

Ceylon Petroleum Corporation



Annual Report

2010



Ceylon Petroleum Corporation

2010

ANNUAL REPORT

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OUR VISION

To be the premier customer driven, environmental friendly, enterprise in the petroleum and related industries in the region while contributing towards the prosperity of our nation.



OUR MISSION

To achieve excellence in petroleum refining, sales and marketing of high quality products through a loyal and efficient dealer network and by providing total solutions and services exceeding customer expectations, while utilizing a high technology base for growth and development of the enterprise by employee participation and innovation and maintaining high ethical norms in all its activities with highest concern for health, safety and environment and meet the expectations of the stakeholders.

CORPORATE INFORMATION

BOARD OF DIRECTORS

CHAIRMAN & MANAGING DIRECTOR

Maj. Gen. Asoka Thoradeniya, USP (From 01.01.10 to 16.02.2010)

Ms. Kanthi Wijetunga (From 17.02.2010 to 12.05.2010)

DHS Jayawardena (since 13.05.2010)

DIRECTORS

Mr. Methsiri Wijegunawardana

Ms. M T I V Amarasekera(17.03.2010 – 26.05.2010)

Capt. Nihal Keppetipola(from 01.01.2010 to 19.01.2010)

Mr. W K B Weragama(01.01.2010 to 06.04.2010)

Mr. Udaya Ranjith Seneviratne(from 24.06.2010 to 10.11.2010)

Mr. L Gunawardena(since 06.09.2010)

Ms. Kanthi Wijetunga(upto 24.11.2010)

Ms. Sandya Wijayabandara(since 25.11.2010)

Ms. C D Amarasekara(since 19.08.2010)

Mr. D C Gooneratne(from 01.01.2010 to 29.04.2010)

Mr. M U M Ali Sabry(from 01.07.10 to 31.08.2010)

Mr. C Ekanayake(since 23.07.2010)

AUDITORS

The Auditor General

REGISTERED OFFICE

“Rotunda Tower”, No. 109, Galle Road, Colombo 3.

Telephone	:	2473644(9 lines), 5455455-465
Telegrams	:	2473644 “LANKA OIL”
Cables	:	CEYPETCO
Telex	:	221167,221235,221624 CEPETCO-CE
Fax	:	2473979
E-mail	:	cpcsec@ceypetco.gov.lk .

BANKERS

People’s Bank

Citi Bank N.A.

Hatton National Bank Ltd.

Bank of Ceylon

Commercial Bank

Standard Chartered Bank

SENIOR MANAGEMENT

D H S Jayawardena
Chairman/Managing Director

N R R Jayasekara
Actg. Refinery Manager

J R Wickramasinghe
**Deputy General Manager
(Planning & Development)**

A R Abel
**Deputy General Manager
(Marketing)**

S W Gamage
**Deputy General Manager
(HR & Admin.)**

Ms. R T A Dabare
**Actg. Deputy General Manager
(Finance)**

N N I R Fernando
**Deputy Refinery Manager
(Technical Services)**

N R Amarasinghe
**Actg. Deputy Refinery Manager
(Manufacturing & Operations)**

K S W Kottahachchy
Commercial Manager

P G H Samarawickrama
Manager (Engineering & Premises)

W S Perera
Manager (Internal Audit)

A Lambiyas
Manager (Agrochemicals)

Samantha Pushpalal Withana
Manager (Human Resources)

Ms. R A K C Ariyaratna
Actg. Chief Legal Officer

Ms. P.H.N. Samarasinghe
Head of Secretariat

W.M.K.R.B Wickramasinghe
Marketing Manager (Lube Oil & LPG)

M.K. Garusinghe
Manager (Development)

Maj. M.R.S.P. Samarasinghe
Manager (Security & Investigations)

S.M.C.P. Samarakoon
Actg. Marketing Manager (Retail)

S D S Rajapakse
Actg. Dy. Manager (Supplies)

R S Suntharalingam
Actg. Addl. Finance Manager

REPORT OF THE DIRECTORS

In accordance with Section 32(3) of the Ceylon Petroleum Corporation Act No. 28 of 1961, the Directors of the Ceylon Petroleum Corporation have pleasure in presenting their report together with the Audited Financial Statements for the year ended 31 December 2010. The draft Financial Statements for the year ended 31.12.2010 were approved by the Board at the Board Meeting held on 30.06.2011. However, the Draft Financial Statements were submitted to the Auditor General on 11.05.2011 after obtaining approval for the Financial Statements which were submitted to the Auditor General.

Principal Activities

The principal activities of the Corporation are importing, refining, selling and distributing petroleum products in Sri Lanka.

Associated Company

CPC has contributed 1/3 of share capital at Ceylon Petroleum Storage Terminals Ltd. (CPSTL) which engages in provision of storage and distribution facilities and information technology services to the Corporation.

Review of Business

The Chairman's Review on pages 11 to 18 deals with the year's performance of the Corporation and on the Sri Lanka economy

Systems of Internal Controls

The Board of Directors has instituted an effective and comprehensive system of Internal Controls required to carry on the business of the Corporation in an orderly manner, to safeguard its assets and secure the accuracy and reliability of the Corporation's Records as far as possible.

Human Resources

Corporation while continuing to implement appropriate Human Resource Management policies and practices to enhance employees' skills, HR Division is in the process of preparation of the revised cadre proposal as approved by the Board of Directors. Our Human Resources Management policy emphasize on providing all employees with new opportunities including foreign and local training to

equip to develop their skills and competencies to achieve goals of the Corporation. The newly HR Plan would contribute to improve the efficiency of the management within the entire organization.

Audit Committee

Audit Committee consists of three members, who are Non-Executive Directors including Chairman of Audit Committee. The Committee operates within a clearly defined Terms of Reference (TOR) given by the Public Finance Circular No. PF/PE 7 dated 15 March 2000. Duties and responsibilities of the Audit Committee were included in the audit charter which was approved by the Board of Directors.

Financial Performance

Turnover

The turnover for the year had increased to Rs.256.329 Bn. from the previous year figure of Rs.237.662Bn. which accounted for an increase of 7.85%.

The total turnover of the Corporation during the year is comprised of domestic Sales 95.4% and Indirect Exports 4.6% for the year. Diesel, Petrol, Kerosene and Furnace Oil are the major components of the domestic sales.

Profit / (Loss)

Corporation has continued to incur a loss of Rs. 26,922.819 Mn. during the year. The main contributory factor for the financial loss was due to absence of cost reflective domestic retail selling prices in line with international oil price movement during the year. In addition, supply of furnace oil to CEB and individual power produces at a subsidized rate and sale of diesel and kerosene and furnace oil at subsidized rates resulted for this massive loss.

The loss incurred on sale of Furnace Oil (1500 high sulphur, 1500 low sulphur, Naphtha and 3500 high sulphur) for power generation and industries was recorded at Rs.23,958Mn. while losses due to sale of diesel and kerosene at subsidized rates recorded at Rs.4,676Mn. and Rs.4,295Mn. respectively. The loss due to sale of Jet A-1 to Airlines stood at Rs. 531Mn.

Details of segmental loss of the year 2010 is noted below :-

Segment	Loss – Rs. Mn.
Transport – Supply of Diesel at Subsidized rate	4,676
Power Generation – Supply of Naphtha and Fuel oil at subsidized rates 1500 H/S, 1500 L/S, 3500 L/S)	20,217
Aviation – Supply of Jet A-1 at highly subsidized rate	531
Industries – Supply of Fuel Oil and Kerosene	8,036
Domestic – Supply of LPG at subsidized price	103
Farmer Community – Supply of Agro Chemicals	30
Export Sector – Naphtha & Fuel Oil	129

Despite the heavy losses incurred due to the above reasons, the sale of Petrol 90 octane, 95 octane and super diesel, bitumen and lube oil and other income had contributed positively which resulted to limit overall loss to Rs.26,922.819 Mn.

The details of our profits / (loss) are given below:

	2010 Rs. Mn	2009 Rs. Mn.
Revenue	256,329.157	237,622.619
Cost of Sales	(265,603.764)	(233,540.920)
Gross Profit	(9,274.607)	4,121.700
Operating Income (Finance & Other Income)	532.847	2,290.064
Operating Profit/(Loss)	(8,741.760)	6,411.764
Selling & distribution Exp.	(9,716.083)	(10,421.38)
Administrative Exp.	(1,606.078)	(2,602.887)
Financial Charges	(6,858.899)	(4,740.663)
Profit/(loss) Before Tax	(26,922.819)	(11,353.224)
Taxation	--	(213.733)
Profit/(loss) after Taxation	(26,922.819)	(11,566.957)

Contribution to the Government

	2010 Rs. Mn.	2009 Rs. Mn
Value Added Taxes	7,789	9,007
Excise Duty	18,579	17,864
Social Responsibility Levy	269	461
Dealers Turnover Tax & Imports Turnover Taxes	2,776	2,248
PAL	8,353	5,783
Customs Duty	1,246	18,341
Debit Tax	262	125
NBT	95	166
TOTAL	39,369	53,995

Operating Expenses

The total operating expenses increased to Rs.18,181.06 Mn. during the year under review when compared with Rs.17,764.99 Mn. recorded during the previous year which is a 2.34% increase.

Capital Expenditure

The total Capital Expenditure for the year was Rs.347.596 Mn. whereas the same for 2009 recorded as Rs.270.642 Mn.

Property, Plant & Equipment

Details of Property, Plant & Equipment of the Corporation and their movements are given in Note 6 to the Financial Statements on page 45.

Reserves

As at 31.12.2009, recorded a negative equity capital stood at Rs.13,038.05 Mn. had been deteriorated upto Rs. 39,951.63 Mn. The main contributory factor for deterioration of equity reserves was due to accumulated financial losses since 2008. The movement of the changes in equity is stated on page 30.

Contributed Capital

The total Contributed Capital of the Corporation as at 31 December 2010 was Rs. 1,000 Mn.

Board of Directors

The Board comprises 7 Directors including the Chairman. The Directors of the Corporation during the year under review were:

Mr. D H S Jayawardena – Chairman& Managing Director

Ms. Sandhya Wijayabandara

Mr. Methsiri D Wijegoonawardane

Ms. Champika Amarasekara

Mr. Chethiya Ekanayake

Mr. Lakshman Gunawardena

Ms. Kanthi Wijetunga

Directors' Interest in Contracts & Related Party Transaction

During the year under review Mr. M. Wijegonawardena and Mr. C. Ekanayake functioned as Directors at CPSTL for which CPC has contributed 1/3 of its share capital. With effect from 01/07/2010 Mrs. S. Wijayabandara - Director of CPC was appointed to the Board of CPSTL to represent CPC.

Compliance with Laws and Regulations

The Corporation has not engaged in any activities contravening the laws and regulations. All those responsible for ensuring compliance with the provisions in various laws and regulations confirm their compliance to the Board.

Statutory Payments

The Directors, to the best of their knowledge and belief are satisfied that all statutory payments due to the Government and in relation to employees have been made on time.

Event after Balance Sheet Date

On the balance sheet date, there were two cases pending relating to the hedging transactions and current position is noted below :-

(i) Citi Bank vs. CPC Arbitration in London

The claim of the Citi Bank NA was for two derivative transactions between July 2007 and July 2008 made by reference to a master agreement.

Citi Bank claimed US\$.195,458,092.67 as a principal sum due from CPC with interest.

The award delivered was on 31.07.2011. Accordingly, to award transactions numbered 1 – 16 made by Citi Bank between 11.07.2007 and 16.07.2008 by reference to master agreement are each declared to have been and to remain legally null and void as being ultra vires and beyond the capacity of Respondent (CPC).

CPC was liable to pay Citi Bank a sum of US\$.17,926,300 together with interest. Citi Bank was liable to pay CPC a sum of US\$.16,723,750 together with interest. The net amount payable by CPC was US\$. 1,202,550.

Both parties are entitled to interest on each payment made to the other from the date of payment to date of re-payment.

The interest calculation made upto 21.11.2011 after setting off interest receivable from Citi Bank NA is US\$. 164,168.29. The total amount payable by CPC to Citi Bank is US\$.1,202,550 + 164,168.29 totaling US\$.1,366,718.29.

The Arbitration Tribunal issued the final award on 15.12.2011. Accordingly, Citi Bank should pay CPC, a total sum of US\$.2,705,760.43 as legal cost.

Accordingly, CPC received US\$.1,339,042.14 as net settlement (LKR – 153,458,915.90).

(ii) Standard Chartered Bank vs. CPC

Standard Chartered Bank (SCB) claimed US\$.161,733,500 plus interest being the sum allegedly due under two derivative transactions entered into with CPC on 28.05.2008 and 09.07.2008 (Transactions 08 & 09).

CPC made a counter claim on various grounds. The Court concluded that SCB's claim in respect of transaction 08 & 09 succeeds and that CPC's counter claim be dismissed. The Court ordered that CPC should pay SCB a sum of US\$.166,476,281.77 plus 50% of cost to be paid was GBP.2,963,546.02. CPC appealed to the Court of Appeal in U.K. against the judgement given and the judgement of the Court of Appeal was in favour of SCB. Therefore, CPC made an appeal to the Supreme Court in U.K. The matter is pending. All legal activities are performed through the Hon. Attorney General.

Going Concern

The Board of Directors has reviewed the Corporation's business plan and is satisfied that the Corporation has adequate resources to continue its operations in the foreseeable future. Accordingly, the Financial Statements are prepared based on the going concern basis. However, Auditor General has reported in his report for the year ended 31.12.2010 that due to negative equity position of Rs.39,952 Mn., the ability of the Corporation to continue as a going concern without the financial assistance of the Government of Sri Lanka and other financial institutions was doubtful.

Internal Controls, Risk Management & Compliance

Directors are responsible for the system of internal controls and risk management and place considerable importance on maintaining a strong control environment to protect and safeguard assets of the Corporation and prevent frauds and mismanagement. Whilst inherent and residual risks cannot be completely eliminated, the Corporation attempts to minimize them by ensuring that appropriate infrastructure, controls, systems and ethical behavior are applied within predetermined procedures and constraints. The Directors and management have put in place risk management policies and guidelines. Senior Management Committee and Audit Committee are established to monitor and manage all material risks.

Appointment of Auditors

The Auditor General is the Auditor of the Corporation. He has been appointed in terms of the provisions in Article 154 of the Constitution of the Democratic Socialist Republic of Sri Lanka.

For and on behalf of the Board of Directors



D H S Jayawardena
CHAIRMAN & MANAGING DIRECTOR
CEYLON PETROLEUM CORPORATION

CHAIRMAN'S REPORT

Introduction

As reported by the Central Bank of Sri Lanka, the economy of Sri Lanka demonstrated an overall growth rate of eight percent in 2010 reflecting a fast recovery from the setback suffered in 2009 and moved to a high and sustainable growth path.

