Land Reclamation and Development Company Limited - 2019

1.1 Qualified Opinion

The audit of the financial statements of the Land Reclamation and Development Company Limited for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 and the statement of comprehensive income**,** statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, 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 provisions of the National Audit Act No. 19 of 2018. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the accompanying financial statements give a true and fair view of the financial position of the Company as at 31 December 2019, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Qualified Opinion

My opinion is qualified on the matters described in paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Company.

1.4 Scope of Audit (Auditor's Responsibility for the Audit of the Financial Statements)

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.

- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company;

- Whether the Company has performed according to its powers, functions and duties; and

- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Financial Statements

1.5.1 Non – Compliance with Sri Lanka Financial Reporting Standards for Medium and Small sized Entities (SLFRS for SMEs)

	Non compliance with reference to the relevant standard	Management Comment	Recommendation
(a)	The income and expenditure of the construction contracts of the Company had not been identified according to the completion of contract method. Hence, identification of construction income amounting to Rs.127.46 million had not been complied with section 23.17 of the SLFRS for SMEs. As a result, the contract income for the year under review amounting to Rs.127.46 could not be identified according to the standard.	According to section 23.17 of the standard, revenue had been accounted based on the value of works certified by the client.	According to the SLFRS for SMEs, the contract income should be identified based on the value of the works certified by the client.
(b)	According to section 13.4 of the SLFRS for SMEs, the stock should be valued for lower of cost or net realizable value (NRV). However, without being considering the NRV, the stock of the Company held as at end of the year under review had been valued at cost for Rs.13.63 million.	All stock records had been kept under FIFO method. When it value the stocks based on Net Realizable value (NRV) and cost, the cost of the stocks was below the NRV. Hence, the stocks had been valued based on the cost.	According to the SFRS for SMEs, the value of the stock should be accounted.

(c)	Contrary to section 25.2 of the SLFRS for SMEs, the interest paid by the Company on the loan of Rs.200 million obtained from the Sri Lanka Land Development Corporation amounting to Rs.22.17 million had been capitalized without recognizing as an expense.	The loan amounting to Rs.200 million form the Sri Lanka Land Development Corporation (SLLDC) had been obtained for the sand project of the REDECO Ltd. Hence, the interest for the loan had been debited to this project and that amount had been shown under the work– in– progress. After being completed the project, that interest expenses will be adjusted to the income.	According to the SLFRS for SMEs, the interest should be accounted.
(d)	According to section 2.26(b) of the SLFRS for SMEs the identified losses should be charged to the income statement, However, the losses on unsuccessful contracts amounting to Rs.30.82 million, relating to the contracts conducted by the Company during the period of 2012-2018, had been accounted as work-in-progress instead of being written off as a loss. As a result the profit for the year had been overstated by that amount.	Until finalize the problems in the questionable contracts, which had been identified during the period 2012-2018, had been accounted for as work – in – progress. That will be adjusted to the profit and loss account in 2020.	According to the SLFRS for SMEs, the assets should be correctly classified.
(e)	According to the SLFRS 01 for SMEs, the current and non – current liabilities should be separately shown in the financial statements. However, the leasing instalments to be payable with in next year amounting to Rs.4.9 million, had been shown in the financial statements as non – current liabilities. As a result, non – current liabilities had been understated by Rs.3.57 million.	The adjustment will be made in 2020 as current and non current liabilities.	According to the SLFRS or SMEs, the liabilities should be correctly classified.

1.5.2 Accounting Deficiencies

	Audit Observation	Management Comment	Recommendation
(a)	The cement block machine had been purchased by the Company on 15 July 2015 on finance lease for Rs.4,508,000 had not been utilized even at the end of the year under review due to the defects of the machine. However, impairment loss of the asset had not been identified.	The current book value of the machine was lower than the market value. Hence, the impairment losses had not been calculated.	The impairment losses of the machine should be identified.
(b)	Due to accounting errors, the contract expenses incurred for the year under review amounting to Rs.18.67 million had been accounted as a work-in-progress. Hence, the contract expenses had been understated by amount. It was observed in audit that the identified loss of the contract amounted to Rs.4.09 million for the year under review would be Rs.22.76 million for the year under review.	Due to the issues revealed in bills, those values had been accounted under the work – in – progress. After being finalized the related issues, the adjustments will be made to the financial statements.	The contract expenses should be correctly shown in the financial statements.

