

National Savings Bank

1. Financial Statements

1.1 Opinion

In my opinion , the financial statements give a true and fair view of the financial position of the National Savings Bank as at 31 December 2012 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

In my opinion, the consolidated financial statements give a true and fair view of the financial position of the National Savings Bank and its subsidiary as at 31 December 2012 and their financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Comments on Financial Statements

1.2.1 Sri Lanka Accounting Standards (LKAS)

LKAS - 16

Although five hundred and forty items costing Rs.361, 158,839 had been fully depreciated ,they had been still continued to be used by the National Savings Bank.It was observed that action had not been taken to revalue and bring them to accounts as required.

1.2.2 Accounting Deficiencies

The value of Rs.6,995,174 of the Uswatakeiyawa land which was acquired by the Navy in 2009 had still been shown under work in progress as at 31 December 2012.

1.2.3 Unexplained Differences

The following unexplained differences were observed.

(a) According to the financial statements of 2012, EPF and ETF contributions amounted to Rs.240,254,639 and Rs.59,942,007 respectively whereas according to the computations based on the adjusted gross salaries shown in the financial statements amounted to Rs.240,079,027 and Rs.60,019,757 respectively and the identified differences amounted to Rs.175,612 and Rs.77,749 respectively.

- (b) A sum of Rs.184, 420,746 had been included in the Financial Statements as investments in a finance company under the investments in Trust Certificates. However, the value of investment amounted to Rs.185,701,000 according to the confirmation of balances and schedules furnished by the Bank, thus a difference of Rs.1, 280,253 had been observed.

1.2.4 Accounts Receivable and Payable

The following observations are made.

- (a) A sum of Rs.260,044,858 receivable from the Treasury on account of dormant accounts had remained outstanding for over five years.
- (b) Action had not been taken on outstanding fraudulent withdrawals amounting to Rs.13,963,717 as at 31 December 2012 and out of that Rs.13,188,717 were outstanding for over one year.
- (c) Refundable tender deposits to customers amounting to Rs. 1,682,084 and Rs.1,924,524 had remained outstanding for over five years and three years respectively.
- (d) A balance of Rs. 2,699,061 older than five years had been shown in the Deposit Clearance Account.

1.2.5. Lack of Evidence for Audit

The following documentary evidences were not made available for audit.

Item in the Financial Statements	Amount Rs.	Documentary evidence not made available
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Sundry Creditors	28,028,481	} Age analysis
Creditors Control A/C	26,006,153	
Bills sent for collection	248,728,135	
Advances to Suppliers	8,062,774	Confirmations

1.2.6 Non – Compliance with Laws, Rules, Regulations and Management Decisions

Instances of Non-compliance with the following Laws, Rules, Regulations and Management Decisions observed in audit are given below.

**Reference to Laws, Rules,
Regulations and Management
Decisions**

Non compliance

- | | |
|--|---|
| <p>(a) Inland Revenue Act No 10 of 2006 as amended by Act No. 10 of 2007</p> | <p>(i) Tax Declaration Statements along with the Application for Opening Accounts had not been obtained from the customers by 15 Branches in 202 instances.</p> <p>(ii) Though 63 customers relating to 15 branches had submitted their tax declarations with their assessable income not exceeding Rs. 500,000, deposits amounting to Rs.756,312,255 had exceeded the above limits.</p> |
| <p>(b) Government Procurement Guidelines of the National Procurement Agency Circular No. 8 dated 25 January 2006 as amended by No. 06 dated 05 October 2006</p> <p>-----</p> <p>(i) Chapter 2.14.1</p> | <p>(i) National Competitive Bidding procedure had not been followed with regard to following procurements.</p> <ul style="list-style-type: none">❖ Purchase of 10 Nos UPS for Rs. 4,895,520.❖ Purchase of Hapan Gift Items for Rs. 96,000,000 |
| <p>(ii) Chapter 3.3</p> | <p>(i) Bids invitation from registered suppliers of the Bank should be directly done. However, the National Savings Bank had not invited bids from registered suppliers when purchasing 75 Informix user Licenses for Rs.8,484,000.</p> <p>(ii) In the case of small number of suppliers, bids should be invited from them together with potential suppliers who would furnish competitive prices. However, the NSB had not invited bids from the other business partners of IBM Company that supplies Informix Licenses.</p> |