International crude oil prices remained high in 2010 compared to lower prices in the previous year. The average international crude oil price increased to US Dollars 80 per barrel in 2010 from US Dollars 62 per barrel in 2009, reflecting an increase of 29%. This has been increased up to US Dollars 92 by the end of 2010 due to strong global demand and geo-political instability in certain oil producing regions.

The average cost and freight (C&F) price of crude oil imported by CPC increased by 25.1% to US Dollars 79.43 per barrel in 2010. However, the retail prices have not been revised during the year and the prices remained the same since December 2009.

Major Milestones taken to Improve Financial and Operational Soundness of CPC

1. CPC increased a lot of spot checks island-wide filling stations to investigate the adulteration and tempering of meters. A lot of dealers were under heavy pressure to stop this malpractice by the Corporation as a result of continuous checks greatly tempering of meters and adulteration was reduced substantially. CPC with the support of the Ministry of Defence raided all the unscrupulous dealers who were dealing with sludge oil leaking into CPC sheds in big quantities. This situation resulted in reducing the sale of adulterated fuel at distribution points at a larger extent. This racket was in operation for number of years and consumers were receiving adulterated oil at distribution points although CPC imported fuels with standard specifications. My special thanks on behalf of Board of Directors, to the Secretary of Defense and the Ministry of Defense for such co-operation extended to CPC in order to maintain rule of law and to have distribution system for petroleum products of CPC on pool proof manner.
2. There were fuel pumps imported from China not upto the specification of CPC's standards that could be easily tempered. As a result, a large number of pumps in filling stations were defective and most of consumers received short measure of fuel. We disbanded purchase of

locally made spare parts which were supplied to the filling stations with imported genuine parts from two manufacturers of dispensing pumps and repaired all defective pumps in the island to give a better service to the consumers at the expense of the suppliers.

3. CPC negotiated with all the banks and reduced the exorbitant interest rates charged to a commercial level in par with other takers in the market thus saved millions of Rupees on interest income.
4. Introduced for the first time in the history of CPC a method to monitor the exchange rates on daily basis and purchased at the right time. Dollars were purchased for settlement of import bills not at the rates quoted by bankers but at the market rates by monitoring market behaviour as and when exchange rates were favourable due to market forces. As a result of this exercise, CPC had obtained a substantial saving which hitherto not known to CPC.
5. Action was taken to reject substandard oil shipments and imposed heavy penalties for acts and omission of such suppliers. Claims were lodged against shipping companies for extra demurrages when such demurrages were not payable by the CPC due to lack of knowledge by not interpreting the charter party clauses. Thereby, saved a huge amount of demurrages during the year. As a result of this, shipping cost of the current year had substantially come down. By this operation over billion of Rupees for the present and the past was saved to CPC which had not been accounted for and claims were lodged for the excess payments made by CPC to the charterers.
6. It is noteworthy to mention that action was taken to strengthen the Finance, Legal, Administration, Retail Marketing Departments by appointing professionally capable experienced Managers, Lawyers and Accountants to improve operational activities and run on commercial basis and placed the CPC on commercial footing.
7. All legal cases filed against CPC were carefully monitored and reasons were examined for losses of past cases. Under a strong enforcement mechanism, with the support of Department of Attorney General and our Legal Officers, defended all cases much vigorously and gained success.
8. During the year under review, Refinery Manager was appointed and refinery operated with minimum breakdowns and continued in a satisfactory manner. Dispensed with the system of purchasing spare parts to the refinery from the lowest tenders and bought the same brands that were originally fitted at the refinery and installed so that breakdowns were minimized. Plant

maintenance programme, cleaning of tanks and all other activities were carried out in a planned manner which enabled to improve the storage capacity of the petroleum products. This resulted supply of fuel at lesser cost compared with high imported cost of finished petroleum products prevailed in the year.

9. Storage tanks which were not renovated for the many past years, (mostly crude oil tanks) tenders were awarded and commissioned many tanks to improve the storage capacity.
10. The biggest achievement during my tenure of office was to arrange a US\$.100 million loan from a private bank on which I was a Director in order to settle a fuel bill that was overdue and both state commercial banks could not accommodate this payment. Had it not been done, no credit facilities would have been extended by any vendor and the country would have declared bankrupt due to CPC not honouring its commitments and would have been a defaulter with no future credit facility. If this happened, the country would have to face untold hardships.
11. Action was taken to get compensation from two manufacturers for supply of sub standard dispensing pumps out of specifications of CPC to minimize short measure pumping air to the consumer tanks. We took timely action by holding manufacturers guarantees and got all required spare parts for the dispensing pumps free of charge. As a result of this process, a substantial amount of money was saved during the year.
12. With the dawning of the peace in the North and East provinces, a large number of filling stations were constructed under 'UthuruWasanthaya' and 'NagenahiraUdanaya' programmes. These activities facilitated all consumers in North and East provinces to have better products directly from filling stations. The supply of fuel to these areas was dispatched by using rail and road transport methods minimizing transport cost and getting more revenue to Sri Lanka Railways Department.
13. Various additions, commissions, transport rebates over and excess mileage relating to transport of fuel was abandoned to a market regular rate revised to the benefit of CPC.
14. The fuel stations that were newly commissioned and monitored to ensure CPC's standard specifications and procedures were maintained. Any such filling station that did not comply to the standard procedure, stringent measures were taken.
15. A large amount of trade debts whose recoverability was in doubt and avoided payment over the years, arrangements were made with such debtors by a mutual understanding and

negotiation to pay in instalment basis to CPC. These debts were categorized in books of accounts as bad and doubtful debts. CPC collected over Rs.250 million from this kind of defaults.

16. A similar arrangement was implemented to collect overdue interest from trade debtors who had failed to pay interest for delayed payments. Rs. 820 Mn. was collected as default payment of interest as a result of this initiative during the year 2010.

17. Approval of the Cabinet of Ministers was received and tenders were called for proposed Aviation Fuel Farm and Fuel Hydrant System at Hambantota International Airport (HIA)-Mattala.

Financial Performance

Corporation has continued to incur a loss of Rs. 26,922.819 Mn. during the year. The main contributory factor for the financial loss was due to absence of cost reflective retail price mechanism in line with international oil price movement. During the year under review, sale of furnace oil to CEB and Individual power producers was made at a subsidized rate and diesel and kerosene were sold at domestic retail market below the refined/import cost.

The Corporation sustained a loss of Rs.4,676 Mn. and Rs.19,695Mn. for the sale of diesel (transport purposes) and high sulphur fuel oil used for power generation (3500, 1500) respectively at subsidized rates. At the same time, the Corporation incurred a loss of Rs.25.839Mn. on sale of low sulphur furnace oil for power generation. Furthermore, supply of naphtha at subsidized rates for power generation purposes CPC had suffered a loss of Rs.495.813Mn. Supply of Jet fuel oil specially to Sri Lankan Airlines and Mihin Air at subsidized rates, CPC incurred a loss of Rs.531.236Mn. CPC also suffered a loss of Rs.3,741Mn. for supply of high sulphur furnace oil (1500 & 800) to the industries. The loss of Rs.4,295.466Mn. and Rs.102.675 Mn. were suffered by CPC on sale of kerosene and LPG respectively during the year. At the same time, Agro chemical Division suffered a loss of Rs. 30.440Mn. during the year under review.

Despite the heavy losses incurred due to the above reasons, the sale of Petrol 90 octane, 95 octane, super diesel, bitumen, lube oil and other income had contributed positively which resulted to limit overall loss to Rs. 26,922.819Mn.

Corporate Governance

An Audit Committee, which consists of three Non-Executive Board Members, reviews independently all strategic issues of the Corporation at regular meetings to achieve the objective of bringing corporate governance in par with global standards. As a part of corporate governance process, the internal controls, financial and operational transparency have been improved by strengthening Internal Audit Function of CPC. The Audit Committee reviews financial and operational activities of CPC.

Corporate Social Responsibility

Corporate Social Responsibility is continued to be our main focus of attention and all attempts are made to meet the needs of the entire nation at the least possible cost to the consumer. As mentioned above, initiatives have promptly taken under the “NegenahiraUdanaya” and “UthuruWasanthaya” programs to supply fuels to the cleared areas within a minimum possible time with the intention of enhancing the livelihood of the affected people in these areas. We also guaranteed uninterrupted fuel supplies to Government institutions at any cost.

CPC has contributed a massive amount of Rs. 39.369 Bn. to the Government coffers by duties and taxes during the year 2010.

Production

Refinery completed 41 years of operation on 06th August. It had operated for 317 stream days and processed 1,752,716 metric tons of Crude Oil during the year. The middle distillate recovery as a percentage of the weight of crude intake was 39.5% and the own use and handling losses were 5.8%.

Import of Crude Oil and Refined Products

The Corporation has imported 1,685 Mn. metric tons of crude oil at a C&F cost of US\$. 983.754 Mn. The average crude oil (C&F) cost was USD 79.43 per bbl compared to USD 63.48 per bbl during the previous year. The freight charges for importing crude oil average to USD 7.12 per metric ton, when compared to 10.47 per MT in the previous year. During the major shutdown, major repairs were carried out in all areas of engineering activities and work connected to preventive maintenance.

Refined Bulk Products Imports were metric tons of 1,900 Mn. and C & F value was USD 1,279.383 Mn.

All crude purchases during the year were based on “Term contracts” with national oil companies of oil producing countries. The import mix comprises of 91% of Iranian light and 09% of Arabian Light.

Services Rendered by Ceylon Petroleum Storage Terminal Ltd. (CPSTL)

With the restructuring of CPC in the year 2003, the storage and operations of Kolonnawa and 12 regional Bulk Depots located island wide, data processing and distribution activities were segregated and brought under the CPSTL.

CPSTL along with CPC hold regular stock review meetings with marketing companies, to monitor and ensure products availability to meet the country’s demand. It recovers a terminal fee for the provision of storage and operation services, and specific charges for distribution and data processing services rendered to CPC.

Revenue

Revenue for the year had reached Rs. 276.550 Bn. when compared to the previous year revenue of Rs. 257.508 Bn.

During the year under review CPC had sold 103.182 Mn. Ltrs. of Auto Diesel, 256.705 Mn. Ltrs. of High Sulphur Fuel Oil (3500), 508.842 Mn. Ltrs. High Sulphur Furnace oil (1500) and 116.605 Mn. Ltrs. of Low Sulphur Fuel Oil (1500) and 78.455 Mn. Ltrs. Naphtha for power generation by Ceylon Electricity Board (CEB) and independent power producing companies.

During the year under review, the sale of Jet A-1 for the foreign Aviation Companies was increased by 19.8% and it generated a total revenue of Rs. 24,199.44 Mn. Out of total aviation sales 54.6% accounted on Sri Lankan Airlines which amounted Jet A-1 189.67 Mn. Ltrs.

Agrochemicals

CPC continues its pricing policy of maintaining reasonable prices for Agro Chemicals used by cultivators and Plantation Sector, thus making a useful contribution towards lower production cost, thereby boosting overall agriculture sector.

The current “Ceypetco” agro chemical product range consist of 5 Weedcides, 4 Fungicides and 6 Insecticides. A serious consideration has been continuously given to extend our product range to cover

other agro based areas in the future. We also plan to promote sales of Ceypetco agro Sales Centers, which would be set up in agro based areas of the country.

Human Resource Development and Welfare

The employee strength by the end of year 2010 was 2661 in the permanent cadre and 83 in the casual cadre.

CPC has provided its employees and their families a Medical Assistance Scheme which is managed by the Thrift Society of the Corporation. The Corporation employs two Medical Officers on fulltime basis to serve employees. The hospitalization costs and indoor treatments amount to Rs. 40.5 Mn. during the year under review. A monthly allowance of Rs. 250/= is also paid to all employees for outdoor medical treatment.

A gratuity equivalent to half a month pay for every year of service is paid under the Gratuity Act and additional retirement and death benefits are paid out of Thrift Society funds. A Death Gratuity is also paid for death of an employee. Corporation also provided financial assistance to the CPC Employees' Sports Club with a view to encourage sports activities. It maintains four Holiday Homes outstation, exclusively for the usage of employees and their families. There are several loan facilities granted at concessionary interest rates to fulfill many necessities of employees.

We have also allocated funds for training employees locally and abroad. Funds are also allocated for improving the knowledge of languages and computer literacy of employees to upgrade their working environment.

The practice of awarding employees who have satisfactorily completed their services is as follows;

20 years	-	Rs. 10,000/=
25 years	-	Gold Coin of 2.5 sovereign
30 years	-	Rs. 20,000/=
35 years	-	Rs. 25,000/=
40 years	-	Rs. 40,000/=

Employees' children who are selected for government University education are awarded scholarships as a welfare activity by the Corporation.

Environment Safety

CPC being the market leader of petroleum products in the island and the owner of the only local refinery in the country, is fully aware of its obligations to minimize environmental pollution, and concerned about the environment safety in handling and usage of petroleum products. In line with world environmental standards, CPC is planning a modernization project at refinery, in order to produce low sulphur Diesel.

Acknowledgement

On behalf of the Board of Directors of the Ceylon Petroleum Corporation, I would like to thank all members of the CPC team, who had stood with me to take all the challenges during this period. I also thank the Hon. Minister of Petroleum and Petroleum Resources Development and his Officials, the General Treasury, the Central Bank of Sri Lanka and all our business partners and customers for their co-operation and their continued support.