1.5.3 Lack of Evidence for Audit

Item	Amount (Rs.million)	Evidence not made available	Management Comment	Recommendation
Contract advances	25.68	Balance Confirmations	The written requests had been made to the contract debtors to furnish the balance confirmations	The letters of balance confirmations should be furnished to audit

1.5.4 Related parties and disclosure of related party transactions

	Audit Observation	Management Comment	Recommendation
(a)	According to the financial statements of the Sri Lanka Land Development	The reason for this difference between those	The transactions between the parent

	Audit Observation	Management Comment	Recommendation
	Corporation, the amounts receivable and payable from/to the company amounted to Rs.539.07 million and Rs.49.34 million respectively. However, as per the financial statement of the Company, corresponding payable and receivable balances amounted to Rs.524.12 million and Rs.54.6 million respectively.	balances, was that not included the current account balances to thereto.	company and the subsidiary should be correctly shown in the current accounts.
(b)	Even though the loan obtained from the parent Company, SLLDC, had been shown in the financial statements of the Company as Rs.224 million, as per the SLLDC's record it had shown as Rs.200 million. Thus, a difference of Rs.24 million was observed between those two values.	The reasons for the difference was that shown the temporally loans given by the SLLDC, under the long term loans.	The transactions between the parent and subsidiary companies should be correctly recorded in the current accounts.

1.6 Accounts Receivable and Payable

1.6.1 Receivable Amounts

	Audit Observation	Management Comment	Recommendation
(a)	The receivables from trade debtors as at end of the year under review amounted to Rs.83,032,226. Out of that amount, sums of Rs.68,324,906, Rs.6,260,395 and Rs.844,692 were remained as unrecovered less than one year, a period ranging from 1 to 5 years and for over more than 5 years respectively.	Actions have been taken to recover the debtor balances.	With a view to strength the cash flow of the Company, action should be taken to recover the debtor balances.

1.6.2 Amounts Payable

	Audit Observation	Management Comment	Recommendation
(a)	The payable mobilization advances as at end of the year under review amounted to Rs.63,372,293. Out of that payables, the payable advances for over a period from 2 to 5 years amounted to Rs.10,376,180 and the advance payable balances over 5 years amounted to Rs.27,744,848.	After being furnished the bills by client's institutions, action will be taken to settle the mobilization advances.	Action should be taken to settle the payable advances as soon as possible and non – liable balances should be written-off to the income.

	Action had not eighter been taken to make the settlement or to write back to the income, the mobilization advances amounting to Rs.12,630,073 related to 11 abandoned projects.		
(b)	The creditor balance as at end of the year under review amounted Rs.72,872,112. Out of that balance, the balance remained as unsettled for a period from 2 to 5 years amounted to Rs.1,685,572 and the balance over 5 years amounted to Rs.11,071,427.	After increase the financial position of the Company up to a favorable level, action will be taken to settle the credit or balances.	The payable advances should be settled as early as possible and action should be taken to write – off the non – liable balances to the income.

1.7 Non – Compliance with Laws, Rules, Regulations and Management Decisions ect.

Reference to Laws, rules, regulations etc.	Non - Compliance	Management Comment	Recommendation
The Public Enterprises Circular No.PED/03/2019 dated 09 December 2019.	The maximum limit of bonus per employee is to Rs.13,500. However, Contrary to that a sum of Rs.43,500 per permanent employee and a sum of Rs.33,500 per casual employee had been paid as bonus exceeding the above limit.	In order to motivate the staff of the Company, this amount of Rs.30,000 had been paid.	The activities should be performed according to the circular instructions.

2. Financial Review

2.1 Financial Results

According to financial statements presented, pre-tax loss of the Company for the year ended 31 December of the year under review amounted to Rs.48.29 million. Compared with the corresponding pre –tax profit for the preceding year amounted to Rs.5.04 million, a deterioration in the financial result amounting to Rs.53.33 million was observed. Compared to the preceding year, decrease of contract revenue by Rs.96 million and increase of financial expenses by Rs.02 million in the year under review were the main reasons attributed for this deterioration in the financial results.

