Ceylon Ceramics Corporation – 2014

The audit of financial statements of the Ceylon Ceramics Corporation for the year ended 31 December 2014 comprising the statement of financial position as at 31 December 2014 and the 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 Section 13(1) of the Finance Act, No. 38 of 1971 and Section 29 of 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 Corporation 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 Auditors' 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 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 judgements, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Corporation'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 Corporation'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 the 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 Basis for Adverse Opinion

Had the matters described in paragraph 2.2 of this report been adjusted, many elements in the accompanying financial statements would have been materially affected.

2. Financial Statements

2.1 Adverse Opinion

In my opinion, because of the significance of the matters described in paragraph 2.2 of this report, the financial statements do not give a true and fair view of the financial position of the Ceylon Ceramics Corporation as at 31 December 2014 and its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.2 Comments on Financial Statements

2.2.1 Going Concern of the Corporation

The following factors such as the existence of a negative net assets position of Rs.138,494,826 and Rs.151,178,241 as at the end of the years 2013 and 2014 respectively, the total assets to liability ratio of the Corporation for the said years being at 1: 1.93 and 1: 2.41 respectively, effect of the problems of the working capital, the permanent staff being limited to 41 employees and non -approval of the staff after voluntary retirement in the year under review, closing down of 04 factories out of 09 factories owned by the Corporation due to the past war situation and lack of raw materials, appointing a Competent Authority by removing the Board of Directors of the Corporation from the year 2010 for the lease of the factories of the Corporation to the suitable investors and implementing the restructuring procedure expeditiously had affected adversely to the going concern of the Corporation.

2.2.2 Accounting Policies

The basis of distribution of the expenditure of the Head Office to the Factories had not been disclosed in the financial statements in the preparation of financial statements.

2.2.3 Accounting Deficiencies

The following observations are made.

(a) Relying upon the balancing of the financial statements presented was problematic in Audit due to non-operation of a systematic Accounting System, non-maintenance of basic source documents, specified subsidiary books and reports . The deficiencies observed are mentioned below.

(i) Even though, the balance of a Current Account of a State Bank according to the Cash Book as at 31 December 2014 amounted to Rs.1,410,570, that balance had been understated by Rs.87,668 as it was shown as Rs.1,322,902 in the statement of financial position presented to audit.

(ii) Even though balances of Bank Overdraft of Rs.9,660 and Rs.15,749 respectively had remained according to the Cash Book as at 31 December 2014 in another two Current Accounts in a State Bank, balances had been overstated by Rs.157,346 as a result of two Bank Accounts had been shown totalling Rs.131,937 according to the Statement of Financial Position as at that date.

(iii) Even though the balance of the Bank Overdraft according to the Cash Book as at 31 December 2014 in the Bank Current Account maintained for the Bingiriya Factory had been Rs.84,128 ,this balance had been under stated by Rs.54,547 as a result of the said Bank Overdraft had been shown as Rs.29,581 in the financial statements.

(iv) The balance of the Cash Book had been overstated by Rs.39,097 due to the above errors. Despite the sum amounting to Rs.884,242 payable from the year 2008 had been paid in the year under review ,this amount had been shown in the financial statements as a money receivable.

(v) Despite the Factories of Oddusudan and Bangadeniya were closed down in 1982 and 2002 respectively, stocks amounting to Rs. 1,750,649 in those 2 factories had been included in the stocks shown in the financial statements .

(vi) The electricity expenditure totalling Rs.64,504 paid in two Factories had been under stated in the financial statements of the Head Office.

(b) Excess stocks and damaged stocks as per the physical verification as at 31 December 2014 relating to 07 Factories amounted to Rs.1,028,510 and Rs.813,442 respectively. However, no adjustments thereon had been made in the financial statements .

(c) A sum of Rs.2,632,010 had been transferred as other new reserve Account from the Assets Exchange Reserve Account as at 31 December 2014 by a Journal Entry without a fair written evidence.

(d) As the Withholding Tax of Rs.272,217 of the Eragama Factory accounted erroneously to the Debtors Account ,the debtors balance and the value of Withholding Tax had been overstated and under stated respectively in the same amount.

(e) The following matters were observed in respect of the Cash flow Statements in the year under review.

(i) In the calculation of the net cash flow of the operating activities made within the cash flow, the interest on fixed deposit adjustable to the pre-tax net profit had been under adjusted by Rs.223,487.

