Sri Lanka Land Reclamation and Development Corporation and its Subsidiary - 2013

The audit of consolidated financial statements of the Sri Lanka Land Reclamation and Development Corporation and its Subsidiary for the year ended 31 December 2013 comprising the statements of financial position as at 31 December 2013 and the statements of comprehensive income, statements of changes in equity and cash flow statements for the year then ended and a summary of significant accounting policies and other explanatory 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 Section 13(1) of the Finance Act, No. 38 of 1971 and Section 17(1) of the Land Reclamation and Development Board Act, No. 15 of 1968 as amended by the Sri Lanka Land Reclamation and Development Corporation (Amendment) Act, No. 35 of 2006. The audit of financial statements of the Subsidiary was conducted by a firm of Charted Accountant in public practice appointed by the Members of the respective Subsidiary. 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.

1:2 Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines necessary to enable the preparation of consolidated financial statements that are free from material misstatements whether due to fraud or error.

1:3 Auditors' Responsibility

My responsibility is to express an opinion on these consolidated financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards consistent with International Standards of Supreme Audit Institutions (ISSAI 1000 – 1810). Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Corporation's preparation and fair presentation of the consolidated financial statements 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 Corporation's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Sub – sections (3) and (4) of the 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.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

1:4 Basis for Qualified Audit Opinion

My opinion is qualified based on the matters described in paragraph 2.2 of this report.

2. Financial Statements

2.1 Qualified Opinion - Group

In my opinion, except for the effects of the matters described in paragraph 2:2 of this report, the consolidated financial statements give a true and fair view of the financial position of the Sri Lanka Land Reclamation and Development Corporation and its Subsidiary as at 31 December 2013 and those financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

Qualified Opinion - Corporation

In my opinion, except for the effects of the matters described in paragraph 2:2 of this report, the financial statements give a true and fair view of the financial position of the Sri Lanka Land Reclamation and Development Corporation as at 31 December 2013 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.2. Comments on Financial Statements

2.2.1 Group Financial Statements

The financial statements of the Corporation for the year under review had been amalgamated with the audited financial statements of the Land Reclamation and Development Company (pvt) Limited which is a Subsidiary of the Corporation. The ownership of the Corporation in respect of the Subsidiary represented 80 per cent of the issued share capital of that Subsidiary.

2.2.2 Sri Lanka Accounting Standards (LKAS)

The following observations are made.

(a) LKAS 01 - Presentation of Financial Statements

(i) It was observed in audit that the several items of expenditure had been set off against the income and other sources which were not directly related to the respective expenses and shown in the statement of comprehensive income inappropriately. In this manner, the repairs and maintenance expenses of motor vehicles amounting to Rs. 1,232,948 and selling expenditure amounting to Rs. 25,239,000 had been set off against the insurance claims received and provision for bad and doubt full debt respectively.

(ii) The fixed deposits of the Corporation valued at Rs. 85,872,486 had been secured against the Letters of Credits (LCs) opened by the Corporation during the year under review and this had not been disclosed in the financial statements.

(b) LKAS 02 - Inventories

According to the information made available for audit, the sales of sea sand had been continuously declined during the past few years due to low demand prevailed in the field of constructions. Therefore, the net realizable value of 2,431,922 cubic meter sea sand stock would be much below than the cost of such stock amounting to Rs. 1,975,225,000 shown in the statement of financial position as at 31 December 2013. However, no action had been taken by the Corporation to determine the actual net realizable value of this stock and brought to account accordingly.

(c) LKAS 08 – Accounting Policies, Changes in Accounting Estimates and Errors

The Corporation had changed its accounting policy relating to overhead expenditure as to charge the overhead expenses not only on client contracts but also the Government funded contracts. The impacts thereon to the financial results had not been disclosed adequately in the financial statements even though revenue thereon amounting to Rs. 200,396,000 had been generated during the year under review.

(d) LKAS 16 - Property Plant & Equipment

(i) Action had not been taken to re-value and determine the actual economic life period of the fully depreciated assets such as buildings, machineries and motor vehicles procured at a cost of Rs. 55,569,805, Rs. 492, 344,796 and Rs.79,802,986 respectively which remained in usable condition at the end of the year under review. Therefore, the cost of property, plant and equipment and the depreciation thereon shown in the statement of financial position had been understand by significant amount.

(ii) A balance of Rs. 815,419,000 was continuously brought to the financial statements as “works completed projects” and shown under the current assets without being analyzed the nature of such balances. Therefore, the value of the assets and the depreciation thereon which represents such balance had remained understated.

