Sri Lanka Cement Corporation and its subsidiary Sri Lanka Cement Company - 2013

The audit of Consolidated financial statements of the Sri Lanka Cement Corporation and its subsidiary Lanka Cement Company Ltd. for the year ended 31 December 2013 comprising the statement of financial position as at 31 December 2013 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 the State Industrial Corporations Act, No. 49 of 1957. 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

Management is responsible for the preparation and fair presentation of these 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

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 Standards of Supreme Audit Institutions (ISSAI 1000 – 1810).

1.4 Basis for Disclaimer of Opinion

As a result of the significance of the matters described in paragraph 2.2 of this report, I am enable to determine whether any adjustments might have been found necessary in respect of the recorded or unrecorded items, and the elements making up the statement of financial position, statement of comprehensive income, statement of changes in equity and the cash flow statement.

2. Financial Statements

2.1 Disclaimer of Opinion

Disclaimer of Opinion – The Group

Because of the significance of the matters described in paragraph 2.2 of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis an audit opinion on the Consolidated financial statements of the Sri Lanka Cement Corporation and its Subsidiary Company, Lanka Cement Company Ltd. Accordingly, I do not express an opinion on those financial statements.

Disclaimer of Opinion – Corporation

Because of the significance of the matters described in paragraph 2.2 of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on those financial statements.

2.2 Comments of Financial Statements

2.2.1 Consolidated Financial Statements

As the Sri Lanka Cement Corporation owns 62.45 percent of the Lanka Cement Company Ltd, the Subsidiary Company of the Sri Lanka Cement Corporation, consolidated financial statements had been presented.

2.2.2 Going Concern of the Institution

The capital of the Sri Lanka Cement Corporation amounted to Rs.967 million while the accumulated loss amounted to Rs.67 million. According to the consolidated statement of changes in equity the capital of the Lanka Cement Company Ltd and the accumulated loss amounted to Rs.2,702 million and Rs.2,238.7 million respectively due to the State Cement Company sustaining losses continuously, though such position has no impact on the going concern of the Corporation.

In view of the erosion of 82.8 percent of capital, it was observed during the course of examination of the accounts consolidated with the Lanka Cement Company Ltd, that an uncertainty on the maintenance of the Company continuously has been created.

2.2.3 Maintenance of Both Institutions for the same Purpose

It was observed that both institutions are performing the same function as the key function of the Lanka Cement Company Ltd is the import of cement and selling in the domestic market. In addition, the Board of Governors of the Corporation function as the Board of Governors of this company.

2.2.4 Sri Lanka Accounting Standards

Sri Lanka Accounting Standard 16 (LKAS 16)

The following observations are made.

(a) Two motor vehicles costing Rs.3,929,169 fully depreciated but being used at present had not been revalued and brought to account.

(b) Even though an asset should be regularly depreciated from the date on which it is brought to usable condition, the assets of three categories valued at Rs.927,898 purchased by the Corporation during the year under review had not been depreciated.

2.2.5 Accounting Policies

The following observations are made.

(a) Corrections had been made in the financial statements for the year 2013 in respect of debit balances and credit balances totaling Rs.11,884,804 and Rs.12,435,964 respectively of the financial statements for the year 2010, debit and credit balances totaling Rs.76,680,411 and Rs.76,362,683 respectively in the financial statements for the year 2011, debit and credit balances totaling Rs.40,853,368 and Rs.40,884,747 respectively in the financial statements for the year 2012. Accordingly, it was not possible to be satisfied in audit that such situation would not recur in the future.

(b) The land belonging to the Corporation situated in Kollupitiya pledged to a State Bank as security for bank overdrafts and loan facilities amounting to Rs.172 million had been disclosed in the Note No. 8.2 presented with the financial statements. A proposal made by a

Review Committee appointed by the Cabinet of Ministers, for the lease of the land on a 99 year lease to a foreign investor had been disclosed in Note No. 2.07(b). Whether such proposal had been approved by the Cabinet of Ministers had not been disclosed.

