

## **1. Financial Statements**

### **1.1 Qualified Opinion**

The audit of the financial statements of the Lanka Electricity Company (Private) Ltd for the year ended 31 December 2024 comprising the Consolidated statement of financial position as at 31 December 2024 and the Consolidated statement of profit or loss statement, Consolidated statement of other comprehensive income, Consolidated statement of changes in equity and Consolidated cash flow statement for the year then ended, and notes to the financial statements, including material accounting policy information, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with provisions of the National Audit Act No. 19 of 2018. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the accompanying financial statements give a true and fair view of the financial position of the Company as at 31 December 2024, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

### **1.2 Basis for Qualified Opinion**

My opinion is qualified on the matters described in paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

### **1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements**

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Company.

## 1.4 Audit Scope

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company and the Group internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company;
- Whether the Company has performed according to its powers, functions and duties; and

- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

## 1.5 Audit Observations on the preparation of Financial Statements

### 1.5.1 Non-Compliance with Sri Lanka Accounting Standard

Non-Compliance with the reference to particular Standard	Management Comment	Recommendation
(a) According to paragraph 5.5 of the Conceptual Framework for Financial Reporting issued under SLFRS/LKAS, the initial recognition of assets or liabilities arising from transactions or other events may result in the simultaneous recognition of both income and related expenses. However, it was observed that the Company had not recognized the cost of solar energy purchases amounting to Rs.2,855,274,443 and corresponding liability under the net accounting and net plus methods as cost of sales in the financial statements for the year under review. However, an adjustment of Rs. 482,800,000 relating to the Uniform National Tariff (UNT) for the year 2024 had been recognized during the year under review. Therefore, the cost of sales had been understated by Rs. 2,372,472,443 for the year under review.	We acknowledge paragraph 5.5 of the Conceptual Framework for Financial Reporting under SLFRS/LKAS, which requires simultaneous recognition of related income and expenses to reflect the economic substance of transactions in line with the matching concept. In practice, rooftop solar systems are connected to LECO's network, with the Transmission Licensee (TL) as the sole legal buyer. Although LECO processes payments to rooftop solar generators, PUCSL directives require LECO and other DLs to recover these from the TL. As DLs use this energy, the TL invoices them accordingly, with both inflows and outflows adjusted through the Uniform National Tariff (UNT) mechanism. This ensures compliance with SLFRS/LKAS and faithful presentation of the transaction's economic substance.	Recognize the full cost of solar energy purchases and the corresponding liabilities in accordance with paragraph 5.5 of the Conceptual Framework and applicable SLFRS /LKAS requirements.
(b) The Company recognized Uniform National Tariff (UNT) adjustments in its financial statements year ended 31 December, relating to prior years, which is not in line with the SLFRS/LKAS requirement to match income and expenses in the same period. These included cost of sales adjustments for the years 2021 and 2023 amounting to Rs. 1,108,129,877 and credits to the Purchases of Electricity account for revisions relating to 2021, 2022, and 2023. Therefore, the cost of sales had been overstated by Rs. 1,108,129,877 for the year under review.		
(c) In terms of paragraph 51 of the Sri Lanka Accounting Standards on Property plant and Equipment (LKAS- 16) the residual value and the useful life of an assets shall be reviewed annually and, if expectations differ from previous estimate, the changes shall be accounted for in accordance with LKAS 8,	It is not practical to review the usable lifetime of the entire Supply of Infrastructure asset class, as these assets are widely dispersed along the coastal belt of the Western and Southern provinces and may include	Ensure periodical review of residual values and useful lives of all assets and account for changes if any to comply with

However, the assets with carrying value of Rs. 11,978,829,318 relating to four categories as at 31 December 2024 had not been reviewed and accounted as required by the standard.

different asset types with varying usable lifetimes within the same category. However, management intends to review the asset values and depreciation policy for asset classes, excluding distribution assets, in 2025. This non-compliance with LKAS 8 has been disclosed in the financial statements under Note 10.6

relevant Accounting Standards.

