

Natwealth Securities Limited - 2016

The audit of the financial statements of the Natwealth Securities Limited (“The Company”) for the year ended 31 December 2016 comprising the statement of financial position as at 31 December 2016 and the statement of 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. To carry out this audit I was assisted by a firm of Chartered Accountants in public practice.

This report is issued in terms of provisions in Article 154(6) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

1.2 Board’s 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 Accounting Standards and for such internal control as the Board 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. 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 Company’s preparation and fair presentation of the financial statements that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Board, as well as evaluating the overall presentation of the financial statements.

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

2. Financial Statements

2.1 Opinion

In my opinion, the financial statements give a true and fair view of the financial position of the Company as at 31 December 2016, and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.2 Other Matter

The financial statements of the Natwealth Securities Limited for the year ended 31 December 2015 were audited by another firm of Chartered Accountants in public practice who expressed an unmodified opinion on those financial statements on 27 May 2016.

2.3 Report on Other Legal and Regulatory Requirements

As required by Section 163(2) of the Companies Act, No.07 of 2007, I state the followings:

- (a) The basis of opinion and scope and limitations of the audit are as stated above.
- (b) In my opinion :
 - (i) I have obtained all the information and explanations that were required for the audit and, as far as appears from my examination, proper accounting records have been kept by the Company.
 - (ii) The financial statements of the Company comply with the requirements of Section 151 of the Companies Act, No. 07 of 2007.

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

The following instances of non-compliance were observed in audit.

Reference to Laws, Rules and Regulations	Non – compliance
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(a) Section 32(1) of the Inland Revenue Act, No. 09 of 2015	Even though the Company had received income tax assessments aggregating Rs.270,368,574 for the previous five years of assessments commencing from 2008/2009 from the Department of Inland Revenue, actions had not been taken to remit that tax to the Commissioner General of Inland Revenue even up to 27 December 2017. As a result 50 per cent of penalty totaling Rs.126,061,875 on delaying the payment had been imposed by the Department of Inland Revenue. However, the Company had not provided any provision for the tax liability other than disclosed as a note to the financial statements.

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| (b) Government Procurement Guidelines | Although the Company required to be complied with the Government Procurement Guidelines, it had not been complied with. |
| (c) Section 5.1 of the Public Enterprises Circular No. PED 12 of 02 June 2003 | A Corporate Plan had not been prepared by the Company since its inception. |
| (d) Section 75 of the Articles of Association of the Company. | Three Directors out of five had resigned from their duties on 31 December 2016. However, action had not been taken to appoint new directors even up to 23 January 2017. |

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the financial results of the Company for the year ended 31 December 2016 had been a loss of Rs.499,587,470 as compared with the corresponding loss of Rs.200,080,851 for the preceding year, thus indicating a deterioration of Rs.299,506,619 in the financial results as compared with the previous year. Decrease of investment income by Rs.594,855,612 as compared with the previous year due to adverse market conditions was the main reason attributed to this deterioration in the financial results for the year under review.

4. Operating Review

4.1 Management Activities

It was observed in audit that the Company had failed to properly implement the marketing strategies in order to meet the market demand by minimizing cash outflows. Moreover, a strong client base had not been developed by the Company. Therefore, Company had sustained a cumulative loss of Rs.699.67 million only in the years 2015 and 2016.

4.2 Irregular Transactions

The following observations are made.

- (a) The company has registered as a primary dealer with the Central Bank of Sri Lanka in 2003. According to Section 2.1 of the agreements entered into between the Mahapola Trust Fund and National Wealth Corporation, all the investment decisions should have been taken by the Investment Committee appointed by the Trust. However, in contrary that requirement then CEO and Chief Dealer of the Company had involved in taking an investment decision on perform repurchase transactions with two private companies namely Trillion Securities (Pvt) Ltd and Virtual Investment & Trading Lanka (Pvt) Ltd. Further no approval in this connection had been obtained.

Subsequently, the Company had conducted a forensic audit in this regard and according to the forensic audit report, it was revealed that the above officers were involved in an irregular transaction.

The following observations are also made in this connection

- (i) It was observed that no action had been taken by the Company against the parties concerned even up to the date of audit.
- (ii) The Central Bank of Sri Lanka (CBSL) had issued a directive on 07 August 2015 to the Company by instructing that to honour all dues arising from repurchase transactions to the said clients in terms of master repurchase agreement with the above two clients in terms of powers vested by Regulations 11(2) of the Local Treasury Bills (Primary Dealers) Regulations No.01 of 2009 dated 24 June 2009 and Regulations 11(2) of the Registered Stock and Securities (Primary Dealer) Regulations No. 01 of 2009 dated 24 June 2009. Since the CBSL had not revoked this directive, Company is responsible to act accordingly.
- (iii) The Company had filed an appeal in the Court of Appeal on 18 August 2015 against the directive made by the CBSL and the Court of Appeal had issued an interim order stating that to not implement said directive until 04 September 2015. However, after considering the requests made by the all responded parties, the above interim order had been withdrawn by the Court of Appeal on 29 March 2016. Subsequently, the Company had made another appeal in the Supreme Court on 18 April 2016 by challenging the judgment delivered by the Court of Appeal. But no judgment had been delivered in favour of the Company by the Supreme Court. Nevertheless, the Company had submitted the Forensic Audit Report to the CBSL on 27 December 2016. However, the CBSL had not given any directive to the Company in this regard even up to the date of this report.

(b) Unauthorized Brokerage Payments

The Company had made a complaint in the Criminal Investigation Department (CID) during the year 2016 in respect of unauthorized brokerage fees amounting to Rs.19,725,000 paid to two private companies (White Grove Holdings and Astral Capital Holdings) in 2014. It was further observed that the Company had not got confirmed whether these companies had registered at the CBSL as financial companies before making the payment. Further, the company had failed to disclose this transaction in the financial statements prepared for the year 2016.