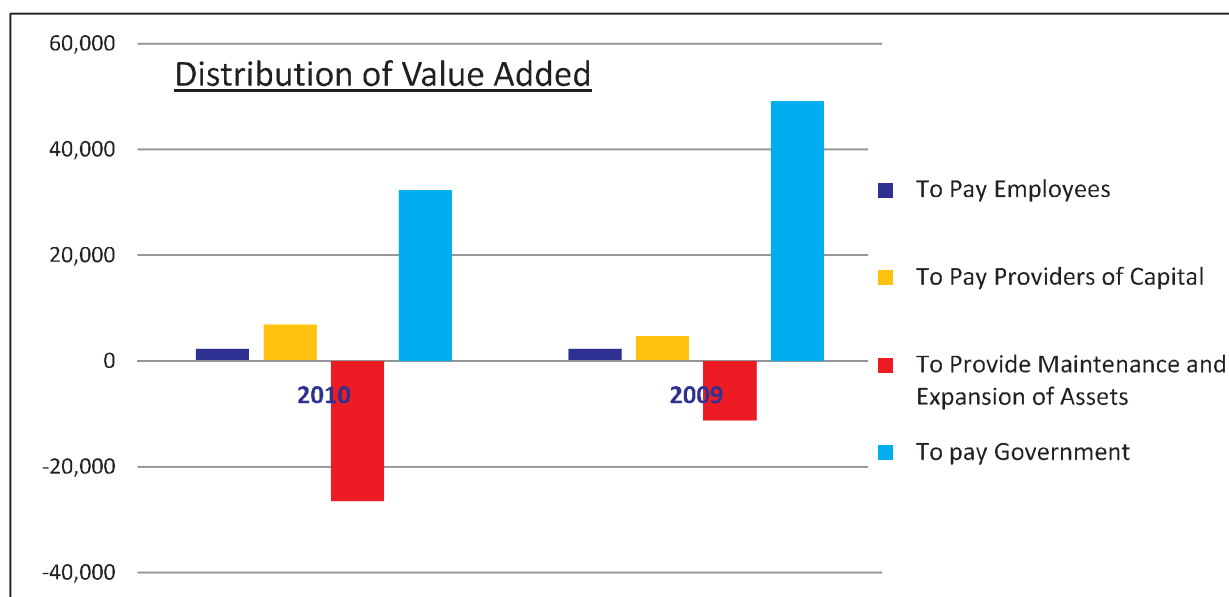


D H S Jayawardena

**CHAIRMAN & MANAGING DIRECTOR
CEYLON PETROLEUM CORPORATION**

STATEMENT OF VALUE ADDED

	2010		2009	
	Rs. Mn.		Rs. Mn.	
Turnover	279,167		257,508	
Bought in Materials & Services	(264,250)		(212,680)	
Value Added	14,917		44,828	
Applied the following way	%		%	
To Pay Employees				
Wages & Fringe Benefits	2,308	15.47	2,301	5.13
To Pay Providers of Capital				
Interest on Loans	6,859	45.98	4,741	10.58
To Provide Maintenance and Expansion of Assets				
Depreciation	374	2.51	353	0.79
Retained Profit / (Loss)	(26,923)	(180.49)	(11,664)	26.02
To pay Government				
Taxes, Duties, Stamp Duty and Contribution to the General Treasury	32,299	216.53	49,096	109.52
Value Added	14,917	100	48,828	100



HIGHLIGHTS

FINANCIAL	UNIT	2010	2009
Gross Revenue (after Sales Taxes)	Rs. Mn.	256,329.157	237,662.619
Gross Profit/(Loss)	Rs. Mn.	(9,274.607)	2,935.631
Operational Profit/(Loss)	Rs. Mn.	(8,471.760)	4,121.700
Finance Charges	Rs. Mn.	6,858.899	4,740.664
Profit/(Loss) before Taxation	Rs. Mn.	(26,922.819)	(11,353.224)
Net profit / (Loss) after Taxation	Rs. Mn.	(26,922.819)	(11,566.957)
Capital and Reserves	Rs. Mn.	(39,951.634)	(13,038.049)
Long Term Borrowings	Rs. Mn.	29,224.531	33,514.223
Capital Expenditure	Rs. Mn.	347.596	270.642
IMPORTS			
Crude Oil Imports	Metric Tons	1,684,601	1,931,529
Refined Bulk Products Imports	Metric Tons	1,900,032	1,449,969
C&F Value	Rs. Mn.	252,714.231	189,848.570
OPERATIONS			
Sales	Metric Tons	3,087.351	4,208.348
Refinery Throughput	Metric Tons	1,752,716	1,894.910
MARKETING			
CPC Owned	Number	250	252
Dealer Owned	Number	733	712
Dealer Controlled	Number	47	48
EMPLOYEES			
No. of employees at the yearend	Number	2,744	2,792
Total emoluments for the year	Rs. Mn.	2,308.165	2,055.826
Value added per employee	Rs.	841,168	736,327

CORPORATE GOVERNANCE

Corporate Governance embodies the principles of honesty, objectivity, integrity, transparency and ethics in carrying out operational activities of an Organization. Concept of Corporate governance deals with the relationship with many stakeholders involved in business operations and goals for which the Corporation is governed. The Board of Directors is committed to ensure the operational activities of the Corporation are always conducted in accordance with accepted rules and regulations, highest ethical standards and in the best interest of all stakeholders. The Corporation ensures to practice the principles of corporate governance to achieve transparency, integrity and accountability in its functions which are vital for achieving core objectives of a sustainable energy Corporation with a strong environment friendly process and playing pivotal role in national economy.

The Corporation is guided by the requirements of the code of best practice on Corporate Governance issued by Institute of Chartered Accountants of Sri Lanka.

CPC being a Public Corporation established by an Act of Parliament and is governed by Finance Act No.38 of 1971 which provides for finance control of the Corporation specifying the requirements of Corporate Plan, budgets, accounts, audit, appropriation of surpluses and borrowing powers etc. In addition the Corporation is to conduct its operation in line with circulars issued by the Ministry of Finance & Planning, Ministry of Public Administration.

Composition of Board of Directors

The Board of Directors comprises of a Chairman & Managing Director and six Non-Executive Directors. The Chairman and Managing Director and other Directors are appointed by Hon. Minister of Petroleum and Petroleum Resource Development in accordance with the Ceylon Petroleum Corporation Act No.28 of 1961 and subsequent amendments. One such Director is a representative of the General Treasury (Ministry of Finance & Planning)

Subject to reappointment, the Directors have initial tenures not exceeding a period of three years on the Board. In taking decisions the Board obtains relevant information from Corporate Management and if required, obtains information from External Professionals.

The Board of Directors is responsible for conducting the business affairs of the Corporation while adhering to the statutory requirements under which the Corporation is governed. The Board of Directors is also responsible for granting approval for annual financial statements, the Annual Budgets, Corporate Plan, Action Plan and reviewing financial performance on regular basis. The Board oversees the granting of approvals relating to key appointments, staff promotions, major capital expenditure investments and credit facilities to Corporate Customers.

Board Meetings

Regular Board Meetings are held on monthly, while special Board Meetings are convened as and when required. Senior Managers also attend meetings on invitation.

The Board Meetings are conducted on a formal agenda and Directors are provided with relevant background information by Corporate Managements prior to meetings. Eight Board meetings were held during the year under review, and there was full attendance at all these meetings.

Compliance and Transparency

The Ceylon Petroleum Corporation is committed to maintain transparency in all its dealings. The Corporation complies with Sri Lanka Accounting Standards and relevant regulations to ensure accountability. The strong internal control compliance measures have been integrated into the Corporation's daily operations. In accordance with Finance Act No.38 of 1971, financial statements are published annually and tabled in Parliament. Also in compliance with Finance Act, the Auditor General carries out the External Audit of the Corporation.

Corporate Management

The Chairman/Managing Director manages the day-to-day affairs of the Corporation based on strategic direction, Policy formation and Procedures approved by the Board of Directors from time to time. Operations and main administration of CPC can be divided into two broader categories namely Refinery operation and Head Office operation including Regional Offices. Refinery operation is headed by Refinery Managers who is assisted by Deputy Refinery Managers in different core technical areas such as Electrical, Chemical and Mechanical.

Each Function at Head Office level is headed by a Deputy General Manager or a Manager who assist the Chairman/Managing Director in day-to-day functioning of the Corporation. The Corporate

Managers are well qualified with academic degrees and relevant Professional qualifications in their respective functional areas.

The Audit Committee

Composition of the Audit Committee

The Audit Committee appointed by and responsible to the Board of Directors, comprises of three Non-Executive Directors.

Two Committees were chaired by Mr. Methsiri Wijegunawardena a Non-Executive Director and other two Committees were chaired by Mr. Udaya Ranjith Seneviratne. The other two members comprise of Mr. David Charitha Gunarathne – Non-Executive Director (up to 45 Audit Committee) and Mr. W K B Weragama – Non-Executive Director upto 46 Audit Committee, Ms. Champika Dilhara Amarasekara and Ms. Sandhya Wijayabandara – both non-Executive Directors. The Chairman of the Audit Committee is a Senior Chartered Accountant – Association of Certified Accountants – U.K., acclaimed for his professional knowledge and expertise in financial and he had held Senior Management positions in Private and Public Sector Enterprises.

The Manager – Internal Audit acts as Secretary to the Audit Committee.

Terms and Reference of the Committee is governed by the Charter of Audit Committee approved by the Board of Directors which include key functional areas prescribed in circulars issued by the Department of Public Enterprises at the General Treasury.

Tasks of the Audit Committee

The Committee reviewed the financial reporting system adopted by the Corporation in preparation, presentation and adequacy of disclosures in Annual Financial Statements to ensure reliability of the process, consistency of accounting policies and concepts adopted and their compliance with the Sri Lanka Accounting Standards.

Meetings

During the year, the Committee had four meetings to discuss the matters within its purview.

The Committee members who were present at the meetings are as follows :-

S/No.	Date	Venue	Strength of the Committee	No. of Members present	Names of Members present
45	26/03/10	CPC Head Office Colombo 03	03	03	Mr.M Wijegunawardena Mr.W K B Weragama Mr.D C Gunarathne
46	20/09/10	” ”	03	03	Mr.U R Seneviratne Mr.M Wijegunawardena Ms.C D Amarasekara
47	29/10/10	” ”	03	03	Mr.U R Seneviratne Mr.M Wijegunawardena Ms.C D Amarasekara
48	01/12/10	” ”	03	03	Mr.M Wijegunawardena Ms.C D Amarasekara Ms. S Wijayabandara

Works Performed by the Audit Committee

During the year under review, the Audit Committee discussed following strategic issues faced by the Corporation and submitted their reports to the Board of Directors for necessary action.

- (i) Idle properties of the Corporation
- (ii) Identification of Strategic Business Units, cost centres in order to generate management information and reliable internal financial information for decision making purposes.
- (iii) Reviewed by internal and external audit queries and actions taken to expedite the submission of replies
- (iv) Reviewed matters reported in Auditor General Report and discussed reply sent to Auditor General
- (v) Discussed strategic issues faced by CPC and actions required to mitigate such risks
- (vi) Reviewed closely the progress of Head Office construction Project, Project relating to Enterprise Resource Planning (ERP)
- (vii) Recoverability of trade debts receivable from state owned departments and commercial enterprises
- (viii) Approval of Annual Audit Plan and review of performance of Internal Audit.

Senior Management Committee

Senior Management Committee consists of two non-executive Directors and one of the Non-Executive Directors is headed by the Senior Management Committee. The Management Committee sits once a month prior to monthly Board meeting to discuss all matters reported for Board of directors. The Committee submits its report to the Board meeting for final approval. All Senior Managers, Heads of Functions take part in Senior Management Committee.

Financial Disclosures

The Board of Directors is responsible for presenting Financial Statements that provide a true and fair view of the operations of the Corporation. Financial Statements are prepared in accordance with the requirements of Sri Lanka Accounting Standards, Finance Act and CPC Act.

Internal Controls

The Board of Directors is responsible for maintaining a sound system of internal control for safeguarding assets against an unauthorized use or disposition and to ensure maintaining of proper accounting records for reliability and usefulness of financial information used within the Corporation.

Such internal control procedures are designated to manage rather than eliminate the risks of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatements, errors, losses or frauds. The key procedures established by the Board of Directors are designated to provide effective internal control within the Corporation.

The Internal Audit Department of the Corporation is entrusted to review all internal control procedures and their adequacy and regular recommendation for improvements of internal controls.

Internal Audit

Internal Audit Department of the Corporation is headed by professionally qualified Accountant. The main tasks of Internal Audit Functions are to carry out internal audit reviews, risk analysis and compliance and substantive audit review to assess the reasonableness, effectiveness of internal control mechanism in relation to all operational system within the Corporation.

During the year under review, the Internal Audit Function has performed the following activities in addition to routine audit texts.

- (i) Internal Audit reviewed the Accounting Policies used in preparation of Financial Statement of the Corporation and their adequacy and relevance.
- (ii) Systems and procedures are in place to identify, control and report on the major risks including credit, operational risks.
- (iii) Reports and external Audit queries raised by external audit and assessed the adequacy and reasonableness of replies sent by the Corporation.
- (iv) With the support of external audit, to share the resources and discussed the major areas of audit concerns that required attention of Internal Audit Department.
- (v) Internal Audit raised Audit Queries after reviewing the operational system and drew the attention of the Corporation to improve existing internal controls that required safeguard its assets and reliability of financial records.

Relationship with the General Treasury & Central Bank

The Corporation is closely associated with the Central Bank of Sri Lanka (CBSL) and the General Treasury and obtains their advices when managing Corporation's treasury operations. The Corporation also seeks advice and guidance for major expansion programmes and borrowings relating to imports of fuels.