### 1.5.2 Accounting Deficiencies

Audit Issue	Management Comment	Recommendation
(a) Two procurements aggregating to the amount of Rs.122, 974,205 had been recorded in twice time. As a result of that Goods In Transit and liabilities (Creditor control account) had been overstated by same amount.	We acknowledge the Auditor's comments. The issue arose from miscommunication between the suppliers' division and the stock control division. Corrective actions will be implemented following a thorough review of the relevant accounts.	Should be take corrective measures and strength the internal review process.
(b) Due to the non-recovery of Lien advance payments made for interim payment certificates (IPC) amounting to Rs. 116,389,312 related to the construction of head office building had been erroneously shown under the work-in-progress account, instead of showing under the advances account. Therefore, work-in-Progress had been overstated, and Lien advance account was understated by same amount for the year under review.	Based on our calculations, cumulative payments from IPC-11 to IPC-19 have resulted in an overpayment of approximately Rs. 9,192,069 to the contractor. Payments made through the Lien Account must be reimbursed via the IPC, and some entries show negative values. The overpayment also relates to unverified work corresponding to the amount. As per your clarification, further attention will be given to address this matter.	Action should be taken to reclassify the lien advance amount.
(c) According to the financial records pertaining to the construction of the customer service Centre (CSC) at Negombo, the advance accounts of interim payment Certificate had been overstated by Rs.36,452,909 and the work-in-progress (WIP) had been understated by a same amount for the year under review.	Noted the observation. There is a classification mismatch in recording of relevant working progress, and this will be rectified accordingly. However, there is no impact on the declared net assets position of the company.	Action should be taken to adjust the financial records by reclassifying Rs. 36,452,909 from the advance accounts of interim payment certificates to the work-in-progress account.

### 1.5.3 Documentary Evidence not made available for Audit

Item	Amount Rs.	Evidence not available	Management Comment	Recommendation
Share certificates of the Lanka Broad Band Network (Private) Limited	5,000,000	Share certificates or any other appropriate documentary evidences to confirm the value and existence of the investment	Instructions have been obtained from the Attorney General's Department in this regard. It has been informed that legal action cannot be taken regarding this matter as this investment made in the year 2001. The internal investigation is still ongoing this regard.	Action should be taken to obtain and maintain proper documentary evidence, such as share certificates or other relevant records, to substantiate the existence and valuation of the investment."

## 1.6 Accounts Receivable and Payable

### 1.6.1 Receivables

Audit Issue	Management Comment	Recommendation
(a) The total debtors balance presented in the billing system as at 31 December 2024 was Rs.3,372,405,052 and out of that a balance of Rs. 326,812,943, had remained over one year without being recovered.	LECO Management stated that recovery actions are ongoing for 31,141 consumers overdue for more than one year, with specific measures for active, disconnected, inactive consumers, and those with printed notices or orders.	Action should be taken to recover the outstanding balances.
(b) Trade receivable of related party for miscellaneous services, mainly related to energy purchases from 2017 to 2024 under net accounting methods as at 31 December 2024 was Rs. 6,126,712,991. However, this balance had not confirmed by the CEB, and no formal agreement was signed between the parties. As a result, the recoverability of the amount could not be verified and Rs. 3,175,469,035 had been recognized as impairment provision for over three Years debtors value only in the financial statements.	LECO Management stated that energy purchase transactions are governed by PUCSL directives, but agreed that a formal agreement with CEB is needed and has proposed relevant terms for inclusion in a Power Purchase Agreement. They noted that CEB settled Rs. 1.885 billion for 2023 through UNT adjustments in May 2025, with potential for future recoveries via the same method. However, older balances from 2017–2020 remain uncertain, and negotiations will be initiated to recover them.	Action should be taken to formalize agreements with CEB and obtain confirmation for outstanding balances to recover the outstanding balances or make any arrangement to settle/set off any payable balance to the CEB.
(c) A sum of Rs. 6,705,420 remains receivable from the Ministry of Power for more than two years as at the end of the year under review without any follow-up actions.	Noted the observation. We will make arrangements to coordinate with the Ministry and expedite the recovery of this amount	Action should be taken to recover the outstanding balance.

