Telecommunications Regulatory Commission - 2014

The audit of financial statements of the Telecommunications Regulatory Commission of Sri Lanka for the year 2014 comprising the statement of financial position as at 31 December 2014 and the statement of financial profit or loss and other comprehensive income, 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 read in conjunction with Section 13(1) of the Finance Act,No.38 of 1971 and Section 22(a)(2) of the Sri Lanka Telecommunications Act, No. 25 of 1991 as amended by the Telecommunications (Amendment) Act, No. 27 of 1996. My comments and observations which I consider should be published with the Annual Report of the Commission 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 financial statements in accordance with Sri Lanka Accounting 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 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 financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Commission's preparation and fair presentation of the 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 Commission'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 financial statements. Sub-sections (3) and (4) of Section 13 of the Finance Act, No. 38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

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 Opinion

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

2. Financial Statements

2.1 Qualified Opinion

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 Telecommunications Regulatory Commission of Sri Lanka as at 31 December 2014 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 Sri Lanka Accounting Standards

Non-compliance with the following Sri Lanka Accounting Standards were observed during the course of audit.

Reference to Sri Lanka Accounting Standards	Non-compliance
(a) Accounting Standard No. 1	Even though an institution should show its expenditure either according to the nature of the expenditure or as they relate to the activities of the institution, a sum of Rs.930.8 million spent by the Commission on activities extraneous to the activities of the Commission had been shown as Regulatory Expenses in the financial statements. That expenditure represented 92 per cent of the regulatory expenditure of the year under review. The Chairman of the Commission informed me on 19 June 2015 that from the inception of the Commission, expenditure incurred on Corporate Social Responsibility had been shown as regulatory expenses, that it cannot be shown as an administrative expenditure as it is not an administration expenditure and that it was shown in the financial statements as regulatory expenses as the Commission in its role as the regulator of the Telecommunications in Sri Lanka, it can introduce Corporate Social Responsibility as an expenditure related to Good Governance.
(b) Accounting Standard No. 8	A sum of Rs.195 million identified as a rectification of errors had been shown as a deduction from the expenditure of the year under review without making a retrospective adjustment to the comparative information.
(c) Accounting Standard 16	(i) Even though the depreciation of property, plant and equipment should commence from the date on which they are made fit for use, the Commission had adopted an accounting policy of not depreciating during the full year of purchase and during the year of disposal. (ii) Out of the land 112 Acres 01 Rood 10.5 perches owned by the Commission, an extent of about 50

per cent had been acquired by the Divisional Secretary, Katana and the value of the entire land amounting to Rs.45 million had been shown under property, plant and equipment. Even though action should have been taken to revalue the assets and disclose at fair value in the financial statements, this had been shown only as a note to the financial statements during the preceding 12 years.

(iii) Disclosure had not been made in the financial statements, in connection with fixed assets costing Rs.445.7 million fully depreciated as at 31 December of the year under review, had being used for operations.

(d) Accounting Standard 18

(i) As the Operator Licences are renewed once every 10 years or 5 years, in the renewal of licence fees, the fees recovered in the year of renewal had been recognized as income of the year of renewal. But the related accounting policy had not been disclosed in the financial statements. As such the Operator Licence Fees which amounted to Rs.2,060 million in the preceding year had varied down to Rs.261 million during the year under review.

(ii) The accounting policy on the recognition of income from the sale of Frequency Upfront had not been disclosed in the financial statements.

(iii) The amount exchanged with the operators out of the recoveries made under International Telecommunication Operator Fees, had not been shown in the financial statements as an expenditure (refunded). Instead the net sum collected amounting to Rs. 5,493 million only had been recognized as the income in the financial statements.

(e) Accounting Standard 23

Out of loan of U.S.$ 88.655 million obtained in the year 2012 for the Lotus Tower Project a sum of U.S.$. 34.98 million had been spent up to the end of the year under review. Even though a borrowing cost of Rs.1,413 million had been incurred on this loan up to the end of the year under review, the eligible account of borrowing cost capitalized in terms of this Standard and the ratio of capitalizing had not been disclosed in the financial statements.

2.2.2 Accounting Deficiencies

The Frequency Licence Fee income for the year under review had been overstated in the financial statements by a sum of Rs.113 million as invoices valued at Rs.113,052,702 had been issued in respect of the preceding year during the year under review.

2.3 Accounts Receivable and Payable

The following observations are made.

(a) Out of the debtors of the Commission as at the end of the year under review, a sum of Rs.355 million had been classified as debtors older than 2 years. Nevertheless, that balance included debtor balances remaining recoverable over periods exceeding 20 years.