FINANCIAL STATEMENTS

- + Income Statement
- + Balance Sheet
- + Statement of Changes in Equity
- + Cash Flow Statement
- + Accounting Policies
- + Notes to the Accounts

INCOME STATEMENT

Year Ended 31 December

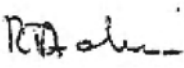
	Note	2010 Rs. Mn Year Ended 31.12.2010	2009 Rs. Mn Year Ended 31.12.2009
Revenue	1	256,329.157	237,662.619
Cost of Sales	2	(265,603.764)	(233,540.920)
Gross Profit/(Loss)		(9,274.607)	4,121.700
Other Operating Income	3	302.233	1,186.069
Selling & Distribution Expenses	3.1	(9,716.083)	(10,421.438)
Administrative Expenses	3.2	(1,606.078)	(2,602.887)
Finance Charges	3.3	(6,858.899)	(4,740.663)
Finance Income	3.4	230.614	1,103.995
Profit /(Loss) Before Tax	4	(26,922.820)	(11,353.224)
Income Tax Expense	5	0.000	(213.733)
Profit /(Loss) for the year		(26,922.820)	(11,566.957)

STATEMENT OF FINANCIAL POSITION

Year Ended 31 December

	Note	2010 Rs. Mn Year Ended 31.12.2010	2009 Rs. Mn Year Ended 31.12.2009
ASSETS			
Non - Current Assets			
Property, Plant & Equipments	6	8,280.084	5,041.139
Investment in Associated Companies	7.1	2,500.000	2,500.000
Other Investments	7.2	41.876	41.876
Trade and Other Receivables - More than one year	8	6,699.985	4,201.681
Deferred Tax Asset	5	689.623	689.623
		18,211.568	12,474.319
Current Assets			
Inventories	9	41,433.109	25,568.278
Trade & Other Receivables - Due within one year	8	80,022.307	77,232.516
Income Tax Recoverable		244.357	106.369
Cash and Cash Equivalents	10	13,312.111	31,762.640
		135,011.884	134,669.803
Total Assets		153,223.452	147,144.122
EQUITY AND LIABILITIES			
Capital and Reserves			
Contributed Capital	11	1,000.000	1,000.000
Capital Reserve	12	4,992.686	4,992.686
Revaluation Reserve	13	25.696	25.696
Insurance Reserve	14	619.432	610.198
Retained Earnings		(46,589.448)	19,666.628)
Total Equity		(39,951.634)	(13,038.048)
Non - Current Liabilities			
Retirement Benefits Liability	15	746.337	735.165
Interest Bearing Loans & Borrowings	16	28,478.194	32,779.058
		29,224.531	33,514.223
Current Liabilities			
Trade and Other Payables	17	145,632.415	120,421.143
Current Portion of Interest Bearing Loans & Borrowings	18	18,147.450	6,076.113
Provision for Deemed Dividend		170.691	170.691
		163,950.556	126,667.947
Total Equity and Liabilities		153,223.452	147,144.122


Titus Jayawardene
CHAIRMAN


R T A Dabare
ACTG. D.G.M. (F)


R S Suntharalingam
ACTG. ADDL. FINANCE MANAGER

STATEMENTS OF CHANGES IN EQUITY

Year Ended 31 December

		Reserves.....				
	Contributed	Capital	Revaluation	Insurance	Retained	Total
	Capital	Reserve	Reserve	Reserve	Earnings	(Restated)
Balance as at 31st December 2005	1,000.000	1,917.043	25.696	474.013	(432.626)	2,984.126
Surplus during the year				8.197		8.197
Net Profit/(Loss) for the Period					7,710.889	7,710.889
Deemed Dividend					(1,105.400)	(1,105.400)
Net re-structuring sale proceed		3,075.643				3,075.643
Balance as at 1st January 2006 as previously stated	1,000.000	4,992.686	25.696	482.210	6,172.863	12,673.455
<u>Correction of Prior Period Errors Prior to 01.01.2006</u>						
(a) Reversal of Over provision made to Thrift Society in 2004					100.000	100.000
(b) Provisioning for non recoverable ACT					(376.000)	(376.000)
(c) Recognition of Deferred Taxation					(109.380)	(109.380)
Balance as at 1st January 2006 (restated)	1,000.000	4,992.686	25.696	482.210	5,787.483	12,288.075
Accounting Period 2006						
(e) Correction of the excess Finance Cost to accounting period 2006					(82.416)	(82.416)
(f) Correction of non provisioning for arrears in Turnover Tax related to the accounting period 30.09.2003 to 30.09.2005					(158.803)	(158.803)
Deemed Dividend					(54.568)	(54.568)
Surplus during the year				19.878		19.878
Net Loss for the Period					(946.220)	(946.220)
Balance as at 1st January 2006 (restated)	1,000.000	4,992.686	25.696	502.088	4,545.476	11,065.946
Accounting Period 2007						
Surplus during the year				20.991		20.991
Net Profit for the period					2,862.337	2,862.337
Deemed Dividend					(381.464)	(381.464)
Balance as at 1st January 2007	1,000.000	4,992.686	25.696	523.079	7,026.349	13,567.810
Accounting Period 2008						
Surplus during the year				44.735		44.735
Net Loss for the period					(14,952.518)	(14,952.518)
Deemed Dividend					(76.459)	(76.459)
Balance as at 1st January 2008	1,000.000	4,992.686	25.696	567.814	(8,002.628)	(1,416.432)
Accounting Period 2009						
Surplus during the year				42.384		42.384
Net Profit/(Loss) for the period					(11,566.957)	(11,566.957)
Deemed Dividend					(97.044)	(97.044)
Balance as at 31st December 2009	1,000.000	4,992.686	25.696	610.198	(19,666.629)	(13,038.049)
Balance as at 1st January 2010	1,000.000	4,992.686	25.696	610.198	(19,666.629)	(13,038.049)
Accounting Period 2010						
Surplus during the year				9.234		9.234
Net Profit/(Loss) for the period					(26,922.819)	(26,922.819)
Deemed Dividend						
Balance as at 31st December 2010	1,000.000	4,992.686	25.696	619.432	(46,589.448)	(39,951.634)

CASHFLOW STATEMENT

Year Ended 31 December

	2010 Rs.Mn Year Ended 31.12.2010	2009 Rs.Mn Year Ended 31.12.2009
Cash Flows From/(Used in) Operating Activities		
Profit/(Loss) before Tax from Continuing Operations	(26,922.819)	(11,353.224)
Adjustment for :		
Depreciation	369.118	355.465
Foreign Currency Translation	(1,324.435)	443.355
Investment Income	(0.112)	(0.001)
Interest Received	(230.614)	(438.287)
Provision for Insurance Reserve	9.234	42.384
Provision for Stores Non Moving Items	57.247	27.535
Provision for Bad & Doubtful Debts & Recoveries	(4.132)	(367.536)
Interest Expenses	6,858.899	4,740.663
Adjustment for Valuation of Shares	-	-
Provision for Retirement Obligation	44.593	191.036
(Profit)/Loss on Sale of Property, Plant & Equipment	(1.154)	(8.669)
Operating Profit/(Loss) before Working Capital changes	(21,144.176)	(6,367.278)
Changes in Working Capital		
(Increase)/ Decrease in Inventories	(15,922.077)	5,941.683
(Increase)/ Decrease in Trade and Other Receivable	(5,283.962)	(9,315.962)
Increase/ (Decrease) In Trade and Other Payables	25,211.640	56,618.857
Cash Generated from/ (Used in) operating activities	(17,138.576)	46,877.301
Interest Paid	(6,858.899)	(4,740.663)
Retiring Gratuity Paid	(33.789)	(22.413)
Income Tax /WHT paid	(137.988)	(77.931)
Net Cash Generated from Operating activities	(24,169.251)	42,036.294
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of Property, Plant & Equipment	(3,608.064)	(833.409)
Proceeds from Sale of Property, Plant & Equipment	1.154	88.589
Income from Investment	0.112	0.001
Interest Received	230.614	438.287
Net Cash Used in Investing Activities	(3,376.183)	(306.532)
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of Long Term Loans	(4,379.068)	(21,538.358)
Net Cash From/(Used in) Financing Activities	(4,379.068)	(21,538.358)

CASH FLOW STATEMENT

Year Ended 31 December

	2010 Rs.Mn Year Ended 31.12.2010	2009 Rs.Mn Year Ended 31.12.2009
Net Increase/(Decrease) in Cash & Cash Equivalents	(31,924.503)	20,191.404
Cash & Cash Equivalents at Beginning of the Year	27,963.381	7,771.977
Cash & Cash Equivalents at End of the Year	(3,961.122)	27,963.381
 Note 1. Cash & Cash Equivalent as at the Beginning of the Year (Note 10)		
Cash & Bank Balances	31,762.640	9,244.432
	31,762.640	9,244.432
Bank Overdraft (Note 18)	(2,870.372)	(82.670)
Cash & Cash Equivalents before Adjusting the Foreign Currency Translation	28,892.268	9,161.762
Adjustment for Foreign Currency Translation	(928.887)	(1,389.785)
Cash & Cash Equivalents after Adjusting the Foreign Currency Translation	27,963.381	7,771.977
 Note 2 .Cash & Cash Equivalent as at the end of the Year		
Cash & Bank Balances (Note 10)	13,312.111	31,762.640
	13,312.111	31,762.640
Bank Overdraft (Note 18)	(15,019.911)	(2,870.372)
Cash & Cash Equivalents before Adjusting the Foreign Currency Translation	(1,707.800)	28,892.268
Adjustment for Foreign Currency Translation	(2,253.322)	(928.887)
Cash & Cash Equivalents after Adjusting the Foreign Currency Translation	(3,961.122)	27,963.381

ACCOUNTING POLICIES

1. CORPORATE INFORMATION

1.1 General

Ceylon Petroleum Corporation is a Public Corporation incorporated under Ceylon Petroleum Corporation Act No.28 of 1961 and domiciled in Sri Lanka. The registered office of the Corporation is located at No.109, Galle Road, Colombo 03.

1.2 Principal Activities and Nature of Operations

The principle activities of the Corporation are refining, selling & distributing and exploring Petroleum products in Sri Lanka.

1.3 Parent Entity and Ultimate Parent Entity

The Corporation is under the purview of the Ministry of Petroleum and Petroleum Resources Development. In the opinion of the directors, the Corporation's ultimate parent undertaking and controlling party is the Government of Sri Lanka.

1.4 Date of Authorization for Issue

The Financial Statements of Ceylon Petroleum Corporation for the year ended 31 December 2010 were authorized for issue in accordance with a resolution of the Board of Directors on 30 June 2010.

2. BASIS OF PREPARATION

The Financial Statements are prepared under the historical cost basis (except revaluation) in accordance with generally accepted accounting principles of the Accounting Standards laid down by the Institute of Chartered Accountants of Sri Lanka and the provisions of the Finance Act No.38 of 1971 and subsequent amendments .

The Financial Statements are presented in Sri Lankan Rupees and all values are rounded to the nearest Million except when otherwise indicated.

2.1. Statement of Compliance

The Financial Statements of Ceylon Petroleum Corporation have been prepared in accordance with Sri Lanka Accounting Standards (SLAS).

2.1.1 Going Concern

The Directors have made an assessment of the Corporation's ability to continue as a going Concern and they do not intend either to liquidate or to cease trading.

2.1.2 Comparative Information

The accounting policies have been consistently applied by the Corporation and except for the changes in accounting policy (policies) discussed more fully in Note 25 consistent with these used in the previous year. The changes made to comparative figures are discussed more fully in Note 21.

2.2 SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

Judgments

In the process of applying the Corporation's accounting policies, management has made the following judgments, apart from those involving estimations, which has the most significant effect on the amounts recognized in the Financial Statements.

Deferred Tax Assets

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.3.1 Foreign Currency Transactions

The Financial Statements are presented in Sri Lanka Rupees, which is the Corporation's functional and presentation currency. Transactions in foreign currencies are initially recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to profit or loss. Non monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

2.3.2 Taxation

Current Tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date.

The provision for income tax is based on the elements of income and expenditure as reported in the Financial Statements and computed in accordance with the provisions of the relevant tax legislations.

Deferred Taxation

Deferred income tax is provided, using the liability method, on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit or taxable profit or loss.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets and unused tax losses can be utilised except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax relating to items recognised directly in equity is recognised in equity and not in the income statement.

Sales Tax

Revenues, expenses and assets are recognised net of the amount of sales tax except where the sales tax incurred on a purchase of assets or service is not recoverable from the taxation authorities in which case the sales tax is recognised as a part of the cost of the asset or part of the expense items as applicable and receivable and payable that are stated with the amount of sales tax included. The amount of sales tax recoverable and payable in respect of taxation authorities is included as a part of receivables and payables in the Balance Sheet.

2.3.3 Borrowing Costs

Borrowing costs are recognised as an expense in the period in which they are incurred.

2.3.4 Inventories

Inventories are valued at the lower of cost and net realisable value, after making due allowances for obsolete and slow moving items. Net realisable value is the price at which inventories can be sold in the ordinary course of business less the estimated cost of completion and the estimated cost necessary to make the sale.

The cost incurred in bringing inventories to its present location and conditions are accounted using the following cost formulae:-

Raw Materials	- At purchase cost on first-in first-out basis
Finished Goods a) Refined Products	- At the cost of direct materials, direct labour and an appropriate proportion of manufacturing overheads based on normal operating capacity, but excluding borrowing Costs.
b) Imports	- At purchase cost on first-in first –out basis.
Work-in-progress a) Refined Products	-At the cost of direct materials, direct labour and an appropriate proportion of manufacturing overheads based on normal operating capacity, but excluding borrowing Costs.
b) Imports	- At purchase cost on first-In first –out basis
Other Finished Goods	-At purchase cost on weighted average basis
Consumables & Spares	-At purchase cost on weighted average basis
Good in Transit	-At Purchase

(By Location)

Net realizable Value is the estimated selling price in the ordinary course of business, less estimated cost of completion and estimated costs necessary to make the sale.

2.3.5 Trade and Other Receivables

Trade receivables are stated at the amounts they are estimated to realise net of allowances for bad and doubtful receivables. In certain cases specific provisions are provided on specific Trade Receivable other than the normal provision made for Trade Receivables.

Other receivables and dues from Related Parties are recognised at cost less allowances for bad and doubtful receivables.

2.3.6 Cash and Cash Equivalents

Cash and cash equivalents are cash in hand, demand deposits and short-term highly liquid investments, readily convertible to known amounts of cash and subject to insignificant risk of changes in value.

For the purpose of cash flow statement, cash and cash equivalents consist of cash in hand and deposits in banks net of outstanding bank overdrafts. Investments with short maturities i.e. three months or less from the date of acquisition are also treated as cash equivalents.

2.3.7 Property, Plant and Equipment

Plant and equipment is stated at cost, excluding the costs of day to day servicing, less accumulated depreciation and accumulated impairment in value. Such cost includes the cost of replacing part of the plant and equipment when that cost is incurred, if the recognition criteria are met.

Land and buildings are measured at cost less depreciation on buildings.

When each major inspection is performed, its cost is recognised in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement in the year the asset is derecognised.

The asset's residual values, useful lives and methods of depreciation are reviewed, and adjusted if appropriate, at each financial year end.

2.3.8 Investments

a) Initial Recognition:

Cost of investment includes purchase cost and acquisition charges such as brokerages, fees, duties and bank regulatory fees. The Corporation distinguishes and presents current and non current investment in the balance sheet.

b) Measurement

Current Investment:

Current investments are carried at the lower of cost and market value, determined on the basis of aggregate portfolio.

Long Term Investments

Long term investments are stated at cost. Carrying amounts are reduced to recognize a decline other than temporary, determined for each investment individually. These reductions for other than temporary declines in carrying amounts are charged to income statement.

Investments in Associate Companies

Investments in Associate Companies are stated at Cost.

Disposal of Investment

On disposal of an investment, the difference between net disposals and proceed and the carrying amounts is recognised as income or expense.

2.3.9 Provisions

Provisions are recognized when the Corporation has a present obligation (legal or constructive) as a result of a past event, where it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. When the company expects some or all of a provision to be reimbursed, the reimbursement is recognised as a separate assets but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as an interest expense.

2.3.10 Retirement Benefit Obligations

a) Defined Benefit Plan – Gratuity

Gratuity is a Defined Benefit Plan. The Corporation is liable to pay gratuity in terms of the relevant statute. In order to meet this liability, a provision is carried forward in the balance sheet, equivalent to an amount calculated based on a half month's salary of the last month of the financial year of all employees for each completed year of service, commencing from the first year of service. The resulting difference between brought forward provision at the beginning of a year net of any payments made, and the carried forward provision at the end of a year is dealt with in the income statement.

