Cey–Nor Foundation Limited – 2015

The audit of the financial statements of the Cey – Nor Foundation Limited for the year ended 31 December 2015 comprising the statement of 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. My comments and observations on the above financial statements appear in this report.

1.2 Board's Responsibility for the Financial Statements

The Board of Directors ("Board") 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 Board 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. 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 judgment, 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 Foundation'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 Foundation's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Board, as well as evaluating the overall presentation of the financial statements.

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 Qualified Opinion

My opinion is qualified base on the matters described in paragraph 2.2 of this report.

2 . Financial Statements

Qualified Opinion

In my opinion, except for the effects of the matters described in paragraph 2.2 of this report, the financial statements give a true and fair view of the financial position of the Cey – Nor Foundation Limited as at 31 December 2015 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.1.1 Report on Other Legal and Regulatory Requirements

As required by Section 163 (2) of the Companies Act, No.07 of 2007, I state the followings:

a. The basis of opinion and scope and limitations of the audit are as stated above.

b. In my opinion :
   - I have obtained all the information and explanations that were required for the audit and as far as appears from my examination, proper accounting records have been kept by the Foundation.

   - The financial statements of the Company comply with the requirements of Section 151 of the Companies Act, No. 07 of 2007.

2.2 Comments on Financial Statements

2.2.1 Compliance with Sri Lanka Accounting Standards (LKAS)

The following observations are made.

(a) LKAS 01 – Presentation of Financial Statements:

Although, assets and liabilities shall not be offset, the Foundation had offset its credit and debit balances aggregating Rs.824,824 and Rs.16,805,846 against other receivables and payables respectively.

(b) LKAS 26 - Accounting and Reporting by Retirement Benefit

There was no proper investment plan for the retirement benefit in order to address the future retirement obligations, However, a provision for gratuity amounting to Rs.11,496,747 had been made as at 31 December 2015.

(c) LKAS 40 – Investment Property

(i) Although, the Foundation had earned a sum of Rs.16,266,502 as investment income, investment property had not been disclosed separately in the financial statements.

(ii) Foundation had not determined the fair value of the investment of Rs.1,961,850 made in a private company registered in Bangladesh for boats manufacturing purposes and brought the respective value into accounts.

2.2.2 Accounting Deficiencies

The following observations are made.

(a) Building rent amounting to Rs.294,000 payable to the Central Fish Market Complex at Peliyagoda as at the end of the year under review had not been brought to accounts.

(b) Provision for depreciation made during the year under review had been overstated by Rs.4,841,527 in the financial statements, due to erroneous postings of journal entries to the ledger accounts.

(c) A sum of Rs.1,267,650 receivable for the year under review on properties owned to the Foundation at the Mattakkuliya Yard which leased out to an outside party for a project for processing of fish products had not been brought to the financial statements.

(d) An amount of Rs.162,119,000 spent to upgrade the Mattakkuliya Yard, out of the grants received from the General Treasury for Dikowita Harbour Project through the Ministry of Fisheries and Aquatic Resources Development had not been brought to accounts.

(e) It was observed that the investments amounting to Rs.325,950 made in the Sri Bangalas Boats Manufacturing Company and a sum of Rs.1,635,900 spent on transportation of molds of boats had only been shown in the financial statements. However, the cost of molds of the boats and cost of technical supports thereon amounting Rs.2,778,208 had not been included therein.

2.2.3 Un-explained Differences

The following observations are made.

(a) A difference of Rs.717,294 was observed between the output taxes shown in the statements of the Value Added Tax for the third and fourth quarters of the year under review and the monthly statements of tax for the respective period. Further, a difference of Rs.2,563,819 was also observed between the input taxes shown in the above mentioned statements.

(b) According to the Value Added Tax returns, the output taxes amounted to Rs.9,312,055. However, according to the ledger account it was Rs.14,534,963. Therefore, a difference of Rs.5,222,908 was observed.

(c) According to the Value Added Tax returns, a sum of Rs.18,897 had to be paid as at 31 December 2015. However, it was shown in the financial statements as receivable balance of Rs.15,190,312. Therefore, a difference of Rs.15,209,209 had been observed.