(e) LKAS 18 - Revenue

Rental income amounting to Rs. 47,836,982 to be recovered from tenants of Sudunelumpura Housing Scheme for over next 28 years and a sum of Rs. 17,508,851 to be recovered from the Subsidiary for over next 30 years relating to the above Housing Scheme had not been disclosed in the financial statements.

(f) LKAS 21 - The effect of Changes in Foreign Exchange Rates

A sum of Euro 575,000 equivalent to Rs. 84,768,000 payable as at 31 December 2013 to a contractor who had assigned the Sea Sand Excavation Project was understated by Rs.18,992,015 due to erroneous currency conversion made on 31 December 2013.

2.2.3 Accounting Deficiencies

The following observations are made.

(a) A land acquired at a cost of Rs. 287,353,000 had been separately accounted under the current assets as an inventory item without being considered its capital nature.

(b) As a practice, the Corporation had written off the total cost of the inventories and other consumable items amounting to Rs. 8,133,000 procured during the year against the income for the year without being ascertained the value of the stocks in hand at the end of the year through Boards of Surveys. It was observed in audit that the inventory and other consumable items procured at a cost of Rs. 1,170,572 had remained in the stores of the Corporation at the end of the year under review even though the cost of such items had been written off against the income of the Corporation.

2.2.4 Accounts Receivable and Payable

The following observations are made.

(a) According to the age analysis, the total debtor balances aggregating Rs. 431,950,843 at the end of the year under review had included the debtor balances of Rs. 29,815,591 remained outstanding for over a period ranging from 2-5 years. Further, there were debtor balances aggregating Rs. 15,208,384 remained outstanding for over 5 years which also included therein.

(b) Out of total sales advances aggregating Rs. 517,471,282 as at 31 December 2013 received by the Corporation from outside parties relating to sales of land, an advance of Rs. 489,683,191 had remained unsettled for over 05 years. Further, the other advances paid aggregating Rs. 1,035,242 had also remained unsettled for over a period ranging from 1-5 years. A sum of Rs. 3,000,000 payable to a related party had also remained unsettled since 2012.

(c) Provision for Royalties payable on proceed of sales of land amounting to Rs. 44,538,761 had been remained in the financial statements since 1999 without being remitted the same to the General Treasury.

(d) A mobilization advance amounting to Rs. 50,000,000 obtained on a construction contract from a private company had remained unsettled for over four years.

(e) A debit balance amounting to Rs. 1,912,544 which remained outstanding for over 4 years had been set off against the balances of creditors on construction contracts.

2.2.5 Lack of Evidence for Audit

The evidence such as passports (certified copies of relevant pages), bills and other details of relating to advances taken for foreign training amounting to Rs 3,259,714 and the amount refunded thereon had not been presented for audit.

2.3 Non-compliance with Laws, Rules and Regulations etc.

The following non-compliances were observed in audit.

	Reference to Laws, Rules and Regulations	Non-compliance
(a)	Section 2 (a) (4) of the Sri Lanka Land Reclamation and Development Corporation (Amendment) Act, No. 35 of 2006.	There were several instances where legal action had not been taken against unauthorized land reclamations.
(b)	Motor Traffic Control Act, No 14 of 1951	
	(i) Section 2(i) of Authority 203	Three electric cars are using for passenger transports at Diyatha Uyana without registering at the Department of Motor Traffic.
	(ii) Section 99	Insurance Coverage even for third parties had not been obtained for the respective electric cars.
(c)	Public Enterprises Circular No. PED/12 of 02 June 2003 (i) Paragraph No. 9.14	Every Corporation should be prepared a Manual of Procedures including a chapter on Human Resources Management in order to provide guidance in settling issues related to Human Resources Management, otherwise the provisions in the Establishments Code could not be adopted. However, Corporation had not taken action accordingly.

(ii) Paragraph 8.3.9	The Corporation had released 05 employees to outside institutions and a sum of Rs. 2,521,873 had been spent during the year under review as salaries and allowances on behalf of them contrary to the Circular instruction. Further, a vehicle owned to the Corporation had been released to the Line Ministry and running cost thereon amounting to Rs. 495,435 had been incurred during the year under review. Action had not been taken to reimburse the costs incurred by the Corporation from the respective Institutions.
(e) Sri Lanka Land Reclamation and Development Corporation's Internal Circular of 05 December 2007	
(i) Paragraph 2.7	Estimates should be presented at the time of requesting advances on procurement of goods and services. However, advances in several instances had been released without such estimates.
(ii) Paragraph 3.1	Penalties of 25 per cent on amount of advances should be imposed if those delayed to settle in time. However, penalties amounting to Rs 1,045,625 had not been imposed on such occasions.

