

Lanka Sathosa Limited - 2014

The audit of the financial statements of Lanka Sathosa Limited for the year ended 31 December 2014 comprising the statement of financial position as at 31 December 2014 and the statement of changes in equity and cash flow statement 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. My observations relating to the operation of the Company in the year under review which I consider should be furnished to the Parliament in terms of Article 154(6) of the Democratic Socialist Republic of Sri Lanka appear in this report. A Firm of Chartered Accountants in public practice assisted me in carrying out this audit.

1.2 Board of Directors' Responsibility for the Financial Statements

The Board of Directors ("Board") is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Auditing Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

1.3 Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. However, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion due to the matters described in the Paragraph, Basis for Disclaimer of Opinion.

1.4 Basis for Disclaimer of Opinion

(a) Property, Plant and Equipment

It could not be satisfied in the audit relating to the completeness, existence and the accuracy of the Property, Plant and Equipment due to not having a complete Register relating to Property, Plant and Equipment. Unidentified and non-reconciled values of assets included in some opening balances, in the Register.

(b) Work in Progress and Project Advances

(i) Kilinochchi Mega Project- Rs.255,223,652

The Sathosa Supermarket Complex of Kilinochchi had been constructed in a land belonging to the Government of Sri Lanka under the project. The ownership of this land had not been entrusted to the Lanka Sathosa Limited even by the date of the Audit Report. Moreover, the construction functions of the project had been entrusted to the Cooperative Wholesale Establishment, deviating from the procurement procedure.

(ii) Welisara Project- Rs.97,222,803

The deed of the land had not been furnished to confirm the ownership of the land. The construction functions had been entrusted to the Cooperative Wholesale Establishment, deviating from the procurement procedure.

(c) Stocks of Goods

It could not be satisfied relating to the amount of stocks remaining as at 31 December 2014 in the financial statements as at 31 December 2014 on the Bin Card Method or any other alternative method not being implemented for the Trade Centres of the Company operating, deviating from the computer system.

(d) Trade and Other Receivable Balances

(i) Control of the Credit Memo

It could not be satisfied relating to the accuracy, existence and the completeness of the Credit Memo Balance amounting to Rs.193,048,673 on not furnishing the age analysis and the events after the Balance Sheet date with the relevant Schedules.

(ii) Balance Receivable from the Ministry of Sports- Rs.36,453,533

Confirmations were not furnished for this receivable balance. It could not be satisfied on the ability of recovering this balance on not having events or confirmations since the date of the Balance Sheet. Moreover, the Company had not made Bad Debt Provisions relating to those balances.

(iii) Lease Rent Advances

It could not be satisfied relating to the accuracy, completeness and the existence of the Lease Rent Advance Balance amounting to Rs.139,119,000 on not furnishing the completed Schedules and Confirmations to audit.

(e) Trade Creditors and Other Payable Balances

Sufficient appropriate audit evidence could not be obtained due to the following positions for the confirmation of the accuracy, completeness and the existence of the Trade Creditors and Other Payable Balance.

(i) Trade and Other Creditors

It could not be satisfied relating to the accuracy, completeness and the existence of the Trade Creditors and Other Creditors Balance due to not furnishing the Schedules, age analysis and Confirmations of Balances relating to the Trade Creditors and Other Creditors Balance totalling Rs.2,367,614,606.

(ii) **Unidentified Credit Balance- Rs.14,368,296**

Details had not been received for the verification of the above Unidentified Loan Balance.

2. Financial Statements

2.1 Disclaimer of Opinion

Because of the significance of the matters described in paragraph Basis for Disclaimer of Opinion of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

2.2 Report on Other Legal and Regulatory Requirements

I state the following matters as prescribed by Section 163(2) of the Companies Act, No.07 of 2007.

- (a) Basis for Opinion and the limitations of the scope are as given above.
- (b) I do not express an opinion on these financial statements on not have been able to obtain all the information and explanations necessary for audit, as given above.

2.3 Non- compliance with Laws, Rules, Regulations and Management Decisions

Even though the Monthly Bank Reconciliation Statements should be prepared by the 15th of the forthcoming month as per the Financial Regulation 395(d) of the Democratic Socialist Republic of Sri Lanka, Bank Reconciliation Statements relating to 05 Bank Accounts had not been prepared as at the due date.

