## Colombo Commercial Fertilizers Limited – 2016/2017

The audit of financial statements of the Colombo Commercial Fertilizers Limited for the year ended 31 March 2017 comprising statement of financial position as at 31 March 2017 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 observations on the performance of the Company in the year under review which I consider should be presented to Parliament in terms of Article 154(6) of the Constitution of the Democratic Socialist Republic of Sri Lanka appear in this report.

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

The 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. 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 misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company'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 Company'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.

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

### 1.4 Establishment of the Company

The Colombo Commercial Fertilizers Limited was registered as a Company in the year 1872 and was controlled by the Great Britain for over a century from the year 1872 to 1976. The Company was acquired by the Government in year 1976 under the Business Undertakings (Acquision) Act, No. 35 of 1971 and the business activities had been run under the name of the Colombo Commercial Fertilizers Limited under a Competent Authority.

The Company was registered as a State Company in accordance with the Conversion of Government Owned Business Undertakings into Public Companies Act, No. 23 of 1987 and was privatized in the year 1994 according to the State policy. It was vested again in the year 1997 under the Rehabilitation of Public Enterprises Act, No. 29 of 1996 and is under the Control of the Line Ministry. The Company has been registered at present as a company under the Companies Act, No. 07 of 2007.

### 1.5 Basis for Qualified Opinion

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

## 2. Financial Statements

### 2.1 Qualified Opinion

In my opinion, except for the effects of matters described in paragraph 2.2. of this report the financial statements give a true and fair view of the financial position of Colombo Commercial Fertilizer Company Limited as at 31 March 2017 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 Company.

- 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 Sri Lanka Accounting Standards

The following observations are made.

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

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(i) The following matters on total inventories which should be disclosed in the financial statements, had not been disclosed.

* The total carrying amount of inventories and the carrying amount in classifications appropriate to the entity,
* The carrying amount of inventories carried at fair value less costs to sell
* The amount of inventories recognized as an expense during the period

(ii) Adjustments of impairment losses had not been made for the 695,998 metric tons of fertilizer stock valued at Rs.12,796,873 that was over 5 years and become unusable which included in the stock of Rs.2,245,769,383 shown in the financial statements.

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

**--------------------------------------------**

Even though fixes assets costing Rs.38,318,368 had been fully depreciated as the useful life of non-current assets had not been reviewed annually, they were being further used. Accordingly, action had not been taken to revise the estimated error in terms of Sri Lanka Accounting Standard 8.

**2.2.2 Accounting Policies**

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Even though the final stock should be measured by the First in First Out method as per Note 3.5.1 of the financial statements, the stock had been measured by the Last in First Out method.

**2.2.3 Accounting Deficiencies**

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The following observations are made.

(a) Advances totalling Rs.441,480 paid for the purchase of property, plant and equipment during the year under review had been shown as a cash out flow for the purchase of fixed assets in the cash flow statement instead of showing under working capital movement in the cash flow statement.

(b) Even though the tax liabilities amounted to Rs.31,015,338 according to the tax computation performed by the Company in respect of the year under review , the tax liabilities of the year as per the Note 17.1 of the financial statements amounted to Rs.18,493,956. As such, the liabilities of the year under review had been understated by Rs. 12,521,382.

(c) In the computation of tax liabilities in terms of Inland Revenue Act, No.10 of 2006, instead of the loss of Rs.51,337,088 adjusted in the year , a sum of Rs.17,967,981 had been recorded, thus resulting in an overcomputation of tax liabilities. As such, the tax liabilities of the year amounted to Rs.23,430,143 after being deducted the loss and computed accurately. Accordingly, the tax liabilities shown in the financial statements had been understated by Rs.4,936,187.

### 2.2.4 Lack of Evidence for Audit

The following observations are made.

(a) The reports of physical stock verifications had not been made available to audit in respect of the stock of Central Stores valued at Rs.1,776,845,021 included in the stock of Rs.2,245,769,383 shown in the financial statements.