(b) A sum of Rs.116 million remained recoverable from the Sri Lanka Broadcasting Corporation as at 31 December of the year under review and 08 Frequencies had not been invoiced by December of the year under review.

(c) The employees debtor balance remaining without being recovered over a period exceeding 02 years amounted to Rs.2 million.

(d) Action had not been taken since June 2011 for the recovery of a sum of Rs.71.6 million being the cost of electricity bills and fuel for the electricity generators recoverable from the operators using the Kokavil Antenna and Transmission Tower.

(e) According to the list of debtors balances, the number of debtors with negative balances amounting to Rs.999,418 had been 248 and those had been shown in the accounts continuously over a long period without taking action for the write off of the negative balance.

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

Non-compliances with the following laws, rules, regulations, etc., were observed during the course of audit.

Reference to Laws, Rules, Regulations and Management Decisions	Non-compliance
(a) Section 11 of the Finance Act, No. 38 of 1971 and the Public Finance Circular No. PF/PE/09 of 27 June 2000	The Commission had invested a sum of Rs.14,700 million in fixed deposits in a Bank and Treasury Bills without the approval of the Treasury and the Commission had invested US$ 420,000 in a Savings Bank Account in the year 2003.
(b) Public Enterprises Circular No.PE 56 of 27 January 2011	Even though the funds exceeding the capital requirements for 06 months of the Commission should be remitted to the Consolidated Fund, the Commission had not taken action accordingly.

(c)	Public Contract Agreements Act, No. 3 of 1987	
	(i) Section 6(1)(a)	Whenever the cost of contract agreements exceeds Rs.5,000,000 every bidder should register with the Registrar of Public Contracts. Nevertheless, action had not been taken to ensure whether all the bidders for the construction of the Telecommunications Media Centre at the Hambanthota Information Technology Park, costing Rs.2,494 million had been bidders so registered.
	(ii) Section 12	Even though the Procurement Committee and the Technical Evaluation Committee should ensure that the bidders are in possession of valid registration certificates, it had not been so done.
(d)	Establishments Code of the Democratic Socialist Republic of Sri Lanka	
	(i) Section 2.3 of Chapter II	Even though a Scheme of Recruitment of officers and employees of the Commission prepared and approved by the Commission had been used, the approval of the Director General of Establishments had not been obtained for that. The Chairman of the Commission informed me on 19 June 2015 that the Commission had approved the Scheme of Recruitment in accordance with the powers vested in the Commission in terms of Section 22(c)(2) of Sri Lanka Telecommunications Act, No. 25 of 1991 as amended by the Telecommunications (Amendment) Act, No. 27 of 1996.
	(ii) Sections 12.5.4 and 12.6.1 of Chapter VII	When an acting appointment is made, only 25 per cent of the salary of the acting post can be made. Nevertheless, two officers of the Commission appointed to act in posts had been paid 50 per cent of the salary of the acting post. The overpayment of 50 per cent allowance made from September 2013 to December 2014 amounted to Rs.460,000. The Chairman of the Commission informed me on 19 June 2015 that the payments were made in accordance with the Establishments Code approved by the Commission in terms of the above Section.
	(iii) Section 7.2.5 of Chapter XXIV	Even though a motor vehicle loan can be obtained only once in 05 years, a Translator who had obtained a motor vehicle loan in May 2006 had settled that loan in June 2010 and obtained a further motor vehicle loan of Rs.1 million in the same year.

