

Lanka Sugar Company (Pvt.) Limited - 2018

The audit of the operational activities of the Lanka Sugar (Pvt.) Company (“Company”) Limited for the year ended 31 December 2018 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 in terms of Article 154 (6) of the Constitution of the Democratic Socialist Republic of Sri Lanka appear in this report.

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

Each audit entity should maintain its own books and records of its income, expenditure, assets and liabilities to enable it to prepare annual and periodic financial statements on that entity in terms of Section 16 (1) of National Audit Act No. 19 of 2018 . The Annual Financial Statements for each audit entity should be submitted to the Auditor General by the Chief Accounting Officer along with the Annual Performance Report of such instances as may be specified by the rules in terms of Section 16 (2) of the Act. It should be ascertained to prepare Annual Reports and other financial statements within the required time period in terms of Section 38 (1) (d) of the Act and in addition to that the Chief Accounting Officer should responsible for presenting of the Annual Reports related to the entity which was being audited to Parliament.

1.5 Report on Other Legal and Regulatory Requirements

Special provisions are consisted in respect of the requirements appear below in terms of the National Audit Act No. 19 of 2018 and the Companies Act No. 7 of 2007 .

The Board of Director of the Company should ensure that the person who is responsible for preparing the financial statements certify within six months from the date of the Balance Sheet in terms of Section 150 (1) of Companies Act No. 7 of 2007.

2.1 Financial statements

Audit Observation	Comments of the Management	Recommendation
Even though the Financial Statements of the year 2018 should be submitted to the	The financial statements for the year 2018 have been submitted for the approval of	Actions should be taken as per provisions of the

Auditor General within 60 days after the closure of the accounting year, the financial statements had not been presented for audit even by the date of this report in terms of Section 6.5.1 of the Public Enterprises Circular No. PED /12 of 02 June 2003 and the Treasury Circular No. 01/2004 of 24 February 2004 .

the Board of Directors. Actions will be taken to submit it immediately to the Auditor General.

Circular.

2.2 Non-compliance with rules, regulations and management decisions

The following non-compliances were observed.

References to Non-compliance Laws, Rules, Regulations, etc.		Comments of the Management	Recommendation
(a) Companies Act No 07 of 2007			
(i) Section 131	Although the Annual Report should be prepared within 30 working days of the Annual General Meeting of the Company, the Company had not prepared an Annual Report for the year under review.	The Company has made arrangements for the preparation of an Annual Report for the year under review.	Actions should be taken to prepare the Annual Report within the relevant period as per the provisions of the Companies Act.

(ii) Section 133	<p>Even though the Board of Directors of the Company shall call an Annual General Meeting of Shareholders to be held once in each calendar year not later than six months after the date of the Balance Sheet of the Company, the Company had not held such a meeting since 2014 .</p>	<p>The Treasury is the sole shareholder of the Company. Actions will be taken to held an Annual General Meeting in future.</p>	<p>Actions should be taken to held the Annual General Meeting within the prescribed time in accordance with the provisions of the Companies Act.</p>
<p>(b) National Environmental Act No. 47 of 1980</p>	<p>The Environmental Protection License which should be obtained for the Factory and the Distillery had not been obtained by the Sevanagala Sugar Company even by the end of the year under review.</p>	<p>The Environmental Protection License for Factory and Distillery has not been obtained. Since the Waste Water Treatment Plant of the Factory has been commenced, the samples of them were taken by the Environmental Authority for testing. After the analysis of those samples, the Protection License is applied. After constructing a Bio Gas Production Plant in the Distillery, an Environmental Protection License for the Distillery can be obtained. As the preliminary work has been done it will take about 02 years at least. According to an investigation conducted by the</p>	<p>Actions should be taken to obtain the Environmental Protection License expeditiously in terms of the relevant Act.</p>

Sugarcane Research Institute, that waste water is currently being used for sugar cane cultivation.

3. Operating Review

3.1 Management Inefficiencies

The following observations are made.

