**Lanka Coal Company (Private) Limited - 2021**

## 1. Financial Statements

### 1.1 Qualified Opinion

The audit of the financial statements of the Lanka Coal Company (Private) Limited ("Company") for the year ended 31 December 2021 comprising the statement of financial position as at 31 December 2021 and the statement of profit or loss and other 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 2021, 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 Standards

| Non Compliance with the reference to particular Standard | Management Comment | Recommendation |
|---|---|---|
| According to the paragraph 88 of the Sri Lanka Accounting Standard on Income Tax (LKAS 12), with regard to the value added tax assessments, a sum of Rs.287,139,348 relating to additional tax payable, and a sum of Rs.220,628,092 relating to penalty payable thereon for the years of assessment 2017/2018 and 2018/2019 had not been disclosed in the financial statements. | LCC has submitted the 04 amended VAT returns to IRD along with the appeals for value added tax assessment received and negotiation is going on for same. First meeting was successfully done dated 06/06/2022 with assistance of the Tax consultant. If necessary as per the Sri Lanka Accounting Standards, disclosure will be made in next financial year. | Should be complied with the provisions of the accounting standard. |

### 1.5.2 Accounting Policies

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| When importation of coal, a mark-up of 10 per cent, which had not been actually incurred, had been added to the value at the point of the Customs as a notional adjustment in ascertaining the value for the Custom purpose. The Company had added a 10 per cent mark-up amounting to Rs.5,324,423,778 to the revenue, and later, that amount had been recognized as discounts to the debtors and adjusted to the cost of sales. As a result, the cost of sales and revenue had overstated by similar amount. | LCC was given a directive by Inland Revenue Department (IRD) to add the customs margin to cost in the issuance of VAT invoices to CEB. This pricing mechanism was adopted following a meeting held in the ministry on 28th June, 2018 with the attendance of an official from Inland Revenue Department (IRD). IRD official is on record and minuted having told that LCC's base value for VAT on invoices to CEB cannot be less than the value for customs purposes. The 10% is, therefore, added solely on the directive of IR official. CEB has challenged the directive and written to IR by their letter dated 2018.09.07 to which the response is yet to be received. | The Company should take immediate action to receive the IRD directions on the matter. |

### 1.5.3 Accounting Deficiencies

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| According to the information made available, it was observed that the Company had paid a sum of Rs. 205,000,000 as penalty to the Sri Lanka Customs due to non-declaration of correct value of the coal imported during the period from 19 September 2016 to 09 April 2018. The penalty payment made in 2019 had been accounted for under the Sri Lanka Custom VAT payable account, VAT control account and CSCL liability account instead of being accounted as expenditure in the respective years. As a result, the retained earnings had overstated by Rs.205,000,000, and the Sri Lanka Custom VAT account, VAT control account and CSCL liability account had understated by Rs.158,186,165, Rs.39,970,418 and Rs.6,843,417 respectively in the year under review. | As per the investigation done by Sri Lanka Customs, Lanka Coal Company has not declared the correct transaction values of the coal imported during the period from 19/09/2016 to 09/04/2018. During that time, the custom declaration totally handled by Ceylon Shipping Corporation (CSC) for a charge of Rs.1,000,000/- per shipment and S.L Customs had imposed a forfeiture of Rs.205,000,000 to LCC on above wrong declaration. The investigation officers of S.L Customs had informed to LCC Officers that no any final VAT payment to be done after this payment. CEB is currently working on the aforementioned payable to LCC, which will be finalized in the near future. Further LCC has identified the actual penalty Rs.6,843,417.00 due to above wrong declaration and debited against CSC liability. | The Company should record this payment as penalty expenses and obtain approval from Board of Directors for this payment. |

### 1.5.4 Unreconciled Control Accounts or Records

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| There was an unidentified difference amounting to Rs.4,003,372 between the balance shown as payable to Ceylon Shipping Corporation in the financial statements of Lanka Coal Company (Private) Limited and the balance confirmed by the Ceylon Shipping Corporation as receivable from Lanka Coal Company (Private) Limited as at the end of the year under review. However, the Company had not taken proper actions to reconcile the difference. | The LCC and the CSC are currently in discussions to resolve the existing discrepancies and unidentified differences in the year end balances as of 31 December 2021. | Company should recognize the unidentified difference and record accordingly. |

### 1.5.5 Unauthorized Transactions

| Description of unauthorized transaction | Management Comment | Recommendation |
|---|---|---|
| The Company had paid a sum of Rs.136,236,370 as Custom VAT for the Shipment No. 123. However, according to the Cusdec, the actual VAT amount was only a sum of Rs.106,969,404. Accordingly, it was observed that the Company had overpaid a sum of Rs.29,266,965. | Due to a wrong declaration done by Ceylon Shipping Corporation, Lanka Coal Company (Pvt) Ltd overpaid VAT of Rs.29,266,966 to Sri Lanka Customs for shipment no. 123. LCC has already filed a refund claim, and the Customs Department is working on the appropriate formalities to complete the refund or set off against LCC's outstanding Customs due balances. LCC is holding equal CSC outstanding sum until the refund claim is resolved. | Company should get resolved the matter immediately after negotiating with the IRD. |