		Subsequently on 05 February 2014 the loan balance had been settled and another loan of Rs.2.7 million had been obtained on 12 March 2014. The Chairman of the Commission informed me on 19 June 2015 that such motor vehicle loans were paid in terms of circular No. TRC/04/2012 of 14 August 2012.
(e)	Financial Regulation 757(2) of the Democratic Socialist Republic of Sri Lanka	The Commission had not conducted a Board of Survey for the year under review and furnished reports to the Auditor General.
(f)	Circular No. 15/2007 dated 12 June 2007 of the Ministry of Public Administration and Home Affairs	Even though instructions had been issued that motor vehicle loans should be granted though Commercial Banks, the Commission had paid motor vehicle loans amounting to Rs.64 million from the funds of the Commission to 35 officers during the year under review based on the Circular No. TRC/04/12 of 14 August 2013.
(g)	Paragraph 2.2 (b) of the Public Administration Circular No. 15/2007 of 12 June 2007 and Sub-section 7.4.1 of Chapter XXIV of the Establishments Code	Interest at the rate of 4.2 per cent per year only had been recovered in terms of the above circular without making enquiries from the General Treasury on the interest that should be charged on motor vehicle loans.
(h)	Public Enterprises Circular No. PED/27 of 27 January 2005	The draft Annual Report had not been furnished along with the annual accounts.
(i)	Circulars of Ministry of Finance and Planning	
	(i) Paragraph 6 of the Circular No. 012010/01 of 11 October 2010	Combined Allowance at US$ 400 per day had been paid to 15 officers in Category II who had attended a Programme held in Korea from 19 October to 08 November 2014 considering them as belonging to Category I. As the Combined Allowance payable amounts to US$ 320, the overpayment made amounted to Rs.1.9 million.
	Section 6(v)	Where the payment of allowances for foreign travel exceeds 15 days, the approval of the Deputy Secretary to the Treasury should be obtained and such approval had not been obtained. Combined Allowance and Incidental Allowance amounting to Rs.870,844 had been paid to three officers at the rate of 6 days per officer without obtaining such approval.

	(ii) Paragraph 04 of Circular No. BD/CPB/1/1/2012 of 30 December 2011	Even though the maximum amount payable per officer as distress loan has been limited to Rs.250,000, a sum of Rs.9 million exceeding such limit had been paid to 39 officers in accordance with the Circular No. TRC/2012.
(j)	Letter No. PRE/2015/43 dated 22 November 2014 of the Commissioner of Elections	According to the Circular, any recruitment, appointment, promotions and transfer other than recruitments appointments, promotions and transfers duly made under the powers of the Public Service Commission and the Judicial Commission should not be made, from 21 November 2014, the date on which nominations were called for the Presidential Election 2015 and up to holding the election and declaration of results contrary to that, the Authority had conferred permanent status with effect from 01 January 2015 to 15 officers who had been recruited on contract basis.
(k)	Treasury Circular No. IAI/2002/02 of 28 November 2002	A separate Register of Fixed Assets had not been maintained for computers, accessories and software.

2.5 Transactions not supported by Adequate Authority

The following observations are made.

(a) Attendance allowance, bonus, communication allowance and rent allowance amounting to Rs.39 million had been paid based on the decision of the Commission without obtaining the approval of the Treasury.

(b) Even though a monthly transport allowance of Rs.2,000 had been approved for the non-staff grade employees by the letter No. NSCC/3/ABC/24 dated 01 June 2007 of the National Salaries and Cadre Commission, a transport allowance of Rs.6,000 per month which exceeded the approved allowance had been paid. As such, the payments made exceeding the authority during the year under review amounted to Rs.17 million.

(c) According to the Inland Revenue Act, No. 10 of 2006 and the subsequent amendments thereto, the Pay As You Earn Tax should be recovered from the salary of the officers and remitted to the Department of Inland Revenue. Nevertheless, Pay As You Earn Tax totaling Rs.6,782,889 had been remitted to the Department of Inland Revenue from the funds of the Commission without making recoveries from the officers.

(d) A sum of Rs.455,000 per officer had been paid to 05 officers of the Commission for work done in connection with the Lotus Tower Projects contrary to the Management Services Circular No. 33 of 05 April 2007 and without obtaining the approval of the Cabinet of Ministers. Such payments made up to 31 December of the year under review amounted to Rs.10.9 million.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the pre-tax profit of the Commission for the year under review amounted to Rs.46,266 million as compared with the corresponding pre-tax net profit of Rs.47,367 million in the preceding financial year, thus indicating a deterioration Rs.1,101 million in the financial results of the year under review as compared with the preceding year. The decrease of the fees received on the Operator Licences and the auction of frequencies by Rs.7,459 million had been the main reasons for the deterioration.

3.2 Legal Action instituted against the Commission

External institutions, external individuals and the employees of the Commission had filed 13 cases in Courts against the Commission. Two external institutions had claimed compensation of Rs.47,346 million on account of non-operating of the Frequency Project and breach of contract agreement.

4. Operating Review

4.1 Implementation of the Telecommunications Networks

The following observations are made.

(a) Even though ensuring the proper functioning of the Telecommunications Networks of Sri Lanka in different provinces is one of the objectives of the Telecommunication Regulatory Commission, it was observed that various obstructions occur in the use of Frequencies. The Telecommunications Regulatory Commission of Sri Lanka had received 27 complaints from the Frequency operators and other individuals during the year under review on the obstructions that occurred in the use of Frequencies in corroborating the existence of such situation. The signal observation system of the Telecommunications Regulatory Commission is over 17 years old and as such the Chairman of the Commission informed me on 19 June 2015 that difficulties were experienced in the observation of the new radio waves.