- (iii) Chapter 4:2:1 Master Procurement Plan and detailed Procurement Plan had not been prepared for the year 2012.
- (vi) Chapter 8.9.3 Formal contract agreement should be signed for contract value in above Rs. 500,000. However in respect of following procurements this requirement had not been fulfilled.
- a. Procurement of 57,100 Nos Blenders and 30,000 Nos Sauce pans for Rs. 64,117,500.
 - b. Purchase of 10 Nos UPS for Rs. 4,895,520.
 - c. Purchase of 40 Numbers floor switches for Rs.11,891,196.
 - d. Service contract of Cleaning Service for the year 2012 for Rs. 7,866,000
 - e. Purchase of 80 Numbers Digital Media Systems for Rs. 27,065,000.
 - f. 75 Informix user Licenses for Rs.8,484,000.
- (c) Inland Revenue Act No. 38 of 2000 and the Public Finance Circular No. PF/PE/06 of 31 January 2000 The Bank had paid PAYE tax amounting to Rs. 50,963,789 for the year 2012 out of its own funds for the employees of the Bank contrary to the relevant provisions.
- (d) Circular No 425/97 of the General Manager of the National Savings Bank Even though the fixed deposit should not be released until the settlement of loan amount, eight Fixed Deposit accounts had been closed without settling the respective loans amounting to Rs. 766,353 in relation to 4 branches.

2. Financial and Operating Review.

2.1 Financial Review

According to the financial statements presented, the operations of the Bank during the year under review had resulted in a pre-tax net profit of Rs. 6,169 million as compared with the

corresponding pre-tax net profit before income tax of Rs.9,255 million in the preceding year, thus indicating a decrease in financial results by Rs. 3,086 million or 33.34 per cent.

The operations of the Subsidiary of the Bank during the year under review had resulted in a pre-tax net profit of Rs.52 million as compared to the corresponding pre-tax net profit of Rs 156 million in the preceding year thus indicating a decrease in financial results by Rs 104 million.

- (a) Loss of the Head Office amounting to Rs3,651 million, profits of 166 Branches (Bank Branches, Postal Branches, Piyasa Units and Divisions) aggregating Rs. 10,075 million and losses of 55 Bank Branches and 02 Divisions aggregating Rs. 255 million consists of the Pre Tax Net Profit of the Bank of Rs. 6,169 million for the year under review.
- (b) The overall income of the National Savings Bank for the year under review was Rs.53,045 million as compared with Rs.46,545 million of the preceding year which was showing an increase of Rs.6,500 million or 14 per cent , mainly due to increase in interest rates.

2.2 Significant Ratios and Percentages

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

	<u>2012</u>	<u>2011</u>
(a) <u>Profitability Level</u>		
(i) Return on average Shareholders' funds (ROE) (%)	18.28	26.61
(ii) Return on average Assets (ROA) (%)	1.26	2.13
(b) <u>Capital Adequacy</u>		
Equity : Total Assets	1: 20.94	1: 20.21
(c) <u>Liquid Assets</u>		
Liquidity Ratio (%)	69.5	74.4

The following observation is made in this regard.

Return on Equity, Return on Assets and Liquidity Ratio had decreased by 31per cent, 41 per cent and 7 per cent respectively during the year under review as compared with the preceding year.

2.3 Loan Administration

2.3.1 Details of loans granted and loans categorized to non performing of the Bank for the years 2012 and 2011 are given below.

	<u>2012</u>				<u>2011</u>			
	Loans granted		Non - performing loans as at 31/12/2012		Loans granted		Non - performing loans as at 31/12/2011	
	No of Loans	Amount Rs (mn)	No of Loans	Amount Rs (mn)	No of Loans	Amount Rs (mn)	No of Loans	Amount Rs (mn)
Alankara Loans	11	8.80	07	6.32	21	21.67	06	3.45
Auto Loans	53	143.54	02	2.47	43	58.77	-	-
Commercial Loans	02	1,225.95	-	-	-	-	-	-
Foreign Loans	52	141.15	43	85.58	70	174.14	31	55.22
Government – House & Property Loan	5,563	4,261.45	664	395.33	3,890	2,929.71	690	422.92
House & Property	3,212	3,957.57	3,643	1,904.99	2,160	2,629.48	3,729	2,092.83
House & Property Loan- Mihindu	-	-	07	7.16	-	-	10	9.32
NHD Jana Sewana	-	891.54	-	-	-	-	-	-
Personal Loan on Guarantee	153	116.11	16	10.69	19	13.73	-	-
Personal Loans	10,591	2,410.14	1,223	108.39	5,819	1,215.35	1,160	60.89
Project Loans	01	1,373.13	-	-	02	1,263.90	-	-
Staff Loans	352	351.67	-	-	522	532.86	-	-
University Staff Loans	15	16.23	01	1.00	-	-	-	-
Rata Ithuru Loans	-	-	482	18.70	-	-	-	-
Total	20,005	14,897.28	6,088	2,540.63	12,546	8,839.61	5,626	2,644.63