2.2.6 Accounting Deficiencies

The following observations are made.

(a) The following deficiencies were observed in connection with the lands and buildings owned by the Corporation.

(i) The land 5,352 acres in extent at Aruwakkalu in Puttalam where the limestone deposit is situated had not been valued and brought to account.

(ii) The limestone deposit of 751 acres in extent, the factory and the buildings complex situated at Kankasanthurai and stated as belonging to the Corporation under Note No. 8.2 of the notification published the Gazette No. 14012 of 1964 had not been valued and brought to account. Even though 104 acres of the land had been rented out to the Lanka Cement Company, rent income had not been received up to date.

(iii) Out of 221 acres 03 roods 27.8 perches of the Atta Villu Forest situated at Kalladi in Puttalam, the value of 69 acres had not been assessed and brought to account.

(iv) The land 1,191 acres in extent including the Kaolin and limestone deposit with an extent of 604 acres situated at Puliyadi Irakkam in the Mannar District, revealed from the documents as owned by the Corporation on the long term lease basis, had not been disclosed in the financial statements.

2.2.7 Lack of Evidence for Audit

Action had not been taken to identify accurately the lands and buildings belonging to the Corporation and bring to account. The schedules relating to the current assets totaling Rs.111,576,652 and the current liabilities totaling Rs.37,705,069 had not been furnished to audit.

2.3 Balances Receivable and Payable

The following observations are made.

(a) The trade liabilities balances payable as at 31 December of the current year under review totalling Rs.85,224,411 and out of that balances totalling Rs.11,712,123 , Rs.14,434,353 and Rs.30,846,822 had been balances old between 1 – 2 years, 2-3 years and over 3 years respectively.

(b) The trade and other balances receivable as at 31 December of the year under review totalling Rs.89,809,582 and out of that balances totaling Rs.19,855,327 , Rs.2,985,059 and Rs.54,718,680 had been old between 1 – 2 years, 2-3 years and over 3 years respectively.

2.4 <u>Non-compliance with Laws, Rules, Regulations and Management Decisions</u>

The non-compliances with the following laws, rules, regulations and management decisions were observed during the course of audit.

Reference to Laws, Rules, Regulations, etc.,	Non-compliance
(a) Financial Regulation 756 of the Democratic Socialist Republic of Sri Lanka	Even though a survey of the assets should be conducted immediately after the close of the financial year and furnish reports thereon to audit, it had not been so done in connection with fixed assets valued at Rs.779,485,898.
(b) Treasury Circular No. IAI/2002/02 of 28 November 2002	A separate Register of Fixed Assets had not been maintained for computers, accessories and software.
(c) Public Enterprises Circular No. PED/12 of 02 June 2003	
(i) Section 4.2.2	Even though the Corporate Plan, budget and performance should reviewed on a timely basis, it had not been so done in connection with the year under review.
(ii) Section 8.3.8	Donations and assistance amounting to Rs.75,000 had been made in the year under review without obtaining the prior approval of the Cabinet of Ministers.
(iii) Section 8.3.9	Even though the resources of Public Corporations and Boards should not be given for the purposes of the Line Ministry, the double cab motor vehicle purchased of January 2011 by the Corporation for Rs.4.8 million had been given for use security duties of the Line Ministry since the date of purchase up to the date of audit.
(d) Section 2 of the Nation Building Tax Act, No. 09 of 2009	Nation Building Tax totaling Rs.4,641,762 which should have been remitted to the Commissioner General of Inland Revenue had not been remitted.
(e) Section 2.1 of the Value Added Tax Act, No. 14 of 2002	Value Added Tax totaling Rs.9,147,692 which should have been remitted to the Commissioner General of Inland Revenue during the year under review had not been remitted. Action had not been taken to adjust the reimbursable Value Added Tax totaling

