Mahapola Higher Education Scholarship Trust Fund – 2016

The audit of financial statements of the Mahapola Higher Education Scholarship Trust Fund for the year ended 31 December 2016 comprising the statement of financial position as at 31 December 2016 and the statement of financial performance and cash flow statement for the year then ended and a summary of 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 10 (4) of the Mahapola Higher Education Scholarship Trust Fund Act, No.66 of 1981. My comments and observations which I consider should be published with the Annual Report of the Trust Fund appear in this report.

1.2 Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the 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 the audit conducted in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000-1810).

1.4 Basis for Disclaimer of Opinion

As a result of the matters described in paragraph 2.2 of this report, I am unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded items, and the elements making up the statement of financial position, statement of financial performance and cash flow statement.

2. Financial Statements

2.1 Disclaimer of Opinion

As a result of the matters described in paragraph 2.2 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 Comments on Financial Statements

2.2.1 Consolidated Financial Statements

The consolidated financial statements had not been prepared and presented to Audit since the year 2013 by amalgamating the two subsidiaries with full ownership of the Trust Fund, named National Wealth Corporation Limited and Natwealth Securities Ltd. Further, no disclosures whatsoever had been made in the financial statements regarding non-preparation of accounts of the Group by amalgamating the financial statements of the Development Lotteries Board and the Trust Fund with 50 per cent shares.

2.2.2 Sri Lanka Accounting Standards

The following observations are made.

(a) According to paragraph 4.56 of the conceptual framework for financial reporting, the entity shall prepare its financial statements based on historical cost or any other bases and that particular basis should be disclosed in the financial statements. The basis of preparing financial statements had not been disclosed by the Trust Fund.

(b) Sri Lanka Financial Reporting Standard 7

(i) According to paragraph 8 of the Standard, the carrying amount of financial assets and liabilities should be classified and shown either in the statement of financial position or in the notes for accounts. However, the Trust Fund had not acted accordingly.

(ii) Even though financial risk management should be disclosed according to paragraphs 31 and 33 of the Standard, the Trust Fund had not made disclosures accordingly.

(c) Sri Lanka Accounting Standard 01

(i) According to paragraph 10 (c), the statement of changes in equity had not been presented along with financial statements by the Trust Fund.

(ii) Financial assets valued at Rs.9,027.951,695 owned by the Fund had not been separately recognized as non-current assets and current assets according to paragraph 60 of the Standard.

(iii) According to paragraph 99 of the Standard, income and expenditure accounts should be prepared using a classification based on the nature and function of expenses of the Fund. However, it had not been so done.

(d) Sri Lanka Accounting Standard 16

Even though an item of property, plant and equipment that qualifies for recognition as an asset shall be measured at its cost according to paragraph 15 of the Standard, it had been brought to account at the book value.

(e) Sri Lanka Accounting Standard 18

Interests shall be recognized using the effective interest method as set out in paragraph 30 (a) of the Standard. However, interest had been recognized on accrual basis.

(f) Sri Lanka Accounting Standard 24

Even though related party transactions shall be disclosed as set out in paragraphs 25 and 26 of the Standard, it had not been so disclosed by the Trust Fund.

(g) Sri Lanka Accounting Standard 39

Debit balances such as Treasury bonds valued at Rs.5,106,669,232, Treasury bills valued at Rs.395,461,300, re-sales valued at Rs.1,102,010,859, debentures valued at Rs.796,979,390, Asset Back Trust Certificates valued at Rs.486,128,823 and the balance of the current account valued at Rs.270,448 and the credit balance of re-purchases of Rs.1,138,209 remained according to accounts presented by the National Wealth Corporation Limited relating to the investment portfolio managed by the said Company, had not been classified and indicated in the statement of financial position in terms of paragraph 45 of the Standard.

(h) Sri Lanka Accounting Standard 40

The land of 25 acres in extent located at Malabe, brought to account at the value of Rs.12,460,179 in the year 2005, owned by the Trust Fund, leased out to the Sri Lanka Institute of Information Technology (SLIIT) had not been brought to account as a separate property of the Trust Fund. Moreover, the said property had not been valued to the current value and disclosed in the financial statements.

2.2.3 Accounting Deficiencies

The following observations are made.

(a) Building rentals amounting to Rs.1,921,500 payable relating to 07 months of the year under review had not been brought to account.

(b) According to the Development Lotteries Board Act, the share of profit entitled to the Trust Fund as the share of profit of the Development Lotteries Board from the President's Fund relating to the year under review amounted to Rs.828,989,083. However, it had been indicated as Rs.680,044,729 in the financial statements, thus understating by Rs.148,944,354.

2.2.4 Unexplained Differences

The following observations are made.

(a) The balance relating to the year under review of the Mahapola Investment Portfolio managed by the National Wealth Corporation Limited amounted to Rs.7,886,381,843 according to the account presented by that Company. Nevertheless, it was Rs.7,914,466,463 in the statement of financial position of the Mahapola Trust Fund, thus indicating an unexplained difference of Rs.28,084,620.

(b) According to the financial statements of the National Wealth Corporation Limited, the total ordinary share capital owned by the Mahapola Higher Education Trust Fund as at 31 December of the year under review amounted to Rs.985,500,070. However, according to the accounts of the Trust Fund, it was Rs.985,000,000, thus indicating an unexplained difference of Rs.500,070.