Audit Observation	Comments of the Management	Recommendation
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(a) A contract had been awarded for the installation of waste water treatment plants at the Sevanagala Sugar Company at a cost of Rs. 27,067,812 and although it was supposed to be completed by May 2014, due to the Management had failed to complete it by the end of the year under review, the Company had also failed to obtain the Environmental Protection License .	The main reason for the failure to be completed the Wastewater Treatment Project of Sevanagala Sugar Company by May 2014 was the disturbances and difficulties encountered in the completion of the civil engineering works. The refinery works were commenced whilst completion of the works in September 2019 and an Environmental Supervision Officer has taken the relevant water samples for inspection by now and it is noted that it is possible to obtain an Environmental Protection License.	The Wastewater treatment works should be successfully completed and the relevant Environmental Protection License should be obtained immediately.
(b) According to the Board of Survey Report as at the end of the year 2018 at Sevanagala Sugar Factory since there was	Steps have been taken to strengthen the stock control system of the Company.	Examine the causes of shortages and excesses in the stock and actions should be

a shortage of 324 stock items valued at Rs. 1,236,195 in the main warehouse, a shortage of 03 stock items valued at Rs. 51,843 in sub stores and an excess of 195 stocks of items valued at Rs. 689,334 were identified, it was observed that the stock control of the Company was poor.

taken to make the rectification.

- (c) When checking the sales data of the Carbon Dioxide Production Project which was commenced at Sevanagala Sugar Industries in the year 2015 and handed over to an external company, the production values of the Production Divisions had been understated less than the sales figures shown by the Finance Division. The number of kilograms in which production was less than sales for the years 2015, 2016, 2017 and 2018 were 7380, 31235, 69086 and 341514 kilograms respectively. Due to the lack of accurate production data, it was observed that the internal control system of Carbon Dioxide production process was at a poor level.
- The sales volume is higher than Carbon Dioxide production. The Company was informed to check by investigating about that. This may be due to a malfunction in meters of the Load cells and it was informed to check and renumbered.
- Necessary steps should to be taken for the production and sale of the Carbon Dioxide amount and to maintain the relevant data accurately.
- Because of the lack of proper indication of the production data from June to September 2018, it has resulted in a dramatic change in production values.
- However, since the products issued after the production process, it is issued after weighing from the weighing scale production and the issuance can be compared.
- (d) Due to the lack of proper administration by field officers in sugar cane cultivation and as a result of the failure of the officials to collect the loan installments periodically from farmers who have obtained loans, the balances of the loan to
- It is a truth that the balance of the loan issued to the sugar cane farmers to be recovered as at 31 December 2010 is Rs. 472,976,690 . A sum of Rs. 245,329,769 has been issued as loans to farmers during the year 2018 and a sum of Rs.348,443,522 has been recovered from old debts
- Make aware of the relevant responsible authorities to recover the loans given to the farmers in installments as scheduled and accordingly, immediate actions should be taken.

be recovered from the farmers at the end of the year under review in the Sevanagala Sugar Company was Rs. 218,139,312 and in the Pelwatte Sugar Company it was Rs. 472,976,690. However, the Company had not taken any action to recover the relevant loans by monitoring the duties of the field officers.

during that year. However, the recovery of loans as compared to the amount of loans issued to the farmers in some years is at a low level. Although the Deputy General Manager of Agriculture, the Superintendents in charge of each zone and the field officers under them are informed frequently in respect of recovery of loans of the farmers, there is a situation where that function is not done properly. Actions had been taken during the year 2019 to set up a separate unit for collecting the loans of the farmers after studying this situation by the Management. At present, the officers attached to this unit are working with the relevant field officers on the recovery of the loans of the farmers.

(e) The total expenditure incurred for water charges by Sevanagala Sugar Corporation for 02 private institutions from the year 2012 to 2018 was Rs. 1,061,245 and there were no written agreements for that and the Company had not taken actions to recover those water charges.

The buildings run by private companies belonging to the Sevanagala Sugar Factories and there is no possibility of entering into a written agreement in this regard and the water supply for these buildings has been providing since 11 November 2011 .