(d) According to the records maintained at the Dikowita Fisheries Harbour Project, the assets valued at Rs.60,556,983 had been transferred to the Foundation during the year 2015. However, it was shown in the records of Foundation as Rs.45,854,541, thus a difference of Rs.14,702,442 was observed.

(e) The Foundation had shown a sales income of Rs.58,195,818 in the financial statements for the year under review. However, sales Division of the Foundation had confirmed that it was Rs.62,646,446. The reasons for difference of Rs.4,450,628 had not been explained to audit.

2.2.4 Accounts Receivable and Payable

The following observations are made.

(a) A policy for provision for bad debt for trade debtors had not been disclosed. However, an amount equal to Rs.6,532,490 had been provided for bad debts since 2011. Although other receivables amounting to Rs.6,028,504 had remained outstanding for over a period ranging from 02 to 04 years, provision for bad debt had not been provided.

(b) Actions had not been taken to settle the Goods and Services Levy, National Defense Tax , Turnover Tax etc. aggregating Rs.2,585,515 shown in the financial statements since 2011 as payables to the Commissioner General of Inland Revenue. Further, other dues such as Value Added Tax and Withholding Tax amounting to Rs.1,458,293 and Rs.3,368,452 respectively had remained unsettled for over 04 years. In addition to that, tax certificates for withholding tax amounting to Rs.1,119,030 shown under other receivables had not been presented for audit.

(c) According to the financial statements of the Foundation, a sum of Rs.1,390,902 had been shown as payable to the Fisheries Harbour Corporation. However, according to the financial statements of the Corporation no Corresponding balance was shown as receivable from the Foundation.

(d) Confirmations in respect of trade debtors, receivables and trade creditors shown in the financial statements amounting to Rs.146,151,830, Rs.9,204,498 and Rs.100,926,391 respectively had not been presented for audit. According to the age analysis, trade creditors aggregating Rs.58,366,542 representing 58 per cent of total creditors and trade debtors aggregating Rs.33,398,577 representing 23 per cent of total trade debtors had remained outstanding for over 03 months and 33 months respectively

(e) A balance of Rs.2,078,392 shown in the statement of financial position as at the end of the year under review as Ministry Grants had remained unsettled for over several years. Further, the information relating to the respective balance had not been furnished for audit.

2.2.5 Lack of Evidence for Audit

The detailed schedules on Value Added Taxes amounting to Rs.22,643,116 collected from the Department of Fisheries and Aquatic Resources were not made available for audit and as a result, the remittances of the respective taxes could not be confirmed in audit.

2.3 Non- Compliance with Laws, Rules, Regulations and Management Decisions

The following instances of non- compliance with Laws, Rules and Regulations were observed in audit.

Reference to laws, Rules and Regulations	Non- Compliance
(a) Paragraphs 25(1) and 25(2) of the Inland Revenue Act, No.10 of 2006	The Foundation had received capital allowances of Rs.14,806,180 for the year of assessment 2014/15 and the tax concession of Rs.4,145,730 on assets valued at Rs.45,854,542 procured for Dikowita Fisheries Harbour Project. Further, at the time of handing over the assets to the Foundation, a sum of Rs.9,633,313 which identified as differed government grants had been treated as a tax exempted revenue. Therefore, it was observed that the tax concessions were obtained in 02 occasions on the same assets.
(b) Public Finance Circular No. 02/2015 of 10 July 2015	Although out of 16 vehicles in the fleet of motor vehicles 06 motor vehicles had been identified to disposed, action had not been taken to dispose those vehicles even up to 31 December 2015.

2.4 Transactions not Supported by Adequate Authority

A retired officer had been recruited on contract basis for the post of General Manager of the Foundation on 18 June 2014 without the approval of the General Treasury and contrary to the approved recruitment procedures. A monthly remuneration of Rs.100,000 had also been paid in contrary to the recruitment procedure and Section 2 (1) of the Public Administration Circular No 09/2007. Further, the interim allowances recommended by the Public Administration Circular had also been paid for this officer who are not entitle for this allowances. In addition to that, the monthly salary had been increased by Rs.25, 000 with effect from 01 November 2014 without even an approval of the Board of Directors.