(b) A sum of Rs.13,501,929,683 had been shown in the financial statements as the capital grants receivable from the General Treasury for the payment of loans obtained from a State bank by the Company. As the reply for the letter of confirmation of the said balance, it was established that the Department of Treasury Operations does not intervene directly in loan agreements.

### 2.2.5 Transactions not supported by Adequate Authority

In supplying fertilizer on credit basis, fertilizers valued at Rs.4,044,135 had been supplied exceeding the credit limit in 5 instances.

## 2.3 Accounts Receivable and Payable

The following observations are made.

(a) The balances receivable in the financial statements included the balance totalling Rs.65,000 of the loans granted in the year 2012 to 06 employees who have left the service at present and it had not been recovered even by the end of the year under review.

(b) In selling fertilizer through cheques to the sellers not registered in the Company, the fertilizer should be issued after realizing cheques. Contrary to that, a Regional Stores Assistant had issued fertilizer to two persons in the years 2011 and 2016 before the realization of cheques whereas no action had been taken to recover a sum of Rs.724,505 recoverable from them further as at 31 March 2017.

(c) Action had not been taken to recover the loan balances totalling Rs.23,630,939 older than 23 years which included in the balances receivable.

(d) Even though a sum of Rs.81,000 had been shown as receivable from the Sri Lanka Insurance Corporation in the financial statements as the penalty for Luxury, Semi Luxury and Dual Purpose Taxes paid on 25 April 2016, there was no documentary evidence that the said amount would be paid by the Sri Lanka Insurance Corporation.

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

The following instances of non-compliance were observed.

| | Reference to Laws, Rules and Regulations | Non-compliance |
|---|---|---|
| (a) | Financial Regulations of the Democratic Socialist Republic of Sri Lanka | |
| (i) | Financial Regulation 371 and Public Finance Circular No.03/2015 of 14 July 2015 | • The sum of Rs.289,918 shown as unsettled advances in the financial statements of the year under review included a balance of Rs.91,215 brought forward from the year 2013, while no action had been taken to settle it.<br>• Even though the advances should be settled immediately after the completion of the purpose for which it is granted, advances totalling Rs.105,000 granted in 05 instances in the year under review had been settled after a delay ranging from 20 days to 72 days. |
| (ii) | Financial Regulation 387 | Even though obtaining overdrafts from State bank account is prohibited, the Company had obtained bank overdrafts totalling Rs.156,595 from a State bank account in the year under review. |
| (b) | Public Finance Circular No.PF/PE/21 of 24 May 2002 | A draft annual report had not been submitted along with the financial statements. |

## 3. Financial Review

### 3.1 Financial Results

According to the financial statements presented, the financial result of the Company for the year under review amounted to a profit of Rs.56,799,204 as compared with the corresponding profit of Rs.180,971,671 for the preceding year, thus indicating a deterioration of Rs.124,172,467 in the year under review as compared with the preceding year. The decrease of income by a sum of Rs.1,015,047,494 had been the main reason for the above deterioration.

An analysis of the financial results of the year under review and the 4 preceding years indicated that the after tax profit of Rs.123,182,724 of the year 2012/2013 were fluctuating and it had decreased to Rs.56,799,204 in the year 2016/2017. However, readjusting the employees' remuneration, Government tax and depreciation on the non-current assets to the financial result, the contribution amounting to Rs.236,461,160 of the Company in the year 2012/2013 had increased continuously up to the year 2014/2015 while it had decreased to Rs.353,446,651 in the year 2015/2016 and further decreased to Rs.171,729,158 in the year under review.

## 4. Operating Review

## 4.1 Performance

According to the Memorandum of Association of the Company the primary objects of the Company are to carry on the business of agents, importers, manufacturers, distributors of and dealers in fertilizers, chemicals, minerals and other natural and synthetic substances whether in finished or unfinished form, re-export them in any form and act as agents and import export packers.

The following observations are made on the achievement of objectives.