Actions should be taken to recover the relevant charges from private institutions because of the Company had to incur an expense for the supply of water.

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| <p>(f) Out of the 04 quarters of the Pelwatte Sugar Factory, the relevant house rent had not been received from the houses handed over to the external parties on rent basis and from 02 houses which had been encroached by retired officers .</p> | <p>Although the Company has handed over to four external parties on rent basis in an agreement, they had not taken actions to pay the monthly rent. In addition to that, due to the two retired employees of the Company had resided in two houses by force, they were also considered as unauthorized occupants until the settlement of a legal dispute with the Company. Steps have also been taken to collect the arrears of rent from the 06 residents who have already obtained the houses on rent basis by now and to take legal actions against them. Similarly, legal actions has been taken against the two retired employees who are still residing in two houses.</p> | <p>Necessary measures should be taken to recover the arrears rent.</p> |
| <p>(g) It was observed that there were 134 unregistered vehicles which had not state the date or value of the purchase and 92 vehicles that could not be used but in the possession of the Pelwatta Factory. Actions should be taken to repair the vehicles repairable to use or to dispose of vehicles which cannot be repaired so out of these vehicles.</p> | <p>Agreed. However, Lanka Sugar (Pvt.) Company does not have the ownership of the relevant vehicles and the registration of such vehicles is not relevant to the Lanka Sugar (Pvt.) Company.</p> | <p>Actions should be taken to take over the unregistered vehicles and to dispose of the vehicles which could not be used.</p> |

3.2 Operational Inefficiencies

The following matters were observed during the audit test checks carried out on the implementation of the main operational activities of the Company.

Audit Observation	Comments of the Management	Recommendation
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<p>(a) Although the total extent of lands cultivatable of sugar cane belonging to the Sevanagala Sugar Company was 4241 hectares, the total area of land cultivated of sugar cane was 3355 hectares in extent by the year 2018. Thus, even though the Company had had sufficient lands to obtain the supply of sugarcane required to maintain the factory operations at its maximum capacity, the Company had not taken actions to uplift the production of the factory by cultivating those lands.</p>	<p>Sugar cane is a grass plant. It is an annual harvested crop which is being maintained as a ratoon crop after planting as a fresh crop. In addition to this, the cultivation is being carried out in the highlands targeting the Yala and Maha seasons of the rainy season depending on the agro-climatic conditions of this area .</p> <p>Similarly, certain lands that have been harvested continuously for 04 to 05 years are being planned for replanting. Our planting programme takes between 600 and 800 hectares in extent annually. There is a time interval that has to be maintained as barren lands until replanting after the last harvesting of some of the lands which were planned for this planting. Therefore, the factory has a capacity of 250,000 MT of sugar cane per year. It consists of two short and long crushing periods of 250 days at 1000 MT per day. These days are variable depending only on the beginning of the rainy season and the ideal dry season for harvesting of sugar cane and crushing. However, we are constantly taking measures to deal with lands which have been illegally abandoned and this situation has arisen due to the problems that have occurred since our institution does not own the entire management rights of the land.</p>	<p>Necessary actions should be taken to utilize the cultivable land for the cultivation.</p>
<p>(b) The sugar content of the sugar cane used in the production had declined from 10.87 to 9.88 per cent to a metric ton in</p>	<p>The percentage of sugar content in the sugar cane and the percentage of sugar extraction in sugar cane from the year 2012 to 2018 is as follows.</p>	<p>Necessary actions should be taken to increase these values by</p>

the Pelwatta Sugar Factory and from 11.05 to 9.17 per cent in the Sevanagala Sugar Company also from the year 2012 to 2018 respectively. Similarly, the percentage of crushing sugar from sugar cane had declined from 8.81 to 7.55 per cent in the Pelwatta Sugar Factory and also from 8.01 to 6.59 per cent in the Sevanagala Sugar Company from the year 2012 to 2018 respectively. However, the Company had not taken steps to improve these conditions.

year	Percentage of Sugar content in Sugar cane	Percentage of sugar recovery
2012	10.87	8.81
2013	10.70	8.52
2014	10.40	7.94
2015	9.86	7.58
2016	10.62	8.21
2017	9.60	7.30
2018	9.88	7.55

examining the matters affected to decrease these percentages by the Research Division of the Sugar cane Research Institute .