3. Financial Review

3.1 Financial Result

According to the financial statements presented, the operations of the foundation for the year under review had resulted in a pre-tax net profit of Rs.70,430,367 as compared with the corresponding pre-tax net profit of Rs. 100,419,522 in the previous year, thus indicating a deterioration of Rs. 29,989,155 in the financial results for the year under review. Decrease of gross profits on construction works and trading activities by Rs. 60,815,482 was the main reason attributed for this deterioration in the financial results.

3.2 Analytical Financial Review

3.2.1 Value Addition

The following observations are made.

(a) In analyzing the financial results of previous 5 years before adjusting the deprecation for non – current assets and personnel emoluments, the value addition of the Foundation had been increased by 49 per cent since the year 2012 to 2015 and the value addition for the year under review was Rs.195,937,736

(b) Even though there was an increase in the value addition of the previous year as compared with the year 2013 by 226 per cent, only 05 per cent of Value addition had been increased during year under review.

(c) Forty seven per cent of value additions for the year under review had represented by the supply of fisheries boats and other fishing gear to the Line Ministry and the Department of Fisheries Aquatic Resources.

(d) Adequate action to improve the Value Addition by way of increasing the profit had not been taken by the Foundation during the year under review.

4. Operating Review

4.1 Performance

The Cey- Nor Foundation Limited had been incorporated as a Public Company under the Companies Act, No.17 of 1982 and under the Conversation of Public Corporations and Government Owned Business Undertakings in to Public Companies Act, No.23 of 1987 and the objectives of the Foundation as per the Memorandum of Association are as follows.

- To carry on the business of building, manufacturing, sales and operating workshops for repair and reconditioning of trawlers boats, fishing vessels, marine motors and other marine equipment.

- To undertake the business of manufacture of ice and marine products and the processing, packaging, marketing and export of these products.

- To carry on the business of the manufacture and sell of fishing nets and allied fishing gears in Sri Lanka or abroad.

- To act as a commission agent, sales agent or manufacturer with regards to the activities of the Foundation.

The following observations are made in achievement of the above mentioned objectives.

(a) Even though the Foundation had engaged with other activities exterior to the above mentioned objectives, and undertaking the manufacturing of ice and allied activities and manufacturing of fishing nets had been withdrawn from the original objectives of the Foundation, actions had not been taken to amend the Memorandum of Association in line with the current requirements.

(b) The physical progress on the achievements of the targets of the Foundation for the year under review had not been presented for audit.

4.2 Management weakness

The following observations are made.

(a) According to the provisions in the management agreement entered into with a private company to renting out the motor vehicle repair workshop located at Mattumagala for 15 years, 3 per cent of annual turnover is required to be paid subject to minimum rentals of Rs.100,000 in first 05 years, Rs.150,000 in second 5 years and Rs.250,000 in third 5 years. However, the minimum fee had only been recovered by the Foundation without considering the annual turnover. Further, action had not been taken to confirm the income through audited financial statements of the relevant Company.

(b) The Foundation had rented out 03 containers to a private company at a monthly rental of Rs.95,000. However, the values of machineries and equipment fixed in the containers had not been considered in determining the monthly rental.

4.3 Operating Inefficiencies

The following observations are made.

(a) Out of the funds received from the General Treasury, on a decision of the Cabinet of Ministers for the implementation of the Dikowita Fisheries Harbour Project, a sum of Rs.207.9 million had been spent during the year for improvement of the boat yard at

Mattakkuliya belonging to the Foundation. However, a plan for the improvement works had not been prepared and presented. Further, according to the records of the Foundation, a significant progress on productions and sales income had not been shown even at the year under review.

