Lanka Mineral Sands Limited - 2019

1.1 Qualified Opinion

The audit of the financial statements of the Lanka Mineral Sands 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 reported 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 2019, 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 Scope of Audit (Auditor's Responsibility on 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 Financial Statements

1.5.1 Internal Control over the preparation of financial statements

Entities are required to "devise and maintain" a system of internal accounting controls sufficient to provide reasonable assurance that transactions are executed in accordance with management's general or specific authorization, transactions are recorded as necessary to permit preparation of financial statements in conformity with the applicable reporting standards, and to maintain accountability for assets, access to assets is permitted only in accordance with management's general or specific authorization, and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

Audit Observation	Comments of the Management	Recommendation
Non-accounting of assets within the relevant period due to delays in issuing of goods received notes and preparation of cost sheets from the date of purchasing the assets.	This will be corrected in the future.	Arrangements should be made to account the assets in relation to the period.

1.5.2 Non-Compliance with Sri Lanka Accounting Standard

The following observations are made.

	Non-Compliance	Comments of the Management	Recommendation
(a)	According to paragraph 38 of Sri Lanka Accounting Standards 1, cost of sales, which was Rs.673,270,905 in the previous year, had been indicated as Rs. 485,770,307 and other operating expenses, which were Rs. 161,150,455, had been indicated as Rs. 349,005,154 in the financial statements as comparative figures of the financial statements for the year under review. Nevertheless, the relevant changes had not been disclosed by notes.	Noted down to correct it.	The changes made in the financial statements should be disclosed by the notes in accordance with the Standard.
(b)	According to paragraph 51 of Sri Lanka Accounting Standards 16 on Property, Plant and Equipment, the useful life of assets should be reviewed at least every financial year and if the expectations are different from the previous estimates, the changes should be brought to accounts according to Sri Lanka Accounting Standards 8. Nevertheless, the useful life of existing motor vehicles and buildings had not been reviewed and had not been brought to accounts accordingly even though they had been fully depreciated.	Action is being taken to revalue in accordance with the Standard.	Assets should be revalued in accordance with the provisions of the Standard and necessary adjustments should be made in the accounts accordingly.
(c)	The Wet High Intensity Magnetic Separator amounted to Rs. 71,565,328 and purchased in August 2019 and used during the year under review, had not been identified as a fixed asset in terms of Sri Lanka Accounting Standards No.16 and stated in accounts as advances.	This will be corrected in the future.	Assets must be capitalized during the relevant period in accordance with the provisions of the Standard.
(d)	The Company identified a stock of 105,205 metric tons as Block A Tailing in the survey of goods conducted in the year 2016. More	That was deducted from the accumulated fund	The impact occurred to the financial statements should be

	than 60 per cent of the production cost from the Ilmenite production account had been added to this stock annually up to the year 2018. Accordingly, a stock of 416,901.76 metric tons worth Rs.879,525,348 had been identified as at 31 December 2018. However, the stock had been written off from the accumulated fund in 2019 since the Company could not sell or process these stocks. However, the profit of the Company had been overstated by those quantities annually owing to this stock. Accordingly, profit-based bonuses as well as statutory payments had increased. Attention had not been paid to the above payments made annually in writing off stocks in this way and the impact occurred to the financial statements had not been rectified retrospectively in terms of the Sri Lanka Accounting Standard No. 8.	according to the unanimous decision taken by the Company.	rectified retrospectively and necessary adjustments should be made with respect to profit-based bonuses as well as statutory payments.
(e)	The capital expenditure amounting to Rs.194,943,317 incurred in the previous years for the work in progress stated in the cash flow statement submitted by the Company in terms of the Sri Lanka Accounting Standards No. 07 had been indicated under the acquisition of assets in the year under review.	A mistake has happened and it will be corrected.	Investment of funds must be accurately stated in the cash flow statement in accordance with the Standard.
(f)	In terms of the Sri Lanka Accounting Standards No. 12, action had not been taken to make provision or to disclose in financial statements the income tax amounting to Rs. 21,520,515, indicated as payable to the Department of Inland Revenue in relation to the financial year 2014/15 and on which a case bearing No. ITA17060600017V1 is being heard presently at the Court of Appeal on taxes.	Noted down to disclose in the financial statements.	Action should be taken to make provision or to disclose in financial statements in accordance with the Standard.

(g)	Employee loan interest had not been calculated at the effective interest rate and adjustments had not been made in terms of paragraph 46 (b) of the Sri Lanka Accounting Standard No. 39.	Noted down to calculate in terms of the Standard.	Calculations should be made in accordance with the Standard and necessary adjustments should be made in the financial statements.

