

1. Financial Statements

1.1 Qualified Opinion

The audit of financial statements of the Kahatagaha Graphite Lanka Limited (“Company”) for the year ended 31 March 2022 comprising the statement of financial position as at 31 March 2022 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 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 2022 and of its financial performance and its cash flows for the year then ended, in accordance with Sri Lanka Accounting Standards for Small & Medium Sized Entities.

1.2 Basis for the 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 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 for Small & Medium Size Entities 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 (Responsibility of Auditor regarding 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 scepticism 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 Observations on the Preparation of Financial Statements

1.5.1 Non- Compliance with Sri Lanka Accounting Standards for Small & Medium Sized Entities

Reference to the Standard and Non-Compliance	Management Comment	Recommendation
(a) Contrary to the paragraph 2.36 of the Accounting Standard for Small and Medium Size Entities, the company's fixed deposit interest of Rs.1,939,610 for the period from year 2018 to 31 March 2021 was accounted as interest income for the year under review on cash basis and therefore the profit for the year was overstated by that value.	The management will take steps to prepare the interest income to the accrual basis in the preparation of future accounts.	Action should be taken to account the revenue on an accrual basis as per Accounting Standards for Small and Medium size Entities.
(b) The information (a) to (d) of paragraph 10.23 of the Accounting Standard for Small and Medium Size Entities relating to prior period adjustments amounting to Rs.3,883,025 was not disclose in the financial statements.	Several accounting errors pointed out by the last year audit have been corrected as per Accounting Standards 10.21 for Small and Medium size Entities	Actions should be taken to disclose the matters that should be disclosed in accordance with the accounting standards.
(c) In accordance with paragraph 79(C) of Sri Lanka Accounting Standards 16, machinery amounting to Rs.23,210,000 not currently in used was not disclosed in the financial statements.	The related equipment are machines of antique value which are not currently use at the Kolongaha work site and these are expected to be used for display in the Graphite Meuseum which is expected to be started. An expected economic value or useful life cannot be determined for those machines as per Accounting Standards for Small and Medium size Entities 17.16 and depreciation cannot be provided for as per LKAS 16.	Actions should be taken to disclose the matters that should be disclosed in accordance with the accounting standards.

1.5.2 Accounting Defeciencies

Audit Issue	Management Comment	Recommendation
(a) Although the company has been continuously recovering the royalty related to the sales from the buyer and the policy in this regard has not been disclosed. Royalty amounted to Rs.827,410 paid in the year under review by the company to Geological Survey and Mines Bureau on behalf of the customers had not been shown in the accounts as receivables.	The payment was accounted in April 2022/23 and the amount was reimbursed by the buyer on 18 April 2022.	The policy of collection and payment of royalties related to sales should be disclosed and the royalties due should be stated in the financial statements accurately.
(b) The change in stock in the cash flow statement was understated by Rs.127,734 and the interest payments were overstated by the same amount.	The management has decided to indicate correctly in the preparation of accounts for the next year.	A cash flow statement should be prepared in accordance with the format to show the cash inflows and out flows accurately.

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

Reference to the Laws, Rules and Regulations etc	Non-compliance	Management Comment	Recommendation
(a) Paragraph 6.6 of operational manual introduced by the Public Enterprises Circular No.01/2021 dated 16 November 2021.	Although the draft Annual report and financial statements should be submitted to the Auditor General within 60 days after the closure of financial year, the financial statements of the company for 2021/2022 were submitted for audit on 3 April 2023.	This work was delayed because the audit of the year 2020/2021 had to be completed and the balance should be taken into the 2021/2022 accounts and the accounts should be prepared.	Financial statements and draft annual report should be submitted on due date as per circular provisions.
(b) Section 40 of the National Audit Act No.19 of 2018.	No.Internal auditor was appointed for the company.	The department of management services has given approval to appoint an internal auditor to the company but due to the existing financial difficulties an internal auditor has been provided from time to time by the Ministry of Industries on an acting basis.	Arrangements should be made to obtain the services of an internal auditor.

2. Financial Review

2.1 Financial Results

The operating result of the year under review amounted to profit of Rs.11,085,760 and the corresponding profit in the preceding year amounted to Rs.11,477,201 Accordingly, a deterioration of Rs. 391,441 was observed in the financial result. Although the interest income increased by Rs.2,734,776 and the direct cost decreased by Rs.2,233,726 ,the decrease in sales income by Rs.2,714,446 and the increase in establishment and administration expenses and maintenance expenses by Rs.1,645,717 and Rs.203,045 respectively are the main reasons for this deterioration.

3. Operational Review

3.1 Management Inefficiencies

Audit Issue	Management Comments	Recommendation
(a) The company was sued in years 2004 and 2007 by two outside persons claiming rights over two blocks of land 26.5 acres and 6 acres belonging to the Kahatagaha mine. Even though, the proceedings were not settled by the audited date of 31 May 2023.	As the proceedings are currently a judicial matter it is unable to intervene to the entity.	Steps should be taken to settle the property owned by the company.
(b) Eleven persons including three persons who worked in the mine are living illegally in quarters located in an area of 8 roods and 87 perches with in the mining areas and although efforts have been made at the ministerial level to evict the illegal residents who have been resident illegally have not been able to evict even 31 May 2023.	The administration has tried to evict squatters and prevent the acquisition of land and property by force, but the activities have not yet stopped completely.	Steps should be taken to settle the property owned by the company.
(c) According to the letter of the Secretary to the Ministry of Policy Planning & Implementation dated 15 October 2003, the Board of Directors had decided on 16 October 2003 to provide the necessary space for the Dodamgaslanda youth corps training centre from the land belonging to the Kahatagaha mine. Accordingly, the land was released in the year 2003 for a period of 3 years and as of the date of audit that period had exceeded 18 years , but the land is being used with out entering into a lease agreement or paying rent.	This work has been delayed due to the ongoing litigation for this land.	In order to enter into a lease agreement, steps should be taken to reach an agreement with the relevant parties, to act according to the agreement and to collect the arrears of rent.