The gratuity liability is not funded nor actuarially valued

Defined Contribution Plans – Employees' Provident Fund & Employees' Trust Fund

Employees are eligible for Employees' Provident Fund Contributions and Employees' Trust Fund Contributions in line with the respective statutes and regulations. The Corporation contributes 15% and 3% of gross emoluments of employees to Employees' Provident Fund and Employees' Trust Fund respectively.

2.3.11 Capital Reserve

Specific amounts received from Government Consolidated Fund and the net value of restructuring sale proceeds which will eventually form the issued capital of the successor to Ceylon Petroleum Corporation are credited to a Capital Reserve.

2.3.12 Insurance Reserve

An amount equivalent to the actual cost of insurance on imports which are not insured with a third party while in transit is credited to insurance reserve.

2.3.13 Revenue Recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow the corporation and the revenue and associated costs incurred or to be incurred can be reliably measured. Revenue is measured at the fair value of consideration received or receivable net of trade discounts and sales taxes. The following specific criteria are used for the purpose of recognition of revenue.

a) Sale of Goods

Revenue from the sale of goods is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on dispatch of the goods.

b) Interest

Revenue is recognised on a time proportion basis that takes in to accounts the effective interest rate on asset.

c) Dividends

Dividend Income is recognised when the shareholders' right to receive the payment is established.

d) Rental income

Rental income is accounted for on a straight-line basis over the lease terms.

e) Others

Other income is recognised on an accrual basis

2.3.14 Segment Information

The activities of the segments are described in the segmental review of operation. Segments have been determined based on primary format. Primary format represents the business segments, identified based on the products which have similar risk and return faced by the customers. Since the Corporation's activities are geographically within Sri Lanka Secondary segment format is not available.

NOTES TO THE FINANCIAL STATEMENTS

1. REVENUE

DOMESTIC SALES	2010		2009	
	QTY. M.Ltrs	Value Rs. Mn	QTY. M.Ltrs	Value Rs. Mn
90 Octane Petrol	614.561	62,597.481	524.698	57,418.763
95 Octane Petrol	21.661	2,560.429	21.403	2,636.372
Auto Diesel	1,680.888	122,360.422	1,687.045	119,046.261
Super Diesel	13.434	1,170.271	10.104	866.145
Kerosene	210.159	10,711.003	191.810	9,754.538
Furnace Oil	1,199.515	28,862.219	1,021.448	27,416.214
Furnace Oil Low Sulper	116.605	6,929.799	134.191	5,740.935
Naphtha	78.455	4,228.518	160.516	8,093.232
Avn. Gasoline	0.256	71.185	0.237	66.103
Avn. Turbine Fuel	215.811	14,102.174	176.457	9,749.853
Asphalt	81.124	7,117.022	92.941	8,049.974
Lub Oil	0.743	1,019.117	1.727	457.944
Agro Chemicles	0.315	152.883	0.407	178.506
Solvent	3.952	392.424	1.353	135.188
L.P.G.	22.782	1,921.262	24.513	1,484.922
Total Domestic sales	4,260.261	264,196.210	4,048.850	251,094.950
EXPORTS				
a) Indirect Exports				
Avn.Turbine Fuel	131.341	10,026.077	113.280	6,298.091
Naphtha	40.811	2,328.684	6.310	115.153
	172.152	12,354.760	119.590	6,413.243
Total Sales		276,550.970		257,508.193
Less : T.T, Ex Duty		(20,221.814)		(19,845.574)
		256,329.157		237,662.619

SEGMENT INFORMATION & REVENUE

The following table presents revenue , cost of sales and gross profit of

Class of the Customer	2010			2009		
	Sales Value Rs. Mn	Cost of sales Rs. Mn	Gross Profit Rs. Mn	Sales Value Rs. Mn	Cost of sales Rs. Mn	Gross Profit Rs. Mn
a) Transport	160,321,509	149,404,171	10,917,337	160,121.967	142,441.754	17,680.213
	160,321,509	149,404,171	10,917,337	160,121.967	142,441.754	17,680.213
b) Power Generation	41,852,901	58,327,325	(16,474,424)	41,250.381	56,740.143	(15,489.762)
	41,852,901	58,327,325	(16,474,424)	41,250.381	56,740.143	(15,489.762)
c) Aviation	24,199,435	23,338,934	860,501	16,114.048	15,312.762	801.286
	24,199,435	23,338,934	860,501	16,114.048	15,312.762	801.286
d) Others	27,626,629	32,215,381	(4,588,752)	20,176.224	19,046.261	1,129.963
	27,626,629	32,215,381	(4,588,752)	20,176.224	19,046.261	1,129.963
e) Naphtha Export	2,328,684	2,317,951	10,732			
	2,328,684	2,317,951	10,732			
Gross Profit as Per Income statement	256,329,157	265,603,764	(9,274,607)	237,662.620	233,540.920	4,121.700

NOTES TO THE FINANCIAL STATEMENTS

Year Ended 31 December

2. COST OF SALES.

	2010 Rs. Mn	2009 Rs. Mn
As Per Gross Margin	269,082.735	232,058.978
Operation Loss/Gain	233.496	212.272
Exchange Variation (Crude/Bulk)	(3,712.467)	1,269.670
	265,603.764	233,540.920

3. OTHER OPERATING INCOME

Dividend Income	0.112	0.001
Fines Recovered from Contractors	1.392	4.539
Sundry Income	294.795	1,167.447
Rent Income	5.934	14.082
	302.233	1,186.069

3.1 SELLING & DISTRIBUTION EXPENSES

Selling And Distribution Cost	8,616.509	9,434.576
Aviation Coast	863.300	754.092
Deprecation	236.274	232.770
	9,716.083	10,421.438

3.2 ADMINISTRATION EXPENSES

Administrator Cost	3,845.166	3,540.591
Exchange Variation	(2,239.088)	(937.704)
	1,606.078	2,602.887

FINANCE COST AND INCOME

3.3 FINANCE COST

Interest on Long Term Loans	3,278.926	124.953
Interest on Bank Overdrafts	149.054	398.224
Interest on Foreign Bills Payables & Other Bank Loans	3,430.919	4,217.487
	6,858.899	4,740.664

3.4 FINANCE INCOME

Treasury Bill Interest Income	230.614	239.471
Interest on R.F.C. A/C	0.000	198.816
Interest on Credit invoice	0.000	665.708
	230.614	1,103.995

4. PROFIT / (LOSS) FOR THE YEAR

	2010 Rs. Mn	2009 Rs. Mn
stated after charging /(Crediting)		
Included in Cost of Sales		
Written Down of Inventories to net Realizable Value	16,203.335	9,110.590
Depreciation -Refinery	132.359	122.179
Exchange Differences-(Gain)/Loss	(3,712.467)	1,269.670
Included in Administrative Expenses		
Employees Benefits including following		
- Defined Benefit Plans Costs -Gratuity	44.593	191.036
- Defined Contribution Plans Costs-EPF &ETF	388.177	208.536
Change in the value of Long Term Investments	-	-
Exchange Differences-(Gain)/Loss	(2,239.088)	(937.704)
Profit on Disposal of Property, Plants and Equipment	1.154	8.669
Reversal of Provisions	-	-
Auditors Remuneration	2.000	1.473
Depreciation -Head Office	236.274	232.767
Donation to Sri Lanka Sumithrayo	-	0.585

NOTES TO THE FINANCIAL STATEMENTS

Year Ended 31 December

5. INCOME TAX

	2010 Rs.Mn	2009 Rs.Mn
Current Tax Expense on Ordinary Activities for the Year (5.1)		205.928
Social Responsibility Levy		3.089
Under /(Over) provision of current taxes in respect of prior years		4.716
		<u>213.733</u>
Deferred Income Tax		
Deferred Taxation Charge/(Reversal)	-	
Income tax expense reported in the income statement		<u>213.733</u>

5.1 Reconciliation between Current Tax Expense and the product of Accounting Profit.

Accounting Profit /(Loss) before Tax	(26,922.819)	(11,353.224)
Aggregate Disallowed Items		717.318
Aggregate Allowable Expenses		(1,742.357)
Adjustment of Income / (Loss) not subject to Tax		13,367.679
Other Source of Income - Interest Income		905.179
Less : Utilization of brought forward tax losses		(316.813)
Taxable Profits		<u>588.366</u>

Tax on Profit from Operations

Operating Income		-
Other Source of Income - Interest Income		205.928
Income Tax Expenses		<u>205.928</u>
Income Tax Expenses Provisional)		<u>205.928</u>

Tax Rate Applicable for Operating Income	35%
Social Responsibility Levy	1%
Deemed Dividend Tax	25%

Tax Rate Applicable for Operating Income	35%
Social Responsibility Levy	1%
Deemed Dividend Tax	25%
Income Tax	<u>210.644</u>
Social Responsibility Levy	<u>3.089</u>
	<u>213.733</u>

Deemed Dividend Tax	95.610
Under /(Over) Provision of current taxes in respect of prior years	(0.620)
	<u>94.990</u>

5.2 Deferred Tax (Assets), liabilities and Income Tax relates to the followings

At the Beginning of the year		(689.623)
Transferred from /(to) Income Statement		-
At the End of the year		<u>(689.623)</u>

Balance Sheet

	2010 Rs. Mn	2009 Rs. Mn
Deferred Tax Liability		
Capital Allowance for Tax purpose		989.460
		<u>989.460</u>
Deferred Tax Assets		
Define Benefit Plans		(189.478)
Unutilized Tax Losses		(965.182)
Other Provisions		(524.424)
		<u>(1,679.084)</u>
Net Deferred Tax (Asset)/Liability		<u>(689.623)</u>

NOTES TO THE FINANCIAL STATEMENTS

Year Ended 31 December 2010

6. PROPERTY, PLANT & EQUIPMENT

6.1 Gross carrying Amounts

Cost	Land & Buildings	Vested Property	Plant, Mach & Equip	SPM Facility	Motor Vehicles	Furn/Fittings Off. Equip & Other Assets	Total
	Rs.Mn	Rs.Mn	Rs.Mn	Rs.Mn	Rs.Mn	Rs.Mn	Rs.Mn
Bal as at 01/01/2010	1,468.604	1.016	3,747.743	2,142.422	380.249	1,473.263	9,213.297
Additions	151.341	-	131.373	-	1.315	63.568	347.596
Disposals	-	-	-	-	(11.622)	-	(11.622)
Adjustment	-	-	-	-	-	-	-
Bal as at 31/12/2010	1,619.945	1.016	3,879.116	2,142.422	369.942	1,536.831	9,549.271

6.2 Depreciation

Bal as at 01/01/2010	181.288	0.348	2,213.991	1,290.634	203.863	1,064.558	4,954.682
Charge for the Year	27.906	0.021	301.894	-	15.700	23.597	369.118
Disposals	-	-	-	-	(11.622)	-	(11.622)
Adjustments	-	-	-	-	-	-	-
Bal as at 31/12/2010	209.194	0.369	2,515.885	1,290.634	207.940	1,088.155	5,312.178
Net Book Value as at 31.12.2010	1,410.751	0.647	1,363.230	851.788	162.001	448.675	4,237.093
Cost as at 31.12.2009	1,468.604	1.016	3,747.743	2,142.422	380.249	1,473.263	9,213.297
Acc.Dep as at 31.12.2009	181.288	0.348	2,213.991	1,290.634	203.863	1,064.558	4,954.682
Net Book Value l as at 31.12.2010	1,287.316	0.668	1,533.752	851.788	176.386	408.705	4,258.615

6.3 Assets and Capital Project in Progress

	2010 Rs.Mn	2009 Rs.Mn
Refinery Expansios projet(SORM)	585.735	-
Buildings	1,223.207	651.568
Plant & Machinery	2,127.395	7.099
Storage Facility	11.447	9.522
Re-structuring of Filling Stations	50.225	114.335
Others	44.982	-
	4,042.992	782.524

6.4 Net Book Values

Property Plant & Equipment	4,237.093	4,258.615
Assets & Capital Projects in Progress	4,042.992	782.524
Total Carrying Amount of Property , Plant & Equipments	8,280.085	5,041.139

6.5 The useful lives of the assets is estimated as follows

Freehold Land	Nil	Nil
Buildings	40 Y ears	40 Y ears
Refinery Tanks & Pipelines	40 Y ears	40 Y ears
Refinery Plant & Machinery	10 Y ears	10 Y ears
Other Location Tanks	40 or 20 Y ears	40 or 20 Y ears
Other Locations Pipelines	10 or 5 Y ears	10 or 5 Y ears
Plant & Machinery	10 or 5 Y ears	10 or 5 Y ears
Browsers & Tank Lorries	5Y ears	5Y ears
Vans & Coaches	4Y ears	4Y ears
Furniture/Fittings & Office Equipments up to 31.12.1998	Fully	Fully
Furniture/Fittings & Office Equipments up to 31.12.1999	3 Y ears	3 Y ears
SPM Facility - Tank Farm	40 Y ears	40 Y ears
- Pipelines	20Y ears	20Y ears
- Buoy	10 years	10 years

NOTES TO THE FINANCIAL STATEMENTS

Year Ended 31 December

7. INVESTMENTS

	2010		2009	
	Rs .Mn At Cost	Rs .Mn Director's Value	Rs .Mn At Cost	Rs .Mn Director's Value
7.1 Non-Current				
a) Investment in Associated Company				
Unquoted				
Ceylon Petroleum Storage Terminals Ltd.*	2,500.000	2,500.000	2,500.000	2,500.000
	2,500.000	2,500.000	2,500.000	2,500.000
	At Cost	Market Value	At Cost	Market Value
b) Other Investments				
Quoted				
Lanka Cement Ltd.	50.500		50.500	31.250
5,000,000 Ordinary Shares of Rs.10/= each fully paid.				
Less:				
Allowance for decline in value	(19.250)	-	(19.250)	-
	31.250	0.000	31.250	31.250
Unquoted				
	Rs .Mn At Cost	Rs .Mn Director's Value	Rs .Mn At Cost	Rs .Mn Director's Value
Associated News Papers of Ceylon Ltd.				
61,206 Ordinary Shares of Rs.10/= each fully paid.	0.539	0.539	0.539	0.539
Lanka Leyland Ltd.				
100 Ordinary Shares of 10/= each fully paid.	0.001	0.001	0.001	0.001
International Coop/Petroleum association				
5,499 Shares of Us \$ 100/= each fully paid Incorporated in USA	5.086	5.086	5.086	5.086
	5.626	5.626	5.626	5.626
7.2 Current				
Investments in Fixed Deposit	5.000		5.000	
	5.000		5.000	
Total	41.876		41.876	

NOTES TO THE FINANCIAL STATEMENTS

Year Ended 31 December

8 . TRADE & OTHER RECEIVABLE

	2010		2009	
	Rs. Mn With in one Year	Rs. Mn After one Year	Rs. Mn With in one Year	Rs. Mn After one Year
Trade Receivables	77,764.748	-	73,755.007	-
Other Receivables	848.772	5,054.175	2,327.730	3,171.653
Deposits	23.360	30.065	8.917	29.928
Advance	1,206.802	-	491.872	-
Prepayments	136.753	-	299.792	-
Loans & Advance to Employee	41.872	1,615.746	349.198	1,000.100
	80,022.307	6,699.986	77,232.516	4,201.681

9. INVENTORIES

	2010 Rs.Mn	2009 Rs.Mn
Crude Oil	12,763.153	6,783.893
Other Raw material	724.625	519.310
Finished Products	26,713.894	15,234.771
Other Materials & Supplies	1,573.349	3,314.969
Less: Provision for Non Moving Items	(341.912)	(284.665)
	41,433.110	25,568.278

9.1 The sum of Rs (2007 -Rs.6,553.910Mn) was adjusted as written down value of Net Realizable Value of Inventory as at the 31.12.2008.