## 1.6.2 Payables

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
(a) A significant difference of Rs. 1,224,075,542 was observed between the payable balance in the financial statements of the company (Rs. 5,931,838,541) and balance confirmation of CEB (Rs. 4,707,762,999) without reconciled.	The discrepancy between the ledger balance payable to CEB and the CEB balance confirmation arises from SSCL payable on electricity purchases from October 2022 to August 2023, recorded in the Company's books but not reflected in CEB's confirmation. Under Section 2 of the SSCL Act No. 25 of 2022, electricity turnover was not subject to SSCL up to August 2023. Due to an ongoing dispute with the Inland Revenue Department, a formal opinion has been requested from the Attorney General, and the matter is expected to be resolved within this financial year.	Action should be taken to promptly reconcile the difference and resolve the discrepancy between two parties if such exists.
(b) An amount of Rs. 20,598,278 has been recorded in the company's books as receivable from the CEB under the net Metering schemes (Ledger Codes 73207AA and 73207OA). However, this balance was not confirmed by CEB in their balance confirmation, resulting in a discrepancy of Rs. 20,598,278 between the two records.	These outstanding balances remain unresolved due to miscommunication between the branches and the Head Office. According to branch records, there are no pending payments for solar generation to customers. To address this issue, the necessary steps are being implemented, including obtaining balance confirmations from the relevant solar customers promptly.	Action should be taken to reconcile differences with CEB and ensure all payables and receivables under Net Metering arrangements are accurately recorded.
(c) The total amount under Refundable Deposits for Temporary Connections was Rs.85,784,619 as at 31 December 2024, Out of that, a sum of Rs. 13,613,391 pertained to customers whose temporary connections had already been disconnected was remained without refund.	The refund process for temporary connections is ongoing. Certain balances remain unsettled due to uncollected or cancelled cheques, pending refunds for disconnected customers, and cases where the recoverable amount exceeds the refundable amount. These issues are actively being addressed to ensure timely resolution and processing of refunds.	Action should be taken to promptly refund deposits for disconnected temporary connections and strengthen monitoring of refundable deposits
(d) A sum of Rs. 186,973,423 of Interest Payable to Consumers on Consumer Deposits (Account Code: 73223) had remained unpaid.	These provisions were established in accordance with instructions from the Public Utilities Commission of Sri Lanka (PUCSL). However,	Should be comply with the existing provisions.

explicit guidance regarding their removal has not been received. We will continue to engage with the PUCSL to seek clarification and determine the appropriate course of action.

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| <p>(e) Invoice Value of purchase of goods 3 times amounting to Rs.21,271,276 had not been identified in the Ledger. However, 90 percent an advance amounting to Rs. 19,135,796 Paid thereon, had been accounted to the creditor control and cash. Therefore, balance of creditor control accounts had been understated by Rs.19,135,796 and goods in transit had been understated by Rs. Rs.21,271,276.</p> | <p>We acknowledge the Auditor's comments. Remedial actions will be taken to be implemented to streamline the process promptly.</p>   | <p>Action should be taken to correct the defecting and should be strength the process promptly.</p>   |
| <p>(f) According to the Accounting System (Pronto) used by the LECO, it was noted that unsettled amounts totaling Rs. 18,071,844 across multiple purchase orders were remained as liability although they marked as settled in the system.</p>  | <p>We acknowledge the Auditor's comments and are committed to implementing remedial actions to streamline the process promptly</p>   | <p>Action should be taken to investigate and resolve the unsettled amounts in the accounting system and should ensure all purchase orders are completion accurately recorded and settled.</p> |
| <p>(g) Due to the duplication of Interim Payment Certificate No. 01, work in progress account had been overstated by Rs. 8,051,287, while the Suppliers payable Account had been correspondingly overstated.</p>  | <p>Noted the observation. As there is a classification mismatch of the observed Lien payments will do the needful to rectify the same. However, there is no impact on the declared net assets position of the company.</p> | <p>Action should be taken to correct the duplication error.</p>   |