Accordingly, there has been a decrease appear in the percentage of content of sugar and the recovery of sugar cane in the year 2015, 2017 and 2018. The Management has decided in late 2017, to use a mixed fertilizer instead of individual fertilizer applied separately after doing the research for this with the advice of the Sugar cane Research Institute. However, there was no significant increase in the percentage of sugar by 2018 .

Investigations are being carried out in respect of the decrease in the percentage of sugar extraction in Sevanagala Factory and it was revealed that the newly introduced sugar cane variety is the main cause. Since it is cleared that the foresaid variety was not suitable for irrigated areas, the discussions are being carried out the changing of the sugar cane variety.

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| <p>(c)</p> | <p>Due to the decrease of supplying of sugar cane, 34 per cent out of the 897,500 metric tons which was the maximum capacity of the factory of the Company had not been utilized during the year under review.</p> | <p>The sugar cane cultivation of the Pelwatta unit of the Ceylon Sugar Company are being carried out using rain water and the rainfall received within the each year has severely affected the sugar cane yield. If the rainfall is not received within the required time period of a year, the amount of sugar cane obtainable will be decreased by 01 hectare of land. Accordingly, the total quantity of sugar cane metric tons obtainable will also be limited.</p> <p>Due to the matters such as limitation of the extent of lands available for sugar cane cultivation and the lack of irrigation, the institute has been unable to achieve this target. However, the present Management of the Project has commenced the implementation of the Gal Amuna Project and the development of small tanks concurrently as a remedy for this. Also focusing on the matters such as expanding the amount of farming land and directing the farmers to cultivate sugar cane by paying higher prices for sugarcane; attempts are being made to increase the supply of sugar cane for the above mentioned capacity.</p> | <p>The Management should take necessary actions to maintain the maximum capacity of Pelwatta and Sevanagala units.</p> |
| <p>(d)</p> | <p>The production in relation to Carbon Dioxide Production Project commenced by Sevanagala Sugar Industries in the year 2015 was 84,580 kilograms and it had increased to 1,147,705 kg by 1257 per cent by the year 2016. Even so, it had decreased to 334,896 kg by 243 per cent by the year 2018 .</p> | <p>The work on the Carbon Dioxide Plant was started in September 2015. Hence, the production was 84,580 kg from September 2015 to December 2015. Since the production in Distillery in the year 2016 lasted only about 243 days, in comparison, the Carbon Dioxide production was increased to 1,147,705kg.</p> <p>Even though the Distillery has been operated for 218 days in the year 2018, since the defects has occurred in the Carbon Dioxide Plant, it has been in operation for about 65 days.</p> | <p>Actions should be taken to rectify the shortcomings immediately in the relevant machinery and to increase the production.</p> |

Therefore, it has dropped to 541,800 kg in the year 2018 .

- (e) Although the budgeted sugar cane crushing in the Sevanagala Sugar Factory was 250,000 metric tons for the year 2018, and thus the actual number of sugar cane crushing was 223,293 and since there was a shortage of 26,713 metric tons, it was failure to crush the sugar cane in the planned quantity. Even though it has been shown in the range of 56 to 58 per cent after the year 2013, the percentage of crushing of sugar cane increased to 68 per cent between the period of 2005-2006. The Company had unable to improve that condition during the past 12 years.
- Various reasons affected for not reaching to these targets. Due to an employee unrest, the sugarcane cannot be grinded for a period of 20 days. About 20,000 tons of sugar cane has lost by that. Since a heavy rainfall from September 2018 , there was a difficulty in transporting sugar cane and difficulty of operating boilers.
- Actions should be taken to achieve the relevant targets.