		Rs.8,725,533 from the Value Added Tax payable to the Commissioner General of Inland Revenue.
(f)	Section 3 of the Finance Statute of the Western Provincial Council, No. 6 of 1990	Business Turnover Tax totaling Rs.7,101,932 which should have been remitted to the Western Provincial Commissioner of Revenue had not been remitted.
(g)	Treasury Circulars No. 842 of 19 December 1978 and No. DMA/2009/02 of the Department of Management Audit	A Register of Fixed Assets in terms of these Circulars had not been maintained.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the operations of the Corporations during the year under review had resulted in a deficit of Rs.424,603,476 as compared with the corresponding deficit of Rs.75,099,975 for the preceding year. The increase of the deficit for the year under review as compared with the preceding year by a sum Rs.349,503,501 indicated a deterioration of the operating results. The financial loss of Rs.411,775,186 resulting from the diminutions of the market value of the investment made in the shares of Lanka Cement Company Ltd. and the decrease of sales income by a sum of Rs.77,419,150 or 21 percent had been the main reasons for the deterioration.

4. Operating Review

4.1 Performance

The following observations are made.

(a) The imports of cement during the year under review amounted to 21,700 metric tonnes of cement or 434,000 bags of cement and 28,249 metrictonnes of cement or 564,980 bags of cement had been imported in the preceding year. The import of cement during the year under review as compared with the preceding year indicated a decrease of 33 percent.

(b) The Cement Concrete Production and Sales Division at Kankasanthurai had been sustaining losses continuously due to incurring expenditure exceeding the total income. The particulars of losses sustained during the seven preceding years are given below.

(c)

Year	Income	Expenditure	Loss
	Rs.	Rs.	Rs.
2007	1,537,141	21,063,774	(19,526,633)
2008	17,916,478	24,782,357	(6,865,879)
2009	36,893,564	43,994,616	(7,101,052)
2010	27,334,174	27,364,472	(30,298)
2011	6,860,513	16,283,680	(9,423,167)
2012	32,456,800	38,120,118	(5,663,318)
2013	4,491,387	19,274,456	(14,783,069)

(d) The Corporation had not paid adequate attention for the achievement of the objectives targeted in the Annual Action Plan and had failed to achieve over 25 percent of the targeted sales of any of the months. The sales during September, October and November of the year under review had been very weak and had not reached even 10 percent. The achievement out of the targeted sales of the Action Plan had been only 16.5 percent.

(e) Even though plans made for the year 2013 included the import of 400 containers of cement per month, construction of a new building on the land at Kollupitiya, increase the production of cement posts at Kankasanthurai and to open a cement packing factory at Kankasanthurai for raising the performance of the Corporation, none of these targets had been achieved even by the end of the year under review.

4.2 Management Inefficiencies

The following observations are made.

(a) The debtors balances remaining recoverable as at the end of the year totalling Rs.61,028,486 due to the management inefficiencies such as the failure to obtain security bond commensurate with the value of credit granted in the award of sales agencies for the sale of cement on credit basis, non-inclusive of the maximum credit allowed in the agreements, non-inclusion of the methodology for the recovery of debts from the debt defaulters in agreement, further supplies made on credit basis in cases of non-settlement of debts, giving false information far Bank Guaranties, failure to take disciplinary action against officers who approve credit irregularly and lack of follow-up action on the debtors balances recoverable.

(b) The inability to cover the cost of import of cement and the administrative, distribution and finance expenses from the sales income indicates that the management continuously sustaining losses under such conditions revealed the existence of the risky situation for the going concern / stability of the Corporation.

4.3 Uneconomic Transactions

The following observations are made.

(a) Even though the Corporation had invested a sum of Rs.6,400,000 in a private firm from the year 2004 and invested Rs.1,083,618,910 in the Lanka Cement Company Ltd. over a period exceeding 16 years, the Corporation had not received any returns up to the end of the year under review.