### 1.6.3 Advances

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
<p>As per the Financial Statements of the company as at 31 December 2024, advances and prepayments amounted to Rs. 877,434,964. Out of that, Amount of Rs.23,497,524 was remained in outstanding for 1 to 15 years. Furthermore, LECO had not yet prepared a Financial Procedures Manual for advances.</p>	<p>During the review of unsettled advances, some relate to ongoing utility services, while others have already been settled in 2025. Detailed explanations are provided in PWR/C/LECO/01/2024/AQ/16. Actions will be taken to expedite settlements from the respective employees or suppliers.</p>	<p>Action should be taken to settle long-outstanding balances and to establish a Financial Procedures Manual to ensure proper management and timely clearance of advances in the future.</p>

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

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) As per the Public Enterprises Circular No.01/2021 (ii) dated on 27 September 2023, the parent company shall introduce the subsidiary policy before 31 December 2023 with the concurrence of Director General, Department of Public Enterprises through the Secretary of the relevant line ministry. Unless the parent entity introduces a subsidiary policy before 31 December 2023, provision of the guidelines on Corporate Governance for SOEs and Operational Manuals for SOEs and circulars should be followed by the subsidiary companies.	Company had not introduced subsidiary policy to Anti-Leco Metering Company (Pvt) limited and Leco Projects Company (Pvt) limited as at 31 December 2024 in compliance with the requirement of the circular.	Management Comment not given	Action should be taken to comply with said circular.
(b) As per internal circulars ADM/EST/002 dated 08 September 2017, ADM/EST/017 dated 29 September 2017, ADM/EST/017/GM/13/2023 dated 10 July 2023 and ADM/EST/017/GM/13(i)/2023 dated 18 July 2023.	(i)According to the circulars, all officers should record their arrival and departure by using finger machine. In the Sample audit test carried out relating to the months of June, July, and August 2024, it was observed that 75 number of executive officers had not use the finger machine to record their arrival and departure	As noted, all officers are required to record their arrival and departure via the biometric attendance system. However, due to the specific responsibilities of many executives, consistent use of the system is operationally impracticable. To address this, management issued General Manager's Circular ADM/Est/017/GM/49/2025, dated 24 March 2025. A copy of the circular is attached for your reference.	Action should be taken to ensure that all officers consistently use the fingerprint machine to record attendance, and compliance with internal circulars should be regularly monitored.
	(ii)In the cases where any employee has to engage on duties	Pursuant to the previous, the requirement outlined	Action should be taken to ensure that all employees

before coming to the workplace and leaves from the workplace for a duty before the time when duties are normally finished it, should be recorded on relevant form with approvals and should be made it available to human resource department. However, it was observed that, majorities of the executives had not complied with this requirement.

under Section II similarly conflicts with the specific responsibilities assigned to the majority of executives, rendering it impracticable to complete the requisite form in real time along with the necessary approvals. Consequently, this requirement shall also be deemed inoperative according to the provisions of General Manager's Circular ADM/EST/017/GM/4 9/2025, dated 24 March 2025.

Although Leaves of Executives had been approved by considering the Leave application, leaves of executives had not been checked with finger print report

In light of the foregoing, while it remains practically difficult to continuously monitor executives via the biometric attendance system, the processing and approval of executives' leave requests continue to be conducted appropriately through the formal leave application process.