The following observations are made in this regard,

- (i) The number of loans granted and values thereon had increased by 59 per cent and 69 per cent respectively during the year 2012 as compared with the year 2011. Out of total number of loans

increased 64 per cent, 14 per cent and 22 per cent represented personal loans, house and property loans and government-House & Property Loan respectively.

- (ii) Personal loans on guarantee had significantly increased by 700 per cent as compared with the preceding year.
- (iii) The number of non performing loan accounts on personal loans and personal loan on guarantee had increased during year 2012 as compared with year 2011. However non performing housing loans and property loans had decreased by 2 percent.

2.3.2 Loans of the Retired Staff Officers

The value of the loans recoverable at the time of retirement of officers amounting to Rs. 13,364,811 remained as unrecovered as at 31 December 2012.

2.3.3 Loans of interdicted and vacated Officers

A sum of Rs.9,140,994 recoverable from 40 officers who were interdicted, vacated posts, resigned, dismissed and terminated from service as at 31 December 2012 had been included in the Employees' Loans of Rs.4,026,833,817 shown in the statement of financial position as at 31 December 2012.

2.3.4 Loan granted to the Paddy Marketing Board for stabilization of the Price of Paddy

A sum of Rs.1,225,946,271 had been granted at an annual interest rate of 12 per cent to the Paddy Marketing Board for the paddy purchasing program of the Government in 2012. According to the Memorandum of Understanding, interest should be settled in full prior to 28 February 2013. Nevertheless outstanding loan balance and the interest repayable as at that date amounted to Rs.615,306,010 and Rs.39,272,067 respectively. Further, the amount of loan and the interest recoverable as at 31 December 2012 amounted to Rs.725,945,270 and Rs.26,782,201 respectively.

2.3.5 Project loans granted to construction of a Housing Scheme

Two loans amounting to Rs.50 million and Rs. 30 million had been granted to a private company at an interest rate of 20 per cent during the year 1996. This loan was expected to be fully settled by July 1999. The following observations are made in this regard.

- (i) The entire loan remained as arrears without any installments being paid.

- (ii) The interests paid to the Bank with regard to the above loans as at 06 November 2004 were Rs.8, 524,520 and Rs.1,546,028 respectively.
- (iii) According to the Board paper dated 10 March 2006, the extent of the property acquired was 6 Acres, 3 roods and 21.75 perches. However, according to the relevant valuation reports, and the survey plans, the extent of the property was 6 Acres, 2 Roods and 12.8 perches and accordingly the difference observed was 1 Rood and 8.95 perches.
- (iv) As a result of not recovering the above loan, the loss of interest income caused to the Bank as at 31 December 2004 amounted to Rs.185, 400,000.
- (v) A part of the above property valued at Rs. 184 million had been acquired by Sri Lanka Navy and out of this, Rs.113 million related to the land belonging to the Bank. However, the value obtained by the bank was Rs.70.3 million only. A comparison with the valuer's amount shows that a sum of Rs.42.7 million had not been obtained.
- (vi) It was observed that only a sum of Rs.70.3 million had been obtained for settlement of the loan of Rs.80 million granted without considering the interest outstanding and due to this a loss of Rs.9.7 million had occurred to the bank.
- (vii) Three blocks of the above lands valued at Rs.13.3 million had been acquired by the Government by the Extra Ordinary Gazette No. 1604/ 16 of 2 June 2008. So far, the Government had not paid any amount in this regard.

2.3.6 Pawning Advances

According to the payment of pawning advances by 15 Branches of the Bank, payments amounting to Rs.21,319,372 had been made in 55 instances in respect of the Gold articles in which the ratio of Gold had been excessively shown but subsequently they were found to be at the ratio between 10 to 18 or low at the physical verification.