- (f) The activities of preparation of cultivating lands of the Sevanagala and Pelwatta Sugar factories had gradually declined when considering from the year 2013 by the year under review. It is observed that management had not drawn attention for the efficient preparation of cultivating lands because of the decrease in the activities such as ripping, ploughing, harrowing, furrowing, planting as compared to the year
- Pelwatta**
- The amount of new lands to be cultivated for each year is determined by the Budget Estimates for that year and the actual extent of cultivated lands have been changed due to various reasons. The estimated amount of lands and the actual extent of lands which were able to cultivate so since 2013 are as follows.
- Actions should be taken to perform the cultivation efficiently by purchasing new machinery and equipment needed for the preparation of farm lands.
- | Year | Budgeted | Actual | Variance |
|-------|----------|--------|----------|
| ----- | d | l | ----- |
| | (Ha) | (Ha) | (Ha) |
| 2013 | 2,757 | 3,734 | 977 |

2013 were 85,65,67,67 and 70 per cent respectively.

2014	2,511	3,061	550
2015	2,844	1,947	(897)
2016	2,573	3,007	434
2017	2,884	2,797	(87)
2018	2,797	1,783	(1,013)

Accordingly, the targeted estimate for the years 2015 and 2018 could not be able to fulfill and the main reasons for this were delays in obtaining approval for preparation of dry land by ripping in the years 2015 and 2018 due to the frequent changes in the top management of the Pelwatta Company, receiving rainfall before the expected time and due to the heavy rainfalls after beginning the rains the desired target cannot be achieved within the limited time by preparation of the wetlands only. However, measures have been taken to reach the targeted extent of cultivation of lands during the year 2019 .

Sevanagala

Year	Program	Progress	Percentage
2013	1252	771	162%
2014	1027	716	143%
2015	591	839	70%
2016	543	632	85%
2017	683	716	95%
2018	850	343	40%

Due to lack of machinery and old scrap machinery in the institute, it was failure to fulfill its targets during the certain years. Also, when farmers are looking for other crops the reduction in yield targets is a problem faced by the Institution. We were able to achieve only 40 per cent of capacity due to the

limited use of only 3 land mining machines belonging to the Institution in the year 2018 .

Since the plans are being set to purchase 10 new machines by 2020, then we will be able to reach our goals after that.

3.2 Idle or Underutilized Assets

Audit Observation

Because of the supplier had not installed the crane machine purchased under lease for a sum of Rs. 128,910,000 in the year 2013 in the company premises as agreed, it was at an unusable condition since the day it was purchased. The value of the lease installments and the interest paid by the Company for this in the year under review was Rs.21,734,748 and since the total installment payable with interest was Rs. 5,433,732 up to two more years, this expense had become a futile expense.

Comments of the Management

It is a truth that the Crane Project which was built in the year 2013/2014 has failed and is not at a condition of being usable by now. The project was due to be completed by June 2014 and to be used for the sugar cane crushing season of the Maha Season that year and after the work was completed, the system collapsed within a very short period of time. Even though the restoration works were done it is still at the condition of unusable. The investigation has been carried out by the Financial Crimes Division of the Government but we have not been informed of the final decision.

The total cost of this Project was Rs. 128,910,000. A 25 per cent of that amount or Rs. 32,000,000 was paid directly as advance to the respective provider called PanCare and the Bank of Ceylon has made arrangements to pay the balance on financial leasing method through the Pelwatta Branch. The payment was withheld after the Bank was notified by our Management before the payment of the amount related to a

Recommendation

A formal investigation should be conducted in relation with this and identifying the relevant responsible persons for that and actions should be taken against them.

lease agreement valued at Rs. 11,812,500 . This amount is shown in the financial statements as lease liabilities and this money is the only retention of this Project. All other lease payments have been settled by April 2019 and it is able to cancel the above suspended lease and withdraw a sum of Rs. 11,812,500 from the lease liability account.

The Top Management of the Company is re-negotiating in respect of the Project with the relevant supplier and it has been referred to the Legal Division of the Company.