2.1.2 Analytical Financial Review

(a) Even though compared to the preceding year, the contract revenue had been decreased by Rs.96 million, salaries and overtime payments for the contracts had been increased by Rs.5.3 million. As a result of decrease the gross profit

by Rs.13.25 million, the gross profit margin was represented minus 8.8 per cent. As well, the accumulated contribution from all factories was minus of Rs.14 million. That trend had also been attributed for this situation.

(b) The debt turnover and debt collection period were in a week level. Thus, the debt management process of the company was not in a satisfactory level. Since the current ratio of the Company was represented lower than one, it was observed that the Company had faced to working capital difficulties.

(c) The contract creditors of the Company as at end of the year under review was increased by Rs.183 million and the current and quick ratios were 0.85 per cent and 0.64 per cent respectively. As a result, the loan repayable ability of the Company was in an adverse level. Thus, due to not paying to the contractors, many contracts carried out by the Company had been suspended without being completed.

(d) The company had not taking over new construction projects and compared to the preceding year, the income generated from the construction projects and factories had been decreased by Rs.71 million and the operating loss of the Company for the year under review amounted to Rs.49.95 million.

3. Operational Review

3.1 Contribution of the Factories

	Audit Observation	Management Comment	Recommendation
(a)	According to the budget prepared for the year under review, the expected contribution from 8 factories and the workshop amounted to Rs.31.66 million. However, the actual contribution as at end of the year under review amounted to minus Rs.14.26 million.	The demand for the factory products was not in the expected level. As well, the production costs ect, had been increased. Those reasons were attributed for the aggregate contribution be coming to a minus value.	By increasing the contributions from the factories, action should be taken to increase the income of the Company.
(b)	Except the Nawala precast concrete factory, the contribution of 7 factories aggregating to minus of 27.99 million. Decrease of selling prices, not applying	It was unable to reach to the expected targets due to the prevailed unfavorable conditions,	By increasing the contribution of the Company prompt action should also be taken to

Audit Observation	Management Comment	Recommendation
of targeted marketing strategies, management weakness etc. had been attributed for this losses. Further, the expected income from those Sections by the Company for the year under review amounted to Rs.184.87 million. However, the actual income amounted to Rs.87.62 million.	the retreat situation in the construction field etc, the demand for the Company's products were decreased. Hence, it was unable to reach to the targets.	improve the income of the Company.
(c) In order to earn Rs.8.22 million per month, the Company had implemented a project for packeting of sea sands for sale, after incurring Rs.404.40 million. Although the expected sea sand packet productions for the year under were 250,000 packets, the actual production were only 2,648 packets. Hence, an expected profit from the project amounting to Rs.28.60 million could not be gain to the Company. The accumulated losses sustained by the Company from that project as at end of the year under review amounted to Rs.28.27 million. As a result, the Company had failed to repay the loan installments, for the loan obtained from the SLLDC amounting to Rs.224 million, and interest thereon and further, payables to the Corporation of project's buildings amounting to Rs.170 million.	Without being conducted a market survey, the sand packeting and selling project had been started Hence, it is expected to immediate decision on this regard.	Prompt action should be taken to improve the income of the Company, by increasing the contributing the factories of the Company.

3.2 Management Inefficiencies

Audit Observation	Management Comment	Recommendation
The Company had recruited 70 officers as at end of the year under review on behalf of the parent company based on a 5 per cent service income. However, to conduct such man power supplying service had not been approved by the Board of Directors. Further, action had not been taken to amend the Article of Association of the Company by including the function of man power supply.	The approval of the Board of Directors had been obtained for that man power supplying function and a service agreement had also been signed.	The Article of Association of the Company should be amended by including the new business opportunities.

3.3 Staff Administration

Audit Observation	Management	Recommendation
The approved cadre of the Company as at 31 December 2019 was 107 and the actual cadre as at that date was 72. Thus, vacancies existed as at that date were 39 and excess cadre was 04. Out of the 39 vacancies, 04 middle management posts were vacant for over 6 years and 10 Management Assistant posts and 24 Labour posts were also existed as vacant.	Even though there were vacancies in the Company, attention had not been drawn to fill the vacancies due to unfavorable financial position of the Company.	The vacancies existed within the approved cadre, should be filled as early as possible.

