

Colombo Commercial Fertilizer Company Limited – 2019/2020

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Colombo Commercial Fertilizer Company Limited for the year ended 31 March 2020 comprising the statement of financial position as at 31 March 2020 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 to Parliament appears 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 March 2020, 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 Audit Scope (Auditor's Responsibilities 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 scepticism 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 Audit Observations on the preparation of Financial Statements

1.5.1 Non-Compliance with Sri Lanka Accounting Standard

Audit Issue	Management Comment	Recommendation
According to Sri Lanka Accounting Standards No. 02, although the stock should be physically verified and should be valued at less than cost or net realizable value, the accuracy of the stock of chemical fertilizer valued of Rs.278,323,718 which is shown in the statement of financial position could not be verified due to the fact that inability to physically verify certain stocks of fertilizer stored at the Hunupitiya warehouse complex.	Even though the fertilizers are same, the net realizable value of those varies according to the crop used. The company has to sell a 50Kg of bag of other crops fertilizer and 50Kg of bag of paddy fertilizer at Rs.1,000 and Rs.500 respectively according to the circular issued by the Fertilizer Secretariat. Therefore, the net realizable value of fertilizers used for paddy fields is different from the net realizable value of same type of chemical fertilizer used for other crops. The General Treasury also subsidizes money to our company based on that difference. Accordingly, stocks were valued as 02 items in accordance with Accounting Standard No. 02.	It should be complied with Sri Lanka Accounting Standards.

1.5.2 Accounting Deficiencies

Audit Issue	Management Comment	Recommendation
(a) Fertilizers which purchased directly by the company are subjected to various processes within the company such as marketing, mixing, processing in to small packet, repackaging and switching among each category. Although the closing stock has been calculated by including the figures that was subjected to the aforesaid processes in relation to the fertilizer which purchased directly during the financial year, the profit for the year under review had been understated by Rs.2,094,550 approximately due to a stock shortage of 41.891 metric tons of fertilizer identified in the stock count had not been adjusted to the cost of sale of Rs.1,182 million.	Agreed with the audit observation. Further study will be done and action will be taken to submit the information in proper manner to the next audit.	Action should be taken to adjust the stock shortages when calculating the cost of sale.
(b) The total value of non-current assets had been increased by that amount due to the land where the head office is located had been revalued to Rs.90,000,000 and reported as Non-Current assets in the financial statements without having any legal acquisition to the Company.	A committee consisting of representatives from the Treasury had been appointed to prepare the initial statement of financial position of the company, at the time the company was taken over back to the government in 1997. The committee had been valued the land at Rs.90,000,000 and included it in the statement of financial position when determine the assets and liabilities. Although the aforesaid land was previously owned by the company, at the time the company taken over by the government, its ownership has been transferred to the Kelaniya Pradeshiya Sabha and later to the Urban Development Authority. Cabinet approval also been granted by now to transfer the ownership of the land to the company.	The legal ownership of the land should be transferred to the company and stated in financial statements.

1.5.3 Unauthorized Transactions

Description of Unauthorized Transaction	Management Comment	Recommendation
The company had been paid Rs.4,926,394 of holiday allowances to company employees for the short leaves and medical leaves saved by the employees of the company and Rs.847,427 of executive allowances for executive officers without approval of the Treasury.	The company had been paid allowances to permanent employees of the company for medical leaves not taken by the employees by using the company's funds for a longer period of time with the director board approval	These payments should be considered as non-legal allowances.

1.6 Accounts Receivable and Payable

1.6.1 Receivables

Audit Issue	Management Comment	Recommendation
(a) The payment had been settled through a short- term loan obtained from the bank due to non-receipt of funds from the General Treasury to pay for the company's fertilizer suppliers on time. Although the short-term loan was later converted into a long-term loan subject to the Treasury's liability, due to the failure in making agreement with the Treasury to recover the interest paid on the short- term loan and failure to incorporate the short term interest in to long term loan, the Rs.158,498,393 short term loan interest which was not guaranteed by the Treasury had been accounted as a balance to be received from the Treasury.	The continued discussions are being done regarding these matters orally and in writing with the Treasury. Action would be taken in the future to obtain this amount.	Action should be taken to ensure the accountability from the General Treasury.