(b) An audit test check of a sample of 166 institutions for which Frequencies had been given, revealed that action on files of 58 institutions or 35 per cent had not been taken. It was further revealed that action on the files of 45 of those institutions had not been taken over a period of 10 years. Even though the normal practices in relation to the non-operating institutions is to seal the equipment of such institutions and close down, such action had not been taken up to date. As such, the possibility of the risk of such institutions operating without the payment of licence fees was observed.

4.2 Operating Inefficiencies

The following observations are made.

(a) Action had not been taken even by 25 March 2015 to obtain the audited final accounts of 07 Telecommunications Operator institutions and as such it had not been possible to establish the accuracy of the cess amounting to Rs.978 million received from those institutions.

(b) Even though the Director General informed me on 28 June 2011 and 16 June 2012 that action would be taken for inclusion of provisions to the Telecommunications Act, to provide legal authority for the recovery of a penalty form the Operators who do not pay or delay the payment of the cess, such action had not been taken up to date.

(c) A proper methodology had not been introduced for the collections of Frequencies income and out of the invoices issued up to 31 December of the year under review, payments had not been made for invoices valued at Rs.68 million even by 03 March 2015. Operators had been allowed to use the Frequencies without licences during the period of delay arising from the delay in obtaining the Frequencies Licences.

(d) Invoices had not been issued over periods ranging from 04 to 20 years in connection with the Frequencies allocated to 20 institutions.

(e) According to the Telecommunications Tax Act, No. 21 of 2011, Telecommunications Taxes should be paid to the Commission before the fifteenth day of the month following. Nevertheless, three institutions which should pay the taxes, had not paid the taxes for the years 2011, 2012 and the year under review.

4.3 Transactions of Contentious Nature

The following observations are made.

(a) The Secretary to the President is also the Chairman of the Commission and in accordance with a request made by him as the Secretary to the President, a sum of Rs.600 million had been paid to the Presidential Secretarial on 15 December 2014 based on a decision of the Commission and without the approved of the General Treasury for the implementation of a programme for encouraging the people to safeguard ethics and religious traditions, that is, for the distribution of sil cloths to elders and school children.

(b) A sum of Rs.18 million had been spent for the printing and distribution of 30,000 diaries of the year 2015 to all the temples in the Island on the basis of a request made by a Co-ordinating Secretary to the President and a decision of the Commission.

(c) A sum of Rs.2.5 million had been paid on a request made by the Ministry of Defence and Urban Development, to a company under the purview of the Urban Development Authority, for the printing of 500,000 copies of a religious booklet.

(d) A sum of Rs.250 million had been granted on 31 December of the year under review to the Southern University which is being constructed at the John Kotelawala Defence University without the approval of the Cabinet of Ministers and the Treasury.

(e) Renting of a building and purchase of office equipment in that connection

(i) A building situated at Longden Place had been hired on rent for a period of one year with effect from November of the year under review on the payment of retention money covering 06 months amounting to Rs.1.8 million at the rate of Rs.300,000 per month based on a decision of the Commission without inviting quotations contrary to Financial Regulation 835(2)(c) and the provisions in the Circular No. CA/1/17/1 dated 14 May 2010 of the Secretary to the President.

(ii) Even though it was informed that building had been hired for the purpose of shifting certain offices of the Commission, necessitated by the proposal for the renovation of the Commission Building, it was, however, observed that neither the renovation of the Commission Building nor the shifting of the offices of the Commission to the hires building had taken place.

(iii) That building had been named as an Investigation Unit and a sum of Rs.10 million had been spent on the purchase of computers and other expenses.

4.4 Uneconomic Transactions

Despite the award of the contract for obtaining consultancy services for the construction of the Hambanthota Information Technology Centre for an agreed sum of Rs.132 million to the Sri Lanka Land Reclamation and Development Corporation according to a decision of the Cabinet of Ministries, an additional sum of Rs.1.2 million had been paid to 03 external Consultants for a period of 04 months at the rate of Rs.100,000.

4.5 Deficiencies in Contract Administration

The following observations are made.