3.4 Deficiencies in Procurement Management

	Audit Observation	Management Comment	Recommendation
(a)	The Company had called bids for purchasing of a water treatment Ro plant valued at Rs.7.55 million (with the custom duty) in the year under review, and a bid for US$ 17,340 (Rs.3.12 million) had been received with the expected water capacity of 100,000 litters. However, that bid had been rejected by the Company indicating that insufficient water capacity of the plant. As a result, the Company had incurred a loss of US$ 15,377 (Rs.2.76 million) due to purchase of a machine for US$ 32,717 (Rs.5.88 million) instead of being purchase the machine for US$ 17,340.	The investigations have been conducted to examine the fraudulent activities took place at the purchasing process of the machine.	The Procurement should be conducted in favour of the Company.
(b)	The lowest value of a bid submitted by the local contractors for the construction of sea sand packet manufacturing building amounted to Rs.199.98 million. However, without being evaluated the bids, the construction works had been awarded to the foreign contractors incurring a sum of Rs.265.03 million. Thus, due to selecting of a foreign contractor, an additional amount of Rs.65 million had to be incurred by the Company.	The investigations have been conducted to identify the fraudulent matters connected to that procurement.	The Procurement should be conducted in favour of the Company.

3.5 Deficiencies in Contract Administration

	Audit Observation	Management Comment	Recommendation
(a)	Even though the Company had issued invoices for contracts valued at Rs.298.25 million as at end of the year under review, only a sum of Rs.218.90 million had been received and a sum of Rs.79.74 million to be further receivable. Not obtaining of approval for the additional works done by the Company, not entered into contract agreements and not obtaining the approval for time extensions etc had been mainly attributed for that situation.	The instructions had been given to the officers to avoid such kind of contract administration deficiencies in future.	The contract activities should be completed in timely manner applying an effective contract management system and the receivables from the contracts should be recovered as soon as possible.
(b)	Even though the Company had received 31 contracts during the year under review, out of that, 13 contracts or about 50 per cent of the contracts had been given to sub – contractors, Further, a loss of Rs.3.94 million had been incurred by the Company from 5 sub – contracts during the year under review and profit margin of the other contracts was at below 20 per cent.	Action will be taken to perform the contracts minimizing the contract losses.	The contract activities should be carried out applying an effective contract management system and action should be taken to increase the profitability of the contracts.

4. Accountability and Good Governance

4.1 Presentation of financial statements

Audit Observation	Management Comment	Recommendation
According to the Public Enterprises Circular No.PED/12 dated 02 June 2003, the financial statements of the Company for the year 2019 should be furnished for audit on before 28 February 2020. However, the financial statements had been furnished for audit after delaying more than 10 months on 18 December 2020.	Instruction have been given to the officers to furnish the financial statements on due dates to audit.	The financial statements should be furnished according to the Treasury circular instructions.

4.2 Corporate Plan

Audit Observation	Management Comment	Recommendation
According to the Public Enterprises Circular No.PED/12 dated 02 June 2003, the company had not prepared a Corporate Plan. As well, the Company had not prepared an Action Plan for the year under review. As a result, the performance of the Company could not be evaluated in audit.	Due to failure of conducting the company's functions in efficient manner in the year, a Corporate Plan and an Action Plan had not been prepared. A Corporate Plan and an Action Plan have been prepared now.	According to the Treasury circular instructions, a Corporate Plan and an Action Plan should be prepared.

4.3 Procurement Plan

Audit Observation	Management Comment	Recommendation
Even though the Company had incurred the capital expenditure of Rs.6,260,711 during the year under review, a procurement plan had not been prepared for those procurements as per the instructions given the Government Procurement Guidelines.	Those capital expenditure had not been pre-planned and incurred based on the decision made by then Board of Directors. Thus, Procurement Plan had not been prepared. Action has been taken to correct the above situation.	According to the Treasury circular instructions, a procurement plan should be prepared.