Lakdiva Engineering Company (Pvt) Ltd and its affairs - 2020

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1. Financial statements

1.1 Qualified Opinion

The audit of the financial statements of the Lakdiva Engineering Company (Pvt) Ltd for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the statement of comprehensive income, statement of changes in equity and cash flow statement and notes to financial statements for the year then ended 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 presented in Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the financial statements give a true and fair view of the financial position of the Company as at 31 December 2020, and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Qualified Opinion

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

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuS). 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 determines 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 Sub-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 the Audit (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:

- Appropriate audit procedures were designed and performed to identify and assess the risk of material misstatement in financial statements whether due to fraud or errors in providing a basis for the expressed audit 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.

- An understanding of internal control relevant to the audit was obtained in order to design 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. 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 relating to the Preparation of Financial Statements

1.5.1 Non-compliances with Sri Lanka Accounting Standards

Non-compliance with Reference to the Relevant Standard	Comment of the Management	Recommendation
The year of purchase had not been mentioned with respect to the assets worth Rs. 8,290,423 included in the balance of fixed assets totaling Rs. 27,075,878 as at 31 December 2020. As no depreciations had been made on those assets up to the year under review in terms of Sri Lanka Accounting Standard 16, the profit of the year under review had been overstated by that value.	Those assets will be revalued in the year 2021, thus taking action either to record such values in the books or not.	Assets should be depreciated correctly in accordance with the accounting standards.

1.5.2 Accounting Deficiencies

	Audit Observation	Comment of the Management	Recommendation
(i)	According to the statement of financial position, the value of cash and cash equivalents amounted to Rs. 4,575,531 as at 31 December 2020, but the same had been shown as Rs. 2,575,531 in the cash flow statement thus observing a difference of Rs. 2,000,000. This difference had been caused by the failure in showing the Government grants of Rs. 2,000,000 under the funds generated through financial activities in the cash flow statement.	The sum of Rs. 02 million had been adjusted to the cash and cash equivalents as at 2020.12.31.	The cash flows should be brought to accounts properly.

(ii)	It was found in the annual survey conducted in the year 2020 that 86 items valued at Rs. 1,400,559 had been shown in excess of the balance of the books whereas 51 items valued at Rs. 244,631 had been understated.	Despite not being brought to the books at the annual survey of stores conducted by the end of the year 2020, the relevant Board of Survey had brought them to the books in view of being used in the manufacturing process or dispose in due course.	Annual surveys of stores should be conducted properly thus making adjustments in the books.

1.6 Non-compliances with Laws, Rules, Regulations and Management Decisions

	Reference to Laws, Rules, and Regulations, etc.	Non-compliance	Comment of the Management	Recommendation
		Rs.		
(i)	Section 23 (a) of the National Environmental Act, No. 47 of 1980 as amended by the Act Nos. 56 of 1988 and 53 of 2000.	Institutions servicing vehicles should obtain a license, but the Company had not taken action even by 31 December 2020 to obtain such a license.	Action will be taken in due course in accordance with the relevant Laws, and Rules.	The Laws, and Rules relating to the environment should be followed.
(ii)	Section 60 of the Inland Revenue Act, No. 24 of 2017.	A company is liable to pay income tax, but it was observed that the Company had not taken action even up to the date of audit on 31 December 2020 to fulfill that requirement.	The relevant Laws and Rules will be followed in due course.	Liability to tax should be fulfilled in terms of the Inland Revenue Act.
(iii)	Public Enterprises Circular, No. PED/12, dated 02 June 2003.	A sum of Rs.1,839,840 had been paid during the year under review as incentives without adhering to an incentive scheme approved by the Treasury and the Board of Directors. Furthermore, a sum of Rs.795,600 included therein had been paid to the staff of the factory by disregarding the failure to meet the time based target.	The relevant Laws and Rules will be followed in due course.	Incentives should be paid under approval of the Treasury through a proper evaluation.

(iv)	Factories (Amendment) Act, No.33 of 2000 Section 39(1)	Fire exit should be provided for the persons employed in the factory. However, it had not been done so.	The relevant Laws and Rules will be followed in due course.	Provisions of the Factories Ordinance, should be followed.
	Section 42 a (1).	Every factory should be equipped with fire extinguishers in accordance with the directives relating thereto, but the Company had not complied to any of those necessities.	The relevant Laws and Rules will be followed in due course.	Provisions of the Factories Ordinance, should be followed.
(v)	Guideline 3.2 (Procurement Guidelines 2006)	Spare parts worth Rs.74,935,429 had been purchased from private companies during the year under review for repairs of the busses without taking action to evaluate bids through national competitive bidding.	The relevant Laws and Rules will be followed in due course.	Purchases should be made in accordance with the Procurement Guidelines.
	Guideline 3.4.3	Registration of suppliers should be done for Procurement of items of small value or for purchases of items used frequently, for which advertising may be uneconomical, thus preparing a list comprising names of suppliers who are able to supply particular categories of Goods and Services. However, it had not been done so.	The relevant Laws and Rules will be followed in due course.	Procurement of items should be done in accordance with the Procurement Guidelines.
	Guideline 4.2	Action had not been taken to prepare a Master Procurement Plan and a Procurement Time Schedule.	The relevant Laws and Rules will be followed in due course.	Procurement activities should be envisaged in accordance with Circulars.

