MagaNeguma Emulsion Production Company (Pvt) Limited - 2020

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1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Maga Neguma Emulsion Production Company (Pvt) Limited 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. 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 December 2020, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards for SMEs.

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

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

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

1.4 Audit Scope

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

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

- Whether the Company has performed according to its powers, functions and duties; and

- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Audit observation on the preparation of financial Statements

1.5.1 Non-Compliance with Sri Lanka Accounting Standard for small and medium sized entities (SMES)

	Non Compliance with the reference to particular Standard	Management Comment	Recommendation
a)	**As per the section 2.52 of SLFRS for SMEs'** an entity shall not offset assets and liabilities, or income and expenses, unless required or permitted by this Standard. However, the Company had offset payables to an outside company amounting to Rs.18,732,000 against the receivable. As a result payables and receivables were understated by the same amount.	This audit observation is unclear.	Adhere to the SLFRS for SME's standard
b)	**As per the section 4.7 of SLFRS for SME's - Current liabilities**, an entity shall classify liability as a current liability if it is due to be settled within twelve months after the reporting date. However, the company had recognized Rs.1,000,000 as current liability that was received from RDA in 2004, and the relevant documents were not made available to ascertain the reason for recognizing it as a Current Liability.	This said 1,000,000 is recorded as an unpaid loan in the company accounts up to date	Adhere to the SLFRS for SME's standard
c)	As per the section 13 of SLFRS for SME's - inventories, the accounting policies adopted in measuring inventories had not been presented in the financial statements. Further, Rs.43.94 million worth of Bituman stock had not been verified as at 31 December 2020 by the company.	Agreed with the audit observation. Already taken action to disclose and comply with the requirement from year 2021.	Adhere to the SLFRS for SME's standard

d)	As per section 17 of SLFRSs for SMEs' Property Plant & Equipment, the residual value and the useful life of an assets shall be reviewed at least each financial year end and, if expectations differ from previous estimates the changes shall be accounted for as a change in an accounting estimates. However, contrary to this provision, it was observed that assets at a cost of Rs. 19,441,364 that was being used by the company had been recognized as fully depreciated assets in the financial statements. Actions had not been taken to revalue these assets.	Noted and agreed subject to the correction of last sentence of the observation. It's incorrect to the say that the non-current assets value has been under estimated. The value of the non- current assets increase or decrease will depend on the result of the assets revaluation.	Adhere to the SLFRS for SME's standard
e)	As per the section 17 of SLFRSs for SMEs'- Property Plant & Equipment, asset should be capitalized and depreciated when it is ready for use. However, an advance and other expenses made to purchase a machine at a cost of Rs.2,400,000 during the year under review amounting to Rs. 1,798,682 had been capitalized as a Non-Current Asset and depreciated by Rs. 359,736. As a result, net value of Property Plant and Equipment overstated by Rs. 1,438,946.	Agreed with the observation.	Adhere to the SLFRS for SME's standard
f)	As per the section 33 of SLFRS for SME's - Related Party Transactions, Proper disclosures relevant to Related Party Transactions had not been presented in the Financial Statements.	Agreed with the audit observation	Adhere to the SLFRS for SME's standard

1.5.2 Accounting Policies

	Audit Issue	Management Comment	Recommendation
a)	The rent expense for plant, machinery, equipment and vehicles taken on rent from RDA had not been recognized in the financial statements for the year under review. As per the invoice submitted by RDA, the rent expenditure for the year under review was Rs.527,693 and aggregated rent for the years 2018 and 2019 was Rs.93,517.	Agreed with the audit observation	Company should be adhered to the identification of relevant expenditure
b)	It was observed that differences aggregating to Rs. 77,069 in relation to four opening balances brough forward from pervious year and the reasons for those differences were not revealed in audit.	Agreed with the audit observation	Company should be adhered to the identification of corrected opening balances

1.5.3 Going Concern of the Organization

Audit Issue	Management Comment	Recommendation
According to the cabinet decision no. CP/23/0394/608/033 on 20th March 2023, cabinet has decided to give an order to the secretary to the Ministry of Transport and Highways to take steps to liquidate three companies including this company. Therefore, the going concern of the Company is doubtful.	Comment not received	Issue in going concern should be disclosed in the financial statements

1.6 Accounts Receivable and payable

1.6.1 Receivables

Audit Issue	Management Comment	Recommendation
The outstanding balance payable to ECB International Company amounting to Rs. 24,500,000 had remained unsettled over 07 years as at 31 December 2020. However, confirmations, for the balance had not been furnished to audit.	The company management has been taken decision to stop that outstanding payable unit receive the judgment of the court case.	The company should produce all the required Evidence to audit for verify the balance.