2.4 Unexplained Differences

A difference totalling Rs.152,451 between the balances of two Bank Accounts including the financial statements in the year under review and the balances mentioned in the relevant Bank Reconciliation Statements. In addition, a difference of Rs.5,319 remained between the Bank Reconciliation Statement prepared as a procedure of internal control relating to the Savings Account maintained with the objective of depositing sales money of the sales outlets, by the Company and the balance mentioned in the financial statements.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the financial result of the Company had resulted in a deficit of Rs.1,722,947,369 as compared with the corresponding surplus of Rs.1,156,456,272 for the preceding year, this indicating a deterioration of Rs.2,879,403,641 or 248.9 per cent in the financial result in the year under review as compared with the preceding year. Selling imported rice at a concessional price as per the policy decisions of the Government and the increase of administrative

expenditure and the distribution expenditure by 35.6 per cent and 28 per cent respectively, as compared with the year under review had been the main reason for this deterioration.

In analyzing financial results in the year under review and of 04 preceding years, the net profit of the Company amounting to Rs.37,867,416 in the year 2010 had been a amounting to Rs.1,722,947,369 with fluctuations in the year 2014. However, in adjusting personnel emoluments, taxes paid to the Government and depreciation to the financial results again, even though the positive contribution amounting to Rs.727,700,314 in the year 2010 had been a sum of Rs.2,416,461,468 in the year 2013 by continuously increasing, it had been a negative contribution amounting to Rs.172,791,952 in the year 2014.

3.2 Analytical Financial Review

According to the financial statements presented, in considering the profit ability ratio of the Company, the gross profit ratio which remained at 13.59 per cent in the year 2013 had decreased to 4.28 per cent in the year 2014 and the net profit ratio which remained at 4.61 per cent in the year 2013 had been a minus value of 5.75 per cent by the year 2014. In considering the liquidated ratio, even though the current ratio remained at a value of 1.36 in the year 2013, it had been a low value of 0.95 by the year 2014.

4. Operating Review

4.1 Performance

The objectives of the Company in terms of the Articles of the Association are given below.

- Maintaining an enterprise for the sale of essential goods and other consumer goods, furnishing for the sale and for the distribution.
- Certifying that there is an ability to purchase essential consumer goods through the Retail Stores of the Company to the consumers at an affordable price.
- The initiation of the import and export enterprise as Stock and Retail Sales Representatives and as Traders of the consumer and other types of goods, its establishment and management. It should be restricted only to the goods not for sale in the Cooperative Wholesale Establishment in the necessary instance, relating thereto.
- Maintaining an enterprise for the purchase, collection, subjecting to the process, storing, packaging, distribution, sale and maintaining a supply entity of agricultural products, consumer and other types of goods. It should be restricted only to the goods not for sale in the Cooperative Wholesale Establishment in the necessary instance, relating thereto.
- The establishment of storage and sales facilities by methods such as outright purchase lease or rent and obtaining storage, sales, storage space and facilities by methods such as sale, lease, rent.
- The supply of the skilled and unskilled labourers and other human resources, to the enterprise and to other private entrepreneurs by agreements.

- The supply of any service to the consumers.
- Confirming the existence of the self- competent enterprise by participating in the business activities permitted by this enterprise excluding the carrying out of the retail sale of the essential consumer goods, this enterprise could be carried out by providing a service to consumers by the Company.

The following observation is made relating to the performance of the Company.

The attention had not been paid by the Management to achieve the objective of supplying skilled and unskilled labourers and other human resources to the enterprise and other private entrepreneurs by agreements, out of the objectives of the Company.

4.2 Management Activities

It had lapsed over 3 months to 6 months to settle a sum of Rs.57,708,419 and it had lapsed over 8 months to 13 months to settle a sum of Rs.35,147,645 out of the Advance amounting to Rs.123,856,064 paid in the year under review to a Clearance Institution by the Company for the imported rice clearance activities and the attention of the Management had not been paid to settle the Advances without a delay.

4.3 Personnel Administration

Even though the Approved Cadre of the Company had been 3075, the Actual; Cadre as at 31 December 2014 had been 3248 and the following observations are made in this connection.

- (a) The Organizational Structure of the Institution had not been prepared and had not been approved, in accordance with the Approved Cadre in terms of Chapter 9.2 of the Public Enterprises Circular No.PED/12 of 02 June 2003. Moreover, a Scheme of Recruitment had not been approved by the Company in terms of the Chapter 9.3 of the above Circular. As such, recruitments of the staff had not been carried out properly and a staff of 323 employees had been recruited relating to the Primary Level of the sales outlets of the Company.
- (b) Recruitments had been made on contract basis for the posts of the Chief Executive Officer and Deputy General Manager, which belong to the Upper Management of the Institution since the initialization of the Company and as such, a high employee turn- over remained relating to the Upper Management Level of the Company.

