

The audit of the financial statements of the National Paper Company Limited for the year ended 31 March 2018 comprising the statement of financial position as at 31 March 2018 and the statement of profit and loss, 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. My comments and observations which I consider should be tabled in Parliament appear in this report

1.2 Responsibilities of Management 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.

1.3 Auditors' Responsibility

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 consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000 – 1810). 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 misstatement 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 these 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 Disclaimer of Opinion

My opinion is disclaimed based on the matters described in Paragraph 2.2 of this report

2. Financial Statements

2.1 Disclaimer of Opinion

Because of the effect of the matters described in the Paragraph 2.2 of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements. Accordingly, I do not express an opinion on the accompanying financial statements of the Company.

2.2 Comments on the Financial Statements

2.2.1 Non-compliance with Sri Lanka Accounting Standards

- a) Even though the cost of lands and buildings should be identified separately in the financial statements in terms of Sri Lanka Accounting Standard No. 16, the cost of the lands and buildings under the property, plant and equipment of the Company totalling to Rs. 132,274,693 had not been identified separately.
- b) Although income and expenses and assets and liabilities should never be offset unless permitted by an accounting standard in accordance with paragraph 32 of Sri Lanka Accounting Standard 01, the company had offset assets Rs.43,153,550 against liabilities of Rs.10,151,947 during the year under review.
- c) Calculation of income tax expenditure and calculation of deferred tax for the year ended 31 March 2018 had not been done by the company according to the Sri Lanka Accounting Standards 12.

2.2.2 Accounting Deficiencies

The annual profit had been understated by Rs. 2,211,114 in the financial statements due to the provision for depreciation of motor vehicles by Rs.2,192,232 and the provision for depreciation for computers by Rs.18,882 which were calculated in excess of the cost value.

2.2.3 Lack of Documentary Evidence for Audit

Management had failed to provide the audit with the necessary evidence to verify of 19 transactions and account balances of one revenue account balance of Rs.775,150 and 06 Expenditure balances of Rs.2,143,837, Property plant and equipment worth of Rs.484,423,303, Capital work in progress of Rs.37,428,597 ,long term investments of Rs.(1,967,061), Closing Stock of Rs.120,820,606 , trade receivables of Rs.105,550,749 ,other receivables of Rs.518,760,175, cash and cash equivalents of Rs.29,263,264 ,loans with interest of Rs.159,958,713, trade payables of Rs.134,039,935 ,Other payables of Rs.1,298,579,271, bank overdraft Rs.13,153,218 ,Statutory payment of Rs.5,725,351 as total amount of Rs.2,908,655,158.

3. Financial Review

3.1 Financial Result

The operating results of the year under review was a profit of Rs. 7,135,792 as against the loss of Rs. 46,888,937 for the previous year. Accordingly, an improvement of Rs.54,024,729 was observed in the financial result. Decrease in administrative expenses by Rs. 87,017,191 was the main reason for this improvement.

4. Operating Review

4.1 Management Inefficiencies

- (a) Although it is required to maintain accounting records and supporting documents that accurately record and explain the transactions of the company as per section 148 of the Companies Act No. 07 of 2007, the competent authorities of the company had not taken steps to keep the accounting books and accounting evidence relating to the transactions and incidents relating to the accounting period.
- (b). The electricity supply to the Valachchenai factory had been temporarily disconnected from 09 February 2015 due to non-payment of the outstanding electricity bill amounting to Rs.483,997,075 to be paid to the Ceylon Electricity Board as at that date, and due to non-availability of electricity supply, any production process had not taken place in the Valachchenai factory until June 2020. However, production activities of the factory had been resumed in July 2020 by obtaining the approval subject to the condition of paying the remaining electricity bill amounting to Rs. 122,004,390, after writing off the penalty interest of Rs. 361,992,685, in instalments within a period of six months after the lapse

of a period of two years from the date of resumption of production activities of the Company by the letter of the General Manager of the Ceylon Electricity Board bearing No. EP/EE(COM)/CS/Bulk Supply dated 08 September 2022 and by the Cabinet Decision No. CP/20/0561/224/015 dated 26 March 2020. Accordingly, the paper company had paid Rs.10,000,000 out of the outstanding electricity bill of Rs. 122,004,390 as at 31 December 2023, and further the Paper Company had to pay a sum of Rs. 112,004,390.