### 1.5.6 Suspense Accounts

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| The Company had not taken proper actions to get settled a balance of Rs.33,317,325 relating to the Suspense Account 154 Shipment, and to get recovered a balance of Rs.1,760,500 relating to the Advance Receivable from CEB Proc-Coal as at the end of the year under review. | <u>The contained of beginning balance of the Suspense account:</u><br>Receivable from CEB Rs.4,323,787.00 : Amount left after settlement of the account with CEB in 2017. Being further investigated to ascertain source/origin.<br><br><u>The contained of the amount transferred with in the year 2021: Rs.30,757,506</u><br>The amount to be paid to Mercator was a result of accounting. The relevant amount had already been received from the CEB, but because it had not been reflected in the accounts, it was kept by debiting it to the suspicious account. Being further investigated to ascertain source/origin to clear the suspense account in 2022 financial year. | Company should ascertain the origin of the balances and clear the suspense account. |

### 1.5.7 Inappropriate Valuation or Estimation

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| Management fees amounting to Rs.22,502,205 had been outstanding for over 3 years as at the end of the year under review. However, any provision in this regard had not been made in the financial statements. | According to a meeting held on the 17th of June 2020 at the LVPP Power Plant Manager Office, AGM (G) requested that LCC send a justification letter for the outstanding management fee receivable for the years 2016, 2018, and 2019, stating that "all expenditure was made to the business transaction with CEB." CEB will settle this outstanding after sending the aforementioned letter. | The company should make provisions for long outstanding receivables. |

### 1.5.8 Documentary Evidences not made available for Audit

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| (a) According to the financial statements, VAT and other receivables amounting to Rs.197,452,711 receivable from the CEB as at the end of the year under review had not been confirmed by the CEB. Accordingly, the accuracy and completeness of that amounts could not be ascertained satisfactorily in audit. | LCC requested confirmation from CEB for the Final VAT & Other Receivables equal to Rs.197,452,711 for the yearend audit 2021, but they did not confirm as of finalizing the Financial Statements. CEB is currently working on the aforementioned payable, which will be finalized in the near future, based on ongoing management negotiations. | Company should get resolved the matter immediately after negotiating with the CEB. |
| (b) Balance confirmations and other relevant evidences relating to the verification of Miscellaneous Debtors amounting to Rs.18,075,801, receivables from a private company amounting to Rs.1,115,987, trade creditors balance of same private company amounting to Rs.85,887,776 and SGS charges of 50 per cent receivable from another private company amounting to Rs. 8,048,531 were not made available to the audit. | i. Miscellaneous Debtors Rs.18,075,802<br>Initial investigations revealed that the amount comprises of Rs.17,839,949 of irrecoverable NBT & PAL . Being further investigated to ascertain source/origin.<br><br>ii. Receivables - Rs.1,115,987<br>There is a credit balance for a sum of Rs.85,887,776 for Noble Resources and we will set off this debtor balance against the same.<br><br>iii. Trade creditors-Rs.85,887,776<br>The balance mainly consists of an under drawn amount by the creditor due to expiry of the LC validity period. | Company should ascertain the sources of the receivable balances, take actions to recover the receivables and should get confirmed the creditors balances and do the needful. |

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| | iv. SGS Charges 50% receivable Rs. 8,048,531 Draft Survey Charges at discharge port for 17 nos of vessels in the season 2015/16 are included. Arbitration process is going on this matter. | |
| (c) Balance confirmations and other relevant documentary evidences relating to a payable balance of Rs.2,362,129 as at the end of the year under review were not made available to audit. | According to the Internal Audit report issued by the CEB Internal Audit branch, the Accounts Payable were caused by incorrect accounting entries made in the years 2018 and prior. We will pass the corrected entries to correct the above error in accordance with the recommendations made by the CEB Internal Audit branch. | Management had commented on a payable balance not included in the audit observation and Company should ascertain the origin of the balance. |
| (d) The Company had not taken appropriate actions to get recovered a long outstanding balance of Rs.539,192,079 receivable from Taurian Iron and Steel Company Ltd (TISCL) through Ceylon Shipping Corporation Ltd (CSCL), and no any provision had been made for impairment. Further, the TISCL/CSCL had not confirmed the due balance. Therefore, it was unable to ascertain the accuracy and existence of the above balance. | A high-level committee handled the Taurian Iron and Steel settlement. The committee has not ruled that the debt is bad, and the buyer has agreed to settle the debt by providing coal. According to information we have, the settlement proposal has been submitted to the Cabinet for consideration. The current status of the outstanding amount receivable from Ceylon Shipping Corporation (Taurian Iron and Steel Company Ltd.) was referred to the Cabinet of Ministers, who appointed a four-member Committee of the Treasury (Chairman), Ceylon Shipping Corporation, Lakvijaya Power Plant, and Lanka Coal Company to negotiate with the Taurian Iron and Steel Company. Furthermore, the Cabinet has advised that the committee's recommendations be submitted to the Cabinet via the Ministry of Ports and Shipping, which has yet to be done. | Company should take actions to expedite the recovery process. |