(b) The Committee on Public Accounts held on 05 March 2013 relating to the Ministry of Fisheries and Aquatic Resources had made a direction to launch a scheme to repair boats at the yard and supply such boats to the fisheries community at subsidized prices in order to refund the allocation released by the General Treasury. However, neither such a scheme had been implemented nor supply of boats to the fishermen at low costs was observed even as at 31 December 2015.

4.4 Transactions of Contentious Nature

The following observations are made.

(a) Renting out a portion of the Boat Yard at Mattakkuliya.

(i) The Foundation had taken action to enter into an agreement with a foreign company registered in Sri Lanka on 29 May 2014 to lease out a part of land with extent of 19,456 square feet belonging to the Boat Yard at Mattakkuliya and buildings thereon for 30 years. However, approval of the General Treasury or Board of Investment had not been obtained for this purpose.

(ii) The respective land had been leased out at a rant of Rs.7.70 per square feet. However, a portion of the land had been leased out at a rate of Rs.21 per square feet in a previous occasion. Therefore, the Foundation had incurred a loss of Rs.4,654,368 by this transaction.

(iii) As a result of defaulted the payment of rentals and non-compliance with the provisions in the lease agreement, the properties leased out had been acquired by the Foundation. However, no action had been taken to recover the outstanding rentals during the year under review.

(b) Investments in Sri Bangalash Boat Manufacturing Company

(i) The Foundation had entered into a joint venture agreement with the above mentioned company registered in Bangladesh for the purpose of manufacturing and selling of fishing boats. According to the agreement, the Foundation is required to make an investment of US$ 80,000 or 40 per cent of the capital of the company. However, actual investment made by the Foundation was US$ 101,265.

(ii) It was observed that no return on investment made in 2008 had been received to the Foundation even as at 31 December 2015 and also action had not been taken to obtain the investment certificates and annual financial statements from the company.

(c) Handing over the Net Manufacturing Business to a Government owned Company

According to the decision taken by the Cabinet of Ministers on 18 November 2010, two fishing nets manufacturing factories belonging to the Foundation located in Lunuwila and Weerawila had been handed over to a Government owned company on 22 June 2011 through a Memorandum of Understanding between the parties. For that purpose, it was agreed to hand over a boats manufacturing factory owned to the Company located in Kareinagar to the Foundation. The following observations are made in this regard.

I. The manufacturing of fishing nets was the main objective of the Foundation. In achieving this objective, the Foundation had able to obtain international standard certificates and earned 64 per cent of total income of the Foundation through manufacturing of fishing nets. However, the Foundation could not be able to continue the operations of manufacturing nets due to the condition in the above mentioned Memorandum of Understanding.

II. The Foundation had not taken action to acquire the factory at Kareinagar which totally damaged during the war time and to prepare a plan to reconstruct the factory.

III. As per the agreement, the assets valued at Rs.53,117,471 and net current assets valued at Rs.29,641,352 had been transferred to the Government owned company at Rs.26,093,191.

4.5 Un-economic Transactions

The following observations are made.

(a) An excavator had been procured at a cost of Rs.40 million in 2014 for the use of the contract undertaken to construct Maradana Yard. Even though it was expected to be used the excavator for 7,000 hours within 02 years period, 420 hours only had been used during the period of 02 year as at 31 December 2015.

In the meantime, this excavator had been rented out to the outside parties and a sum of Rs.5,098,473 had been earned during the year under review thereon. However, a sum of Rs.5,022,311 had been spent for this purpose and as such a profit of Rs.76,161 only had been generated. Therefore, the return on capital invested was only 0.2 per cent.

(b) The Economic Service Charge amounting to Rs.326,626 spent by the Foundation had not been deducted from the income tax paid during the year under review.

4.6 Identified Losses

Withholding tax amounting to Rs.2,630,218 had been written off in 2010 on the approval of the Board of Directors without taking action to set off against the income tax paid.

4.**7 Personnel Management**

Even though the staff cost incurred for production, trading and construction activities required to be represented higher percentage of total staff cost, only a sum of Rs.14,037,045 or 26 per cent of

total staff cost had been spent thereon, thus indicating that staff had not been employed effectively for the main activities of the Foundation.

