time to time will be recorded in the VAT claim accounts. Now, the Inland Revenue Department has started the VAT audit and it has been conducting VAT audits in several months.	The information required to confirm the balance should be submitted to the audit.
(d)	The stock value of consumer goods was Rs.16,463,063 at the end of the year under review in the financial statements and a difference of Rs.484,693 was observed from the value of Rs.15,978,370 according to the physical stock verification report.	The reason for the difference mentioned by the Auditors is the value of the consumable goods stock which was not included in the physical stock survey reports.	The closing stock should be calculated correctly.
(e)	According to the documents at the end of the year under review, although the value related to th stock of graphite which was 1,195.67 metric ton is mentioned as Rs.307,187,042, when valuing the stock, the value of 130.27 metric ton of average waste identified was added to the closing graphite stock instead of being included in the coast of sales of the year and deducted against the gross profit of the year under review.	The company issue the stock on FIFO basis and follow Weighted Average Cost method for stock valuation. Accordingly, the coast of normal waste is automatically taken into account during the issuance of stock.	The cost of normal waste should be included in the cost of sold units.
(f)	When calculating the income tax expense of the year under review, the taxable profit was understated by that amount due to the deduction of gratuity allocation of Rs.3,490,932 against the profit of the year twice.As a result, the income tax allocation for the year under review was also understated by Rs.977,461.	According to the provisions of the Inland Revenue Act, while calculating the gross income tax, the gratuity allocations have been deducted twice and the tax calculations have been made. However, when the audit is completed, the last tax payer will be recalculated and if there is any double counting error as indicated by the Auditors, it is expected to be corrected.	The correct tax liability should be reflected in the financial statements.

1.6 Payable Accounts

1.6.1 Payable Money

Audit Observation	Comments of the Management	Recommendation
Audit fees of Rs.1,313,434 and tax liability of Rs.185,294 under accrued expenses were mentioned in the financial statements as unpaid balances from the period of 2 years.	Due to severe financial difficulties, it is not possible to settle the accrued audit fees. Management has decided to settle these payments as soon as possible. But the nation building tax liabilities mentioned here are in a condition where they can apply for tax exemptions to the Inland Revenue Commissioner. It is hoped that this work will be done in future.	Action should be taken to settle the liabilities on the due date.

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

	Reference to Laws, Rules and Regulations	Non-compliance	Comments of the Management	Recommendation
(a)	Sections 2 and 94 of Chapter I of Inland revenue Act No. 24 of 2017	Although tax returns should be submitted to the Commissioner General of inland Revenue not later than eight months after the end of each assessment year, the company had not submitted tax returns for the assessment years 2021/2022 and 2022/2023 or paid tax quarterly in the year under review.	The observation is accepted and due to various reasons, the submission of the said accounts to the tax preparation institute was delayed due to the delay in the audit of the final accounts. However, currently the 2021/22 and 2022/23 audited accounts have been submitted to the tax preparation institute and due to the financial difficulties faced by the institute, it was not possible to pay the quarterly taxes.	According to the tax Act, tax returns should be submitted within the relevant period.
(b)	Operational Manual on Corporate Governance for Government-owned businesses introduced by Public Enterprises Circular No. 01/2021 dated 16 November 2021			
	(i) Paragraph 6.6	Although the draft annual report and financial statements should be	Due to current staff problems, it was not possible to prepare and submit the accounts on	Action should be taken as per circular provisions.

		submitted to the Auditor General within 60 days of the end of the accounting year, the draft annual report of the company for the 2023/2024 accounting year had not been submitted for audit until the audited date.	time. However, the 2023/24 accounts have been prepared and submitted for audit in later.	
(ii)	Paragraph 6.7	The company had not verified the fixed assets and submitted the relevant reports to the audit by the audited date of 10 September 2024.	This has been delayed due to issues of the staff.	Physical verification reports should be submitted as per circular provisions.

2. Financial Review

2.1 Financial Results

The operating result of the year under review was a profit of Rs.28, 262,020 and the profit of the last year was Rs.57,110,521 in correspondence to that. Accordingly, a deterioration of Rs.28,848,501 was observed in the financial result. The decrease in the revenue of sales was mainly affected for this deterioration.