1.5.3 Accounting Deficiencies

	Audit Observation	Comments of the Management	Recommendation
(a)	The net realized value of the stock of Crude Monazite amounting to 393.15 metric tons had been understated by Rs. 979,021 in adjusting it to the income and expenditure account and the final stock had also been understated by that amount.	Noted down to correct it in the year 2020.	Calculations must be done correctly and necessary adjustments must be made to the financial statements.
(b)	Yan Oya Project and official quarters of the employees amounted to Rs. 190,911,256, which had been mentioned as work in progress since 2017 and had been used, were capitalized as assets in the year under review. However, the depreciation expenditure, which was Rs.16,217,364 had been understated since provision for the depreciation had been allocated only for the month of December in the year.	Noted down to correct in the year 2020.	Adjustments for depreciation should be made in the financial statements from the date of utilizing the assets.
(c)	The loan amount of Rs. 25,495,116, obtained from a bank for the purchase of vehicles under the financial leasing scheme, had been indicated as bank overdraft in the financial statements and as a result, the loan amount had been understated by that amount and the bank overdraft had been overstated.	This will be corrected in the preparation of accounts for the year 2020.	Assets and liability items must be accurately stated in the financial statements in accordance with the Standard.

1.6 Accounts Receivable and Payable

1.6.1 Receivables

	Audit Observation	Comments of the Management	Recommendation
(a)	As per the Cabinet decision dated 9 January 2011, the Company provided an amount of Rs.500 million to the State Resources Management Corporation on 10 January 2012 to pay compensation for the employees of the Ceramics Corporation. The recovery of the amount of loan and the interest had not been specified in Condition 5 of the agreement entered in to between the two parties. Although it had been specified in Condition 6 to set off this amount out of the dividends payable to the General Treasury by the Company without getting the consent of the General Treasury, a sum of Rs. 51,742,144 had been allocated as doubtful debt in the year under review and the loan amount of Rs.517,421,448 and the interest had not been recovered so far.	Allocation has been made in the financial statements.	Action should be taken to recover the loan amount and the interest.
(b)	Although the Company could not recover any amount out of Rs. 25,000,000, which had been given as advances to the Plantation Corporation from the year 2012, provision for doubtful debt for the relevant loan amount had not been made in the financial statements.	A case have been filed in the Colombo Commercial High Court and an agreement is being drafted to recover the money in accordance with a common agreement and the balance confirmations have been obtained.	Adequate provision should be made in the financial statements and action should be taken to recover the loan amount.

1.6.2 Payables

	Audit Observation	Comments of the Management	Recommendation
(a)	Action had not been taken to settle the amount of Rs.14,534,964 retained by the Company from 2011 to 2016 in relation to constructions.	It was not possible to release retention money owing to project issues and non-submission of final certificates and the retention money would be settled by 2020 after obtaining the approval of the Board of Directors.	Action should be taken to settle the balances.
(b)	The amounts payable for the goods purchased for the Pulmudai plant for Rs. 2,110,194 in 2017 and for Rs.1,034,039 in 2018 had not been settled.	Payments were delayed due to differences in invoices and issues in returning and receiving of goods and the amounts would be settled by 2020.	Action should be taken to settle the balances payable.
(c)	Action had not been taken to settle Tender deposits amounting to Rs.21,807,205 obtained for mineral sales in the year 2017 and refundable deposits amounting to Rs. 702,500 received from sand collectors from the year 2006 up to the year 2017 until the year under review.	The deposit amounts will be settled in the year 2020 after confirming the amounts properly.	Action should be taken to settle the balances.

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

The following observations are made.

References to Laws, Rules and Regulations	Non-compliances	Comments of the Management	Recommendation
Public Enterprises Circular bearing No. PED/2015/01 of 25 May 2015	An amount of Rs.48,315,500 had been paid to 537 employees as transport allowances without getting the approval of the General Treasury.	Submitted to the General Treasury through the Ministry for approval.	Approval must be obtained from the General Treasury to give allowances.

1.8 Non-compliance with Tax Regulations

	Audit Observation	Comments of the Management	Recommendation
(a)	The tax liability had been understated by Rs. 38,293,717 owing to miscalculations made in the calculation of income taxes for the year under review.	It will be corrected in the year 2020.	Tax liabilities should be calculated accurately and necessary adjustments should be made in the financial statements.
(b)	During the year under review, the deferred tax expenditure had been overstated by Rs. 31,221,798 and the deferred tax liability had been overstated by Rs. 45,266,684 owing to miscalculations made in the calculation of deferred taxes for the year under review.	It will be corrected in the year 2020.	Necessary adjustments should be made in the financial statements.
(c)	The economic service charge amounting to Rs. 10,145,443 had not been stated in the financial statements separately as payables and receivables.	This amount was paid in the year 2020.	Necessary adjustments should be made in the financial statements.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a surplus of Rs. 2,277,746,050 and corresponding surplus in the preceding year amounted to Rs. 621,729,795. Therefore, an improvement amounting to Rs. 1,656,016,255 of the financial result was observed. The major reason for the improvement was the sale of a stock of semi-finished products.

