

## **Sri Lanka Ports Authority - 2015**

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The audit of consolidated financial statements of the Sri Lanka Ports Authority and Its Subsidiaries for the year ended 31 December 2015 comprising the financial position as at 31 December 2015 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information, 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 the Section 13(1) of the Finance Act, No. 38 of 1971 and Section 33 of the Sri Lanka Ports Authority Act, No. 51 of 1979. My comments and observations which I consider should be published with the Annual Report of the Authority in terms of Section 14(2) (c) of the Finance Act, appear in this report.

### **1.2 Management's Responsibility for the Financial Statements**

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Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

### **1.3 Auditor's Responsibility**

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My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000 – 1810). Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Authority's preparation and fair presentation of the financial statements 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 Authority's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements. Sub-sections (3) and (4) of Section 13 of the Finance Act, No. 38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

### **1.4 Subsidiary and Associate Companies**

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The Jaya Container Terminal Company Ltd. and the Magampura Port Management (Pvt.) Ltd. as Subsidiaries and the Port Management and Consultancy Services Company Ltd. as an

Associate Company functioned under the Sri Lanka Ports Authority. The ownership on these companies was 100 per cent and 39.97 per cent for the subsidiaries and the associate company respectively. The audit of these three companies had been done by three Firms of Chartered Accountants engaged in public accountancy profession.

## **1.5 Basis for Qualified Opinion**

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My Opinion is qualified based on the matters described in paragraph 2.2 of this report.

## **2. Financial Statements**

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### **2.1 Qualified Opinion – Group**

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In my opinion, except for the effects of the matters described in paragraph 2.2.1 of this report, the consolidated financial statements give a true and fair view of the financial position of the Sri Lanka Ports Authority and its Subsidiaries as at 31 December 2015 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

### **Qualified Opinion – Authority**

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In my opinion, except for the effects of the matters described in paragraph 2.2.2 of this report, the financial statements give a true and fair view of the financial position of the Sri Lanka Ports Authority as at 31 December 2015 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

## **2.2 Comments on Financial Statements**

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### **2.2.1 Financial Statements of the Group**

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The following observations are made.

- (a) The opinion on the financial statements of the Magampura Port Management (Pvt.) Ltd, a subsidiary company with 100 ownership of shares to the Port Authority as at 31 December 2015, for the year under review had been qualified based on the following matters. This was prepared in accordance with the qualified audit paragraph of the private audit firm which audited the Magampura Port Management (Pvt.) Ltd.
  - (i) Failure to establish the balance of Tug Claim Receivable amounting to Rs.28.4 million, included in the financial statements which was uncertain to recover ,by the third party confirmation and failure to make provisions in the financial statements in respect of the possible losses that may incur in future.
  - (ii) Termination of Bunkering Operations without the approval of the Board of Directors.

(iii) As the company had suffered a net loss of Rs.450 million during the year under review, the accumulated loss amounting to Rs.1,426 million and the current liabilities exceeding the current assets of the company as at 31 December 2015 had been Rs.1,372 million. Accordingly, it was observed that the company was facing a severe capital loss in terms of Section 220(1) of the Companies Act, No.07 of 2007. Hence, the going concern of the company was uncertain.

(b) In the preparation of consolidated financial statements of the Authority, the unaudited financial statements of the Jaya Container Terminal Company Ltd. and the Magampura Port Management and Consultancy Service Company Ltd., the subsidiaries of the group, had been utilized.

## **2.2.2 Financial Statements of the Authority**

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### **2.2.2.1 Sri Lanka Financial Reporting Standard (SLFRS) 07**

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Although the carrying amount of the financial assets kept as the security for the liabilities should be disclosed, fixed deposit amounting to Rs.2,542.9 million kept as a bank guarantee for a loan amounting to USD 163.4 million obtained from a State Bank for financing of two projects and purchasing of equipment and commitments the fixed deposit valued as Rs.315 million kept for the Rs. 285 million payable to the Tax Appeal Commission for the years 2009/2010 had not been disclosed in the financial statements.

### **2.2.2.2 Sri Lanka Accounting Standards**

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The following observations are made.

#### **(a) Sri Lanka Accounting Standard 02**

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Instead of being recognized unusable stocks and written off as an expenditure of the year under review, the cost thereof had been included in the closing stock by the Authority.

#### **(b) Sri Lanka Accounting Standard 16**

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In terms of the standard and the depreciation policy of the property, plants and equipment of the Authority, depreciation should be made according to the consumption pattern of the economic benefit of the asset. Nevertheless, as a result of computation of depreciation regardless of the date of transfer of the assets valued at Rs.445 million, depreciation of the current year amounting to Rs.77 million had been overstated in the financial statements.