3. Operational Review

3.1 Identified Damages

Audit Observation	Comments of the Management	Recommendation
The company had paid a surcharge of Rs.447,754 during the year under review due to non-payment of electricity expenses on the due date.	Due to severe financial difficulties in the company, these surcharges have arisen due to non-payment of electricity bills from time to time.	Expenses should be settled on the due date.

3.2 Management Inefficiencies

	Audit Observation	Comments of the Management	Recommendation
(a)	The company which was operating under different ownerships since the year 1972 and established as Kahatagaha Graphite Lanka Company in the year 1992 had installed a mine shaft only up to the 1,130 feet level and graphite mining is being done at the 2,000 feet level now. The need for a 2nd mine shaft (2nd Shaft) needed to access a level of 1130 feet to 2000 feet has existed from many years, but the necessary work for that has not been done.	Due to financial difficulties in the company, the excavation work in the second phase has been delayed. This work was planned and started earlier, but due to financial difficulties and shortage of officers with subject knowledge, it was stopped on the way.	Action should be taken to expand operations as per plan.

(b)	When comparing the graphite export quantity and revenue in the year under review and last year, the export quantity had decreased by 23.5 percent and the export income had decreased by 28 percent or Rs.50,962,878.	Sri Lanka is the only supplier of natural static graphite in the world and the Kahatagaha and Bogala mines are its main suppliers. Currently, there are only a few buyers for natural static graphite in the world and Sri Lanka's supply in the world market is less than 1 percent. The company also plans to find new buyers by increasing the added value of graphite. But the actual sales orders were received only from S. Kato Company, Japan with the assumed sales volume based on the customers who were preparing the action plan of the company and their past activities and it is also less than expected. During this period, as the Auditors' said, due to the old customers of the company refrained from giving sales orders and could not find new buyers, the quantity and value of graphite exports decreased in the transition year compared to the previous year.	Export revenue should be increased through access to new markets.
(c)	Out of the total graphite sales revenue of Rs.128,558,961 of the company in the year 2023/2024, Rs.103,708,458 was foreign sales and Rs.24,850,503 were domestic sales. As per the decisions get by the Price Committee of the company held on 11 September 2023, although 1 metric ton of 97-99 percent graphite (lump+10 mm) is fixed to sell at the price of $ 2,400, but on 2 October 2023 the company had sold 40 metric ton of graphite to Bogala Graphite Company at $ 1,600 per ton for an amount of Rs.20,768,126. Due to this, the company had lost an income of Rs.10,384,000 through that transaction.	The Price Committee meeting held on 11.09.2023 has approved the sale of 01 metric ton of carbon 97-99 type graphite to Bogala graphite at USD 1,600 each with considering the financial difficulties and minimum sales orders of the company.	Action should be taken to minimize the losses on the decided price by the Price Committee.
(d)	Cases were filed against the company in the years 2004 and 2007 respectively by outsiders claiming rights over 26.5 acres and two plots of 6 acres of land belonging to the Kahatagaha graphite. However, the proceedings were not settled by the audited date of 26 September 2024.	There is a legal case Nos. P 5745 and P 6070 in the Kurunegala District Court against the company regarding a dispute of 26 acres land. The plaintiff is A.A. Somasiril.	The property owned by the company should be settled.