2.3.7 Properties acquired in lieu of Housing Loans irrecoverable

In view of the inability to recover the balances of loans granted to 09 persons under 11 loan accounts amounting to Rs. 15,403,677, the Bank had acquired the properties relating to those loans. Action had not been taken to auction those properties and settle the loans. The loans relating to 03 loan accounts for which properties had been acquired were Rs.2,053,277. The force sale value realized amounted to Rs.1,400,000 and the loans which exceeded in force sale value realized amounted to Rs.653,277.

3. Operating Review

3.1 Branch Performance

- (a) According to the information made available, the performance of the Bank Branches during the year under review as compared with the preceding year is given below.

	<u>2012</u>	<u>2011</u>
Number of Branches	219	210
Number of Postal Branches	12	-
Number of Post Offices	4053	4058
Number of Account Holders (Mn)	17.4	17.0
Number of ATMs	231	221
School Bank Units	1185	349

Nine new branches had been opened, and 05 post offices had been converted as Branches during the year under review. The number of account holders had increased by 0.40 million and the ATM network had increased from 221 to 231 during the year under review showing a remarkable progress in the operations of the Bank.

3.2 Management Inefficiencies

The following observations are made.

(a) **Other Assets – Advance Account for Misappropriation of Funds**

The misappropriation of funds in 22 Branches of the National Savings Bank amounted to Rs.13,963,717, of that 11 per cent related to periods for over 5 years .The total amount exceeding 01 year had been 94 per cent of the overall amount misappropriated. Further, it was observed that the cashiers' shortages of 05 Branches of the Bank amounted to Rs.1,625,141.

Due to the weaknesses in the internal control of the National Savings Bank, frauds are outside of the conditions for obtaining indemnity from insurance, the other misappropriations amounted to Rs.5,700,258. Payment of indemnity for that had been rejected by the insurer.

(b) **Building Purchased for the Matara Branch**

A land with an extent of 33.44 perches with a building valued at Rs. 120 million situated at Dharmapala Mawatha , Matara had been purchased for maintaining the Matara Branch. But this had not been used for up to 31 December 2012 and it was observed that this had become an idle asset.

According to the decision of the Board of Directors dated 17 November 2009, it had been decided to house the Matara Postal Branch in this building. But, nothing had been done in this regard so far. Had action been taken to establish the Postal Branch, the rental of Rs.1,740,000 paid for the Postal Branch from 30 August 2011 to 31 December 2012, could have been saved by the National Savings Bank.

(c) **Lands purchased by the National Savings Bank for construction of Branches.**

Eventhough, Rs. Rs.161,115,000 had been spent in the years 2008 and 2009 for the designing work of Branches at Bambalapitiya, Negombo and Panadura , constructions had not been commenced even as at 31 December 2012. It was observed that the construction works were at the planning stage as the construction of buildings had not been planned immediately after the purchase of lands.

(d) Payment of Service Charges to the Postmaster General for transactions of the Bank through Post Offices

It was not revealed in audit whether the Bank had identified and implemented a method to pay service charges or to identify a new method to improve the performance of the staff of the post offices so as to further increase the value of deposits.

3.3 Investment in Shares

The following observations are made.

- a) Even though the approval of the Equity Committee had been granted to sell 50,000 shares of a Limited Liability Company on 7 September 2011 at Rs.230 each, 45,500 shares had not been sold.
- b) An estimated loss of Rs.642,188,028 had incurred by the bank as a result of diminution in market value of 74,335,419 of shares in 18 companies during the period of 2011 to 31 December 2012.
- c) The number of shares purchased of a Leasing Finance Company was 142,500 in the year 2011 and the market value as at 31 December 2012 was Rs.4,861,188. The diminution of the value of shares amounted to Rs.3,531,136 and represented 42.08 per cent of the total cost of shares.
- d) The overall cost of investments in shares of 56 quoted companies as at 31 December 2012 amounted to Rs. 8,453,508,446. Of these, a sum of Rs. 2,806,064,502 representing 33.19 per cent had been invested in 3 quoted companies on long term basis. The market value of 51 out of 56 quoted companies had diminished by Rs. 1,925,924,411 during the year 2012 whereas the market value of 5 companies only had improved by Rs. 333,913,787. Accordingly, it was observed that the market value of overall shares invested had diminished by Rs. 1,592,010,624 as at 31 December 2012.
- e) The cost of investment made in the year 2012 in quoted shares of a private Knitting Mill, of which market value had deteriorated in the year 2011 amounted to Rs. 7,216,200. The total investment cost in shares of this Company as at 31 December 2012 amounted to Rs. 21,320,717. The deterioration in value as at 31 December 2012 amounted to Rs. 7,525,652.
- f) No any return from a private Trust Equity Fund investment of Rs. 10,000,000 and an another private Unit Trust investment of Rs.13, 760,593, in the year 2012. The interest paid by the National Savings Bank for fixed deposits ranged from 9 per cent to 11.5 per cent. As such in considering the annual interest paid to customers, the Bank was deprived of a return on Unit trust amounting to Rs.1, 823,106.