#### **(c) Sri Lanka Accounting Standard 24**

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Even though all the transactions carried out with related parties should be disclosed, necessary disclosures in connection with the transactions valued at Rs.114 million

carried out by the Authority with a subsidiary had not been made in the financial statements.

(d) **Sri Lanka Accounting Standard 36**

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 Impairment loss in relation to the assets valued at Rs.208,181 million including the oil tank complex, Hambantota which was implying an impairment risk and the land in which the Oluvil Port is situated and subjected to the sea erosion had not been assessed and adjusted in the financial statements.

(e) **Sri Lanka Accounting Standard 40**

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 Without giving explanations for not presenting the investment property valued at Rs.4,132 million belonging to the Authority as at 31 December of the year under review to the fair value, it had been valued under the cost method.

**2.2.2.3 Accounting Deficiencies**

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 The following observations are made.

- (a) Designing and handling of construction activities of the Suriyawewa International Cricket Stadium had been carried out by the Authority on behalf of the Sri Lanka Cricket Institute. According to the contract agreement entered into between the contractor and the Authority in connection with this construction, the Authority had to pay a sum of Rs.5,027 million inclusive of interest of Rs.2,070 million to the contractor up to 30 July 2015 in respect of the above construction carried out under the Variance Order of the construction contract of the Hambantota port. This money had not been recognized as an amount payable to the contractor and to get it reimbursed from the Sri Lanka Cricket Institute and brought to account in the financial statements.
- (b) Action had not been taken to assess and bring to account the land leased out to the Colombo International Container Terminal on 12 August 2011 and the land of Eastern Container Terminal.

**2.2.2.4 Contingent Liabilities**

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 For a loan of USD 28 million obtained by a subsidiary from a private bank for the purchase of Bunkering Oil stocks, the Port Authority was the Co-operate Guarantee and due to discontinuation of Bunkering Oil stock operating activities, financing of the loan installments by the subsidiary had become uncertain.

**2.3 Non-compliance with Laws, Rules, Regulations and Management Decisions**

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 The following non-compliances were observed.

**Reference to Laws, Rules,  
Regulations, etc.**

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- (a) Section 11 of the Finance Act No.38 of 1971 and Section 8.2.2 of the Public Enterprises Circular No.PED/12 dated 02 June 2003.
- (b) Section 111 (a) of the Inland Revenue Act No.38 of 2000 and Section 8.7 of Public Enterprises Circular No.PED/12 dated 02 June 2003.
- (c) Public Enterprises Circular No.PED/12 dated 02 June 2003
- (i) Section 7.2 and 7.3
- (ii) Section 7.4.5
- (iii) Section 8.3.8
- (iv) Section 9.3.1
- (d) Presidential Secretariat Circular No. PCMD/AD/2/1/1/26 dated 09 April 2012.

**Non-compliance**

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- Without obtaining the sanction of Minister of Finance, the Authority had invested a sum of Rs.2,858 million during the year under review.
- Without being recovered the Pay As You Earn Tax from the salaries of the relevant officers for the tax year 2014/2015, the Authority had remitted a sum of Rs.376 million to the Department of Inland Revenue from the Funds of the Authority.
- As a prominent feature of the administration environment of the Authority, an Operating Procedure Manual/System had been prepared so as to cover all the main operations. Nevertheless, approval of the Treasury had not been granted therefor.
- Although the Authority had physically verified the fixed assets as at 31 December of the year under review, a final report had not been prepared after being compared with the Register of Fixed Assets
- Without being obtained the prior approval of the Cabinet, grants amounting to Rs. 3 million had been awarded to various institutions.
- Although a formal scheme of recruitment and promotion had been prepared for each post, approval of the relevant parties had not been granted therefor.
- Contrary to the instructions in the circular, a sum of Rs.5,652,981 had been spent as accommodation and hotel charges in respect of the officers who participated in the opening ceremony of the oil tank complex, Hambantota.

## 2.4 Accounts Payable and Receivable

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The following observations are made

- (a) In terms of the Section 9.1.3 of the financial procedure of the Authority, the officers who are directly or indirectly responsible for the recovery of money receivable to the Authority should pay attention in every respect to ensure not to give any room for those money to become outstanding, whereas there was a shipping agents debtor balance of Rs.391,260,478 and non-trade debtors balance of Rs.92,178,736 of the Authority that outstanding for more than a year as at 30 June 2016.
- (b) Out of the advance totalling Rs.406 million issued for the purchase of capital assets, the balance that remained more than one year amounted to Rs.96 million. Action had not been taken to settle this advance even by 31 May 2016.