2.2 Trend Analysis of major Income and Expenditure items

The sales of the Company had increased by 152 per cent compared with the preceding year and in relation to that costs of sales had increased by 121 per cent and operating expenses had increased by 40 percent. The sales revenue had increased since a stock of semi - finished products, which could be processed further, amounting to 39,775 metric tons or 43 per cent out of the total sales quantity of minerals of the Company had been sold to a local company. Allocation of 19 per cent out of the total operating expenses to debtors and non-issuing stocks was the reason for the increase in the operating expenditure.

3. Operational Review

3.1 Losses Identified

	Audit Observation	Comments of the Management	Recommendation
(a)	An interest income of Rs.11,264,715 was lost due to the withdrawal of money deposited in 8 fixed deposits worth Rs.606,307,162 prior to the maturity of the deposits.	Amounts deposited were withdrawn since it was not possible to sell minerals on the due time and expenses had to be incurred on repairs and on projects.	Action should be taken to maximize returns on investments.
(b)	Although the Company had incurred Rs. 1,644,505 during the year under review for making recruitments for 9 Posts in the Company, any of the recruitment related thereto had not been made.	Not replied.	The Management must be responsible to incur expenses economically and productively in incurring expenses.

3.2 Operational Inefficiencies

	Audit Observation	Comments of the Management	Recommendation
(a)	Even though the total anticipated quantity of mineral sales of the Company in the year 2019 was 156,025 metric tons, the actual sales volume was 93,028.21 metric tons and its sales value was Rs. 3,891,001,486. The expected targets could not be achieved as a limited number of buyers had responded under international competitive bidding, cancellation of tenders due to various reasons and making arrangements to sell a large stock at the same time.	Sales are carried out with the required approval according to the situation of the market.	The sales process must be carried out according to a plan within the existing level of authority.
(b)	The total amount of Ilmenite, which was the major product of the Company in 2019, a quantity of 49 per cent to 70 per cent of the other major products of the Company and 39,775 metric tons of non-magnetic heavy minerals, which is a semi processed product of the Company had been provided to a Sri Lankan private company and the	Although an extensive international publicity was given for the sale of minerals, only one bidder has submitted bids and the tender was awarded on the	We must strive to obtain high prices through maximum competition and focus attention on methods to add more value to the

relevant company further processes the minerals obtained from Lanka Mineral Sands Ltd. and export them as a raw material without value addition.	approval of the minerals. Cabinet.	

3.3 Contentious Transactions

	Audit Observation	Comments of the Management	Recommendation
(a)	The earned points for one employee should be determined by deducting the bonus of Rs.30,300,767 paid in the year under review based on gross sales revenue from January to March 2019 from bonuses on profit of the year under review. However, without doing so, calculations had been done by adding the interim bonus paid earlier and as a result, an amount of Rs. 26,990,437 had been over paid as bonus. Further, it was observed that these payments were made in contrary to the Circular of 12 March 2019 approved by the Ministry of Industries in relation to the payment of bonuses on profits and even without obtaining the approval of the Board of Directors.	Deducting again is not correct as Interim bonus has been deducted as administrative expenses.	Action should be taken to pay in accordance with the provisions of the Circular and to recover the overpaid bonuses.
(b)	According to the role of the Company, an amount of Rs. 866,900 had been paid to the Sri Lanka Institute of Development Administration to conduct a work study for the development of future human resource. Although the Institution had submitted the relevant report to the Company, human resource had not been planned accordingly. Thus, the aforementioned amount had become an uneconomical expense.	Not replied.	According to the relevant report, human resources should be planned and the maximum benefit should be derived from the expenditure.

3.4 Idle or Underutilized Property, Plant and Equipment

The following observations are made.