(ii) Even though the taxes payable in the year 2014 by the Corporation amounting to Rs.360,000 ,that value had been shown in the cash flow statement as Rs.762,221 thus over stating the tax value by Rs.402,221.

(iii) The value of the interest income received on fixed deposits amounting to Rs.1,090,499 included in the net cash flow generated from investments, had not been adjusted to the cash flow statement.

(iv) In the calculation of the net cash flow generated from operating activities, pensions gratuity of Rs. 123,682 paid in the year under review had not been adjusted as a cash out flow.

(f) The interest income on fixed deposits receivable as at 31 December 2014 had been under stated in the accounts by Rs.141,387.

(g) Even though the audit fees payable as at 31 December 2014 amounted to Rs.1,210,832, it had been understated by Rs.445,950 as it was shown in financial statements as Rs.764,882.

(h) Salaries and production incentive expenses of Rs.14,014,335 paid to the employees who had engaged in the production activities in Factories had been shown as administrative expenses in the financial statements.

(i) According to the Payment of Gratuities Act,No.12 of 1983, in the calculation of the provision for Pensions Gratuity as at 31 December 2014 , a sum of Rs.769,685 had been under calculated .

2.2.4 Unexplained Differences

The following observations are made.

(a) According to the financial statements, the total cost of lands and buildings of the Corporation amounted to Rs.28,952,630. However, according to the schedule presented to audit.that value amounted to Rs. 26,293,421 thus indicating a difference of Rs.2,659,209.

(b) According to the Reports of the Provident Funds, the balance of the Provident Fund payable as at 31 December 2014 amounted to Rs.270,899 . However, it was shown in the financial statements as Rs.6,854,865 thus showing a difference of Rs. 6,583,966 in the financial statements.

(c) Even though the value payable as at 31 December 2014 amounted to Rs.36,940 according to the remittance sheet of the Employees Trust Fund , there was a difference of Rs.19,256 thus it had been shown as Rs.56,196 in the financial statements.

2.2.5 Lack of Evidence for Audit

Due to lack of evidence indicated against the following items of accounts shown , they could not be satisfactorily vouched or accepted in audit .

Item of Account	Value	Evidence not furnished
	Rs.	
Unfinished Stock	3,492,203	Reports of Boards of Survey of Physical Verifications
Fixed Assets	38,884,097	Reports of Physical Verifications on Fixed Assets
Lands and Buildings	23,755,785	Title Deeds, Licenses or formal written evidence to ensure the ownership of the lands relating to 07 Factories of the Corporation.

2.3 Balances Receivable and Payable

The following observations are made

(a) Action had not been taken to recover or write off the balance of festival advances of Rs.262,168 recoverable from the employees of the Oddusuddan factory for over 27 years which was closed down since the year 1982.

(b) The water bills of the Mahiyangana Factory accrued from the year 2009 amounting to Rs.220,463 had not been settled even up to the end of the year under review.

(c) Except the land of the Bangadeniya Factory which had been closed down in the year 2002 on the scarcity of raw materials , all other assets had been auctioned in the year 2012. Even though 12 years had elapsed from closing down the Factory, trade debtors balance, taxes payable and accrued expenditure amounting to Rs.314,380,Rs.13,363,261 and Rs.1,069,613 respectively had not been settled even by the end of the year under review.

(d) Unsettled debtor balances of Rs.975,480 in 05 Factories closed down had existed.

(e) Even though 12 years had elapsed after closing up of the Ceylon Ceramics Ltd , a sum of Rs.26,226,152 had been shown as payable to that Corporation as at 31 December 2014.

(f) Taxes totalling Rs.5,583,755 and Rs. 171,097,334 brought forward from prior to the year 2000 had not been remitted to the Provincial Commissioner of Revenue and the Commissioner General of Inland Revenue even by 31 December 2014.

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

The following instances of non-compliance were observed during the course of audit.

	Reference to Laws, Rules, Regulations, etc.	Non-compliance
(a)	**Financial Regulation of the Democratic Socialist Republic of Sri Lanka**	
	(i) Financial Regulation 135	Action had not been taken in the year under review to delegate authorities for financial control in writing by the Head of the Institution who is the Accounting Officer.
	(ii) Financial Regulation 387	Even though no government bank account should be overdrawn, the Corporation had obtained bank overdrafts totalling Rs.398,253 by using 04 Bank Current Accounts in the year under review.
(b)	**Government Procurement Guidelines of the year 2006 and supplementary.**	
	(i) Sections 1.3.2, 4.3 and 8.12.2	A sum of Rs.1,885,595 had been paid for the repair of the roof of the Factory at Mahiyangana in the year 2014 without following the Procurement Guidelines.
	(ii) Section 2.14.1 and Supplementary No.28	Goods valued at Rs.1,550,050 had been purchased without calling for bids.
(c)	**Public Enterprises Circular No.PED/12 of 02 June 2003**	
	(i) Section 4.2.6	Even though the Corporation should review the Performance Reports once in three months, Performance Reports for the year under review had not been prepared.
	(ii) Section 8.3.8	A sum of Rs.327,000 had been granted as donations and assistance for the Government and private Institutions and Organizations without the approval of the Cabinet of Ministers during the year under review without considering the adverse financial condition of the Corporation.