- (c). There had been 23 employees comprised of 09 employees recruited on permanent basis in head office of the Company from July 2020 and 12 employees recruited on contract basis and 02 employees recruited on daily wage basis and there had been 126 employees at Valachchenai factory comprised of 06 employees recruited on contract basis and 120 employees recruited on daily wage basis and the total number of employees had been 149 and the approval of the Department of Treasury Operations had not been obtained for this staff so far.
- (d). At the time of commencement of production activities at the Valachchenai paper factory, a loan of Rs. 40 million had been obtained from the People's Bank on 09 December 2020 with a Treasury guarantee, subject to a grace period of 06 months, with terms of repayment in 54 instalments over a period of 05 years. Furthermore, the Company had once again taken a loan of Rs. 100 million from People's Bank on 17 May 2021 for meeting the working capital requirements of the Valachchenai factory, subject to the repayment of it in a period of 05 years. This loan had been taken with the guarantee of the General Treasury at market interest rates and the National Paper Company Limited had not received any support from the line ministry, the Ministry of Industries.
- (e). Although there were 02 main machines namely the Paper Machine and the Board Machine to be used for the production activities in the factory, only the Board Machine was being used. In the year 2020, when the production activities of the Valachchenai Paper Mill resumed and were continued, the company's management adopted the method of removing parts from the paper production machine and installing them in the board production machine for proper functioning in cases where the board production machine was not operating and mechanical faults were occurred. In this way, 08 main items from the paper production machine were installed to the board production machine and their value was Rs.34,433,059. Accordingly, the paper production machine was still inoperative to the extent that it could not be used for any purpose even by 22 January 2024, the date of audit, and therefore the cardboard production had been hampered.
- (f). The lessee had not paid Rs. 200 million, out of the Rs. 600 million, which had been agreed upon in terms of the agreement between the State Resources Management Corporation located at No. 561/3, Elvitigala Mawatha, Colombo 05 and the National Paper Company Limited, and the Perth Engineering and Maintenance PVT LTD, with a business address of No. 03/43, Ventnor Avenue, West Perth, Western Australia for a period of 30 years to rehabilitate and redevelop the Embilipitiya Factory in terms of the Lease Agreement No. 1037 dated 19 December 2011. Furthermore, the relevant

Company had carried out production activities for a short period of time and then mortgaged the paper manufacturing machine owned by the Embilipitiya factory to Seylan Bank for a value of Rs. 418,483,037 and left the factory in the year 2012. The second lessee had to pay an amount of Rs. 120 million to the bank to settle this mortgage, and although the relevant lease agreement had been cancelled on 25 September 2014 by the Ministry of State Resources and Enterprise Development on the instructions of the Attorney General due to non-payment of rent instalments, necessary steps had not been taken to recover the rent of Rs. 42 million to be received for the three-year period from 19 December 2011 to 25 September 2014.

Similarly no action had been taken to recover the lossess incurred by the Company from the parties who entered into the agreement representing the National Paper Company to mortgage the production machinery to Seylan Bank and no legal action had been taken by the lessor party regarding the breach of the agreement due to the cessation of production activities by Perth Engineering and Maintenance Pvt Company Ltd which enter into the agreement..

- (g). The Ambilipitiya factory of the National Paper Company Limited had been leased out to KSPA Ambilipitiya Paper Mills (Private) Limited under the lease agreement dated 09 March 2022, on a consideration of Rs. 260 million for a period of 30 years. According to the agreement, production activities should commence within 18 months and during that period, the lessee should pay an annual rent instalment of Rs. 13,000,000 to the company. After the commencement of production activities, a value equivalent to 3% on the sales revenue should be paid as rent instalment as per the tax agreement. However, the relevant company had not yet commenced the production activities.

5. Accountability and Good Governance

5.1 Presentation of Financial Statements

- (i). Although the annual financial statements and draft annual reports should be submitted to the Auditor General within 60 days of the end of the accounting year as per Section 6.5.1 of the Public Enterprises Circular No. PED/12 dated 02 June 2003, the financial statements of the National Paper Company Limited for the accounting year 2017/2018 had been prepared and submitted for audit on 02 November 2023.

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