Further, the return on an another Unit Trust Investment of Rs.50,000,000 amounted to Rs.3, 961,965 and the return on investment represented 7.92 per cent. In considering the annual interest paid to fixed deposits, the return on Unit Trust investment received had been low.

- g) According to the Investment Policy Statement 7.1.2 (i), the investment value in a company should not exceed more than 10 per cent of the overall investment value (Investment Portfolio). However, this percentage had increased by 15.40 per cent and 12.52 per cent respectively in 2 companies in which the value of investments amounted to Rs.1,301,844,864 and Rs. 1,058,577,120. Also as per 7.1.2 (iii) of the Investment Policy Statement, the investment value of an economic sector should not exceed 30 per cent of the overall investment value. However, that limit was 38.8 per cent in the Banking and Finance sector as at 31December 2012.

3.4 Uneconomic Transactions

The following observations are made;

- (a) The Sri Lanka Navy had acquired the land at Chatham Street purchased by the NSB for constructing a branch of the National Savings Bank on 29 January 2009. The acquisition had been published in the gazette and an inspection for compensation had been carried out on 28 June 2012. The Divisional Secretary had stated that compensation and interest thereon from the date of inspection would be paid on the valuation made by the Department of Valuation. But, the Divisional Secretary had informed that the mortgage of the vendor company had not been settled and the matter will be referred for valuation after the settlement of the mortgage.
- (b) A sum of Rs.35,228,367 had been spent during the period of 2008 to 2012 to build a 18 storied building for the National Savings Bank. This had been shown in the Work- in- progress Account as at 31 December 2012. The expenditure on this had been incurred without considering whether it comes under high security zone.

The Board of Directors had not reviewed the situation as at 31 December 2012 regarding the reconstruction of the building and the expenditure already incurred, had been identified as fruitless expenditure in audit.

3.5 Human Resources Management

Details of the approved and actual cadre of the bank as at 31 December 2012 are shown below.

Grade	Approved cadre	Actual cadre	Vacant Positions	Excess	Contract Basis
Executive Grade	737	583	160	6	4
Supervising Grade	1,173	589	584	-	-
Non staff Grade	1,649	1,421	264	36	475
Minor Staff	163	54	109	-	3
Total	3,722	2,647	1,117	42	482

The approved cadre for the year under review was 3,722 and the Bank had employed 2,647 officers / employees on permanent basis and 482 officers/employees on contract basis during the year 2012. Accordingly, there were 1,055 vacancies and the excess cadre was 462 as at 31 December 2012.

4 Accountability and Good Governance

4.1 Corporate Plan and Action Plan

It was observed that the Bank had not achieved following targets given in the Corporate Plan for 2012.

Indicator	Target	Achievement	Non Achievement
(a) Growth in deposits	14%	8%	6%
(b) Assets Growth	14%	9%	5%
(c) Total Assets(Rs.Bn)	530	510	20
(d) Total Deposits (Rs.Bn)	485	458	27
(e) Growth in interest income	16%	12%	4%
(f) Return on assets(times)	1.7	0.85	0.85
(g) Profit Before Tax (Rs.Bn)	6.4	6.17	0.23
(h) Deposit per employee (Rs.mn)	161	146	15
(i) Profit per employee (Rs.mn)	2.13	1.38	0.75

5. Systems and Controls

Deficiencies observed in systems and controls during the course of audit were brought to the notice of the Chairperson of the Bank by my detailed report issued in terms of Section 13 (7)(a) of the Finance Act. Special attention is needed in respect of the following areas of control.

- (a). Accounting
- (b). Budget
- (c). Loan Administration
- (d). Inventory Control
- (e). Documentation
- (f). Compliance with Laws, Rules and Regulations
- (g). Assets Management
- (h). Opening and Closing of customer accounts