Ceylon Petroleum Storage Terminals Limited - 2019

1.1 Disclaimer of Opinion

The audit of the financial statements of the Ceylon Petroleum Storage Terminals Limited ("Company") for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 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.

I do not express an opinion on the accompanying financial statements of the Company. Because of the significance of the matters discussed in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

1.2 Basis for Disclaimer of Opinion

I do not express an opinion on the matters described in paragraph 1.5 of this report.

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

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 Financial Statements

1.5.1 Non-Compliance with Sri Lanka Accounting Standard

Non-Compliance with the reference to particular Standard	Management Comment	Recommendation
As per paragraph 51 of the Sri Lanka Accounting Standard on Property, Plant and Equipment (LKAS 16), the useful life of the assets shall be reviewed at least at each financial year end and if expectations differ from previous estimates, the changes shall be accounted in accordance with LKAS 08. However, the useful life of the fully depreciated property, plant and equipment costing Rs. 6,074 million are being continuously used by the Company had not been reviewed and accounted accordingly. Further, the Company had not re-valued its assets since the inception of the Company in 2003.	Agreed to reassess the zero value assets with the support of CASL.	The Company should comply with the requirement of the Standards.

1.5.2 Accounting Deficiencies

Audit Issue	Management Comment	Recommendation
(a) More than 1,300 types of inventory items which comprises significant quantity were observed in the Enterprises Resources Planning (ERP) system i.e SAP of the Company without being entered the value of such inventory items to the system for longer period. Therefore, the accuracy, valuation and completeness of inventory items valued at Rs.676 million shown in the statement of financial position as at the end of the year under review could not be relied upon in audit.	As per the prevailing procedure for scrap and used items, (ex. old newspapers, used tires, etc) it is mandatory to record all the scrap & used items as used items with zero value. This is an important internal control mechanism to minimize the theft and improve the traceability. Total number of zero value items as at 31.12.2019 are 1,369 and out of those 1,336 items are Category on (used items-scraps) and only 19 items to be reconditioned and 14 items are under category 3.	All the inventory items should be properly valued and account accordingly. And also proper recording and controlling mechanism should be introduced over inventory control of the Company.

(b)	In contrary to the LKAS 08, Tug Boat charges aggregating Rs. 357.7 million which comprise amount of Rs.62.5 million for the period 2010 to 2014, amount of Rs.225.15 million for the period 2014 to 2018 and amount of Rs.70.1 million for the year 2018 had been accounted in the year under review and Rail track maintenance charges aggregating Rs.1.91 million relevant to year 2017 and 2018 had been accounted as expenses of the year under review.	Due to lack of formal agreement between CGR and CPSTL invoice for cost of railway track maintenance was not sent to CPSTL. After discussions with officials of CGR both parties agreed CPSTL settled year 2017 & 2018 in 2019. However, in future railway track maintenance cost would be accrued on time. In the Section 25 of Sri Lanka Accounting Standards –LKAS 08 –Accounting Policies, Changes in Accounting estimates & Errors., when it is impracticable to determine the cumulative effect, at the beginning of the current period, of applying a new accounting policy to all the prior periods, the entity shall adjust the comparative information to apply the new accounting policy prospectively from the earliest date practicable.	Appropriate actions should be taken to account all the expenses in the year it was incurred.
(c)	11 items aggregating Rs.82.62 million which had been purchased in 2018 and 2019 had not been accounted and laying under advance account by the Company as at the end of the year under review.	Out of 11 items, 03 items were materials and cleared in year 2020. 03 items have capitalized in year 2020. Balance remaining items are payments of 90% LC charges and GRN not received.	All the assets should be capitalized in terms of related accounting standards.

1.5.3 Non -compliance with Tax Regulations

Audit Issue	Management Comment	Recommendation
A difference of Rs.437.53 million was observed between total of Income Tax payable, Value Added Tax (VAT) payable, Withholding Tax payable, Pay As You earn (PAYE) payable and Economic Service Charge (ESC) Payable balances appeared in the financial statements of the Company and the corresponding amounts shown in the records maintained by the Department of Inland Revenue as at the end of the year under review.	According to IRD records, they are updating the system as per their assessments whereas in our Financial Statements include tax liabilities payable which are due on the subsequent month, self-assessment payments of income tax. Appeals that are logged against the disagreed assessments raised by IRD are not accounted in our financial statements.	Appropriate action should be taken to rectify those differences with IRD.