(a) Construction of the Lotus Tower

(i) According to the loan agreement entered into by the Excim Bank of China with the Telecommunications Regulatory Commission of Sri Lanka on 17 September 2012, the Excim Bank of China had agreed to make available a sum of US$ 88,655 million to the Commission. According to the contract agreement, it had been agreed to complete the construction work by 12 May 2015, that is within 912 days. But the construction work had not been completed even by 13 July 2015. As such a commitment charge of 0.7 per cent had to be paid for the unutilized amount of the loan amounting to US$ 53 million. As the repayment period of the loan as well had extended, the interest payable thereon as well had increased.

(ii) Even though the Cabinet of Ministers had decided that in view of the national importance of the Lotus Tower Project, the Urban Development Authority should transfer the land selected for the construction of the tower on the basis of recovery of the development cost incurred up to date, action had been taken to pay a sum of Rs.11.7 billion instead of paying only the expenditure incurred by the Urban Development Authority. Out of that, a sum of Rs.2.1 billion had been paid during the year under review.

(iii) A sum of Rs.1,145 million had been paid to an insurance company for insuring the loan. An agreement entered into with the insurance company inconnection with the payment made for insurance had not been furnished and as such the impact of the delay in the construction on the insurance could not be ascertained.

(iv) Even though the audit was informed that the plans will have to be revised from time to time during construction due to the complexity of the project, a report on the changes in the cost of contract had not been prepared despite the elapse of 95 per cent of the work completion period.

(v) According to the preliminary plans, the work of the tower should be in the last stage by the end of the year under review. Nevertheless, the progress of work completion of the project as at 16 March 2015 amounted to 46.87 per cent.

(b) Construction of the Telecommunications Media Centre at the Hambanthota Information Technology Park.

(i) Even though the approval of the Cabinet of Ministers for the Project had been obtained by stating that the overall cost of the Project is Rs.2,000 million approximately, according to the Engineering Estimate of the Project (excluding Value Added Tax) the Project cost had been increased up to Rs.2,663 million.

(ii) The quotation offered by the contractor for the raised floor estimated at Rs.434 million, had been only Rs.130 million. Nevertheless, this contract had been later awarded as a sub-contract for Rs.449 million which included a sum of Rs.15 million as attendance allowance.
As such the overpayment agreed to be made to the contractor amounted to Rs.319 million.

(c) <u>Modernisation of the Auditorium in the Ground Floor of the Commission Building</u>

(i) Instead of inviting open quotations for the modernization work in terms of Section 3.2.1 of the Procurement Guidelines, quotations had been invited from only one institution.

(ii) The contract had been awarded for Rs.1,774,353 based on the quotations furnished by the contractor.

(iii) Bid security and performance guarantee had not been obtained for the contract in terms of Sections 5.3.11(a) and 5.4.10 of the Procurement Guidelines respectively while agreements had not been entered into in terms of Section 8.9.1 (a).

4.6 Staff Administration

The following observations are made.

(a) Even though the approved staff of the Commission as at 31 December 2014 had been 291, the actual staff had been 207. As such 84 vacancies existed. The vacancies in the Spectrum Management Network and Technology Division and the Economic and Legal Affairs Division which make a primary contribution to the execution of the functions of the Commission, had been 42.

(b) Eleven persons had been recruited to posts outside the approved staff. The approval of the Department of Management Services had not been obtained for the excess staff.

(c) Even though an officer released from the Ministry of Public Administration should have been appointed to a post in Class I of the Public Management Assistants' Service, contrary to that he had placed in the post of Assistant Director (Administration) and provided the salary and other privileges attached to that post. He had been given an extension of service up to 31 July 2015.

5. Accountability and Good Governance

5.1 Corporate Plan

A Corporate Plan for the year 2014 had not been prepared.

5.2 Action Plan

An Annual Action Plan in terms of paragraph 04 of the Public Finance Circular No. 01/2014 of 17 February 2014 had not been prepared.

5.3 Procurement Plan

A Procurement Plan for the year under review in terms of paragraph 04(d) of the Public Finance Circular No. 01/2014 of 17 February 2014 had not been prepared by the Commission.

5.4 Budgetary Control

Material variances between the budgeted amounts of the budget prepared by the Commission and the actual amounts were observed. Certain variances ranged between 10 per cent to 19,980 per cent. A sum of Rs.14,478 million had been spent during the year under review for 08 items not included in the budget. Accordingly it was observed that the budget had not been made use of as an effective instrument of management control.

5.5 Tabling of Annual Reports

The Annual Reports for the years 2012 and 2013 had not been tabled in Parliament even by 19 June 2015.

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

(a) Budget
(b) Corporate Plan
(c) Debtors
(d) Investments
(e) Procurement
(f) Payment of Allowances
(g) Contract Administration
(h) Collection of Income