10. CASH AND CASH EQUIVALENTS

	2010 Rs.Mn	2009 Rs.Mn
Components of Cash and Cash Equivalents		
Cash & Bank Balances	13,312.111	23,812.640
Treasury Bills	-	7,950.000
	13,312.111	31,762.640

11. CONTRIBUTED CAPITAL

	2010 Rs.Mn	2009 Rs.Mn
Initial Contribution in Pursuance of Section 23 of Act No 28 of 1961	10.000	10.000
Voted by Appropriation Act no 23 of 1964	4.000	4.000
Voted by Appropriation Act no 15 of 1967	20.000	20.000
Contribution to Capital in 1976	60.000	60.000
Contribution to Capital in 1979	13.110	13.110
Contribution to Capital in 1980	10.710	10.710
Total Contributed by Govt.of Sri Lanka	117.820	117.820
Transferred from General Reserve in 1987	750.000	750.000
Transferred from Retained Profits in 1987	132.180	132.180
	1,000.000	1,000.000

(No authorized capital has been fixed by the Parliament.)

NOTES TO THE FINANCIAL STATEMENTS

Year Ended 31 December

12. CAPITAL RESERVE

	2010 Rs.Mn	2009 Rs.Mn
Balance as at 01 st January	4,992.686	4,992.686
Balance as at 31 st December	4,992.686	4,992.686

* In 2003, the transfer of assets to CPSTL had been done at book values. Subsequently it had been decided to record

13. REVALUATION RESERVE

Balance as at 01 st January	25.696	25.696
Balance as at 31 st December	25.696	25.696

14. INSURANCE RESERVE

Balance as at 01 st January	610.198	567.814
Charged to Profit & Loss Account	9.234	42.384
Balance as at 31 st December	619.432	610.198

15. RETIREMENT BENEFIT OBLIGATION

Balance as at 01 st January	720.308	551.685
Less: Payments made during the year	33.789	22.413
	686.519	529.272
Add: Charge for the year	44.593	191.036
	731.113	720.308
Add: Benefit China Bay /LLL/NYLON/CPSTL Employees	15.224	14.857
Balance as at 31 st December	746.337	735.165

16. INTEREST BEARING LOANS & BORROWINGS

16.1 L.T. Loans not assigned to CPSTL

Treasury (A.D.B) Loan - (Interest 14.0% p.a.) repayable in forty 1/2 yearly installments of Rs.37.977 Mil each commencing July '01.

Indian Line of Credit (Interest LIBOR+0.5 p.a.) repayable in twelve half yearly installments of Rs.1228.030 Mil each commencing May '06

16.2 L.T. Loans assigned to CPSTL

Treasury (Exim Bank) Loan - (Interest 12 .0 p.a %) repayment commencing Oct. 2004 in 24 equal 1/2 yearly installments of final Loan value

16.3 B.O.C Long Term Long -

	25,000.000	25,000.000
	28,477.291	32,778.156
Compensation Payable to Former Owners of properties vested in CPC	0.902	0.902
	28,478.19	32,779.06

NOTES TO THE FINANCIAL STATEMENTS

Year Ended 31 December

2010
Rs.Mn

2009
Rs.Mn

16.3 Loans Repayable within five years from 31st December - 2010 Is as follows.

Amount due within 1-2 years	3,205.741	3,205.741
Amount due within 3-5 years	2,574.198	2,574.198
Amount due after 5 years	1,998.219	1,998.219
	7,778.158	7,778.158

17. TRADE & OTHER PAYABLES

Foreign Bills Payable	122,297.904	109,643.234
Other Creditors		
- Amount due to Inland Revenue & Custom Dept.	261.449	1,905.237
- Accrued Expenses	20,628.685	467.203
- Refundable Deposits & Others	2,393.666	7,106.531
- Amount due to Related Parties	50.710	1,298.938
	145,632.415	120,421.143

18. INTEREST BEARING LOANS AND BORROWINGS WITHIN 01 YEAR

Bank & Other loans		
- Wholly Repayable within one year	3,127.538	3,205.741
- Bank Overdrafts	15,019.911	2,870.372
- Bank Temoprary Loan	-	-
- Short Term Working Capital Loans	-	-
	18,147.449	6,076.113

19. EMPLOYEES

19.1 Staff Cost

Salaries & Wages	2,056.067	1,815.765
Bonus	252.098	240.061
Provident & Trust Fund contribution	208.536	208.536
Gratuity Provision	44.593	191.036
	2,561.294	2,455.398

19.2 No. of Employees

Administration & Marketing	1,191	1,005
Manufacturing	985	1,150
Security	485	493
	2,661	2,648

19.3 Contract & Casual Employees

	83	144
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20. COMMITMENTS FOR CAPITAL EXPENDITURE

	Amount Approved	Amount Spent Up to 31.12.2009
Fuel Quality Improvement & Storage Facilities at Refinery	33.716	358.000
Refinery Main Plant (Minor modifications)	10.260	248.441
Other Capital Expenditure	2,148.483	26.761
Construction of Head Office New Building	1,214.573	592.465
Construction of Fling Yard	50.224	114.334
	3,457.256	1,340.001



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கணக்காய்வாளர் தலைமை அபிபதிதினைக்களம்
AUDITOR GENERAL'S DEPARTMENT



මගේ අංකය
எனது இல
My No

MQE 00D 00B 021

ඔබේ අංකය
உமது இல
Your No.

දිනය
திகதி
Date

24 February 2012

The Chairman
Ceylon Petroleum Corporation

Report of the Auditor General on the Financial Statements of the Ceylon Petroleum Corporation for the year ended 31 December 2010 in terms of Section 14(2)(c) of the Finance Act, No. 38 of 1971

The audit of financial statements of the Ceylon Petroleum Corporation (CPC) for the year ended 31 December 2010 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 Section 13(1) of the Finance Act No. 38 of 1971. My comments and observations, which I consider should be published with the annual report of the Corporation in terms of Section 14(2) (c) of the Finance Act appear in this report. A detailed report in terms of 13(7) (a) of the Finance Act was issued to the Chairman of the Corporation on 25 November 2011.

1.2 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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கோலம்பு 07, சூ. இலாவ

சுதந்திர சதுக்கம்,
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1.3 **Scope of Audit and Basis for Opinion**

My responsibility is to express an opinion on these financial statements based on my audit. Audit opinion, comments and findings in this report are based on review of the financial statements presented to audit and substantive tests of samples of transactions. The scope and extent of such review and tests were such as to enable as wide audit coverage as possible within the limitations of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes the examination on a test basis of evidence supporting the amounts and disclosures in financial statements and assessment of accounting policies used and significant estimates made by the management in the preparation of financial statements as well as evaluating their overall presentation. I believe that my audit provides a reasonable basis for my opinion. Sub – sections (3) and (4) of Section 13 of the Finance Act, No.38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

2. **Financial Statements**

2.1 **Opinion**

In view of my comments and observations appearing in this report, I am unable to express an opinion on the financial statements of the Ceylon Petroleum Corporation for the year ended 31 December 2010 presented for audit.

2.1.1 **Going Concern**

The Corporation had sustained a loss of Rs. 26,923 million (without tax adjustment) for the year under review and had a negative net assets position of Rs. 39,952 million. Thus, the ability of the Corporation to continue as a going concern without the financial assistance from the Government of Sri Lanka and other financial institutions is doubtful.

2.2. **Comments on Financial Statements**

According to the Department of Public Enterprises Circular No. PED/12 of 2 June 2003, the draft annual financial statements should be rendered to the Auditor General within 60 days after the closure of the financial year. However, annual financial statements had been

submitted to the Auditor General on 11 May 2011. The comments and observations in this report are based on the above annual financial statements.

2.2.2 **Sri Lanka Accounting Standards (SLAS)**

The following observations are made.

- a) The General Treasury had transferred 1/3 of the shares of the Ceylon Petroleum Storage Terminal Ltd. (CPSTL) on 21 October 2009 to the Corporation with effect from 01 January 2009. As a result, the total shareholdings of the Ceylon Petroleum Corporation increased to 2/3 of shares of the CPSTL. The Corporation had not disclosed the transfer of these shares in the financial statements and had not prepared the consolidated financial statements for the year 2009 and for the year under review as required by the SLAS 26- Consolidated and Separate Financial Statements.

In this connection the Chairman informed me in December 2011 as follows

However, the Chairman had informed me that due to following reasons the Corporation was not in a position to prepare consolidated financial statements.

- (i) Financial report period of the CPC (Holding Company) was different from that of the subsidiary (CPSTL).
- (ii) Financial statements or audited financial statements of CPSTL were not made available at the time of preparation of financial statements of the CPC for the year ended 31 December 2010
- (iii) Consolidated financial statements shall be prepared using uniform accounting policies for like transactions and other events in similar circumstances. This requires critical examination of accounting policies used by CPC (holding Co.) and CPSTL (subsidiary Co.) at different balance sheet dates.

In addition, there has been a dispute with regard to reconciliation of intercompany current accounts. CPC and CPSTL resolved certain disputes and balance matters were referred to Acting Secretary to the Ministry of Petroleum Industries for an early solution. Due to the circumstances stipulated in SLAS 26 noted above, it was not allowed to CPC for preparation of consolidated financial statements for the year ended 31 December 2010.

- (b) The Corporation had not revalued the assets to ensure that the carrying amounts do not differ materially from the fair value, which would be determined at the balance sheet date, as stipulated in SLAS 18-Property, Plant and Equipment. Further, fully depreciated assets valued at Rs.559 million, which continued to be used by the Corporation had not been revalued. In addition, the assets valued at Rs.18.6 million added during the year 2010 had not been depreciated.
- (c) The Corporation had not adopted appropriate procedures to identify impairment indicators for its assets as required by SLAS 41-Impairment of Assets. Due to this non-compliance the carrying amount of the property, plant and equipment amounting to Rs.9.549 million had not been compared with their recoverable amount.
- (d) Gratuity Formula Method or Actuarial Method should be used in calculating gratuity provision in terms of SLAS 16. However, the Corporation had made provision in terms of Payment of Gratuity Act No. 12 of 1983.
- (e) The investment made in the Associate Company amounting to Rs.2,500 million had not been accounted for by using equity method and the summarized financial information of the Associate, including the aggregated amounts of assets, liabilities, revenue and profit or loss had not been disclosed in the financial statements as required by SLAS 27 – Investments in Associates.
- (f) According to SLAS 03 – Presentation of Financial Statements, Assets and liabilities, and income and expenses, shall not be offset unless required or permitted by a Sri Lanka Accounting Standard. It was observed that credit balances of debtors amounting to Rs.334.1 million had been set-off against the debit balance of debtors amounting to Rs.78,143 million contravening the provisions of Sri Lanka Accounting Standard No.3
- (g) It was observed that bad debt provision amounting to Rs.43.9 million had not been shown in the face of the balance sheet and its set off against trade receivables balances as stipulated in SLAS 3. In addition, the bad debt provision of the carrying amount at the beginning and end of the period had not disclosed as required by SLAS 36 – Provisions, Contingent Liabilities and Contingent Assets.

2.2.3 **Accounting Deficiencies**

The following accounting deficiencies were observed in audit.

- (a) It was observed that accrued bank charges for the year under review had been understated by Rs.82.9 million.
- (b) A sum of Rs.28.7 million relating to the deposits taken from there aviation customers had been credited to the Debtor Accounts instead of the Deposit Account.
- (c) Income tax for the year 2010 had not been provided in the financial statements.

2.2.4 **Hedging Transactions**

According to the minutes of the Board of directors of the Corporation, arbitration proceedings are being conducted at the London Court of International Arbitration. The Corporation was cited as a party in the arbitration proceeding pertaining to hedging contracts entered into with several commercial banks. Pending the outcome of these proceedings at the London Court of International Arbitration, the Corporation had not recognized any resultant liability. Further, the Corporation had not finished the detail pertaining to the transactions to enable to independently verify the liability under these circumstances. Further, it was not possible to satisfy in audit whether the Corporation had adequately recognized all liabilities arising out of these contacts.

2.2.5 **Accounts Receivable and Payable**

The following observations are made.

- (a) The Corporation had not obtained Bank Guarantees from two aviation contract customers and two private customers whose outstanding balances were amounting to Rs.52.8 million and Rs.3,443.6 million respectively as at 31 December 2010.
- (b) The amount receivable from the Ceylon Electricity Board (CEB) as at 31 December 2010 amounted to Rs.52,394 million. Eighty-eight per cent of this amount remained outstanding for a period of over one year. Meanwhile, there was a dispute regarding a balance of Rs.1,031 million due from the Ceylon Electricity Board.

- (c) It was observed that the limit of credit facility provided by the Corporation had been exceeded by 38 dealers, 2 power plant customers and 2 private consumers and such excesses totaled Rs.83 million.
- (d) Out of the debtors balance of Rs.78,143 million shown in the financial statements for the year under review debtors amounting to Rs.46,798 million or 60 per cent represent debtors balances older than 1 year to 17 years. Even though revocability of the debts is doubtful, the Corporation has not made provision for such debts.
- (e) The Corporation had not settled a sum of Rs.14.2 million payable to Lanka Indian Oil Company for the stocks taken from that company and shown in the financial statements as other receivables from the year 2004. However, the Corporation had not taken action to settle this amount up to 31 December 2010.

2.2.6 **Lack of Evidence for Audit**

The following items in the accounts could not be satisfactorily vouched in audit due to the non availability of required evidence as indicated under each item.