**1.6 Accounts Receivable**

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| (a) The difference between the balance payable to Ceylon Shipping Corporation as at 31 December 2021 according to the financial statements of Lanka Coal Company and balance confirmed by the Ceylon Shipping Corporation as receivables as | The LCC has not booked many of the disparities for justifiable considerations and has revealed under Note 24 “Contingencies and Commitments”. The LCC and the CSC are in ongoing discussions to resolve those disparities that have been going on for years. | Disparities of long outstanding balances should be resolved and account accordingly. |

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|---|---|---|---|
| | disclosed in Note no. 24 to the financial statements includes long outstanding balances amounting to Rs.141,097,264, which were not resolved by the Company. | | |
| (b) | Long outstanding accumulating vat receivable balance of Rs.1,340,681 as at 31 December 2021, and the company has not taken actions to claim the balance receivable. | This is the amount of input VAT related to local purchases that we can deduct from the output VAT owed to IRD. We disclosed it in the Financial Statements as of December 31, 2021, by deducting it from the balance of the VAT control account. LCC has settled the VAT due to IRD up to the second quota ended on June 30, 2020, by March 30, 2022, and we have transferred the corresponding input VAT to the VAT control account. | Company should take actions to claim the receivable balances. |

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

| Reference to Laws, Rules Regulations etc. | Non-compliance | Management Comment | Recommendation |
|---|---|---|---|
| (a) Public Enterprises Circular No. No. 05/2016 dated 16 December 2016 | The Company had made a provision for bonus amounting to Rs.1,958,534 without being obtained the required approval. | The Board of Directors has given approval for bones subject to no objection letter be obtained from the CEB, since LCC Expenditure is reimbursed by the CEB, further this is not an additional cost to CEB and also follow and adapt the same procedure for year 2020 as well. | Company should comply with the circular. |
| (b) Procurement Guideline 2006 Sec.4.2.1 | The company had not prepared a Master Procurement Plan for procurement activities envisaged at least for a three years as per the procurement guideline. | Annual procurement plan had been approved by the Board of Directors. | A Master Procurement Plan should be prepared and approved as per the procurement guideline. |

### 1.8 Non -compliance with Tax Regulations

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| Department of Inland Revenue has imposed a penalty of Rs.113, 089 regarding the tax payments made by the Company for the year of assessment 2017/2018 which was not in accordance with the section 113 of Inland Revenue Act, No. 10 of 2006. However the Company neither paid to IRD nor disclosed the penalty for the financial year ended 31 December 2021 as per the paragraph 88 of the Sri Lanka Accounting Standard on Income Taxes (LKAS 12). | We have made the all the income tax on time and we had not accept the additional penalty Rs.113,089 imposed by the Department of Inland revenue. We made an appeal to settle the matter amicably. | Company should get resolved the matter immediately after negotiating with the IRD. |

## 2. Financial Review

### 2.1 Financial Result

According to the financial statements presented, the operations of the Company for the year ended 31 December 2021 had resulted neither pretax net profit nor loss as per the preceding year, due to entering into an agreement with the Ceylon Electricity Board to reimburse the net overhead cost incurred by the Company since the year 2014.

### 2.2 Trend Analysis of major Income and Expenditure items

Analysis of major income and expenditure items of the year under review compared with the preceding year with the percentage of increase or decrease are as follows.

| Income/ Expenditure | 2021 | 2020 | Increase/ (Decrease) | Percentage |
|---|---|---|---|---|
| .......................... | ......... | ......... | ................................ | ................. |
| | Rs. | Rs. | Rs. | % |
| Revenue | 59,046,036,553 | 41,000,383,219 | 18,045,653,334 | 44% |
| Cost of Sales | 58,990,572,660 | 40,954,618,074 | 18,035,954,586 | 44% |
| Administration Cost | 60,718,556 | 53,836,714 | 6,881,842 | 12.8% |

The Revenue and cost of sales had increased by Rs. 18,045,653,334 and Rs.18,035,954,586 respectively for the year under review compared with the preceding year due to increase in coal prices.

## 3. Operational Review

### 3.1 Management Inefficiencies

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| The Company had not maintained a fixed asset register and a list of assets are maintained in a MS Excel document which may prone to risk of unauthorized alterations. | At the end of each year, Lanka Coal Company (Pvt) Ltd conducts an Annual Survey for all fixed assets in accordance with Treasury and Ministry of Power guidelines as per Assets Management Circular No 01/2017 dated 28.06.2017. The authorized officers were directed to take action to include the serial numbers of electrical equipment so that such shortcomings as identified in the audit observations do not occur in the future. | Company should maintain a fixed asset register and introduce appropriate internal controls in maintaining fixed assets. |