## 3. Financial Review

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### 3.1 Financial Results- Group

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According to the consolidated financial statements presented, the operations of the Group for the year under review had resulted in a deficit of Rs.14,580 million as against the surplus of Rs.7,947 million for the preceding year, thus indicating a deterioration of the financial result by Rs.22,527 million or 283 per cent in the year under review as compared with the preceding year. The decrease in the operating income of the Port by Rs.804 million and increase in the net foreign exchange adjustment loss by Rs.20,496 million had mainly given rise to this deterioration.

### Financial Results- Authority

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According to the financial statements presented, the operations of the Authority for the year under review had resulted in a deficit of Rs.14,169 million as against the surplus of Rs.8,897 million for the preceding year, thus indicating a deterioration of the financial result by Rs.23,066 million in the year under review as compared with the preceding year. The increase in the administrative expenditure by Rs.23,379 million had mainly given rise to this deterioration.

In analyzing financial results of 4 preceding years with the year under review, although the net profit of Rs.57 million in the year 2011 had continuously increased up to the year 2014, it had turned out to be a net loss of Rs.14,169 million in the year 2015. However, when taking into consideration the employees remuneration, tax paid to the Government and depreciation for non-current assets, the contribution of Rs.20,768 million in the year 2011 had grown up to Rs.31,044 million in the year under review.

### 3.2 Analytical Review

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The following observations are made.

- (a) The current ratio of 2.5:1 in the year 2013 had deteriorated up to 1.5:1 in the year 2015. Accordingly, it was observed that the Authority may have to face working capital issues in future.
- (b) As compared with the equity capital, the loan capital was 244 per cent in the year 2013 and it was 312 per cent in the year 2015. Accordingly, it was observed that the loan capital of the Authority is continuously on the increase while the cost to be incurred thereupon as well was growing up.

#### 4. Operating Review

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##### 4.1 Performance

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In terms of the Sri Lanka Ports Authority Act, No. 51 of 1979, the main objectives of the Authority were the provision of efficient and regular port operations and protective services, regularization and control of navigation within approaches, improvement and development of ports, co-ordination and regularization of port activities.

The following observations are made on the achievement of the above objectives.

##### (a) Arrival of Container Vessels

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As compared with the preceding year, increase in the arrival of container vessels by 404 or 12 per cent to the Colombo Port was observed during the year under review and as compared with the year 2013, increase in the arrival of container vessels to the Colombo Port by 97 or 3 per cent was observed in the year 2014. Although there was an improvement in the arrival of container vessels to the Colombo Port, the Port Authority had failed to acquire the majority of the market share of that improvement. The following information established that the two private institutions were gradually acquiring that market share.

##### Arrival of Vessels

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<b>Year</b>	<b><u>2015</u></b>	<b><u>2014</u></b>	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
	<b>No. of</b>	<b>No. of</b>	<b>No. of</b>	<b>No. of</b>	<b>No. of</b>
	<b>Vessels</b>	<b>Vessels</b>	<b>Vessels</b>	<b>Vessels</b>	<b>Vessels</b>
Port Authority	1,616	1,926	2,084	1,972	2,103
S.A.G.T	1,026	855	1,011	1,120	1,084
C.I.C.T	1,001	458	47	--	--
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	<b><u>3,643</u></b>	<b><u>3,239</u></b>	<b><u>3,142</u></b>	<b><u>3,092</u></b>	<b><u>3,187</u></b>