(d)	Section 02 of the Public Finance Circular No.02/2015 dated 10 July 2015.	Action had not been taken to dispose of 17 motor vehicles older than 15 years discarded from running which had been recommended to dispose by the Boards of Survey.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the operations of the Corporation for the year under review had resulted in a deficit of Rs.12,683,458 as against the surplus of Rs.5,287,855 for the preceding year, thus indicating a deterioration of Rs.17,971,313 in the financial result for the year under review. Increase in factory wages, incentives and travelling and subsistence by 17,238,655 had mainly attributed to this deterioration.

3.2 Analytical Financial Review

The following observations are made.

(a) The gross profit ratio of the Corporation which was 11.75 per cent in the year 2013 had decreased up to 4 per cent by the year 2014. Gross profit ratio of the year 2014 had decreased as compared with the year 2013 due to the cost of sales of the year 2014 increased by 11.8 per cent as compared with the year 2013 despite the sales of the year 2014 had been increased by 2.8 per cent as compared with the year 2013.

(b) The quick ratio of the Corporation had been 0.07 and there was a stock of finished goods amounting to Rs.53,840,989 within the current assets of Rs.72,519,278 .The quick assets ratio had decreased as the current liability of the Corporation represented such a large value of Rs.249,949,473.

3.3 Legal Cases Initiated against the Corporation

Several legal cases against the Corporation and initiated by the Corporation were observed and the Corporation had not disclosed that matter in the financial statements. The following matters were observed in that connection.

(a) A case filed under Case No.L-168 in the Court of Akkaraipattu by the Corporation in respect of encroachment of a part of the land belonging to the Eragama Factory by another party was being heard.

(b) Eight cases had been filed in various Courts against the Corporation by the employees relating to the matters such as non-extension of their services from 55 years to 57 years and the arrears of gratuity and 50 complaints filed in the labour tribunals relating to the arrears of gratuity by the officers who left the service after being obtained compensations and retired were being pending.

4. Operating Review

4.1 Performance

The main objective of the Corporation is to be the pioneer in the market by producing standard various types of tiles, bricks and clay related productions and supply of materials to satisfy all types of customers under competitive quotations and bear a social responsibility thereon.

A competent authority had been appointed in the year 2010 for the Corporation according to the decision of the Cabinet of Ministers for carrying out the long term leasing of all Factories which was the main objective of the re-structuring of the Corporation. Accordingly, employees were sent on retirement under Volunteer Compensation Scheme on 31 March 2012 as the first step of the long term leasing . Action required for the long term lease of the tile factories of this Corporation are being carrying out at present.

The following observations are made in the examination of the achievement of the objectives of the Corporation.

(a) Out of 09 Factories belonging to the Corporation , four Factories had been closed down on various reasons. Only 05 factories in Eragama, Mahiyanganaya, Bingiriya, Yatiyana and Uswewa were being functioned during the year under review. The profitability of those Factories in the year under review and 02 preceding years are shown below.

Factory	**Profit/(Loss) for the Year**		
	2014	**2013**	**2012**
	Rs.	Rs.	Rs.
Bingiriya	(1,798,937)	934,690	(1,711,014)
Mahiyanganaya	(7,041,142)	1,512,804	3,978,017
Yatiyana	(4,057,263)	(3,155,256)	(4,751,744)
Uswewa	(7,711,925)	(5,303,273)	(8,985,412)
Eragama	20,955,987	11,651,721	22,720,384

(i) Only Eragama Factory had earned a profit of Rs.20,955,987 in the year 2014 while the other 4 Factories had incurred losses totalling Rs.20,609,267. Despite the Yatiyana Factory closed down in the year 2013, a loss of Rs.4,057,263 had incurred due to manufacture of bricks required for the Sandahiru Seya by the Sri Lanka Navy .