3. Financial Review

3.1 Financial Results

According to the consolidated financial statements presented, the operations of the Group and the Corporation for the year under review had resulted in a pre-tax net profit of Rs. 140,945,000 and Rs. 118,295,000 respectively as compared with corresponding net loss of Rs. 15,933,000 and Rs. 42,527,000 in the preceding year, thus indicating the improvements of Rs. 156,878,000 and Rs. 160,822,000 in the financial results of the group and the Corporation respectively. The receipts of Rs. 78,600,000 from the outside parties as claim for price escalation on sales of sea sand, increase of revenue by Rs. 200,396,000 due to charging the overhead expenses to Treasury Funded Projects and earning a profit of Rs. 27,678,000 from Diyatha Uyana activities had been mainly attributed for this improvement in the financial result for the year under review.

3.2 Analytical Financial Review

3.2.1 Profitability of Commercial Activities

According to the information received, the financial results of several commercial activities engaged by the Corporation during the year under review as compared with the previous year are given below.

Activity	Profit/ (Loss) from the Activity for the year ended 31 December	
	2013	2012
	Rs. 000	Rs. 000
Sales of Land	50,457	89,270
Sales of Sea Sand	(8,865)	134,316
Construction Contracts	23,757	58,395
Consultancy Services	5,532	14,776
Reclamations Works	15,505	9,043
Dredging Activities	13,475	53,649
Miscellaneous Projects	(11,370)	55,771

The following observation is made in this regard

According to the above information the profits of the Corporation from the all activities except the activities relating to reclamations had been declined during the year under review.

3.2.2 Stability of the Corporation

The issues described below had made the significant impacts on future stability of the Corporation.

(a) Incurred the continuous operating loss of Rs. 64,818,000 and Rs. 163,288,000 during the year under review and in the previous year respectively.

(b) Withdrawn of fixed deposits amounting to Rs. 564,861,139 during the year under review from the fixed and call deposit of Rs. 1,190,044,000 as end of the previous year. As such the value of fixed and call deposits of the Corporation as at 31 December 2013 declined to Rs. 626,604,000

(c) Withdrawn of other investments made to meet the compensation payable on lands acquired and against the provision for gratuity aggregating to Rs. 793,045,000 during the year under review even though there was a liability of Rs. 535,231,216 thereon as at December 2013.

3.3 Legal Cases

The following observations are made.

(a) It was observed that 37 legal cases had been raised by the outside parties against the Corporation since pending results. Further, 38 legal cases were raised by the Corporation against the outside parties was also not resolved as at 31 December 2013.

(b) The court orders issued against the encroachers of the lands belonging to the Corporation in several instances had not been implemented.

4. Operating Review

4.1 Performance

The following observations are made.

(a) The Corporation had been vested powers under the Section 2(a) (1) of the Land Reclamation and Development Board Act, No. 15 of 1968 as amended by the Sri Lanka Land Reclamation and Development Corporation (Amendment) Act, No. 35 of 2006 to control and prevent unauthorized land reclamations of the Island. Accordingly, the low the lying marshy, barren or muddy lands in all Provinces in Sri Lanka should be specifically identified by the Corporation and published in the Gazette notifications. However, such lands in the Western and Southern Provinces had only been identified and no action what so ever had been taken by the Corporation to discharge the responsibilities of the Corporation in other provinces of the Island.

(b) According to the Action Plan of the Corporation for the year under review, 10 Projects were expected to be implemented at an estimated cost of Rs. 833,600,000. However, such Projects had not been implemented during the year under review as planned.

(c) The activities of two Projects such as constructing of stoles in Hambantota area and improving of drainage system at Madiwela had been commenced during the year under review and sums of Rs. 11,700,000 and Rs. 2,840,000 had been spent respectively thereon. However, such Projects had been suspended subsequently without proper reasons.

(d) As mentioned in Paragraph 2.2.2 (b) of this report, the demand of the sea sand had been declined dramatically during the previous years. As a result the revenue amounting to Rs. 782,550,000 generated through sales on sea sand during previous year had been dropped up to Rs. 77,674,000 during the year under review. However, prompt action had not been taken by the Corporation to obtain the certifications from experts in respect of usability of sea sand for the construction activities and communicated this with the general public to avoid myths prevail among the general public on the use of sea sand for the construction purposes.

4.2 Financial Controls

The following observations are made.