- (a) The provision of Rs.479 million made in the preceding years for contractors' payments, employees' income tax, PAYE tax and other payables relating to the Muthurajawela Project continued to be shown in the financial statements year after year. However, the details thereon had not been furnished to audit. Further, it was observed that the provision had not been reviewed at the balance sheet date and adjusted to reflect the current best estimate as required by SLAS 36 – Provisions, Contingent Liabilities and Contingent Assets.
- (b) The title deeds of the four lands valued at Rs.67 million belonging to the Sapugaskanda Mini Terminal had not been made available to audit.
- (c) Twenty five acres of land valued at Rs.259 million at Muthurajawela had been shown as an asset in the ledger. However, there were no title deeds or Vesting Orders made available to establish the ownership of the land.
- (d) No sufficient evidence were made available regarding the assets valued at Rs.126 million purchased prior to 31 December 2002 under property plant and equipment. As a result, the ownership, existence and completeness of such assets could not be verified in audit.

- (e) Confirmations had not received in respect of a sum of Rs.8,096 million due from Government Departments and Agencies included under trade and other receivables. As such the completeness, existence and recoverability of such balances could not be satisfactorily verified in audit.
- (f) Adequate evidence had not been made available to examine the recoverability of the excise duty amounting to Rs.714 million receivable from the General Treasury and included under trade and Other Receivables.

2.2.7 **Non-compliance with Laws, Rules, Regulations and Management Decisions**

The following instances of non-compliance were observed in audit.

Reference of Laws, Rules

Regulations and Management Decisions Non-compliance

- (a) Payment of Gratuity Act, No.12 of 1983 Gratuity had not been paid within 30 days from the termination of an employee as stipulated in the Act. Further, the Corporation had not paid surcharge for such delayed payments.

In this connection the Chairman informed me in December 2011 as follows.

“Practical reasons for not paying the gratuity within 30 days to a few employees due to reasons beyond the control of CPC. For example, in certain cases, CPC needs to verify legal heirs of the deceased employees whose claims are made by different parties. In certain cases, due to disputes, Commissioner of Labour had given instructions to defer the payment until the determination was made as per complaints filed at the Department”

(b) Inland Revenue Act No. 10 of 2006

The Corporation had not paid PAYE Tax for the non-cash benefit received by the employees.

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

(i) Section 3.2

The Board of Directors of the Corporation did not include at least one member in the field of Petroleum, which is the main objective of the Corporation.

(ii) Section 6.1

The draft Annual Report on accounts for the year under review had not been submitted to the Auditor General.

(iii) Section 6.5

The draft Annual Report and accounts should be rendered to the Auditor General within 60 days after the closure of the financial year, but the draft Annual Report of the year 2007, 2008, 2009 and 2010 had not been submitted to the Auditor General.

In this connection the Chairman informed me in December 2011 as follows

“The draft annual report for the years were prepared but due to remarks made in Hedging transaction process, Hon. Attorney General has instructed not to publish. However instruction for publication of Annual Accounts for the year 2007 was received to CPC on 19 April 2010. CPC had prepared draft Annual reports for the years 2008 and 2009 but did not publish due to the above reason. Annual Reports pertaining to 2008 and 2009 were submitted to the Committee on Public Enterprises (COPE) at the meeting held on 23.08.2011. As CPC had embarked on the ERP Project, direct changeover from manual

system to computerized system, there were system related issues which had to be sorted out for preparation of financial statements”

(iv) Section 4.2.2

The Board Meetings of the Corporation had not been held during May, June and October of the year under review.

(v) Section 8.3.5

Officers who were not entitled to assign official motor vehicles had been assigned motor vehicles on the approval of the Board of Directors or the Chairman, contrary to the Circular instructions. As such, 08 officers of the Corporation had been paid a sum of Rs. 1.8 million as fuel and travelling allowances in 2010 contrary to the circular instructions.

Fuel limits for such assigned motor vehicles had been decided either by the Board or by the Chairman.

In addition, the Chairman had granted approval to certain officers to claim reimbursement of the value of 100 – 120 litres of fuel per month for travel between their residences and office in their private motor vehicles.

(vi) Section 8.7

The Corporation had paid Pay As You Earn (PAYE) tax from its own funds for the employees of the Corporation contrary to the instructions. PAYE tax so paid by the Corporation, for the period 2000 to 2010 amounted to Rs. 155 million. In addition the Corporation had paid tax on tax for PAYE as well.

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| <p>(d) Department of Public Enterprises Circular No. 130 of 18 March 1998</p> | <p>Rate of interest on staff loans had been reduced from 7.2 percent to 4.2 percent without the authority of the General Treasury. The amount under-recovered for the year under review due to this change amounted to Rs. 37.3 million.</p> |
| <p>(e) Circular No. 124 dated 24 October 1997 of the Ministry of Finance and Planning</p> | <p>Even though covering up duties of vacant Post should be limited to a period of 03 months, 05 employees had been covering up duties of vacant posts for periods ranging from 12 to 55 months up to the end of the year under review.</p> |
| <p>(f) Letter dated 19 February 1990 issued by the Ministry of Policy Development and Implementation</p> | <p>Services of private lawyers had been obtained at a higher rate without obtaining prior approval of the Attorney General. The amount paid to private lawyers in the years 2007, 2008, 2009 and 2010 amounted to Rs. 5 million, Rs. 10 million, Rs. 5 million and Rs. 3.5 million respectively.</p> |

2.2.8 Transactions not supported by Adequate Authority.

Following observations are made.

- (a) In terms of Section 8.3.3 of the Public Enterprise Circular No. PED/12 of 2 June 2003 bonus could be paid to employees out of the profit earned by the Corporation. Nevertheless, the Board of Directors had approved and paid bonus amounting to Rs. 147 million, Rs. 148 million and Rs. 179 million in the years 2008, 2009 and 2010 respectively despite the Corporation incurring losses in the respective years.

According to the Board decision dated 08 December 2010 the basic salary and the cost of living allowances only should have been taken for consideration of the computation of bonus. Nevertheless, the bonus paid to the employees of the Refinery had been computed

by taking into account to other allowances such as 15 percent special allowances and the professional allowances paid to the technical staff of the Refinery contravening the said Board decision.

- (b) The technical allowances approved for 204 technical grade employees amounted to Rs.11 million. Nevertheless, a sum of Rs.9.4 million which exceeded the approved amount by sum of Rs. 4.6 million had been paid to 154 technical employees.

2.2.9 Transactions of Contentious Nature

Following observations are made.

- (a) The 676 employees deployed at the Refinery and the security staff from an external institution deployed thereon had been paid a sum of Rs. 70.1 million as payment of security services during the year under review. The cost effectiveness of the payment had not been explained to audit.
- (b) Liquidated damages amounting to Rs. 1.5 million relating to the three refinery projects, which were chargeable from the contractors in accordance with the agreements, had not be deducted from the payments made to the contractors.
- (c) Shutdown maintenance work had been done in the month of February and normally it was expected to run refinery without major failures for two future years after completion of shutdown maintenance works. A sum of Rs.291.9 million had been spent in the year under review including the shutdown maintenance. Nevertheless, it was observed that since the completion of shutdown, operation of certain section of the Refinery had been stopped up to the end of the year under review.
- (d) According to the letter dated 07 July 2010 addressed to the Chairman and Managing Director of the Ceylon Petroleum Storage Terminal Limited by the Chairman of the Corporation, past information had been requested on the usage of Maintenance and Emergency Response Vessel and other facilities since 2004. But it had not been received up to 12 July 2010. Expenses had not been shared due to lack of information with the Corporation and the total expenses had been incurred by the Corporation only. Therefore, the loss of the Corporation could not be quantified.

3. Financial and Operating Review

3.1 Financial Review

3.1.1 Financial Results

According to the financial statements presented, the working of the Corporation for the year under review had resulted in a pre-tax net loss of Rs. 26,923 million as compared with the corresponding pre-tax net loss of Rs. 11,480 million for the preceding year, thus indicating a further deterioration of Rs. 15,443 million in the financial results. This deterioration was mainly due to increase the oil prices in the world market and financial charges on long-term and short-term loans.

3.1.2 Analytical Review of the Financial Results and Financial Position

The following observations are made.

- (a) The following analysis depicted the poor performance in the management of working capital for the year under review.
 - (i) The liquidity ratio at the end of the year under review indicated 0.82 times as compared with 1.06 times of the preceding year and had shown a slight downward move while the acid test ratio had decreased from 0.86 times to 0.56 times at the end of the year under review.
 - (ii) The debtors turnover ratio for the year indicated 3.39 times as compared with 3.9 times for the preceding year and the debt collection period had decreased to 108 days as compared with 165 days for the preceding year.
 - (iii) The stock residence period had increased to 46 days as against 40 days for the preceding year thus showing an increase of 06 days.
 - (iv) The creditors turnover ratio for the year indicated 2.3 times as compared with 3.9 times for the preceding year and the debt collection period had decreased to 108 days as compared with 165 days for the preceding year.
 - (v) The cash operating cycle had decreased to 5 days as against 20 days of the preceding year thus showing a decrease of 25 days.

- (b) Debt equity capital portion of the year under review had increased to 47:40) as compared with 39:14) for the year 2009.
- (c) The gross profit margin for the year under review had decreased to -3.62 percent as compared with 0.92 percent for the preceding year.
- (d) The return on capital-employed ratio showed a negative trend in the years 2009 and 2010.
- (e) The return on total assets ratio indicated negative of 17.57 percent as compared with the negative of 7.79 percent of the preceding year.
- (f) Interest coverage ratio had increased to negative of .9 times as compared with negative of 1.8 times for the preceding year.

3.2 **Operating Review**

3.2.1 **Performance**

The following observations are made.

- (a) The agreement entered into between a private gas company and Ceylon Petroleum Corporation in respect of liquid petroleum gas sales had been expired on 20 October 2006. However, the Corporation has supplied liquid petroleum gas to that company continuously without entering into a fresh agreement or renew the agreement. Instead, the supply of gas had been continued on a letter given by the Minister of Petroleum Industries. In addition, the Corporation has supplied liquid petroleum gas to another company without entering into an agreement.
- (b) Some of the products of the Corporation have been sold at prices less than production cost. It appears that those loss making products had contributed for the huge net loss significantly as well as for the negative equity position of the Corporation at the end of the year under review.

Product	Sales Value Rs. Million	Cost of Sales Rs. Million	Gross Profit/(Loss) Rs. Million	Net Profit/(Loss) at the end of the year 2010
Fuel Oil 3500 (power)	7,482	13,177	(6,295)	Net Loss for the year ended 31 December 2010 amounted to Rs. 26,923 million and power generation fuel oil has contributed a gross loss of Rs. 18,536 million
Fuel Oil 1500 (power)	15,067	27,308	(12,241)	
Fuel Oil (others)	6,313	9,446	(3,133)	
Agro Chemicals	153	184	(31)	
LPG	1,921	1,992	(70)	
Kerosene	10,711	14,321	(3,610)	
Lanka Auto Diesel (Bunkering)	64	74	(10)	

3.2.2 Utilization of Corporation's Resources by Other Government Institutions

Eleven motor vehicles had been released to two Government Institutions and 18 employees had been released to seven Government Institutions without the approval of the appropriate authority and contrary to the provisions of Section 9.4 of the Public Enterprises Circular No. PED/12 of 02 June 2003. In addition, four employees of the Refinery had been released to other Government institutions without having a valid reason and paid Rs. 4.1 million as salary, bonus and other allowances without obtaining any service from them to the Refinery or any other division of the Corporation.

3.2.3 Identified Losses

The following observations are made.

- (a) The Corporation had made bunkering business through a private company in April 2008 with the intention of carrying out that business in the future. According to the Corporation, at the commencement of the business, the environment was not favourable to the Corporation since it had to adopt different strategies to compete with other competitors in the market. Therefore, during the period April 2008 to December 2008 and January 2009 to May 2009,

the Corporation had sold fuel at a reduced price to a private company and as a result, the Corporation had sustained losses amounting to Rs. 85.2 million and Rs. 125 million (approximately) respectively from the bunkering business. However, the Corporation had not engaged with bunkering business since April 2009 and Value of stock as at 31 December

2010 amounting to US\$38,086.32 (approximately) or Rs.4.2 million had been held as stocks at the Jaya Container Terminal Oil Bank. In addition, those storage charges amounting to Rs.0.84 million for 75.38 Metric tons of fuel oil stores at Jaya Container Terminal Oil Bank had not been paid since June 2009.

- (b) According to the current practice and the terms and conditions agreed with Ceylon Petroleum storage Terminal Limited, the Corporation had reimbursed to Ceylon Petroleum Storage Terminal Limited more than the amount collected as slab from dealers. The Corporation had computed the dealer commission based on the outlet spot price, which included the slab. The slab payments to the Ceylon Petroleum Storage Terminal Limited had been computed based on the actual monthly consumption report prepared by the Ceylon Petroleum Storage Terminal Limited. Due to this practice, the Corporation had sustained a loss of Rs. 5.6 million (approximately) for the year ended 31 December 2010.
- (c) There was no standards for allowable operational loss of fuel deliveries through bowsers and wagons and storage at depots and terminals. The practice followed by the Corporation was to allow the Own Use and Process Loss figure at 5 percent for Crude Oil input and to allow a 0.5 percent for evaporation loss for each transfer between two locations. However, it was observed that a loss of Rs.886 million had been occurred in connection with evaporation, processing, operation and stock handling, product transferring etc. during the year 2010.
- (d) General Treasury had paid Rs. 1,273.6 million (US\$. 11.5 million) on behalf of the Corporation in 2008 for importation of fuel oil. Amount payable as overdraft interest to the Treasury amounting to Rs. 65.9 million had been set off against the Government debts during the year. Therefore, the Corporation had occurred a loss of Rs. 65.9 million due to non-payment of advance given by the Treasury.

3.2.4 Management Inefficiencies

The following observations are made.

- (a) No proper evaluation of the risk involved in linking the Corporation data base to an Enterprise Resource Planning (ERP) system developed by Ceylon Petroleum Storage Terminal Ltd. with the assistance of the Indian Oil Company (the parent Company) of the major industry competitor of the Corporation had been made by the Corporation. Since the Corporation has to commit significant amount of its resources (both capital and human) for

this purpose, a proper and in-depth analysis of the impacts that would arise through this system integration should have been done with the assistance of experts in the field of Enterprise Resource Planning Systems. Further, it was observed that there was no agreement or a Memorandum of Understanding amongst the Corporation, Ceylon Petroleum Storage Terminal Limited and Lanka Indian Oil Company with regard to their respective responsibilities under this project before the implementation. It was also important to have an agreement/memorandum as precautionary measure, taking into account the significant outlay of capital and human resources incurred by the corporation to upgrade its equipment etc. to be compatible with the Enterprise Resource Planning System introduced by the Ceylon Petroleum Storage Terminal Limited.