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| <p>(b) The trade debt balance of Rs.4,993,147 due from Ceylon Fertilizer Company as a current asset from the previous year had not been recovered during the year under review either.</p> | <p>The trade debt balance due from Ceylon Fertilizer Company is a balance existing since 2007 and The Audit and Management committee of the Ministry has also discussed this matter and requested that action be taken to pay the above balance to our company. Although the company has informed the Ceylon Fertilizer Company about this on several occasions nevertheless, no action had been taken to pay. Further action would be taken in this regard by contacting the ministry in the future.</p> | <p>Action should be taken to recover the debtor balance.</p> |
| <p>(c) The company had failed to recover the balance of sundry debtors of Rs.5,047,893 also during the year under review which had been as a current asset since 2014/2015.</p> | <p>This is also a balance which has been since year 2006 and it is a balance that occurred at the beginning of the Subsidized Fertilizer program. Since no proper response had been given even, the relevant parties had been informed about the balances on a number of occasions, it would be expected to further actions and the customers who have already taken legal action are also represented in this balance.</p> | <p>Action should be taken to correctly identify the balance of sundry debtors and recover.</p> |

1.6.2 Payables

Audit Issue	Management Comment	Recommendation
<p>The total value of Rs.3,600,816 which was accounted as the accrued expenses in previous years had not been settled by the end of the year under review.</p>	<p>Agreed with the audit observation and corrections were made by Journal No. J/MAR/AQ-sub (07) for Rs.728, 003.19 and also the financial statements were revised. However, it would be mentioned that the payments are to be</p>	<p>Accrued expenses should be properly accounted and settled within the relevant period.</p>

made in the future to the following institutions.

Link Interiors Pvt Ltd - Rs.338,989.28
 Science Land - Rs.275,000.00
 Information Technology
 Architrend - Rs.2,258,823.1
 Consultant

1.7 Non-compliance with Laws, Rules, Regulations and Management Decisions etc.

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) National Building Tax Act No. 09 of 2009	A penalty of Rs.675,558 had been paid in the year under review for the last quarter of 2016 and the first 02 quarters of 2017 as per the Income tax assessment due to non-payment of National Building Tax as scheduled.	This penalty had to be paid since delays in paying taxes on it due to document on sales status of regional warehouses were received late to the head office, a support of courier service had been received to obtain documents twice a month from local warehouses for overcome this default and the information is now duly forwarded to the Head Office. Therefore, the necessary action had already been taken to prevent this problem in the future.	Actions should be done in accordance with the relevant Act.
(b) Paragraph 5.1 of Chapter 06 of the Code of Conduct for Good Governance in Public Enterprises issued with Public Enterprises	Although the all public companies were required to prepared and submit the financial statements to the Auditor General within 60 days of the end of the financial year, the	This issue was arisen due to the fact that the curfew has imposed 03 consecutive months following the outbreak of the Covid 19 pandemic situation in the country which started in March 2020 and having to maintain a minimum	An action should be made to submit the financial statements to the Auditor General in accordance with the provisions of Circular.

	Circular No. PED/12 dated 02 June 2003.	financial statements had been submitted to the Auditor General after 200 day of the end of the financial year.	number of staff in the company as per the health guidelines.	
(c)	Paragraph 8.3.3. of the Code of Conduct for Good Governance in public Enterprises issued with Public Enterprise Circular No. PDE/12 dated 02 June 2003.	Incentive of Rs.15,806,604 had been paid to the employees during the year under review without any formal approval as per the incentive scheme approved by the General Treasury and the National Salaries and Grants Policies.	The company had been making incentive payments to the permanent employees for a long time and incentive payments had also been making incentive payments subject to the Director Board approval during the year under review. However, the Treasury approval has now been obtained for these incentive payments.	These payments should be considered as non-legal allowances.
(d)	Circular No. PED/1/2015 dated 25 May 2015 and Paragraph No. 3 of Circular No. PED/1/2015(i) dated 25 October 2016.	On the decision of the Board of Directors, total of Rs.600,000 had been given to the 05 middle-level managers who do not covered by the circular as Rs.10,000 vehicle allowance per each officers by exceeding the provisions of Circular.	This allowances had been given considering the methodology adopted by the Ceylon Fertilizer Company on the decision of the Board of Directors due to the practical difficulties in providing group transport facilities to the middle-level managers according to the Paragraph No.04 of Enterprises Circular PED 1/2015 dated 2015 May 25, and the high cost involved.	These allowances should be considered as non-legal expenditure.