1.5.4 Related Parties and Related Party Transactions not disclosed

Audit Issue	Management Comment	Recommendation
The accuracy, existence, valuation and completeness of the Inter Company balances between the Ceylon Petroleum Corporation (CPC) and Lanka Indian Oil Company (LIOC) were not assured in audit due to following reasons.		
(i) As per the information available for audit, the receivable amount of Rs. 1,173 million from CPC, the Parent, had been written off from their accounts to eliminating the loan interest components of throughput charges of 13 cents per litre considering the settlement of Exim Bank Loan in the year 2018. However, it has not concluded or no any impairment provision had been made in this regard by the Company up to date. Therefore, the recoverability of this receivable balance is critically doubt in audit.	CPC had been written off to eliminate the interest component of the throughput charges without considering the existing Tri-party Agreement and been informed to the CPSTL board of Directors. The decision to eliminate the interest component of the throughput charges by CPC had been arrived arbitrary, without considering the Management of CPSTL. Many discussions had been taken place between the two managements (Finance division of CPC & CPSTL) with the participation of CPSTL / CPC Board members to sort out the matter. No	It should come to a settlement considering the intention of such a loan and legality of them with the CPC and LIOC.

	provision has been made for any impairment due to the above-mentioned recoverable balance as at 31st December 2019.	
(ii) As per the financial statements of the Company, the amount receivable from the CPC at the end of the year under review was Rs.6,248.87 million. However, as per the financial statements of the CPC the amount payable to the Company (before deducting the cash in transit of Rs. 1,029.45 million) at the end of the year under review was Rs. 4,625.74 million Hence, an un-reconciled difference of Rs.1, 623.13 million was observed between those two balances.	As per your differences of Rs. 2652.58 Mn between CPSTL & CPC of Trade Receivable and payable outstanding as at 31st December 2019, we observed that there were no any differences between those balances on the said periods.	Appropriate actions should be taken to clear all unreconciled balances without delay.
(iii) According to balance confirmation received from the LIOC, the amount payable to the Company was Rs.370.9 million, whereas according to the financial Statements of the Company the corresponding amount was shown as Rs. 376.0 million. Hence, an un-reconciled difference of Rs.5.1 million was observed between those two balances.	The discussions are in progress to reconcile the difference and finalize.	Appropriate actions should be taken to clear all unreconciled balances without delay.

1.5 Accounts Receivable and Payables

1.5.1 Payables

Audit Issue	Management Comment	Recommendation
(i) Debit balances of 48 trade and other payables aggregating Rs. 38.96 million which comprise of Government Supplies, Procurement Supplies, General Voucher Supplies and Transport's Vendors were observed at the end of the year under review. It shows 14 vendors aggregating Rs. 2.98 million from the year 2010 or before, 03 vendors aggregating Rs. 0.55 million over 05 years to 10 years and 31 debit balances aggregating Rs. 35.42 million over 01 year to 05 year were remained unsettled. It was observed that the Company has made subsequent transaction with those venders who are having debit balances without settling the	Most of the debit vendor balances are reversal of erroneously done invoice verification in SAP (MIRO) without clearing.	Appropriate actions should be taken to settle all unreconciled balances without delay.

	existing debit balances. Therefore, the existence, accuracy and valuation of those debit balances were not assured in audit due to absence of sufficient and appropriate audit evidences.		
(ii)	Trade payable balances aggregating Rs. 7.18 million of 81 parties since year 2010 or before, 310 payable balances aggregating Rs. 40.18 million over 05 to 10 years and 18 payable balances aggregating Rs. 39.45 million over 01 year to 05 years were remained unsettled as at the end of the year under review. However, audit was unable to ensure the existence, accuracy and valuation of those balances due to absence of sufficient and appropriate audit evidences.	There are certain vendor liabilities in long outstanding which are no longer required to be paid. The Sri Lanka Financial Reporting Standards (SLFRS 9), or IFRS-9, provides a list of criteria that must be met before any account payable can be written off. According to those guidelines, financial liabilities should only be derecognized by the company when the obligation to pay is expired, canceled, or discharged. As such, they are not written off based on the time frame Therefore we are seeking the Audit & Management Committee recommendation with the Board of Directors approval to written back those vendor balances after completing due diligence for each vendor account.	Appropriate actions should be taken to clear all the Long outstanding balances.