(a) The financial controls over the special advances granted for procurement of goods and services were not satisfactorily implemented by the Corporation. The instances observed during the course of audit are described below.

(i) The Corporation had granted the special advances aggregating Rs. 11,468,867 in 512 occasions and out of that, the entire advances had been refunded in 03 occasions without being utilized for the intended purposes. Further, in 14 occasions, the refunded amounts were Rs. 10,000 or above. It indicated that the proper estimations had not been done at the initial stages of granting advances and allows rooms for misuse of public funds.

(ii) In addition to the above, the expenditure ranging from Rs. 20,000 to Rs. 80,000 incurred by the procuring officers in 19 occasions out of their personal funds due to inadequacy of advances obtained had been reimbursed by the corporation.

(b) Even though the provision for Gratuity amounting to Rs. 206,880,216 had been made in the financial statements, a separate investment had not been made thereon.

4.3 Contract Administration

The following observations are made.

(a) The Corporation had entered into an agreement with an investor in private sector on 27 June 2007 to develop a housing scheme in the land belonging to the Corporation and sell them to the general public. An advance of Rs. 489,683,191 had been obtained thereon by the Corporation. However, the investor had not commenced the works as agreed, even after laps of 07 year since the date of the agreement. Further, the Corporation had faced with a risk on cancellation of the agreement and vest the rights of the land, as the Corporation had agreed to pay the advance back within 14 days of the cancellation of the agreement. Therefore, the land with a significant commercial value had remained idle for over 07 years without taking action either to cancel the agreement or enforcing the investor to commence the development activities by revalidating the agreement.

(b) The Corporation had not followed the instructions issued by the Public Sector Information Communication Technology Agency on procuring of intranet system at a cost of Rs. 5,160,183. Therefore, the supplier who quoted third higher price had been selected. Even though the supplier had provided five year guarantee for the system, the viability of the business operations of the supplier was in doubt due to continuous losses incurred in previous years. Further, according to the liquidity ratios of the supplier it was observed that he had been faced with severe working capital difficulties. In addition to that, a sum of Rs. 610,612 (including taxes) had been spent to procure a security software from the same supplier due to failure to identify the need of such security system for intranet facilities at the initial stage.

(c) The Corporation had procured solar power generating systems for the four Island areas at Diyatha Uyana at a cost of Rs. 11,863,600 on 24 August 2013. The evidence which based for the determination of actual requirement of the solar power units had not been rendered for audit. Later these systems had been rejected by the Corporation due to poor performance. The supplier had refunded only a sum of Rs. 7,944,375 on 17 July 2014. In this ground the Corporation had retendered and awarded the contract at a cost of Rs. 17,478,400 to another party on 31 December 2013 without being followed the procurement procedure.

(d) The contract for erecting of water fountain at Diyatha Uyana had been awarded to Sri Lanka Army at a cost of Rs. 16,950,000 without considering the bids submitted by other parties. However, Sri Lanka Army had outsourced the works to a private party without obtaining the concurrence of the Corporation. Further, the works had been commenced without approving the work design and the respective design had been approved by the Corporation at the time of making first interim payment.

4.4 Fruitless Transaction

It was observed that the taxes overpaid during the year 2013 amounting Rs. 15,349,908 had remained outstanding as at 31 December 2013 without being recovered

4.5 Matters of Contentious Nature

The following observations are made.

(a) The Corporation had procured three electric cars at a cost of Rs. 11,245,000 from a private company which is not a registered vehicle importer, without following procurement procedures. However, according to the information made available, the total cost of the cars including CIF value and local taxes was Rs. 4,765,096. Therefore the gross profit margin of the supplier was Rs. 6,479,905. Further, it was revealed that chassis numbers of the cars had not been agreed with the respective numbers mentioned in the document furnished to audit.

(b) Un-utilized Treasury grants aggregating Rs. 722,769,000 received for implementing the Grater Colombo Flood Control and Environment Improvement Project, Kalu Oya Project at Ragama and Mayurapura and a Project at Hambantota had remained in the accounts of the Corporation over several years without being taken prompt action to refund such balances to the General Treasury.

(c) It was observed in several instances that the Corporation was not adhered with the rules and regulation stipulated in the respective Acts and Circulars etc., in calculating the contributions required to be remitted to the Employees Provident Fund and Employees Trust Fund, as such the possibility for making additional payments and interest thereon could not be ruled out in audit.

(d) The compensation and interest on lands acquired for development purposes in terms of Section 38(a) of Land Acquisition Act, No. 09 of 1950 amounting to Rs. 287,214,101 had remained outstanding as at 31 December 2013 since 1979.