1.8 Cash Management

	----- Audit Issue -----	----- Management Comment -----	----- Recommendation -----
(a)	Due to the failure in proper working capital management during the financial year, it had been incurred an unavoidable loan interest of Rs.2,109,634 for a	The company has issued fertilizer on credit basis to the Agrarian Service Centers in order to provide fertilizer in free of charge to the farmers with the change in the methodology of the Subsidized Fertilizer Programs. The payment for this will be made by Department of Agrarian Development and it	The actions should be taken to minimize the interest on loans.

bank overdraft of
Rs.78,269,924.

will take more time. However, the stock of imported fertilizer should be cleared on time and it should be delivered to the Agrarian Service Centers on time. And also there is a huge cost involved with it. Then this problem arises due to non-receipt of funds from the General Treasury and the Department of Agrarian Development at the right time. The company has been able to reduce the interest expenses due to obtained the overdraft facilities by pledging company's fixed deposits to meet the working capital requirements for clearance and distribution of stock of fertilizer on time as per the decision of the Board of Directors.

If not, a bank loan facility will be required to meet by the company to fulfill the above working capital requirements and a higher interest rate will be charged. Interest on the bank overdraft is charged only on the value of the overdraft facility that we used and its interest rate will be only 2% higher than the fixed deposit interest rate. That is 12.75% and the fixed deposit interest rate is 10.75%. Also it would like to mention that, if the company gets a bank loan facility at this moment, company will have to pay an interest rate of around 14.5%. Otherwise we have to clear the

fixed deposits of the company before maturity. There is also an additional cost involved in clearing before maturity. That is to say, if the fixed deposit initiated at an interest rate of 10.75% is cleared before maturity, there will be a reduction of about 5%.

When considering above situations, the most appropriate procedure is to obtain a working capital requirement by securing a fixed deposit and obtain an overdraft facility. The relevant work can be done at lowest interest expenses.

(b) The suppliers had supplied fertilizer at Rs.6,642,835 less than the order and that amount had been

Agreements are entered in to considering the probability of a shortage or excess quantitative variation of 5% in the importation of fertilizer. Accordingly letters of credit are opened based on the value and

Only the amount of fertilizer received should be taken into account.

accounted as refundable from the suppliers and company had to paid to the supplier by short-term bank loan and an additional loan interest expense was incurred.

size of the invoice issued. It is also emphasized that there is no possibility to revising the value of letters of credit once the relevant orders have been cleared from the port and necessary actions will be taken to formally address this issue in the future.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs.162,858,311 and the corresponding profit in the preceding year amounted to Rs.147,640,231. Therefore, an improvement amounting to Rs.15,218,080 of the financial result was observed. The reasons for the improvement was the decrease in the income tax expenditure.

3. Operational Review

3.1 Management Inefficiencies

	Audit Issue	Management Comment	Recommendation
(a)	Action had not been taken to prevent avoidable administrative, operational and transportation cost which arise due to the fact that the company maintains 13 warehouses in various areas of the island without establishing a low-cost distributing system and without recognizing the need for warehousing	These warehouses are being used to implement the Government Fertilizer Subsidy Scheme and these warehouses facilitated to distribute the fertilizer at right time without shortage. These regional warehouses are specially useful to overcome the difficulties in obtaining the necessary transport facilities to meet the huge demand that arise in a very limited period of time with the starting of the Yala and Maha seasons. Also all these warehouses are located near the Agrarian Service Centers which are entrusted with the task of distributing fertilizer to our company.	Action should be taken to establish an effective and efficient distribution system.
(b)	The approval of the National Fertilizer Secretariat had not been received for the issuance of 3,575 metric tons of TPS (due to failure of laboratory reports) related to 06 letters of credit imported during the	This stock of fertilizer was imported with an intention of distributing it during the Maha season and requested to obtain a sales license after the clearance of the stock of fertilizer. However, issuance of fertilizer was delayed due to the continuous delay in obtaining the sales license and as a result there was a severe shortage of fertilizer in the country.	Fertilizer should not be distributed among farmers without the approval of the National Fertilizer Secretariat.

financial year to the farmers. However, before the release of the laboratory reports, the company had distributed the above stocks of fertilizer to the farmers without approval. Although the National Fertilizer Secretariat did not recommend the payment of fertilizer subsidy for aforesaid stocks of substandard fertilizer distributed to farmers by Colombo Commercial Fertilizer Company, the company had taken actions to make payment for the fertilizer on the due date by the short-term bank loan and convert it into a long-term loan with the Treasury liability and obtain the subsidy without formal approval.