1.5.2 Receivables

Audit Issue	Management Comment	Recommendation
Other receivables totaling Rs. 8.8 million was remained unrecovered for over 5 years as at the end of the year under review. Therefore, recoverability of this balance were not assured in audit due to absence of sufficient and appropriate audit evidences.	Sundry Customer balances are due to erroneously raised invoices, disagreements of invoices raised, rates or no traceable material evidence to pursue further to collect the outstanding. Most of these balances are coming from before the SAP system implemented in year 2010 and we have referred this	Appropriate actions should be taken to recover all Long outstanding balances.

		to Audit and Management Committee of CPSTL to get necessary recommendation and Audit and Management Committee has recommended to write off the balance as this has been long outstanding and likelihood that these balance would not be recovered.	

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

The following instances with Laws, Rules, Regulations and Management Decisions, etc. were observed in audit.

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) Public Enterprises Circular No. PED/12 of 2 June 2003 - Guidelines for Good Governance			
(i) Guideline 5.2.2	Thirty-eight (38) capital projects which have an estimated cost of aggregating Rs. 6,981 million had been carried without a proper feasibility study.	Though the feasibility studies haven't been presented as reports, all the projects relevant to Engineering Function were initiated and carried out after analyzing the feasible conditions of the appropriate requirements. Such analyses were included in the Chairman Approval Papers and Board Papers. However, for the future projects over Rs. 10 M, feasibility study reports will be prepared prior to obtain Board approval as per the Guideline 5.2.2 of Public Enterprises Circular No. PED/12 of 02 June 2003 (Guidelines for Good Governance).	The Company should comply with the Guideline

(ii)	Guideline 5.2.2 (b)	Approval of the Ministry and the concurrence of the Department of Public Enterprises, General Treasury had not been obtained for the capital expenditure exceeds Rs. 10 million.	Management has not commented.	The Company should comply with the Guideline.
(iii)	Guideline 9.2	The Company does not have an organization Chart registered with the Department of Public Enterprises, General Treasury with an approved cadre. In the event of creation of a new cadre, or instances where there is excess cadre, the Company had not taken actions in consultation with the Department of Public Enterprises, General Treasury.	It was sent to Department of Public Enterprises for approval and not received the approval yet.	The Company should comply with the guideline.
(iv)	Guideline 9.3	The Company does not have schemes of recruitment and promotion (SORAP) approved by the Board and the Ministry with the concurrence of the Department of Public Enterprise, General Treasury.	At present CPSTL apply the same Scheme of Recruitment & Promotions (SORAP) prepared by CPC. Action has been taken obtain the approval of the Board of Directors, Ministry and Department of Public Enterprises, General Treasury.	The Company should comply with the Guideline
(v)	Guideline 9.10	Approvals of the Secretary to the Treasury had not been obtained by the Company for the appointment of	These 29 contract employees have been recruited to CPSTL before 2019. At present Board has restricted normal contract recruitments to the	The Company should comply with the guideline.

		contract employees. There were 29 contract basis employees at the end of the year under review.	Company. As per the Public Administration Circular we have made arrangement to obtain the Treasury Approval to absorb these contract employees into permanent cadre.	
(vi)	Guideline 9.12	Approval of the Department of Public Enterprises in General Treasury for the welfare scheme adopted by Company had not been submitted for audit. However, a sum of Rs. 239.29 million had been paid as staff welfare during the year under review by the Company.	Company is providing rang of welfare schemes to employees in par with CPC. These facilities enjoy by employees in many years. Action will be taken to obtain Treasury approval.	The Company should comply with the guideline.
vii)	Government Procurement Guidelines -2006	A tender procedure had not been followed when selecting outside transporters (Bowsers). Further, even the approval of board had not been obtained when selecting outside transporters.	Transport rates are decided by CPC and payments made to hired bowsers are reimbursed by CPC. There is no formal procedure to select hired bowsers as pre-determined rates are used for payments. It was decided to do pilot project to follow the tender procedure and, Tender document is being prepared.	The Company should comply with the Guideline.
(viii)	Department of Public Enterprises Circular No. FP/06/35/02/01 of 04 November 2013 and No. PED 03/2016 of 29 April	Without deducting the Pay As You Earn (PAYE) tax from personal emoluments of employees, the Company had borne the employees PAYE tax amounting to Rs.162.2 million during the year under review.	It has been the practice in CPC and CPSTL to born the PAYE tax by the employers.	The Company should comply with the Circular instructions.