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

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) Companies Act No. 7 of 2007 (i) Section 78	Every company shall, within 2 months from the date of allotment of any of its share and within two months from the date on which a transfer of any such share is lodged with the company, complete and have ready for delivery the certification of all shares. However the share certificates issued by the company as per the above requirement had not been submitted to the audit until the date of audit report.	Not comment received	Action should be taken to follow the companies Act. No 07 od 2007.
(ii) Section 133 (1)	The Board of a Company shall call an Annual General Meeting of shareholders to be held once in each calendar year, not later than six months after the balance sheet date of the company and not later than fifteen months after the previous annual general meeting. However,	Not comment received	Action should be taken to follow the companies Act. No 07 od 2007.

		after 2016 Annual General Meetings had not been held.		
(b)	Section 3.1 of the public Enterprises Circular No. PED 01/2015 dated 25 May 2015.	Fuel allowance aggregating to Rs. 1,545,360 had been paid exceeding the entitled limits in the circular for four officers during the year under review.	PED circulars in 2015 were not applicable for this company. The fuel allowance has approved by the Board of the Directors of the company.	Action should be taken to follow the public enterprises circular instruction
(c)	Section 2 of the public Enterprises Circular No. PED 01/2015(i) dated 27 October 2016.	An officer who is entitled to an office vehicle has the option either to use the official vehicle or to avail a monthly transport allowance of Rs. 50,000. However, the company had paid of Rs. 3,180,000 million exceeding the entitled limits for four officers of the company during the year under review.	This payment of vehicle allowance for the executives' has approved by the Board of the Directors of the company.	Action should be taken to follow the public enterprises circular instruction
(d)	Section 5 (2) of Public Finance Circular 01/2014 dated 17 April 2014.	Company had not been prepared a proper Action Plan according to the circular instruction.	The company had prepared and action plan for year as per the instruction given by the management	Action should be taken to follow the public Finance circular instruction
(e)	Public Enterprisess Circular PED/12 dated 02 June 2003 (i) Section 5.1.1	State owned companies should prepare a Corporate Plan effectively for a period not less than three years. However, company had not prepared a Corporate plan.	Will be consider year 2023.	Action should be taken to follow the public enterprises circular instruction

2. Financial Review

2.1 Financial Result

The operating result for the year under review amounted to a loss of Rs. 8,034,329 and the corresponding loss in the preceding year amounted to Rs. 30,865,549. Therefore, an improvement amounting to Rs. 22,831,220 of the financial result was observed. The main reasons for the improvement of the operating result were increasing of revenue by 855 per cent as well as reductions of personnel expenses, and finance costs by 45 and 31 percent respectively.

2.2 Trend Analysis of major Income and Expenditure items

Item	Year 2020	Year 2019	Change	Percentage of the change
Revenue	83,442,327	8,739,704	74,702,623	855
Cost of Sales	70,428,335	12,247,620	58,180,715	475
Other Income	13,130,264	22,416,541	(9,286,277)	(41)
Personnel Expenses	17,563,651	32,125,005	(14,561,354)	(45)
Administrative Expenses	5,613,843	4,641,467	972,376	21
Selling & Distribution Costs	1,147,214	307,258	839,956	273
Finance Costs	3,095,960	4,463,998	(1,368,038)	(31)

Following observation is made.

Revenue was increased mainly from the sale of emulsion and bitumen further, more other income was increased from fixed deposit interest and disposal profit.

2.3 Ratio Analysis

	2020	**2019**
Current Assets Ratio	**1.57**	**1.83**
Quick Ratio	**1.05**	**1.19**
Gross Profit Ratio-percentage	**15.60**	**(40)**
Net Profit Ratio-percentage	**(9.63)**	**(353)**

Following observations are made.

i. As per the Current Assets Ratio, it was observed that the company had been maintained slightly below the range of acceptable level and Quick Assets Ratio had been maintained within the Acceptable range by the company as at the reporting date.

ii. The gross profit ratio and net profit ratio had indicated significant improvement when compare with preceding year. Because of that, improvement of revenue and detoriation of expenditure.

3. Operational Review

3.1 Transactions of Contentious Nature

	Audit Issue	Management Comment	Recommendation
(a)	As per the financial statements of the company, for the year under review it was stated that shareholding of the Road Development Authority over the company were 50 percent and share value were Rs. 100. However, as per the financial statements of the Road Development Authority for the year under review, it was stated that controlling interest over the company were 99 percent and share value was Rs. 1,000,100. Therefore, it was observed a difference of Rs. 1,000,000 of the shareholding value, between the financial statements of RDA and the company.	It is informed that no proper documents have been received from RDA mentioning the said amount as an equity contribution by the RDA to the Company.	Shareholding value should be reconciled with the RDA.
(b)	When examining the minutes of the shareholding meeting for the year 2016 held on 20 February 2018, two shareholders have participated and voted for the proposals. In approving two proposals, the shareholder, who is the chairman and the managing director voted for the proposal and approved the proposals in contrary to the provision of 10 (7) of the first schedule of Companies act No. 07 of 2007 and also to the best practices in corporate governance.	Please refer the first paragraph of article of association of this company in which the article has made reference to the prat II of the table 'A' of company Act No, 17 of 1982	Company should comply with the companies Act No. 07 of 2007