5. Accountability and Good Governance

5.1 Establishment of the Institution

This Company had been established on 26 October 2005 under the Companies Act, No.17 of 1982 and had been re- registered on 19 March 2010 under the Companies Act, No.07 of 2007.

5.2 Presentation of Fanatical Statements

Even though the Annual Financial Statements and the Draft Annual Report should be furnished to the Auditor General within 60 days after the end of the Financial Year in terms of the Public Enterprises Circular No.PED/12 of 02 June 2003, the financial statements of the year under review had been furnished on 12 July 2017 after a delay of 2 years and 4 months and the Draft Annual Report had not been furnished.

5.3 Procurement and Contract Process

The following observations are made.

(a) Importing Rice

Thirty- thousand three- hundred and two metric tonnes of rice had been imported by spending a sum of Rs.1,914 million in the year under review by the Company and the following observations are made in this connection

- (i) The stock of rice had been imported on the instructions of the Chairman without the approval of the Board of Directors.
- (ii) Eighteen- thousand one hundred and thirty- four metric tonnes of imported rice valued at Rs.1,199 million had been purchased under various prices from selected local suppliers deviating from the procurement process, without paying attention to the rice importing process, despite the rice importing progress was in progress, in the year 2014.
- (iii) Even though a proper agreement should be entered into, relating to the procurements exceeding a sum of Rs.500,000 in terms of the Guideline 8.9.1(b) of the Government Procurement Guidelines, agreements had not been entered into with the suppliers by the company in purchasing rice, as mentioned above.

(b) Building Rent

The number of buildings obtained on lease rent basis as at 31 December 2014 for the maintenance of the sales activities by the Company had been 314 and the rent expenditure as at that date according to the financial statements had been a sum of Rs.317,469,400. The following matters were revealed in the audit test check carried out in this connection.

- (i) The Government Procurement Guidelines had not been followed in selecting these suppliers of the buildings.
- (ii) Specifications had not been prepared by the Company relating to the quality that should be maintained in the buildings which, the sales outlets are established.
- (iii) Even though the documents which confirm the ownership of the lessee should be obtained by the lessor according to the conditions of the Lease Rent Agreement, the documents that confirm the lessor's ownership relating to the majority of the sales outlets had not been obtained by the Institution.
- (iv) Even though it had been stated in the agreements that the agreements should be renewed 3 months prior to the end of the term of the remaining agreement in the instance where the remaining in entering into new agreements after exceeding the contract period in the majority of the sales outlets .

- (v) Sales outlets are being maintained without entering into agreements in 18 buildings belonging to various Government Institutions and information relating to the rent paid to those Institutions relating to the year 2014 had not been furnished to the audit. In addition, a sum of Rs.795,000 had been paid as rent in the year under review without entering into agreements for two buildings obtained from the private sector.
- (vi) Even though the period of entering into agreements for the buildings should not be more than 03 years in terms of the Financial Regulation 835(2)(e), agreements had not been entered into for the periods from 5 years to 10 years by the Institution.
- (vii) The accuracy of the lease rent payments could not be examined owing to the agreements were misplaced in connection with 10 sales outlets of which a total sum of Rs.6,892,300 had been paid in the year under review.
- (viii) A total sum of Rs.636,000 had been paid to an external party as rent in the year under review, a sum of Rs.53,000 for each month, without an approval instead of the rent amounting to Rs.48,000 as per the Sheet including the details of the building, recommended by the Chief Engineer and being approved by the Chairman for a building obtained for rent for the maintenance of the Ratmalana- 02 sales outlet without confirming the ownership of the building and without entering into a proper agreement. As such, a sum of Rs.60,000 had been overpaid.

(c) Making payments for Rented Vehicles

A sum of Rs.18,081,747 had been paid in the year under review for obtaining transport services from a selected Institution which supplies vehicles for rent, deviating from the procurement procedure.

5.4 Procurement Plan

A Procurement Plan for the year under review had not been prepared in terms of the Guideline 4.2 of the Government Procurement Guidelines.

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 Company from time to time. Special attention is needed in respect of the following areas of control.

Areas of Systems and Controls -----	Observations -----
(a) Procurement Process	Not following the Guidelines of the Government Procurement Guidelines in procurement activities.
(b) Financial Control	Not preparing the Bank Reconciliation Statement accurately and on the due date.
(c) Control of Human Resources	Not having an approved Scheme of Recruitment and making recruitments and promotions improperly.
(d) Stocks Control	Not maintaining the Stocks Reports accurately.
(e) Control of Assets	Not accurately maintaining the Reports on Fixed Assets.
(f) Control of Contracts	Carrying out constructions in the lands of which the ownership had not been vested.