(e) According to the financial statements, a sum of Rs. 77,706 had been shown as receivable from a Subsidiary known as Water Front Development Company since 2012. However, it was observed that there is no any company in operation on such name at present.

(f) The Corporation had earned an income of Rs. 37,815,000 by way of rent out the premises at Diyatha Uyana during the year under review. However, the properties at Diyatha Uyana could not be recognized as revenue generating assets due to the legal ownership of the respective land had not vested to the Corporation.

4.6 Apparent Fraudulent Transactions

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The following observations are made.

(a) It was observed that a heavy vehicle driver had misappropriated the funds amounting to Rs. 34,620 by way of submitting foraged bills during the year under review. Further, unauthorized disposal of vehicle spare parts and other accessories had been observed in 5 occasions.

(b) The Corporation had offered a contract to a contractor for transport the soil at a cost of Rs. 6,000,000 who was the only one bidder responded for the contract. However, this transaction was apparently fraudulent nature as the selected supplier had submitted the bid documents prior to calling the bids.

4.7 Idle or Underutilized Assets

It was revealed that the stock items in various categories valued at Rs. 89,114,981 had remained in slow moving and out of that, some of the stock items valued at Rs.33,681,466 had remained in stories for over 05 years.

4.8 Identified losses

An investment of Rs. 2,000,000 made in the share capital of an Associated Company which responded 14 per cent of the issued share capital of that Company had not generated any financial return up to end of the year under review, as the respective Company was remained under liquidation and a provision for write off this investment had been made in the financial statements.

4.9 Human Resources Management

Even though the approved cadre of the Corporation as at 31 December 2013 was comprised with 1,525 officers, the actual cadre was only 1,317, thus indicating that the Corporation had not taken necessary stapes to fill 208 vacancies excised by 31 December 2013. Further, 45 posts in senior management levels were remained vacant as at that date. In the meantime, the employees of the Subsidiary had been deployed in the activities of the Corporation on temporary basis during the year under review and incentives amounting to Rs. 793,689 had been paid directly to them.

5. Accountability and Good Governance

5.1 Corporate Plan

The Corporation is entrusted to identify the low lying marshy, barren or muddy lands in Island wide and published in gazette notifications as enable to control and monitoring of unauthorized land reclamations, However, the activities to be carry out under the respective tasks had not been included either in the Corporate Plan 2013 - 2017 or in the Action Plan for 2013.

5.2 Action Plan

It was observed that the activities to be carried out under 78 Projects including 10 Project commenced in 2012 had not been included in the Action Plan for the year under review, thus indicating that the activities to be carried out in annual basis had not been recognized fruitfully through the Action Plans.

5.3 Procurement Plan

The progress of the activities identified under the Procurement Plan had not been prepared for the year under review in terms of National Budget Circular No 128 of 24 March 2006 as enable to effectively control and monitor the financial and other resources of the Corporation.

5.4 Internal Control

Even though the internal audit should be used as an important tool for providing the guidance needed by the management on the areas which should be rectified, proper attention had not been paid by the Corporation as a large scale construction contractor to empower the internal audit staff along with the expansion of the activities of the Corporation to achieve the meaningful results.

5.5 Budgetary Control

Significant variances were observed between the estimated and actual revenue and expenditure in respect revenue on dredging, sale of sea sand, consultancy services and fines and expenditure on dredging and sundries etc. thus indicating that the budget had not been made use of as an effective instrument of management control.

5.6 Unresolved Matters pointed out in Previous Audit Reports

The following issues raised in the previous audit reports had remained unresolved even at the end of the year under review.

(a) The Corporation continues the payment of professional allowances to the staff without being obtained the approvals from relevant parties.

(b) The interest on vehicle loans is reimbursed to the respective officers of the Corporation continuously.

(c) The Committee on Public Enterprises had made a direction at its meeting held on 31 November 2012 to take prompt legal action against the party who build a Kovil in a land with extent of 3.5 acre which was developed by the Corporation at a cost of Rs.30.2 million with the assistance of the Divisional Secretary of the area. However, no action what so ever had been initiated by the Corporation to implement the direction.

5.7 Discharge the Environmental and Social Responsibilities

The unauthorized land reclamations prevailing in island wide had created many environmental and social issues and these will be attested to the future generations as well. However, the Corporation had not used the powers entrusted to it for educate the people and avoid such unauthorized land reclamations.

6. Systems and Controls

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

(a) Procurements
(b) Payment of Compensations
(c) Accounting
(d) Settlement of Advances