	Audit Observation	Comments of the Management	Recommendation
(a)	The Company had spent Rs. 39,481,066 for the construction of a building for a new plant and installed machinery at a cost of Rs.179,229,302 as the current Block A plant of the Company was old and the building had dilapidated and it was not possible to get the maximum capacity. Machine parts purchased for the Kokilai project were also installed at this plant. The capacity of the new plant is 16 metric tons per hour and accordingly, the annual capacity is 140,160 metric tons. However, the contribution in production for the year 2018 was as low as 16,693 metric tons and the contribution in production for the year 2019 was as low as Rs. 14,835.	Idle time has increased due to electricity failures, maintenance, installation of new machines.	Action should be taken to get the maximum capacity from the machines.
(b)	The Company had acquired a mineral rich land in extent of 17.6 hectares for the Kokilai project in Kokilai area in the year 2013 and had paid a sum of Rs. 2.25 million to the District Secretary of Mullaitivu in 2012 and Rs. 39,339,473 had been incurred for the purchase of machinery in 2013. Excavation work had not been carried out in the area until the year under review due to not getting the required excavation permit. Further, all the assets purchased for the project were installed in the other areas of the Pulmudai plant and they were idling and some of the machinery were stored idly in the depots. Even though a part of these machines were installed in the Block A plant, 24 spirals of it were not in working condition. One hundred and seventeen (117) employees were recruited for the Kokilai project in the year 2015 and attached to various locations in the plant.	Agreed.	Action should be taken to obtain the Kokilai excavation permit and start the project.

(**c**)	Even though 4 years had lapsed after importing and installing a dryer machine after incurring a sum of Rs.62**,**370**,**234 on 30 June 2016 for saving fuel costs by 50%, the Company had not been able to put the machine into its working condition and to use it in manufacturing activities even by the date of this report. Further, the Company had also paid a late fee of Rs. 1,164,350 for the machine.	The dryer machine was very old and therefore, a new machine has been purchased and action is being taken to make the Dutch engineers revisit for commissioning.	Management must take action to put the machine in to its working condition and achieve the desired objectives.
(**d**)	The Company had decided in the year 2014 to import a new hydrosizer machine for the wet sand plant from a Sri Lankan Agency of Mineral Technologies Ltd., Australia after considering it as an urgent and essential purchase for improving the production activities of the Company and had purchased the machine for Rs. 15,426,302 in January 2016. Even though a period of four years had elapsed after the purchase of the machine, the Company could not use the machine for production activities even by the date of this report.	A new machine was purchased as the old machine had not worked properly. However, the old machine was restored and the capacity can be increased if the new machine is installed.	Action should be taken to use the machine for manufacturing activities.

3.4 Human Resource Management

	Audit Observation	Comments of the Management	Recommendation
(a)	Although action should be taken to permanently fill the vacancy of the Post of General Manager, which remained vacant since 2015 in order to implement the policies and decisions taken in relation to the production, administration, accounts and other functions of the organization as a whole, officers had not been recruited on secondary basis for the relevant Post without permanently filling this Post.	Although applications were called, a suitable candidate could not be selected and a request was made to the Department of Management Services to reduce the approved qualifications for the Post.	Action should be taken to recruit a permanent officer for the Post of General Manager of the Company.
(b)	Although the Posts of the Senior Management Level of the Company such as the Post of Chief Chemist had been vacant for 9 years and the Post of Medical	Not replied.	Action should be taken expeditiously to recruit officers for the major posts on

	Officer had been vacant for 4 years and the Post of General Manager Finance had been vacant since April 2019, the Company had not taken action to recruit officers for the relevant Posts on permanent basis.		permanent basis.
(c)	The Company had attached 21 officers in 7 posts, recruited from 2011 to 2019 to the Pulmudai plant, where all operations of the Company are carried out, to the head office while there were vacancies at the plant.	Not replied.	Management should take action to deploy the officers recruited to the plant for the operations of the plant.

4. Accountability and Good Governance

4.1 Internal Audit

Audit Observation	Comments of the Management	Recommendation
Even though the Accounting Officer shall ensure that an effective internal control system for the financial control exists in the Company and carry out periodic reviews to monitor the effectiveness of such systems and accordingly make any alterations as required for such systems to be effectively carried out and such reviews should be carried out in writing and a copy of that should be presented to the Auditor General in terms of Section 38 (f) of the Audit Act No. 19 of 2018, there was no information that such a review had been carried out. Further, the Internal Audit Reports had not been submitted to the Department of Management Audit in terms of Section 40 (4) of the Audit Act and although five officers, including two senior management level officers, had been attached to the Internal Audit Unit, an adequate audit had not been carried out according to the audit plan.	Not replied.	The Management should function in terms of the provisions of the Audit Act and ensure that adequate internal audit is carried out.

4.2 Budgetary Control

Audit Observation	Comments of the Management	Recommendation
Eighty six (86) per cent or Rs. 1,483 million out of the capital expenditure was saved. Actual sales had decreased by Rs. 801 million or by 17 per cent when compared with the budgeted sales. Administrative expenditure was saved by Rs. 48 million, or by 20 per cent and overhead expenditure had been over spent by an amount of Rs. 153 million more than the budgeted amount. Accordingly, it was observed at the audit that the budget had not been used as an effective instrument of control as there were significant variations in the budgeted revenue, expenditure and capital expenditure.	Not replied.	The Management must work in accordance with the budgeted goals and achieve targeted objectives.