(ii) The loss of the Factories at Uswewa and Yatiyana had been increased in the year 2014 as compared with the year 2013. Nevertheless, Mahiyanganaya and Bingiriya Factories which had earned profits in the year 2013 had incurred a loss totaling Rs.8,840,079 in the year 2014. Increase the electricity expenses ,increase damages and losses due to usage of machines older than 50 years and incurring lots of expenses on transportation of raw materials had been the reasons to incur losses from the Factories.

(b) In the examination of the progress of the production capacity in the year 2014, the expected capacity of all production items was 4,354,000 units while the actual production capacity was 2,162,836 units. Accordingly, the actual production capacity had decreased by 2,191,164 items or 50.32 per cent and the production capacity of all 5 factories was at a low level of the expected position,taken as a whole.

4.2 Management Activities

Written information was made available as to encroach the land belonging to the Corporation where Mahiyanganaya Factory was situated by external individuals from May 2015 .However, the Management had failed up to 31 July 2016 to settle the ownership of the land by solving this problematic condition.

4.3 Identified Losses

A stock value of damaged and cracked totalling Rs.813,442 relevant to 07 manufacturing Factories as at 31 December in the year under review had been revealed at the physical stock verification.

4.4 Personnel Administration

The following observations are made.

(a) According to the Paragraph 9.2 of the Public Enterprises Circular No. PED/12 of 02 June 2003,the Treasury approval for the approved cadre should be obtained . However, action had not been taken to approve the required cadre for the carrying out of the future activities of the Corporation after the removal of employees by granting compensations under the restructuring of the Corporation in the year 2012.

(b) As the approved cadre of the Corporation had not been determined, it could not be decided whether there were vacancies or excess of the cadre in the Corporation.The productions of four Factories had been carried out by deploying 10 officers of the Executive level and 195 primary level employees on contract and daily payment basis without a proper written approval as at the end of the year 2014.

(c) In term of Section 9.10 of the Public enterprises circular No. PED/12 of 02 June 2003 the approval of the secretary to the Treasury should be obtained in recruiting for vacant posts on primary, casual or other basis. However without obtaining such approval 28 persons had been recruited on contract basis after the restructure.

5. Accountability and Good Governance

5.1 Presentation of Financial statements

Even though the financial statements should be presented to the Auditor General along with the draft annual report within 60 days of completion of the financial year in terms of Section 6.5.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003, the draft financial statements of the year under review had been presented to audit on 25 February 2016.The final financial statements had been presented to audit on 30June 2016.

5.2 Corporate Plan

A Corporate Plan had not been prepared even from the year 2012 for the Corporation in terms of Paragraph 5.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003.

5.3 Action Plan

An Action Plan in terms of Section 2 of Paragraph 5.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003 had not been prepared.

5.4 Internal Audit

Even though 12 areas to be examined had been shown in the Internal Audit Plan prepared for the year under review by the Corporation, only one area had been examined within the year.

5.5 Audit Committees

Even though Audit Committee meetings should be held at least once in three months according to Section 7.4.1 of Public Enterprises Circular on Good Governance No.PED/12 of 02 June 2003 , only one Audit Committee meetings had been held for the year under review.

5.6 Procurement Plan

A Procurement Plan for the year 2014 had not been prepared in terms of 4.2 of the Government Procurement Guidelines.

5.7 Budgetary Control

According to Section 5.2 of the Public Enterprises Circular on Good Governance No.PED/12 of 02 June 2003, a budget for the year under review had not been prepared . As such, the budget had not been made use of as an instrument of management control.

6. Systems and Control

Deficiencies in systems and controls observed during the course of audit were brought to the notice of the Competent Authority of the Corporation from time to time. Special attention is needed in respect of the following areas of control.

Areas of Systems and Control	Observations
(a) Financial Control	Action not taken to maintain Ledger Accounts, books and documents of the Corporation in an updated manner, non-recovery of the balances receivable and to settle and pay the taxes payable.
(b) Fixed Assets Control	Non –maintenance of Register of Assets properly and appointing Boards of Survey and surveys had not been carried out under proper supervision.
(c) Stores Control	Proper attention had not been paid on maintenance ,storing and maintenance of finished Stock.
(d) Internal Control	Action had not been taken to introduce internal control systems and maintaining controls by implementing them properly.
(e) Accounting	Consolidated trial balance had not been prepared for 09 production factories and the Head Office , preparation of journal entries and accounted by the private Institution by which the Accounts were prepared,without the approval.