Accordingly, action was taken to distribute this stock of fertilizer in consultation with the National Fertilizer Secretariat and based on the prior approval given by the National Fertilizer Secretariat to bring this stock of fertilizer to the port of Colombo according to the quality certificate issued by an internationally recognized laboratory when loading the relevant stock of fertilizer with the intention of preventing the occurrence of farmer's agitation and in order to stop the government from causing great inconvenience.

3.2 Operational Inefficiencies

Audit Issue	Management Comment	Recommendation
<p>Since the distribution by free of charge during the year of a damaged fertilizer of 369 metric tons which was arise due to failure in distribution of subsidized fertilizer stocks with proper management, the company has incurred loss of Rs.22,140,000.</p>	<p>The 369 of metric tons of damaged fertilizer was distributed free of charge during the year under review. This free distribution was made only for government institutions with the instructions of the Secretary of the Ministry dated 21 May 2019 and the approval of the Board of Directors held on 30 May 2019.</p> <p>It is also informed that this stock of fertilizer is not a stock caused by stock damage and there was no loss to the company or the government and such stock of fertilizer has been accumulated in the company due to the following reasons.</p>	<p>Action should be taken to distribute subsidized fertilizer stocks of the government with proper management.</p>

- Damage to imported stocks.
Fertilizer were damage due to various reasons (mechanical and climatically etc.) such as fertilizer become wet, become heavy granules, fertilizer discoloration, etc. during the voyage of the ship from the loading port to the Colombo port. The financial loss will be recovered from the supplier and the damage stock will be taken to the inventory books as Sweeping stock of fertilizer.
- The fertilizer scattered on the deck when unloading imported fertilizer i.e. unpacked fertilizer (bulk) from the ship to the packaging machines or when unloading packaging fertilizer from the ship in to the lorries is collected and packed in unmarked bags and delivered to the warehouses and after that added to the Sweeping stock of fertilizer.
- The fertilizer scattered on the deck of lorries when transporting fertilizer from the port to the central warehouse are added to the Sweeping stock of fertilizer after wiping, collecting, packaging and weighing.
- A certain amount of scattered fertilizer on floor which is unusable due to the use of hooks during unloading and loading of bags fertilizer is added to the stock as Sweeping stock of fertilizer. There was no stock damage in here due to the bags contain more fertilizer than the net weight of the bag often.

3.3 Idle or underutilized Property, Plant and Equipment

Audit Issue	Management Comment	Recommendation
Although the total amount of initial expenditure including consultancy fees for the construction of warehouse on the lease land of the Hambantota district was Rs.3,732,901 including the Rs.3,534,711 in the previous years and Rs.198,190 in the year under review as accounted as capital in working progress, the above expenses had become an idle cost due to the non-construction of warehouse on the relevant land.	Although it has been proposed to construct the warehouse complex on this land according to a plan to import chemical fertilizer by using the Hambantota port, this project has been temporarily stopped until the practical problems that arise in importing fertilizer from Hambantota are resolved. It is hoped to implement the project which is currently being planned in line with the policy decisions of the government and therefore cost incurred at present will be applied to the project in the future.	A feasibility study should be done before starting a project.

3.4 Human Resources Management

Audit Issue	Management Comment	Recommendation
An officer had been appointed for acting in the post of Marketing Manager with effect from 04 April 2016 (until the end of the year under review) without functioning to appoint a qualified officer for Marketing Manager which remained vacant from the year 2016.	Although the post of Marketing Manager had been vacant since 2016, it was not possible to recruit an officer due to the suspension of the officer who was working in the post and internal investigation was being carried out. After resolving this issue, even though a number of advertisements had been published for the recruitment of a new Marketing Manager in several instances, an officer who had fulfilled qualifications had not applied. Action is being taken again to invite applications to recruit a qualified officer.	Action should be taken to fill the vacancies in the approved posts.