- (c) As per the paragraph 2(a) of internal Circular No. ADM/EST/017/GM/13/2024(ii), dated 21 March 2024, the said 75 executive officers.
- All allowances linked to employee attendance must be calculated exclusively based on records generated through the fingerprint attendance system. However, 75 executive officers failed to use the fingerprint system during the months of
- Even should the policy mandating "All allowances tied to employee attendance must be computed solely from records captured via the fingerprint attendance system" be strictly enforced, in practice, such payments have been disbursed based on attendance reports
- Action should be taken to cross-verify leave approvals with fingerprint attendance records.
- Action should be taken to ensure that all attendance-linked allowances are calculated based on verified biometric records, and measures should be implemented to enforce compliance with internal circulars.

June, August, and September 2024, even though the five circulars had been issued since 2017 emphasizing the mandatory use of biometric attendance and the company had made payments amounting to Rs. 59,087,804 as annual incentives and medical leave allowances to the said 75 executive officers without getting the biometric attendance.

- (d) As per Section 6 of the “Key Characteristics” of the Internal Circular No. ADM/EST/017/GM/14/2023 dated 14 August 2023.
- As per internal Circular it is required to 2% deduction from payments made to solar electricity suppliers under the variable tariff method and it should be deposited as a performance guarantee throughout the 20 years contract period. This requirement was introduced to ensure supplier compliance and to provide financial recourse in case of non-performance, in line with the Cabinet Decision for one of the Recommendation of Cabinet Memorandum and No. ୧୩୨/23/0798/621/01 6-II dated May 20, 2023. However, LECO had failed to implement above
- prepared from leave applications submitted through the respective supervisors and duly approved. This practice has ensured both procedural compliance and the accurate payment of mentioned incentives and allowances.
- LECO could not fully implement the 2% supplier security deposit due to practical and legal constraints. With the variable tariff declining and the fixed tariff not in effect, monthly deposits are no longer necessary. Delays in tariff updates caused supplier disputes and customer complaints. Following the Cabinet’s cancellation of the variable tariff, LECO offered a one-time voluntary transition to the fixed tariff, which involved no additional cost or financial gain, and was implemented within the company’s authority.
- Action should be taken to implement the 2% deduction requirement for all relevant payments to solar energy suppliers and to ensure compliance with the Cabinet-approved performance guarantee guidelines

requirement, as a result a sum of Rs. 2,341,941 had not been deducted from the solar energy suppliers.

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| (e) | Cabinet Decision No.අමප/23/0798/621/016-II dated 9 May 2023. | Solar electricity suppliers had originally signed agreements under the variable tariff method approved by the Cabinet. However, a management directive issued by Lanka Electricity Company (LECO) on February 24, 2025, allowed these suppliers to switch to a fixed tariff of Rs. 27.00 per unit. This was given as a one-time option. Accordingly, as at date of the report, 21 suppliers under the Kelaniya branch signed new agreements under the fixed rate, replacing their previous 20 years variable tariff contracts. This change was made without getting Cabinet approval, even though the original tariff was approved by the Cabinet. In addition, no financial analysis was done to ascertain the possible cost to the company before making this decision. | The Cabinet Memorandum did not allow suppliers to switch from the variable tariff scheme to another scheme, and Section 07 of the institution's circular also did not provide such an option. However, based on a management order dated 24 February 2024, the institution introduced a practical alternative, permitting migration of fee schemes with suppliers' consent. This opportunity was extended to all suppliers, and by that time the Cabinet had already abolished the variable tariff scheme. Accordingly, the institution emphasizes that it has not acted outside the approval of the Cabinet of Ministers. | Action should be taken to obtain appropriate Cabinet approval for tariff changes and to conduct thorough financial analysis prior to amending supplier agreements to ensure compliance. |
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| <p>(f) As per the internal Circular No. ADM/EST/017/GM/14/2023</p> | <p>Tariff of the solar electricity suppliers under the variable tariff method should be revised quarterly. However, tariff revision was carried out with a delay of 11 months. Nevertheless, the Company had paid a sum of Rs. 155,100,144 to the solar electricity suppliers without revising the tariff. As a result, an extra payment of Rs. 38,003,066 had been paid to the above suppliers as solar energy payments.</p> | <p>Tariff rates under the variable tariff system are to be revised quarterly by the Ceylon Electricity Board (CEB). However, while the 4th quarter 2023 rates were issued on 13 December 2023, the next revision was only published on 14 August 2024. As a result, no rates were published for the 1st, 2nd, and 3rd quarters of 2024. Consequently, the institution continued payments to suppliers using the previous quarter's rates and notified the Additional General Manager, Transmission (Non-Wired) of CEB on 23 July 2024, requesting the publication of the relevant tariff revisions.</p> | <p>Action should be taken to ensure timely tariff revisions in accordance with internal circulars.</p> |
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## 2. Financial Review