	2016.			
(ix)	No. 124 of 24 October 1997 of the Ministry of Finance and Planning	Twenty-Seven officers had been assumed for cover up duties of vacant posts over 03 months period as at the end of the year under review which contrary to the circular provision.	Vacant posts have been advertised in 2019 and had planned to fill before end of 2019. However, Due the Presidential Election held in November unable to complete the process. Therefore, these cover up positions are continuing.	The company should comply with the Circular instructions.

2. Financial Review

2.1 Financial Result

The operating result of the year under review was amounted to a profit of Rs. 1,765.33 million and the corresponding profit in the preceding year was amounted to Rs. 197.32 million. Therefore, an improvement amounting to Rs. 1,568.01 million of the financial result was observed. The main reasons for the increase were increase of throughput revenue as a result of the changes of throughput rates, increase of other operating Income and finance Income and decrease of tax expenses in the year under review.

2.2 Trend Analysis of major Income and Expenditure items

The operations of the Company had resulted in a markup (Gross Profit/Direct Cost) of 78.78 per cent for the year under review thus indicating an increase of 12.65 per cent as compared with the markup of 66.13 per cent in the preceding year. Similarly, the Gross Profit for the year under review had increased by Rs. 1,533 million or 29.33 per cent as compared with the corresponding Gross Profit of Rs. 5,227 million in the preceding year. This increase is summarized and shown below.

Description	**For the Year ended 31 December**		**Variance**	
	2019	**2018**	**Favorable/ (Adverse)**	**Percentage**
	Rs. Million	**Rs. Million**	**Rs. Million**	
Revenue	15,340	13,130	2,210	16.83
Direct Cost	(8,580)	(7,903)	(677)	8.57
Gross Profit	6760	5,227	1,533	29.33
Other Income	852	704	148	21.02
Other Operating Expense	(70)	0	(70)	
Administration Expense	(4,937)	(4,527)	(410)	9.06
Operating Profit	2,605	1,404	1,201	85.54

Finance Income	323	118	205	173.73
Finance Expenses	-	-	-	-
Profit/(Loss) Before Income Tax	2,928	1,522	1,406	92.38

2.3 Ratio Analysis

According to the information made available, some important accounting ratios of the Company for the year under review and the preceding year are given below.

Ratios	**2019**	**2018**
Profitability Ratios		
Gross Profit Ratio (GP) (%)	44.07	39.81
Operating Profit Ratio (%)	16.98	10.69
Net Profit/ (Loss) Ratio (NP) (%)	11.5	1.5
Liquidity Ratios		
Current Assets Ratio (Number of times)	6.55:1	6.18:1
Quick Assets Ratio (Number of times)	6.25:1	5.86:1
Working Capital (Rs. million)	12,244	10.903
Investment Ratio		
Return on Assets (ROA) (%)	5.48	0.65

3. Operational Review

3.1 Operational Inefficiencies

	Audit Issue	**Management Comment**	**Recommendation**
(a)	**Non-availability of a formal monitoring process over terms and conditions of the Settlement Agreement** As reiterated in my previous years audit reports, according to the section 03 of the Settlement Agreement signed on 05 January 2007 between the Government of Sri Lanka and LIOC, it was restricted to deliver petroleum products by LIOC from its China Bay installation to a maximum 5 per cent of the Country's throughput	In the Settlement Agreement there is no formal process available to monitor the compliance of the conditions. Audit Committee has recommended adopting a proper formal process to establish with this regard. As per the provisions in Settlement	A proper formal process should be established to monitor the Compliance of the conditions.

