

## **Magampura Port Management Company (Pvt) Limited – 2016**

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The audit of financial statements of the Magampura Port Management Company (Pvt) Limited for the year ended 31 December 2016 comprising the statement of financial position as at 31 December 2016 and the comprehensive income statement, the statement of changes in equity and the cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka. I was assisted by a Firm of Chartered Accountants in public practice to carry out this audit. A detailed report on the Company was issued to the Chairman of the Company on 09 August 2017.

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

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Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

### **1.3 Auditor's Responsibility**

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My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements.

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

### **1.4 Basis for Adverse Opinion**

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Had the matters described in paragraph 2.2 of this report been adjusted, many elements in the accompanying financial statements would have been materially affected.

## **2. Financial Statements**

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### **2.1 Adverse Opinion**

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In my opinion, because of the significance of the matters described in paragraph 2.2 of this report, the financial statements do not give a true and fair view of the financial position of the Magampura Port Management Company (Pvt) Limited as at 31 December 2016 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

### **2.2 Comments on Financial Statements**

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#### **2.2.1 Going Concern of the Company**

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The accumulated loss as at 31 December 2016 amounted to Rs.1,960,685,373 and the net assets of the Company as at that date had been a negative value amounting to Rs.1,885,685,373, and as such, the Company had been running at a serious scarcity of capital. Therefore, this matter should be brought to the notice at an extraordinary General Meeting of the shareholders within 20 days in terms of Section 220 of the Companies Act, No. 07 of 2007. Nevertheless, the Board of Directors had failed to take action accordingly. However, in the preparation and presentation of financial statements, the company had taken action on the assumption of a going concern. Further, a confirmation had not been obtained in support of financial assistance of the Sri Lanka Ports Authority being the Mother Institute, for its operating activities and settlement of liabilities.

#### **2.2.2 Sri Lanka Accounting Standards**

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##### **Sri Lanka Accounting Standard 01**

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Instead of classifying as loans and current and non-current liabilities valued at Rs.2,931,386,743 and showing them in the financial statements in terms of Sri Lanka Accounting Standard 01, those had been shown under only non-current liabilities. If the classification had been done as current liabilities in terms of the Standard, the net current assets of the Company should have been a negative value. Further, a confirmation of balance had not been received from the Bank in respect of this loan balance.

#### **2.2.3 Accounting Deficiencies**

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The following observations are made.

- (a) The Authority had not taken action to recover the ground rent totalling Rs.197,888,250 due from 243 motor vehicles retained in the Port Yard over a period of 07 days. Further, 40 per cent out of the said amount receivable to the Company had not been taken to included as receivables in the financial statements.

(b) The balance of the Tug Claim Receivables of Rs.25.7 million included in the financial statements of which the recovery is uncertain, had not been supported with third party confirmation. As such, necessary provisions had not been made in the financial statements for any probable future impairment losses.

#### 2.2.4 Unexplained Differences

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Differences of 1,264 metric tons and 1,647 metric tons were observed between the stock balance shown in the books and the physical balance as per the stock verification reports respectively relating to the two types of fuel namely IFO 380 and MGO as at 31 December 2016.

#### 2.2.5 Lack of Evidence for Audit

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The evidence indicated against following items was not made available to audit and as such those could not be satisfactorily vouched or accepted.

Item	Value (Rs.)	Evidence not made available
01. Write off of bunkering oil stocks	585,496,943	Decisions of the Board of Directors
02. Interlock Concrete Blocks	1,761,247	} Stock Verification Reports
03. Concrete Blocks	3,989,926	
04. Oil stocks	2,658,595	

#### 2.3 Non-compliances with Laws, Rules, Regulations and Management Decisions

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The following non-compliances were observed.

Reference to Laws, Rules, Regulations etc.	Non-compliances
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(a) Financial Regulations of the Democratic Socialist Republic of Sri Lanka Financial Regulation 396	Action in terms of Financial Regulations had not been taken in respect of 4 cheques valued at Rs.118,389 outstanding for 06 months relating to a bank current account.