(b) In view of the failure to take action in accordance with the terms of an agreement entered into with a company domiciled in the United States of America in the year 1990 for the import clinker, a raw material used in the manufacture of cement, compensation amounting to U.S.$ 1.3 million had to be paid to that company. Out of that U.S.$ 1 million had been paid by the Puttalam Cement Company. The payment of the balance amount had been agreed to in terms of the decision of the Cabinet of Ministers No. CM/12/1458/553/019 dated 01 November 2012. Accordingly, the Corporation had paid the balance sum of U.S.$ 0.3 million in the preceding year by obtaining a Bank loan of Rs.38,704,668. Interest on the loan amounting to Rs.6,152,681 had to be paid during the year under review.

4.4 Identified Losses

The following observations are made.

(a) A sum of Rs.6,169 had been paid during the year under review as surcharge due to the failure to remit the contributions to the Employees Trust Fund on the due dates.

(b) A loss of Rs.258,576 had been caused due to 7,679 cement bags damaged and 189 cement bags lost, out of 434,000 cement bags imported during the year under review. Action had not been taken for the recovery of the money from those responsible.

4.5 Idle and Underutilised Assets

The following observations are made.

(a) Even though sums of Rs.577,429 and Rs.27,429 had been spent in the year 2011 for the container machine and its accessories respectively, the machine had been kept idling since the date of purchase without being used.

(b) Lands 152 acres in extent belonging to the Corporation situated in Puttalam, Palavi and Kalladi had been idling. Unauthorized occupants had built houses on 9 acres overgrown with scrub and left unprotected and without being used.

(c) The land 751 acres in extent situated in Kankasanthurai and the buildings including the factory owned by the Corporation situated in the High Security Zone remaining under the charge of Sri Lanka Army and the land 211 acres in extent at Murunkan, Mannar had been idling over long periods due to the war.

4.6 Staff Administration

The approved staff for the year 2013 had been 76 officers while the actual staff had been 63 and the number of vacancies had been 13.

4.7 Resources of the Corporation given to other Government Institutions

(a) The Engineer who served the Corporation had been released to the National Equipment and Machinery Organisation on the basis of reimbursement of salary and an Office Aide had been released to the Presidential Secretariat with effect from 12 March 2013. The Corporation had Aide a sum of Rs.654,819 as the salary of the Engineer up to 31 December 2012. Action had not been taken to obtain reimbursement of the salaries and allowances paid to the above two officers during the year under review together with the above amount.

(b) A sum of Rs.464,607 had been paid during the year under review to an officer without the basic qualifications required in terms of the Circular No. MSD/30 of 17 November 2011, to the post of Sales and Marketing Officer.

5. Accountability and Good Governance

5.1 Action Plan

The targeted sales income according to the Action Plan for the year under review amounted to Rs.3,750,000,000 whereas the actual income amounted to Rs.307,462,755. Accordingly the progress represented 8.2 percent of the targeted income.

5.2 Procurement Plan

A Procurement Plan had not been prepared in terms of Section 5 of the Public Enterprises Circular No. PED/12 of 02 June 2003.

5.3 Budgetary Control

Reconciliation of the budgeted income and expenditure of the budget for the year 2013 with the actual income and expenditure revealed variances ranging from 26 percent to 231 percent, thus indicating that the budget had not been made use of as an effective instrument of management control.

5.4 Unresolved Audit Paragraphs

Sri Lanka Cement Corporation had leased out to a private company a limestone deposit situated in a land 5,352 acres in in extent at Aruwakkalu in the year 1995 for a period of 50 year for mining of limestone for the production of cement. According to the agreement, the annual lease rental amounted to Rs.26,516,620 and the Corporation could not revise the annual rental during the entire period of 50 years as the agreement did not include a clause on revision of the lease rent periodically. Even though the Committee on Public Enterprises had, at the meeting held on 16 August 2011, derected the Corporation to revise the lease agreement, action thereon had not been taken even by 30 November 2014.

6. Systems and Controls

Deficiencies observed during the course of audit were brought to the notice of the Chairman from time to time. Special attention is needed in respect of the following areas of control.

(a) Financial Control
(b) Debts Receivable and Payable
(c) Fixed Assets
(d) Stores Control