2. Financial Review

2.1 Financial Results

The operating result of the year under review was a loss of Rs. 26,326,283 as against the profit of the preceding year amounting to Rs. 23,956,337, thus observing a deterioration of Rs. 50,282,620 in the financial result. This deterioration had mainly been attributed by the decrease in operating revenue by a sum of Rs. 57,275,145 and the cost of sales being decreased only by a sum of Rs. 5,415,376 as compared to the preceding year.

2.2 Analysis of Trends in the Main Items of Revenue and Expenditure.

- The operating revenue had decreased by 31 per cent whereas the cost of sales had decreased by 05 per cent in the year under review as compared to the preceding year.

- The value of other revenue of the Company had decreased by 80 per cent in the year under review as compared to the preceding year.

2.3 Ratio Analysis

- Current ratio of the year under review was 0.30 as compared to that of the preceding year being 0.25.
- Gross profit ratio of the year under review was 05 per cent which was observed to have been a decrease by 26 per cent as compared to that of the preceding year being 31 per cent. Increase in the cost of sales had mainly attributed to that deterioration.

3. Operating Review

3.1 Operating Inefficiencies

Audit Observation	Comment of the Management	Recommendation
A number of 106 busses had been sent for repairs in the year 2020, but 27 of those busses had remained parked without being repaired over a period of 03-09 months up to 18 March 2021, and that represented 25 per cent of the busses sent for repairs. Repairs on the rest of the 79 busses had been completed though, a period ranging from 02 months to 01 year had been spent with labor on repairs obtained on contract basis.	Penalties for delay at Rs. 1,000 per day will be charged with effect from the year 2021.	Contracts should be completed within the specified duration.

3.2 Management of Procurements

Audit Observation	Comment of the Management	Recommendation
The main bin cards maintained at the Procurement Division had not been updated, and maintenance of stocks for regularly used items had been neglected, thus paving way for the lack of buffer stocks. As such, instant purchases had been made to the value of Rs. 38,348,373 which was attributable to the 80 per cent increase in the total purchases. Furthermore, it was observed in examining the bin cards that action had not been taken to eliminate a stock of 90 items no more in use.	The manufacturing process could not be continued properly with enough buffer stocks owing to the spread of pandemic in the year 2020. However, action will be taken correctly in due course.	Stock control should be done properly, and bin cards should be maintenance accurately.

3.3 Human Resource Management

	Audit Observation	Comment of the Management	Recommendation
(i)	The approved cadre of the Company was 121 as at 31 December 2021, and 96 employees of them had been recruited permanently whereas 12 had been recruited on contract basis. The chief managerial post of General Manager had not been included in the approved cadre of the Company, and recruitment to the post of Factory Engineer had also been done on contract basis. Although 06 posts of Foreman had been approved for the Company, 03 of them remained vacant up to February 2021.	Necessary recruitments will be made in accordance with financial position of the Company as soon as the Scheme of Recruitment for the Company is approved.	Vacancies should be filled in a suitable manner.
(ii)	Approval on the new structure of employees had been granted through the Letter, No. DMS/1623 of the Department of Management Services dated 03 October 2018. However, action had not been taken even up to the end of the year under review to prepare and approve the Scheme of Recruitment.	Action will be taken to obtain approval for the Scheme of Recruitment in the year 2021.	The Scheme of Recruitment should be prepared and approved.
(iii)	Covering appointments had been given on 04 posts of the Company over extensive periods without taking action to recruit officers permanently. Furthermore, 20 laborers had been approved though, the actual number of laborers was 62. As such, 42 laborers had been recruited in excess of the approved number.		Permanent appointments should be made to the relevant posts.

4. Accountability and Good Governance

4.1 Corporate Plan

Audit Observation	Comment of the Management	Recommendation
Section 05 of the Public Enterprises Circular, No. PED/12, dated 02 June 2003 requires that a Corporate Plan be prepared for a period not less than 03 years in order to achieve the vision and mission of the Company. Nevertheless, a Corporate Plan had not been prepared by the Company.	Not commented.	The Company should prepare a Corporate Plan in terms of the Circular.

4.2 Internal Audit

Audit Observation	Comment of the Management	Recommendation
And Internal Audit Unit had not been established for the Company.	Not commented.	An Internal Audit Unit should be established.