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| (d) | The need for a second shaft from the first 1130 feet level to the 2000 feet level of the mine was recognized a few years ago and preliminary work was started, but further work was not done. | The start of second shaft was postponed due to the Corona situation and the work has been made difficult due to the shortage of explosives. It is planned to start the work in 2023. | Steps should be taken to expand the operations as per plans. |
| (e) | Actions had not been taken to settle the value of Rs.6,207,281 stated in the accounts as value added tax receivables. | It was unable to release or set off the Value Added Tax receivable until audited and released by the Department of Inland Revenue. | Arrangements should be made to settle this value in agreement with the Department of Inland Revenue. |

3.2 Operational Inefficiencies

Audit Issue	Management Comments	Recommendation
(a) Although the company planned to mine high carbon graphite and increase the monthly production up to 90 metric tons, the monthly average production in the year under review was 29 metric tons and the total production was 342.35 metric tons. Accordingly, With compared to the previous year production of 599.30 metric tons , the production had decreased by 256.95 metric tons in the year under review.	The graphite pits were flooded and closed due to the heavy rainfall in 2021 , due to the Corona disaster situation in the country, due to strikes and worker unrest, due to the fuel and electricity crisis in the country and due to the limitations of the workers attendance and working time the desired production level could not reached.	Plans should be taken into consideration of the practical conditions and arrangements should be made to implement them as per plans.
(b) According to the action plan, it was planned to earn an income of Rs.219.7 millions by processing and exporting 680 metric tons of graphite in the form of raw materials, but in the year under review, 384.81 metric tons of graphite was sold locally and internationally and earned only an income of Rs.123.4 million.	Existing stock was preprocessed and upgraded and initially 10 metric tons of graphite are processed. Despite various efforts, a market for the new product (KP97/99) has not been found.	Plans should be taken into consideration of the practical conditions and arrangements should be made to implement them as per plans.
(c) Though the vision of the company is to be the unique source of the natural cristaline vein graphite in the world and the company had not follow the international tender process to select it buyer and continued to export the entire	Currently we are working with the co-operation of the Ministry to invite tenders for this purpose and even though we tried to remove the graphite stock held by the	According to the vision of the company the objectives should be established and necessary steps should be taken in a planned

production of the company to two foreign buyers. As a result, according to the company's vision, there was no task management and it was not possible to create competition among foreign buyers and obtain a high price for graphite and find new markets. Here, the planned activities in the reviewed year for sales promotions such as the marketing campaigns, obtaining support from embassies, obtaining world prices from international sources etc were not implemented.

company by inviting international tenders twice before no one came forward to buy this graphite, which is in the nature of raw materials.

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| (d) | Although the company's laboratory was established with the aim of carrying out value adding processes for graphite mineral, no related work was done there and only the measurement of the percentage of carbon contained in the graphite samples prepared for export was done there. Until now the company had only exported graphite in the form of flakes(97%-99%) and chips (90%-92%) and had not done value added finished or semi-finished products. | Research activities related to various graphite value addition activities have been carried out in the laboratory and these activities are being neglected due to financial difficulties. | Necessary steps should be taken to initiate value addition processes for graphite. |
| (e) | Most of stock 57 percent consisted of graphite with a low carbon percentage and although according to the action plan it was expected to buy a flotation machine and increase the carbon percentage of low carbon graphite with the help of it and increase the income, due to non-availability of money it was not implemented even by 30 June 2023. | A grant of Rs.20 Million has been approved from the treasury to install the flotation machine and the purchase and installation of this machine is currently underway. | Plans should be prepared considering the practical conditions and operations should be promoted according to the plans. |
| (f) | The company's jeep which had been removed from use since 2006, was idle in the company's premises without being repaired and used or to dispose. | The board of directors has decided to repair this jeep and use it in the company. | Arrangements should be made to repair and use the vehicle or to dispose. |
| (g) | The company's coconut cultivation income of Rs.1,609,395 shown as miscellaneous income instead of being recognized as a separate source of income. The related expenses were | It is compulsory to clean and maintain the mine on the 102 acres of land owned by the company and since the past, the management had worked | Income generating material sources should be identified separately and accounted for. |

Rs.2,587,823 and the net loss was to account for the income generated by the coconut cultivation in a part of it as another income of the mining business itself.

3.3 Human Resources Management

Audit Issue	Management Comment	Recommendation
<p>According to the approved cadre, the company should have a staff of 79 persons to be recruited on contract basis, there were 126 staff including 42 permanent staff, 74 on contract basis, one officer on acting basis and 9 casual workers at the end of the year under review.</p>	<p>It has been submitted to Department of Management Services to get approval to recruit the required staff for the institution. Currenly 5 senior level posts have been approved and applications have been invited for a part them. The management had taken steps from time to time to recruit workers as needed to run the mine.</p>	<p>The staff should be approved and the employees should recruited accordingly.</p>