3.3 Operational Inefficiencies

	Audit Observation	Comments of the Management	Recommendation
(a)	Although the company had planned to mine high carbon graphite and increase the monthly product to 80 Metric Tons, the company had failed to reach the expected production targets due to the monthly average production was 44 Metric Tons and the total production was 530 Metric Tons in the year under review.	One of the reasons for the decline in production is the start of exploration for new graphite deposits, which had been stopped for a long time due to the decrease in graphite sales and the employment of workers in underground development work. Production was also affected by labor shortages during this year as many skilled workers retired, some workers left from the service and those were not replaced. Also, production activities were stalled due to heavy rain, many graphite rich workplaces were flooded due to ground water flooding and the limited number of employees was employed in removing the ground water. Natural graphite deposits are naturally located in different ways and graphite exploration and mine development should be done simultaneously and the location of the deposits is often impossible to accurately predict. Accordingly, it was observed that the graphite mining activities could not reach the desired level.	Should be made practical plans and act accordingly.
(b)	According to the letter of the Secretary to the Ministry of Policy Planning and Implementation dated 15 October 2003, it was decided in the Director Board meeting held on 16 October 2003 to provide the necessary space for the Dodamgaslanda Youth Crops training canter from the land belonging to the Kahatagaha mine. Accordingly, although the land had been released for a period of 03 years from the year 2003, the land is being used for the training canter without entering into a lease agreement or paying rent even though the period has exceeded 19 years until the audited date.	Accept the audit observation and the management has decided to act in future about the land given for the Dodamgaslanda Youth Corps training center and the arrears of its tax revenue.	Action should also be taken to enter into a lease agreement and collect the arrears of rent.

(c)	The basic work of the second shaft from the first 1,130 feet level to the 2,000 feet level of the mine was started a few years ago for the purpose of underground development and even though an allocation of Rs. 8 million was made in the year under review, further work related to it had not been done.	Due to severe financial crisis faced by the institute, the excavation work of the second shaft in the underground could not be started as planned.	Action should be taken to expand operations as per the plan.
(d)	The jeep of the company, which had been removed from use since the year 2006, was parked idle in the company premises without any repairs or disposal.	The jeep bearing No. 31 Sri 415 is currently fully depreciated and management has decided to repair and use this idle vehicle. But, this work has been delayed due to financial difficulties.	Assets should be repaired and used or disposed immediately.
(e)	Although the laboratory of the company was established with the objective of carrying out value addition processes for graphite mineral, the related work had not been done there and only the measurement of the percentage of carbon contained in the graphite samples prepared for export had been done there. The company had only exported graphite in the form of flakes (Flake-97 percent and 99 percent carbon) and chips (Chips-90 percent and 92 percent carbon) until now and value-added finished or semi-finished products were not produced.	Due to the resignation of skilled employees and the decrease in sales revenue during this year, it was not possible to identify new graphite products and access to product development and value addition activities.	Action should be taken to initiate value addition processes for graphite.

3.4 Human Resource Management

Audit Observation	Comments of the Management	Recommendation
Although 60 workers were to be hired on contract basis, 75 workers were actually hired. As a result, it was observed the excess of 15 labors.	The staff of 79 employees was approved on contract basis by the Management Services Department with considering the situation in the year 2007 when the mine that was closed in the year 2006 was restarted and production started. But as hiring new employees is a mandatory and essential task in the improvement of the mine and necessary to recruit new employees based on the existing needs in maintaining the mine, the management has worked to expand the number of employees and the new staff has been prepared and submitted to the Management Services Department for approval.	Arrangements should be made to hire the approved staff.

4. Accountability and Good Governance

4.1 Annual Action Plan and Performance

Audit Observation	Comments of the Management	Recommendation
According to the action plan of the company, it was expected to sell 647 Metric Ton of graphite annually, but only 264 Metric Tons had been sold in the year under review. That was 57 percent below than expected sales. Also, the company had not taken advantage of the competition during this period and 220 out of the 264 Metric Ton of sold graphite was sold to one foreign buyer.	Sri Lanka is the only supplier of natural static graphite in the world and the Kahatagaha and Bogala mines are its main suppliers. Currently, there are only a few buyers for natural static graphite in the world and Sri Lanka's supply in the world market is less than 1 percent. Considering these facts, the company has planned to sell existing stocks of graphite and to find new buyers and to find new buyers by increasing the value added of the graphite. But the actual sales orders were received only from S. Kato Company, Japan with the assumed sales volume based on the customers who were preparing the action plan of the company and their past activities and it is also less than expected. Due to old customers of the company refrained from placing sales orders during this period and new buyers could not be found, the quantity and value of graphite exports were lower in the transition year than in the previous year as said by Auditors.	Marketing plans should be implemented to achieve desired sales targets.