(b) Public Enterprises Circular No. PED/12 of  
02 June 2003

- (i) Section 5.1.1 Even though every Public Enterprise should prepare a Corporate Plan, the Company had not prepared such plan.
- (ii) Section 5.1.2 Even though every Public Enterprise should prepare an Action Plan in conformity with the Corporate Plan, the Company had not prepared such a plan.
- (iii) Section 7.2 Even though a Procedure Manual/System should be prepared as a main item of the Administrative Division so as to cover all major operations, the Company had not prepared such an Operating Manual.
- (iv) Section 7.4.1 Even though the Audit Committee should meet and give recommendations to improve the internal control system and operations of the Company based on the findings by internal audit, there was no Internal Audit Unit in the Company and Audit Committee meetings as well had not been held.
- (v) Section 8.5 An Insurance Coverage had not been obtained in respect of the value amounting to Rs.9,744,499,541 of oil tank complex located at Magampura Port premises with a view to minimizing the risk of damages. Even though the owner of the oil tank complex was the Ports Authority , the Magampura Ports Management Company being the Ports Management Company had not paid the attention in this connection.
- (vi) Section 9.3.1 Even though every public enterprise should formulate a proper Scheme of Recruitment for each post and obtain the approval of the line Ministry and the concurrence of the Department of Public Enterprises, the Company had not formulated such Scheme of Recruitment and obtained the approvals of the relevant parties for the existing recruitment procedure.

### **3. Financial Review**

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#### **3.1 Financial Results**

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According to the financial statements presented, the operating result of the Company of the year under review had been a loss of Rs.535 million as compared with the corresponding loss of Rs.449 million for the preceding year thus indicating an increase of Rs.86 million in the loss for the year under review as compared with the preceding year. The impairment of the stock of bunkering oil amounting to Rs.585,496,943 had been the main reason therefor.

In the analysis of financial results of the year under review and 3 preceding years, despite the net profit of Rs.7,991,434 of the year 2013, continuous losses had sustained from the year 2014 up to the year 2016. However, readjusting the employees' remuneration, Government tax and depreciation on the non-current assets to the financial result, the favourable contribution in the year 2013 had been Rs.27, 657,651. Nevertheless, the contribution from the year 2014 up to the year under review had been a negative value amounting to Rs.763,106,656, Rs.28,954,245 and Rs.94,343,252 respectively.

#### **3.2 Analytical Financial Review**

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The net profit ratio in the year 2015 had been negative 29 per cent and it had deteriorated up to negative 66 per cent in the year 2016 and the profitability and the efficiency of the Company had been at a weak level.

### **4. Operating Review**

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#### **4.1 Performance**

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The Company had been established for the achievement of the following objectives.

- (a) Perform duties and functions which are assigned to the Company from time to time by the Sri Lanka Ports Authority and carry out management and operating activities of the Magampura Port.
- (b) Develop the Mahinda Rajapaksha Port in Hambanthota as a modern International Sea Port.
- (c) Establish an industrial zone within the limits of the Mahinda Rajapaksha Port in Hambanthota
- (d) Supply marine fuel, water and other services to vessels.

Even though establishment of an industrial zone within the limits of the Port in Hambanthota is one of the major objectives, the Company had failed to achieve that objective even by the end of the year under review.

## 4.2 Management Activities

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The Company had maintained the operating activities of Interlock Blockings and Crushers which is not included in the objectives of the Articles of Association of the Company. As such, a gross loss of Rs.5,375,253 had occurred in the year 2014 and gross profits of Rs.4,149,757 and Rs.753,558 had been earned in the years 2015 and 2016 respectively.

## 4.3 Operating Activities

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The following observations are made.

- (a) The income from oil operations during the year 2016 had been only Rs.9,605,884 whereas the expenditure incurred amounted to Rs.851,688,203 comprising the decrease in the stock value by Rs.585,496,943 , direct expenditure on operations of bunkering oil amounting to Rs.30,537,384, payment of loan interest of Rs.119,395,460 and administrative expenditure and other expenditure amounting to Rs.116,258,416. Accordingly, a net loss of Rs.842,082,319 had been sustained in the year under review and a total operating loss of Rs.2,718,638,138 had been sustained from the operating activities of oil sale from 25 April 2014, the date of commencing the sale of bunkering oil up to 31 December 2016. The main reason for the increase in operating loss had been the increase in impairment loss on total stock of bunkering oil due to the repurchase of a stock of 7,368 metric tons which remained unsold, despite the 10,419 metric tons of bunkering oil stock in hand. However, the operating activities of bunkering oil in the Port had been ceased in the year 2016.
- (b) According to the Letter No.GM/MPMC/399 dated 20 July 2016 forwarded to the Government Audit by the Magampura Ports Management Company, it was informed that the colour of the stock of 14,582 Metric Tons of Marine Gas Oil (MGO) had changed due to the lapse of time as at 30 June 2016. As such, it was observed in audit that problems would be arisen and losses sustained in selling the said stock of oil.