(a) As the paddy cultivation is a main crop in the Agriculture Sector in Sri Lanka, opportunity had been provided to farmers for the purchase of a fertilizer bag of 50 kilograms at a concessionary rate of Rs.350 from the year 2006 to 28 February 2016 as a State policy. Further, 35 per cent of the requirement of fertilizer in respect of that subsidy programme had been fulfilled by the Colombo Commercial Fertilizers Limited.

(b) Instead of fertilizer, the financial assistance programme had been implemented from 01 March 2016. Based on that programme, even though an income of Rs.5.69 billion was targeted from the sale of direct fertilizers such as Urea, MOP and TSP and mixed fertilizers, the actual sales income had been Rs.0.82 billion. As such, the sales income earned had been at a minimum level representing 14 per cent.

(c) Even though the Company should prepare the advance plans to face the future business risks, action had not been taken accordingly. Action had not been taken for the promotion of sales through the strengths and weaknesses in the organizations and the external threats and opportunities analysis and giving priority.

## 4.2 Management Activities

A land belonging to the Mahaweli Authority had been obtained by the Company on lease basis from the year 2012 for the construction of a fertilizer stores and a sum of Rs.779,700 had been spent therefor as at the end of the year under review. Nevertheless, the construction work had not been carried out even by 30 October 2017, the date of audit.

## 4.3 Operating Activities

The following observations are made.

(a) In terms of the Economic Service Charges Act, in case of reaching the tax limit payable as turnover by any enterprise after 01 April 2016 (up to 31 March 2017, if the turnover of a quarter exceeds Rs.50 million ) it should be registered for the Economic Service Charges Nevertheless, the Company had not so registered , thus the Government had deprived of Economic Service Charges amounting to Rs.4,202,453 of the year 2016/2017.

(b) In terms of Item (a) (x) of Part 2 of first Schedule of the Value Added Tax (Amendment) Act, No. 14 of 2002, only the import and supply of fertilizer are exempted from the Value Added Tax. Nevertheless, rentals, sale of scrap items and sundry income totalling Rs.3,279,501 had not been considered in the computation of Value Added Tax.

**4.4 Identified Losses**

Taxes had not been paid on due dates in terms of Inland Revenue Act, No.10 of 2006, Nation Building Tax Act and Pay As You Earn Tax Act, thus the Company had paid fines amounting to Rs.2,588,918 during the year under review.

**4.5 Staff Administration**

The following observations are made.

(a) Even though the approved cadre of the Company as at the end of the year of accounts stood at 151, the actual cadre had been 135 and as such the vacancies and the excesses stood at 27 and 11 respectively. The Chairman had informed me that, out of the excess cadre, 9 posts were personal to holder basis.

(b) Even though a qualified Legal Officer from whom the service as a Secretary of Company could be obtained was serving in the institution, an external person had been recruited as a Secretary of Company on 28 February 2016 and a sum of Rs.219,050 had been paid for the year 2016/2017 in this connection.

**5. Accountability and Good Governance**

**5.1 Budgetary Control**

Variances ranging from 21 per cent to 368 per cent were observed between the budgeted and the actual income and expenditure of 53 items in the year under review, thus it was observed in audit that the budget had not been made use of as an effective instrument of management control.

**6. Systems and Controls**

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

| Areas of Systems and Controls | Observations |
|---|---|
| (a) Financial Control | (i) Failure to maintain accounts so as to obtain the information on credit sales, cash sales and returns made during the period.<br><br>(ii) Failure to maintain a formal cash book and non-preparation of Bank Reconciliations in a timely manner. |
| (b) Sales Control | Credit sales of fertilizer had been made without checking the possibility of recovery. |
| (c) Stock Control | (i) Failure to implement an internal control on receipts, issue and classification of stocks and failure in taking action to identify the slow moving, immovable and damaged stocks.<br><br>(ii) Non-reconciliation of the value of 52 items and closing stock balance pertaining to stationery and other stocks. |
| (d) Accounts Control | (i) Failure to obtain insurance coverage for the mitigation of risks.<br><br>(ii) Failure to confirm the accuracy of transactions due to the complicated accounting system as a result of non-utilization of a suitable electronic accounting system. |