4.8 Market Share of the Foundation

The Foundation had not carried out a market survey to determine its market share.

5. Accountability and Good Governance

5.1 Rendition of Financial Statements

Although the draft annual report and financial statements for the year 2015 are required to be submitted for audit before 28 February of every year in terms of Section 6.5.1 of the Public Enterprises Circular No.PED/12 of 02 June 2003, the financial statements for the year ended 31 December 2015 had been submitted for audit only on 03 May 2016 with a delay of 64 days and a draft annual report had not been presented even up to 31 December 2016.

5.2 The Corporate Plan

The Foundation had prepared a Corporate Plan for the period from 2013 to 2017. The following observations are made in this connection.

(a) The Corporate Plan had not been approved by the Board of Directors of the Foundation and it had not been reviewed and updated periodically.

(b) The Corporate Plan and Budget for the year under review had not focused on achievement of the objectives such as manufacturing of marine motors and equipment, processing, promoting and export of ice which had been set out in the establishment of the Foundation.

(c) Significant variances were observed between the targeted income set out in the Corporate Plan and the actual income. Hence, it was observed that the Corporate Plan had been prepared without carrying out a proper evaluation.

5.3 Action Plan

An annual action plan had not been prepared in order to achieve the objectives and targets included in the Corporate Plan.

5.4 Internal Audit

The following observations are made.

(a) Even though the Cadre of Internal Audit Unit of the Foundation should be comprised with a Senior Internal Auditor and 2 Subordinate Audit Officers. The subordinate officers were not recruited even as at 31 December 2015.

(b) In terms of Internal Auditing Standard No.1100 introduced by the Circular No. DMT/2009(3) of 01 October 2009 of the Management Audit Division of the General Treasury, the Internal Auditor should be directly responsible to the accounting officer of the Institution. However, list of duties of Internal Auditor of the Foundation had been issued by the General Manager and the directions had been given by the General Manager/Managing Director in respect of carrying out the audit works. Accordingly, the Internal Auditor had performed the assignment given by the General Manager/Managing Director and Private Secretary to the Minister contrary to the instructions given by the above Circular.

(c) Internal audit reports had been referred to the Divisional Heads through the General Manager instead of directly forwarding to the Chairman.

(d) The General Manager had approved an additional allowance of Rs.3,000 for Internal Auditor in attending the project activities and it had been increased up to Rs.10,000 since 17 March 2015. Therefore, the status of independency of the Internal Auditor was questionable in audit.

(e) Same subject areas had been covered in preparing the Internal Audit Programme for the four years from 2013 to 2016. Further, the areas planned to be covered through the Internal Audit Programme of the year under review had not been covered.

5.5 Budgetary Control

The following observations are made.

(a) The budget of the Foundation had not been prepared in rational manner and reviewed periodically.

(b) Although 5 retail sales outlet had been established at the end of the year under review, no information relating to the operations of the sales outlet had been included in the annual budget of the Foundation.

(c) The budget of the Foundation had not been forwarded to the relevant parties before the specified period in terms of Section 5.2.4, 5.1.3 and 5.2.5 of the Public Enterprises Circular No.PED/12 of 02 June 2003 and it had been prepared exterior to the standard format as per Section 5.2.1 of the above Circular.

(d) Significant variances were observed between the budgeted and actual figures of the Foundation, thus indicating that the budget had not been made use of as an effective instrument of management control.

6. Systems and Control

Weakness observed in systems and controls in audit were brought to the notice of the Chairman of the Foundation in time to time. Special attention is needed in respect of the following areas of control.

Area	Observations
(a) Procurements	i. Handing the purchasing by Sales Division exterior of the Supply Division ii. Procurement of goods and services in contrary to the Procurement Guidelines. iii. Procurement of similar items by placing several orders to keep within the financial authority limit of the Sales Manager.
(b) Procurement minor product material	i. The petty cash imprest had to be reimbursed in 161 instances during the year under review due to using the petty cash imprest for purchase of minor production material worth Rs.1,732,266. ii. The Federation had failed to introduced a proper mechanism for purchase of minor product materials