\* S.A.G.T.- South Asia Gateway Terminal

\* C.I.C.T.- Colombo International Container Terminal

(b) **Analysis on Container Handling**

	<u>2015</u>		<u>2014</u>		<u>2013</u>		<u>2012</u>		<u>2011</u>	
	TEUS	%	TEUS	%	TEUS	%	TEUS	%	TEUS	%
<b>Ports Authority</b>										
Local	541,152		643,317		676,937		665,291		647,482	
Re-export	1,691,267		1,882,057		1,779,882		1,584,985		1,583,195	
Others	19,904		33,965		45,044		66,573		68,769	
Total	<u>2,252,323</u>	43	<u>2,559,339</u>	52	<u>2,501,863</u>	58	<u>2,316,849</u>	55	<u>2,299,446</u>	54
<b>S.A.G.T.</b>										
Local	327,750		337,357		341,510		354,964		399,404	
Re-export	1,028,538		1,298,434		1,385,552		1,479,782		1,540,633	
Others	14,957		26,152		19,740		35,525		23,404	
Total	<u>1,371,245</u>	27	<u>1,661,943</u>	34	<u>1,746,802</u>	41	<u>1,870,271</u>	45	<u>1,963,441</u>	46
<b>C.I.C.T</b>										
Local	349,069		146,314		13,530		--		--	
Re-export	1,168,516		519,219		42,683		--		--	
Others	44,314		21,103		1,328		--		--	
Total	<u>1,561,899</u>	30	<u>686,636</u>	14	<u>57,541</u>	1	<u>--</u>	--	<u>--</u>	--
Grand Total	<u>5,185,467</u>	<u>100</u>	<u>4,907,918</u>	<u>100</u>	<u>4,306,206</u>	<u>100</u>	<u>4,187,120</u>	<u>100</u>	<u>4,262,887</u>	<u>100</u>
(Colombo Port)										

The following observations are made on the arrival of the vessels to the port and handling of containers

- (i) Although arrival of container vessels as well as arrival of vessels for reshipping and repackaging to the Colombo Port showed an increase as compared with the preceding year, container handlings of the Port Authority had decreased by 12 per cent in the year under review as compared with the preceding year.
- (ii) According to the above table, 43 per cent, 27 per cent and 30 per cent market contribution of the entire container handling had been acquired by the Sri Lanka Port Authority, South Asian Gateway Terminal (S.A.G.T) and Colombo International Container Terminal (C.I.C.T) respectively

- (iii) In evaluating container handling efficiency as at 31 December of the year under review, when the number of containers handled per employee of the Port Authority was 1,388, whereas the number of container handled per employee of the Colombo International Containers Terminal had been 6,323, which was 4.5 times. Accordingly, it was observed that in comparing the efficiency of the Company to which the terminals had been leased out with the efficiency of the Port Authority, the efficiency of the Port Authority had been at a low level.
- (c) For the construction and development activities of the Hambantota Port, a sum totalling Rs.144,170 million comprising Rs.73,834 million for the first phase and Rs.70,336 million for the second phase had been spent by 31 December 2015 and a foreign loan amounting to Rs.129,849 million had been obtained for that purpose. As the Port was utilizing only for the re-export of vehicles by the year under review, it was sustaining a continuous losses.

#### **4.2 Management Activities**

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For the prevention of sever land erosion taking place in the Northern Land after the construction of Oluvil Naval and Fisheries Port, 3 breakwaters of 100 meters in length had been constructed at a cost of Euro 1.8 Millions, but those constructions too could not prevent the erosion. Further, Port had been constructed with a low depth of 9 meters and as such only small vessels can arrive in the Port. Since the Oluvil harbour being internally filled with sand, it could not be able to further use as a port.

#### **4.3 Transactions of Contentious Nature**

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The following observations are made.

- (a) In granting rebates according to the agreements entered into with the shipping Agencies engaged in the re-export and other container handling activities as per the capacity, the Authority had granted Rs.295 million to the Agencies as rebates in terms of Section 37(1) of the Sri Lanka Ports Authority Act, No. 51 of 1979 contrary to the Tariff book prepared relating to the year under review.
- (b) Without getting prepared the Equipment Interchange Report (EIR) by the staff of the Authority, EIR's had been prepared through a private institution and as such, a sum of Rs.538 million had been paid to an Associate Company of the Authority for 6,174,580 reports from the year 2006 to June 2015.
- (c) Notwithstanding the availability of a media unit of the Authority, a sum of Rs.79,208,867 had been paid to an external institution for planning media activities and documentation of television and radio programmes for the Hambantota Oil Tank Complex opening ceremony.

#### 4.4 Idle and Underutilized Assets

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Although the Oluvil Naval and Fisheries Harbour constructed by spending a loan of Euro 46.09 million obtained from the Nordia Bank of Denmark and a sum of Rs.531 million of the Port Authority had elapsed a period over 3 years from its opening in the year 2013, and as it had not been possible to arrive any vessel into the harbour even by the end of the year under review, it could not be earn any income. This assets had remained idle from the year 2013 up to the end of the year under review. However, since the value of this assets had not been shown in the financial statements of the Port Authority, assets had been understated by the end of the year under review.

#### 4.5 Uneconomic Transactions

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Despite the Port Authority had the capacity to carry out sanitary, consultancy and other operating services directly, a sum of Rs.6 million had been spent as the commission during the year under review for carrying out those services from an Associate Company of the Authority.