### 2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs. 9,842 million and the corresponding profit in the preceding year amounted to Rs. 4,129 million. Therefore, an improvement amounting to Rs. 5,713 million of the financial result was observed. The reasons for the improvement are Increase of other operating income by Rs. 2,015 million and decrease of operating expenses by Rs. 3,924 million.

### 2.2 Trend Analysis of major Income and Expenditure items

- (a) The revenue for the year under review had decreased by 5.3 per cent compared to the previous year. Simultaneously the cost of sales had decreased by 5.7 per cent and gross profit for the year under review had decreased by 3.5 per cent.
- (b) Other operating income for the year under review had increased by 85 per cent compared to the previous year.

## 2.3 Ratio Analysis

- (a) Net profit margin had increased from 6 per cent to 8 per cent compared to the preceding year.
- (b) Return on Equity (ROE) had increased from 9 per cent to 11 per cent compared to the preceding year.
- (c) Current ratio of the Company had decreased from 2.4 to 3.2 compared to the previous year.

## 3. Operational Review

### 3.1 Management Inefficiencies

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
According to the certified interim payment certificates related to the head office building construction project of the LECO, the value of work certified as at 30 April 2025 was Rs. 935,085,691. However, the total payments made to the contractor was Rs. 1,094,457,389. As a result, it was observed that significant deviating from the agreed contractual payment procedures and highlighting weaknesses in financial oversight and contract management controls during the period under review an overpayment of Rs. 159,371,698 had been made to the contractor.	Management comment not given	Action should be taken to recover the overpaid amount, strengthen contract management procedures, and enhance financial oversight to prevent similar overpayments in the future.

### 3.2 Operational Inefficiencies

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
(a) According to the company's established accounting structure, VAT-related transactions at branch level should be transferred to the Head Office for centralized processing. However, it was observed that an unsettled balance of Rs. 6,188,495 under VAT Payable (Account Code: 73350) at the Kotte Branch was as at 31 December 2024 without transferring to the head office.	Company Tax consultants are in the process of checking the possibility of getting the relevant VAT refund from Department of Inland Revenue (IRD) after setting off the payable VAT balance and the matter is still under discussion level with IRD	Action should be taken to promptly transfer branch-level VAT transactions to the Head Office and ensure centralized processing to maintain accurate financial records
(b) Estimates should be based on the best available information at the time of preparation. However, in	The UNT adjustment is a sector-wide calculation determined by PUCSL using	Action should be taken to strengthen the estimation process by using the best available information and reliable

relating to UNT estimates for prior years that significant deviations between the original value of Rs.1,443,646,679 and revised amount of Rs.305,639,299 was observed.

complex variables such as assumptions. DL sales revenue, energy purchases, capacity and energy payments, distribution losses, and allowed revenue. Due to data complexity and CEB's structure, final UNT adjustments are often delayed. To meet reporting deadlines, LECO uses the most recent provisional estimates from PUCSL, which are externally sourced and align with LKAS 8 guidance. While LECO ensures diligent reporting, the accuracy of these estimates is PUCSL's responsibility, and the treatment follows prudence and accrual principles, matching revenue and costs in the correct period.