- (b) The bays No. 4C, 1D and 1A at Muthurajawela Tank Farm of the Corporation were not in operation due to a technical failure. However, no action had been taken to repair the bays by the Corporation.
- (c) The Corporation had paid demurrage charges amounting to Rs. 20.3 million due to delay in establishing the letters of credit.
- (d) The Corporation had made major investments amounting to Rs.2,556 million in various portfolios. However, no income had been generated on these investments as at 31 December 2010.
- (e) According to the Board paper dated 08 August 2006 and the amendment letter of Senior Deputy Finance Manager (Revenue) dated 24 March 2008 interest of 24 percent per annum should be charged from the customers on overdue recoverable balances. An audit text check revealed that interest amounting to Rs. 1.2 million and Rs.1.1 million had not been charged in the aviation customers and the dealers respectively.

- (f) It is observed that 20,000 metric tons of High Sulphur fuel oil 1500 valued at Rs.1,140 million imported by the Corporation had been contaminated and it had affected the independent power producers in the country and the Corporation had consulted the Attorney General in this regard. The Attorney General's opinion was that the fuel specifications and the tender conditions laid down for the import of High Sulphur fuel oil 1500 in this instance were not in favour of the Corporation and therefore taking legal action against supplier could be a wastage of money. Hence, the Board of Directors had taken a decision to cancel the registration of this particular supplier. It was observed that the Corporation had entered into contracts with conditions unfavourable to the Corporation.
- (g) According to the agreement entered into with Lanka Indian Oil Company, and the Government of Sri Lanka and the Corporation in the year 2003 relating to the taking over of possession and related matters of the China Bay installation, the Corporation had agreed to lease the storage facilities and the land to the said Company for a period of thirty five years and that lease agreement should be executed within 06 months from the date of the agreement. However, the Corporation had not yet entered into any lease agreement and any related lease rentals had not been received from this company for the usage of this storage facility, although the facility had already been used by the Company since February 2003.

In this connection the Chairman informed me in December 2011 as follows

“CPC did not have ownership of China Bay land to sign lease agreement with Lanka IOC. However, after a series of negotiations with the Department of Lands and other relevant state agencies, CPC has now liaised with the Divisional Secretary, Trincomalee and has forwarded the documents as Divisional Secretary has agreed to give to the CPC a long lease. Once the lease is granted, CPC can sub-lease to Lanka IOC of the lands occupied by Lanka IOC under the Gazette Notifications”.

(h) Physical Verification of Inventory

The Corporation had conducted the physical verification inventory of as at 31 December 2010 on 31 December 2010 and 01 January 2011. The following observations are made in this regard.

- (i) Thirteen (13) Count Sheets out of 87, which included 172,165,422 litres of fuel, had not been signed and confirmed by the Depot Manager.

(ii) Both the Corporation and the Lanka Indian Oil Company maintain oil stocks in the same tanks at Kolonnawa Terminal. Due to this reason, following risks are identified.

- Inability to separate the physical inventory balance of the Corporation at the count.
- As product imported by the Corporation and the Company were stored in the same tanks, it could lead to complication in the identification of the balances of each institution as well as in mixings of product of two different qualities.
- Some of the officers who were nominated for the physical verification team had not participated while some officers had attended to the physical verification without the prior approval. The list of substitute officers deployed in place of the absentees from the selected officers were not furnished to audit.

Therefore, it appears that the Corporation had not paid attention to safe-guard its interest in relation to the transaction of this venture.

3.2.5 Operating Inefficiencies

The intermediate products had been valued at crude oil value. A proper costing system had not been introduced to value the intermediate products.

3.2.6 Procurements

Following observations are made.

- (a) The bid applications received after bid closing time had been accepted in contrary to the provisions in Section 6.3.2 of the Procurement Guidelines of the Government. Such bids had been evaluated by the Bid Opening Committee as received prior to the closing time and also most of times bidders had been allowed to make such late bids.
- (b) The demurrage on import of crude oil and bulk oil amounting to Rs. 78.4 million remained without being settled for a period ranging from one year to nine years as at 31 December 2010

- (c) The vessel surcharges, outturn losses and demurrages relating to 16 instance of import of crude oil and bulk oil during the years 1996 to 2008 amounting to Rs.37.7 million had not been recovered while vessel surcharge amounting to Rs.1.1 million relating to the year 2010 had not been recovered up to 31 December 2010.
- (d) The contamination of the imported products under package No. BK/30/2010 during the year 2010 amounted to Rs. 1,025.6 million and in addition the Corporation had to pay Rs.0.4 million as overtime for product handling charges to the Ceylon Petroleum Storage Terminal Limited.

3.2.7 Assets Management

The following assets had been allowed to idle since the acquisition of those assets.

Nature of the Asset	Comments
(a) Wanathamulla – Halgahakumbura Land	This land had been acquired for Rs.10.6 million for the purpose of LP Gas project and a playground. However, it had not been utilized due to encroachments. In addition, this land is being illegally occupied by squatters since 1973, and it was observed that about 623 families are occupying this land at present.
(b) Mahahena Land	According to the correspondence available, the Corporation had paid a sum of Rs. 0.625 Million for the acquisition of this land. However, this land had not been accounted in the books of the Corporation, and is being used by the previous owner since 1986.

3.2.8 Human Resource Management

Following observations are made.

- (a) Certain personal files did not contain the job description of the employees while the documents in the personal files had not been numbered serially.
- (b) It was observed in audit that overtime hours were allocated to employees considering only the annual overtime budget and no evaluation had been made for the requirement and justification for the overtime before allocation of work.

3.2.9 Apparent Irregularities/Irregular Transactions

As mentioned in my previous audit reports, an Employees' Welfare Association (Ceylon Petroleum Corporation Thrift Society) is being maintained from the funds made by the Corporation from time to time. The following observations are made in this connection.

- (i) A sum of Rs.40.57 Million had been released to the Society during the year under review to implement the Medical Scheme of the Corporation, which could have been done by the Corporation itself. The above contribution had been made to the Society in addition to the medical allowance of Rs. 3,000 per annum paid to each employee with their monthly salary to meet outdoor treatments.
- (ii) The balance outstanding from the loans granted to members of the society by the Corporation out of the funds of the Corporation as at 31 December 2010 amounted to Rs.151.7 million and a sum of Rs.3.4 million had been received as interest income from this society.

3.2.10 Corporate Plan

The Corporate Plan of the Corporation had not reviewed and updated annually, in terms of the Public Enterprises Circular No. PED/12 of 2 June 2003 and it had not been forwarded to the Ministry, Department of Public Enterprises and the Auditor General at least 15 days before the commencement of each financial year. Further, Corporate Plans for the period 2007-2011 and 2009-2013 had not been forwarded to the Auditor General.

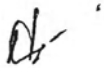
3.2.11 Budget

Significant variances were observed between the budget and the actual income and expenditure for the year under review thus indicating that the budget had not been made use of as an effective instrument of management control.

4. Systems and Controls

Significant deficiencies observed in systems and control during course of audit were brought to the notice of the Corporation from time to time. Special attention is needed in respect of the following areas of control.

- (a) Property, Plant and Equipment
- (b) Debtors and Other Receivables
- (c) Trade Creditors and Other Payables
- (d) Hedging Transactions
- (e) Taxation
- (f) Accounting
- (g) Compliance with Laws, Rules, etc.



H A S Samaraweera
ACTG. AUDITOR GENERAL

TEN YEAR SUMMARY

FOREIGN EXCHANGE EARNINGS & PAYMENTS

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Aviation fuel sales										
Foreign Airlines-US\$ Mn	31.100	32.400	48.300	57.000	77.420	84.540	75.280	104.747	54.795	88.072
Direct Exports-US\$ Mn	16.500	13.100	-	7.000	-	23.090				20.456
Total-US\$ Mn	47.600	45.500	48.300	64.000	77.420	107.630	75.280	104.747	54.795	108.528
Rupee Equivalent	3,561.500	3,977.700	350.800	6,458.500	7,159.010	8,714.050	8,264.680	11,262.986	6,298.137	12,354.760
Import cost										
Crude oil US\$ Mn	353.900	408.000	431.000	597.000	747.200	1,028.500	1,023.000	1,330.902	964.925	983.753
Refined product-US\$ Mn	304.000	286.000	300.000	464.000	653.000	761.300	996.000	1,449.394	774.937	1,280.126
Total US\$ Mn	657.900	694.000	731.000	1,061.000	1,400.200	1,789.800	2,019.000	2,780.296	1,739.862	2,263.879
Avg. Crude (C&F) Price US\$/Bbl	24.670	25.000	29.290	37.380	52.140	65.070	71.970	97.645	63.48	79.73
Avg. Exch. Rate-US\$ 1= Rs.	89.620	96.340	96.420	101.900	100.530	103.960	111.490	108.330	114.94	113.84

OTHER MANAGEMENT INFORMATON

TRADING RESULTS

Revenue	95,103.188	105,001.924	111,389.486	135,351.978	174,554.976	211,012.846	253,344.379	358,002.116	257,508.193	276,550.970
Profit/(Loss)after Taxation	1,169.310	9,986.088	4,874.194	3,907.862	7,710.890	(946.220)	2,862.337	(14,952.518)	(11,566.957)	(26,922.819)

ASSETS EMPLOYED

Property, Plant & Equipment	7,630.244	10,844.721	4,504.432	4,450.672	4,512.448	4,460.920	4,374.649	4,624.068	5,041.139	8,280.085
Net Current Assets	(16,738.531)	(12,165.676)	(6,785.125)	(2,728.739)	17,763.403	14,519.333	15,138.460	(2,585.377)	7,323.200	(28,938.672)
Total	(9,108.287)	(1,320.955)	(2,280.693)	1,721.933	22,275.851	18,980.253	19,513.109	2,038.691	12,364.339	(20,658.587)

FUNDS EMPLOYED

Capital	1,000.000	1,000.000	1,000.000	1,000.000	1,000.000	1,000.000	1,000.000	1,000.000	1,000.000	1,000.000
Reserves	(15,039.418)	(8,588.861)	(2,253.785)	1,984.126	11,673.455	10,065.946	12,557.400	(2,416.400)	(14,716.700)	(40,951.600)
Total	(14,039.418)	(7,588.861)	(1,253.785)	2,984.126	12,673.455	11,065.946	13,557.400	(1,416.400)	(13,716.700)	(39,951.600)
Capital Expenditure	(2,306.025)	(4,001.341)	(5,255.000)	(255.000)	(78.000)	(255.000)	(242.680)			

EMPLOYEES EARNINGS

Wages	1,620.893	1,496.242	1,461.006	1,201.357	986.434	1,221.585	1,429.796	1,668.718	1,815.765	2,056.067
Bonus	125.804	112.884	186.671	101.931	84.739	129.689	149.007	211.852	240.061	252.098
Annual Average Earnings per Employees (000' Rs.)	243.510	224.863	759.298	531.530	419.410	461.188	538.657	664.043	736.327	841.168
No. of Employees	7,173	7,156	2,170	2,452	2,540	2,930	2,931	2,832	2,792	2,744

FINANCIAL RATIO

Return on Capital Employed %	-	-	-	130.900	60.840	(15.770)	21.100	-	-	-
Return on Turnover %	21.000	14.650	5.670	3.220	4.760	(0.870)	1.200	(4.38)	(5.22)	(0.11)
Debtors to Turnover %	0.050	0.030	0.040	0.060	0.080	0.090	0.130	0.19	0.31	0.30
Turnover to Fixed Assets times	9.780	7.390	19.070	27.310	35.870	44.450	53.430	78.10	55.50	60.50
Finished Stock to Turnover times	0.050	0.050	0.050	0.070	0.060	0.090	0.090	0.065	0.064	0.10
Current times Ratio	0.500	0.600	0.700	0.920	1.480	1.330	1.220	0.977	1.057	0.82
Liquid times Ratio	0.230	0.240	0.450	0.530	1.000	0.740	0.640	0.69	0.86	0.57
Interest times Cover	1.470	9.910	9.960	6.780	8.810	0.350	1.280	(4.73)	(2.60)	(3.93)

GLOSARY OF FINANCIAL TERMS

Cash Equivalents - Short term investments readily convertible to known amounts of cash subject to insignificant risk of changes in value.

Contingent Liabilities - Conditions or situations at the Balance Sheet date, the financial effects of which are to be determined by future events which may or may not occur.

Current Ratio - Measures the number of times current liabilities be recouped with available current assets.

Debtors to Turnover - Measure of the credit extended to customers (i.e. average debt settlement period if stated in days)

Deferred Income - Income yet to be realized or realized but not recognized as income.

Interest Cover - Measures the extent to which interest charges be covered by profit before Tax.

Liquid Ratio - Measures the number of times current assets be recouped with available current liabilities.

Post Balance Sheet Events - Significant events that occur between the Balance Sheet date and the date on which financial statements are authorized for issue.

Provisions - Liability of uncertain timing or amount.

Related parties - Parties who could control or significantly influence the Financial and operating decisions/policies of the Corporation.

Segments - Constituent business units grouped in terms of nature and similarity of operations.

Working Capital - Capital required financing the day-to-day operations (current assets less current liabilities).

ABBREVIATIONS

Avn	-	Aviation
Bbl	-	Barrel (Basic unit in international petroleum sales)
bps	-	Basis points
BTR	-	Bulk Transfer
CEB	-	Ceylon Electricity Board
CIF	-	Cost Insurance Freight
CPC	-	Ceylon Petroleum Corporation
EPF	-	Employees Provident Fund
ETFB	-	Employees Trust Fund Board
FIFO	-	First in First Out
FOB	-	Free on Board
FOREX	-	Foreign Exchange
GOSL	-	Government of Sri Lanka
ICPA	-	International Coop/Petroleum Association
Int	-	Interest
CPSTL	-	Ceylon Petroleum Storage Terminals Ltd.,
LIOC	-	Lanka Indian Oil Corporation Ltd.,
LMS	-	Lanka Marine Services (Pvt.) Ltd.,
LPG	-	Liquid Petroleum Gas
Ltr	-	Litre (Basic unit in domestic Petroleum sales)
MOU	-	Memorandum of Understanding
NDB	-	National Development Bank
OPEC	-	Oil Producing and exporting Countries
PERC	-	Public Enterprise Reforms Commission
SPBM	-	Single Point Buoy Mooring Facility
TT	-	Turnover Tax
VAT	-	Value Added Tax
VRS	-	Voluntary Retirement Scheme