## 4.4 Transactions of Contentious Nature

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In terms of Sections 69 and 135 (amended Chapter 235) of the Customs Ordinance No.35 of 1879, the Magampura Ports Management Company had been informed to submit a bank guarantee of Rs.220 million to the Customs at earliest possible in respect of the tax liabilities payable to the Customs for a stock of bunkering oil remaining at the Stores at present. However, that requirement had not been fulfilled. As such, the letter No.INDS/PRJ/0004/2016 dated 02 February 2016 addressed to the General Manager of the Magampura Ports Management Company by the Sri Lanka Customs, stated that retaining oil stocks over 2 years without submitting a recognized guarantee was a violation of Section 135 of the Customs Ordinance. Therefore, an injunction had been imposed and an investigation had been initiated on retaining a stock of bunkering oil of 17,210 metric tons valued at Rs.1,975,057,705 without authority.

#### **4.5 Idle and Underutilized Assets**

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The Ports Management Company had decided to cease the operating activities of bunkering oil in the year 2015. As such, 9 oil tanks valued at Rs.6,987,638,384 representing 71.7 per cent of the total value of assets amounted to Rs.9,744,499,541 of the Company as at 31 December 2016 and Transport System thereto had been underutilized since the date of cessation of oil selling.

#### **4.6 Uneconomic Transactions**

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A post of Deputy General Manager (Oil Warehouse) which was not included in the Organization Chart (Cadre) of the Magampura Ports Management Company had been created and a Consultant had been recruited to streamline the operating activities of bunkering oil with effect from 02 December 2013. The service of this Consultant had been terminated by the letter dated 18 December 2015 issued by the Managing Director and a sum of Rs. 20,826,983 comprising salaries and allowances amounting to Rs.19,837,500 and transport facilities with fuel and highway charges totalling Rs.989,483 had been paid up to 20 January 2016, the date of termination of service. A loss of Rs.1,876,555,819 had sustained from the operating activities of bunkering oil during the period in which the consultation service was obtained, thus it cannot be ruled out in audit that the expenditure incurred on that service had been a fruitless expenditure. Further, the said Consultant had filed a court case against the Company claiming a compensation of Rs.100 million for the termination of service and it is still a pending court case.

### **5. Accountability and Good Governance**

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#### **5.1 Performance of Environmental and Social Responsibilities**

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The granites and soil removed in the construction of Hambanthota Port had been piled up in several places and pot holes had formed in a manner that water was being collected in the Port premises. Furthermore, remainders of demolished buildings were existed in the lands acquired for the development activities of the Port. The letter No.HDS/LND/12/F/1 issued in this connection on 08 February 2017 by the Divisional Secretariat, Hambanthota had informed the Ports Authority that the Public Health Inspector had identified these lands as Dengue risk areas due to the rainy weather prevailing in the Hambanthota area and to take necessary remedial measures for this issue. As such, the Magampura Ports Management Company had been informed by the letter No.SPD/H/02/09 dated 06 February 2017 of the Ports Authority to take necessary action in this connection. Nevertheless, it had been failed to take action accordingly even as at 30 April 2017, the date of audit.

## 6. **Systems and Controls**

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

<b>Areas of Systems and Controls</b> -----	<b>Observations</b> -----
(a) Staff Administration	Failure in obtaining the approval for the Scheme of Recruitment.
(b) Internal Audit	Non-establishment of an Internal Audit Unit and failure to carry out an internal audit.
(c) Stocks Control	Failure to take necessary action on the unusable stocks.
(d) Assets Control	Failure to take necessary action on the underutilized assets.