- (c) During the year, the Company purchased Energy valued Rs. 57,199 million from the Ceylon Electricity Board (CEB). However, these transactions were conducted without a formal, Power Purchase Agreement (PPA) with them.

The Power Purchase Agreement was initially drafted by the CEB. A series of discussions were held with the participation of CEB & LECO officials to finalize the draft document from the year 2023.

Subsequently, PUCSL arranged a meeting to discuss the final draft on 25<sup>th</sup> of February 2025 with the participation of CEB and LECO officials. During the discussion LECO proposed several amendments to the draft agreement. However, CEB has not yet submitted the finalized document.

Action should be taken to ensure that all agreements, including the Power Purchase Agreement with CEB, are properly signed and documented to submit audit or any other legal parties for verification process.

### 3.3 Procurement Management

#### Audit Issue

According to the Master Procurement Plan (MPP) for the year 2023, the estimated unit cost per 7.6-meter pole was Rs. 52,500, and for a 9-meter pole, was Rs. 82,500 and according to the Standard Cost Manual prepared by the LECO for the same year, the standard costs for the above poles were Rs.23,223 and Rs.38,734, respectively. However, the highest bids received during the actual procurement process were only Rs. 17,800 for the 7.6-meter pole and Rs. 45,500 for the 9-meter pole. As a result, it was observed that the cost estimates included in the MPP were significantly overstated. The reasons for the above differences were the lack of coordination between the committee responsible for preparing the MPP and the committee that compiled the Standard Cost Manual. Therefore, the allowed revenue (allowed Gross Profit) of the Company was overstated, and further, the electricity tariff calculation by the Public Utilities Commission of Sri Lanka (PUCSL) are primarily based on the Company's budget, therefore, such overstatements may result to increase the tariff rate.

#### Management Comment

The Standard Cost Manual (SCM) is prepared in line with PUCSL guidelines by considering the recorded stock-in prices available for the latest procurements.

At the time of the preparation of MPP 2023 in late 2022, the high price escalations of the ongoing pole procurements at the time were noted. (The cost of RC 7.6m pole awarded on 11/03/2021 for Rs. 16,250.00 was increased up to Rs. 28,041.88 on October 2022 as per variation formula) Considering the unpredictable increases in raw materials and gradient of price increase for poles (in the latest procurement at the time) due to the economic recession amidst pandemic, revised unit price of Rs.52,500.00 had been taken during the preparation of MPP 2023.

In case of underestimating the unit price, the procurement process would have been negatively affected during processing.

#### Recommendation

Action should be taken to ensure proper coordination between the committees preparing the MPP and the Standard Cost Manual to reflect accurate cost estimates, thereby preventing overstatement of revenue and avoiding potential impacts on electricity tariffs.

### 3.4 Defects in Contract Administration

#### Audit Issue

According to the section 13.7 (c) of the ICTAD SBD-02, non-adjustable element which are listed under clause 13.7 in the contract data, shall not be considered for valuations of price adjustments,

#### Management Comment

Up to IPC-10, all preliminaries were treated as non-adjustable in price escalation calculations. However, according to Cl. 13.7 of the Conditions of Contract, CIDA

#### Recommendation

Action should be taken to ensure that price escalation calculations strictly follow the contract

However, when calculating the price escalation for interim payment certificate under the construction of head office building, the company had considered non-adjustable element as adjustable element. As a result, the company had to pay an extra payment of Rs. 12,410,238 to the contractor as price escalation.

opinion (23 June 2023), and the CIDA formula method, time-related preliminaries should be adjustable. Accordingly, the amount is payable to the contractor, and its financial impact has already been factored into LECO's project budget and expenditure forecasts.

provisions, and overpayments due to incorrect treatment of non-adjustable elements should be recovered from the contractor.