#### 4.6 Delayed Projects

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Under the agreement entered into between the Sri Lanka Government and the Japan Bank for International Cooperation (JBIC) on 28 March 2006, the Japan Government had agreed to grant Yen 14,495 million for the construction of a multi-purpose terminal in the Galle Port. For the creation of comprehensive design and for the completion of all services up to the pre-construction phase including technical and financial evaluation, a sum of Rs.549 million or Japan Yen 458 million for a foreign consultancy company and a sum of Rs.13 million as the loan interest up to 31 December 2015 had been spent. Nevertheless, construction had not been commenced by obtaining the approval of the UNESCO.

#### 4.7 Market Share

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In terms of the Alpha Liner Report issued on the world ports operations for the year 2015, having been operated 5,185,467 Twenty Equivalent Units, the Colombo Port stood at its 26<sup>th</sup> place. As compare with the year 2014, a growth of 5.7 per cent had been achieved during the year under review.

The gradual decrease in container handling of the Authority during the past fifteen years is given in the following table.

<u>Year</u>	<u>S.L.P.A.</u>	<u>Percentage</u>	<u>S.A.G.T</u>	<u>Percentage</u>	<u>C.I.C.T</u>	<u>Percentage</u>	<u>Total</u>
2001	1,396,946	86	229,670	14			1,626,616
2002	1,206,694	68	558,025	32			1,764,719
2003	1,334,900	68	624,439	32			1,959,339
2004	1,320,845	59	899,720	41			2,220,565
2005	1,523,794	62	931,526	38			2,455,320
2006	1,743,669	57	1,335,411	43			3,079,080

2007	1,834,734	54	1,546,497	46			3,381,231
2008	1,747,670	50	1,739,668	50			3,487,338
2009	1,714,488	49	1,749,809	51			3,464,297
2010	2,167,173	52	1,970,268	48			4,137,441
2011	2,299,446	54	1,963,441	46			4,262,887
2012	2,316,849	55	1,870,271	45			4,187,120
2013	2,501,863	58	1,746,802	41	57,541	1	4,306,206
2014	2,559,339	52	1,661,940	34	686,636	14	4,907,915
2015	2,252,323	44	1,371,245	26	1,561,899	30	5,185,467

Accordingly, it was observed that the function of container handling, which is the main operation of a port was gradually leaving from the hands of the Authority as a Government port and it was grasping by the private sector.

Awarding the best and the deepest dockyard (15 meters in depth and 18 meters in depth) on long term lease basis to the above two companies for a period of 35 years under the Built, Operator and Transfer method, the existence of a dockyard with the depth less than 15 meters to the Authority at present and failure to purchase of cranes and other equipment required for the operations of the Eastern Container Terminal with the depth of 18 meters, the construction of which had been completed in the year 2015 at a cost of Rs.10,800 million under the Colombo Port Expansion Project and failure to make it fit for the use by installing them even as at 31 December 2015 had mainly affected the above situation.

## 5. **Accountability and Good Governance**

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### 5.1 **Internal Audit**

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The following observations are made.

- (a) The internal audit staff consisted of 43 members. Out of 20 executive and staff officers 11 officers did not have the professional knowledge of Accounting and Auditing and 04 posts of executive level had fallen vacant during the year under review. As such, it was failed to make an adequate coverage on the content included in the internal audit plan expected for the implementation in the year under review.
- (b) In terms of the Management Audit Circular No.DMA/2010 (5) dated 26 July 2010, an internal audit should be carried out on the projects implemented under foreign aid or local funds. Nevertheless, the Authority had not carried out an internal audit on the foreign aid projects.

### 5.2 **Fulfilment of Environmental and Social Responsibilities**

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As a result of aggravating the sea erosion following the construction of the Oluvil harbour, it had hampered the day to day activities of the fisheries community who had maintained their livelihood by the sea shore. Further, due to the construction of 03 breakwaters up to 100

meters, issues had cropped up for the traditional fishermen in the sue of their shore upon the failure to berth their boats.

## 6. Systems and Controls

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Deficiencies in systems and controls observed during the course of audit was brought to the notice of the Chairman of the Authority from time to time. Special attention is needed in respect of the following arrears of control.

<b>Areas of Systems and Controls</b>	<b>Observations</b>
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(a) Personnel Administration	Failure to obtain approval for the Scheme of Recruitment.
(b) Accounting	Failure to fulfill the requirements of the accounting standards.
(c) Debtors Control	Existence of long outstanding unrecovered balances.
(d) Internal Audit	Failure to make an adequate coverage on the matters included in the audit programme.
(e) Stock control	Failure to distinguish the unusable items