	of petroleum products and Ceylon Petroleum Corporation (CPC) to a maximum 5 per cent excluding deliveries from Sapugaskanda Refinery. However, a regular process had not been established to monitor the compliance of the above provisions. As a result, there is a possibility of losing considerable amount of throughput income to the Company.	Agreement a regulator has to be appointed to monitoring purpose and that has to be done by the Government not by CPSTL. Currently Ministry of Petroleum Resources Development acts as the regulator.	
(b)	**Delay in Revising Pricing Formula due to Expiry of Shareholders Agreement and Share Sale Purchase Agreement for Common User Facility** It was noted that Shareholders Agreement and Share Sale Purchase Agreement for the common user facility between CPC, LIOC and the Company was expired on 31 December 2008. Neither an extension had been obtained, no new agreement had been signed by participating all the related parties with a proper evaluation and approval of the board. Therefore, the pricing formula used for the purpose of determining the throughput charges, transport income including slab recoveries had not been revised since 2011.	Ministry has written to the Attorney Generals Department seeking legal advice on validity of Tri-party agreement signed by CPC/ LIOC and Treasury during the year 2003.	The Price Formula should be revised with the agreement with all related parties without delay.
(c)	**The Common User Facilities** **-------------------------------------** The Company had entered into a common user facility agreement with CPC without LIOC on 13th May 2019. According to this agreement, terms and condition in relation to storage and transport of petroleum product and the way of deciding the throughput between CPC and Company were agreed. However, the terms and condition in relating to the same subject affected to the LIOC, a main user and a party who were in the Common User Facilities Shareholders’	Formal agreement between CPC & CPSTL was signed in 2019 including all the related business activities.	An agreement should be signed with the consent of all related parties.

Agreement of the year 2003, were not cleared audit. Therefore, it was observed that any unfavorable conditions and cost had to be borne by the Company in any event of LIOC refusing the terms and condition entered between the Company and CPC.		

3.2 Resources Released to Other Organizations

Audit Issue	Management Comment	Recommendation
In contrary to the instructions of the circulars, particularly in the Public Enterprises Circular No. PED/12 of 02 June 2003 on Public Enterprise Guidelines for Good Governance, the Letters Nos. CSA/PI/40 of 04 January 2006 and CS/1/17/1 of 14 May 2010 issued by His Excellency the President, and the Public Enterprises Circular No.21 of 08 January 2004, the Company had released three (03) employees and incurred a sum of Rs. 4.73 million as their remuneration and other allowances during the year 2019.	No answer had been given by the Management.	The company should comply with the relevant Circulars Instructions.

3.3 Human Resources Management

Audit Issue	Management Comment	Recommendation
Out of the approved cadre of 3,249 of the Company, 343 post were in vacant as at 31 December 2019. Out of that, 44 posts of vacancies were in senior staff level including, Deputy General Manager (Operations), Deputy General Manager (Eng.and SS), Chief Information Officer, and Manager (Fire and Safety), Manager (Internal Audit) etc... However, it was observed that 833 persons had been recruited out of approved cadre.	All vacant positions have been advertised internally. But due to the Presidential Election 2019 interviews could not be held. As mentioned in the report, it is not clear the excess recruitment of 833 persons out of approved cadre. We have not recruited anyone externally without cadre vacancies. But due to the implementation of Political Victimization Promotions (PVC) there are many positions created in excess to the approved.	The cadre of the Company should be critically evaluated and get the approval from relevant authorities for the appropriate cadre and actions should be taken to fill the carder in order to continue the operation of the Company in an efficient and effective manner.

4. Accountability and Good Governance

4.1 Corporate Plan

Audit Issue	Management Comment	Recommendation
As per the Guideline 5.1.1 of Public Enterprises Circular No. PED/12 of 2 June 2003 - Guidelines for Good Governance, The Company should prepare a Corporate plan for 3 years and update it annually as a rolling plan. The copies of plan approved by the Board together with the updated Annual Budget should be forwarded to the line Ministry, Department of Public Enterprises, General Treasury and the Auditor General 15 days before the commencement of financial year. The Company had not prepared a Corporate Plan for 3 years and presented to the audit as required by the guideline.	Preparation of Corporate Plan was initiated in 2018 and Draft Corporate Plan was submitted by the Consultant M/s. E&Y in October 2018. It was submitted to the 198th Board meeting but not taken up that day. However, a fresh corporate plan will be developed for the period of 2021-2024.	The Company should comply with the guideline.