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

In terms of Section 47 of the Employees' Provident Fund Act, No.15 of 1958 and Section 44 of the Employees' Trust Fund Act, No. 16 of 1980, the Cost of Living Allowance should be included in the computation of contribution to the Employees' Provident Fund and the Employees' Trust Fund. However, it had not been so done and as such, contributions had been under paid by Rs.290,550 and Rs.34,866 respectively by the Trust Fund in the year under review to the Employees' Provident Fund and the Employees' Trust Fund.

2.4 Accounts Receivable and Payable

Expenditure totalling Rs.3,832,874 payable by the School Development Fund for constructions carried out in several schools was being brought forward in the financial statements since the year 2013 without taking any action whatsoever.

3. Financial Review

3.1 Financial Result

According to the financial statements presented, the financial result of the Trust Fund for the year ended 31 December 2016 had been a surplus of Rs.240,528,891 as compared with the corresponding surplus of Rs.750,907,256 for the preceding year, thus indicating a decline of Rs.510,378,365 in the financial result of the year under review as compared with the preceding year. The increase in Mahapola Scholarship Grant Payments by Rs.501,401,690 as compared with the preceding year had been the main reason for the above decline.

The analysis of financial results of the year under review and 4 preceding years revealed that there had been a surplus with fluctuations from the year 2012 to the year under review. However, in readjusting employees remuneration and depreciation for non-current assets to the financial result, the contribution of Rs.688,827,839 for the year 2012 had increased up to Rs.1,086,213,752 in the year 2013. It had declined continuously to Rs.302,031,160 by the year under review.

4. Operating Review

4.1 Performance

4.1.1 Planning

The targets expected to be achieved had not been indicated materially and financially in the Corporate Plan prepared relating to the period from the year 2014 to the year 2017 by the Trust Fund and an Action Plan and progress reports had not been prepared based on the Corporate Plan. As such, the progress thereof could not be examined.

4.1.2 Function and Review

The following observations are made.

(a) Even though providing assistance required for youth who have completed their secondary education satisfactorily, so as to enable them to complete their academic or industrial education at a technical or higher educational institute is an objective of the Fund, out of 5,120 students admitted to technical colleges in the year under review, only 1,500 students had been granted scholarships of Rs.1,500 monthly.

(b) The Fund had not paid attention on achieving objectives such as the establishment and management of schools, institutions, foundations and other such institutions.

4.2 Management Activities

The following observations are made.

(a) A sum of Rs.2,300,000 had been spent as the initial expenditure for the construction of a building for the Trust Fund without legally vesting the land located within close proximity to the Ratmalana Airport, owned by the Department of Agriculture and without carrying out a feasibility study thereon. However, the constructions thereof had been prohibited by the Civil Aviation Authority. As such, the Ministry of Agriculture had agreed to provide a land from Narahenpita in its place. Nevertheless, it had not been provided. Even though the Trust Fund had purchased a land in the year 1989 by spending a sum of Rs.5,600,000, subsequently that land as well had been sold for a sum of Rs.221,500,000 and the School Development Society had been established by those funds. Even though a period of 29 years had lapsed after the establishment of the

Mahapola Trust Fund, the office of the Trust Fund had been operated in four places during that period. A sum of Rs.18,379,695 had been paid as rent from the year 2011 to April 2016 and from May 2016 a place with inadequate space had been obtained again on rent at the J.R.Jayewardena Centre for a monthly rental of Rs.274,500.

(b) A sum of Rs.675,000,000 had been invested in the year under review by the Trust Fund from the funds existing in the Investment Portfolio in ordinary shares of Natwealth Securities Ltd. which had sustained losses of Rs.200,242,875 and Rs.499,181,284 respectively in the years 2015 and 2016.

(c) In terms of Sections 6.2 (a), (c) and (d) of the Trust Fund Act, the Trust Fund has the powers to raise funds and to receive grants, gifts or donations in cash or kind, whether from local or foreign sources and to conduct lotteries with the approval of the Government. Nevertheless, a sum of Rs.464,394,380 had been withdrawn from investments made in fixed deposits in the year under review without taking action to raise funds by such sources and it had been used for the payment of bursaries.

4.3 Transactions of Contentious Nature

The approval had been granted by the Cabinet Paper No.98/995/11/052 of 08 July 1998 to establish an institute of information technology with the contribution of the Trust Fund with a view to providing the opportunity for higher education in the field of information technology to students who are unable to enter universities. Accordingly, it had been decided at the meeting held on 28 January 1999 chaired by the Secretary to the Ministry of Internal and International Commerce and Food to establish an Institute of Information Technology (Guaranteed) Limited for carrying out as an interim arrangement and to take over this institute under purview of the University of Moratuwa after the interim period is over. Accordingly, a company named Sri Lanka Institute of Information Technology (Guaranteed) Limited including the name “Sri Lanka” as well had been incorporated in terms of Companies Act, No.17 of 1982 and the responsibility of providing resource contribution by supplying necessary funds therefor, had been assigned to the Mahapola Higher Education Scholarship Trust Fund. Matters observed thereon are given below.

(a) According to the agreement entered into on 19 March 2003 with the Sri Lanka Institute of Information Technology (Guaranteed) Limited., (SLIIT) the Campus established on a land of 25 acres in extent located at Malabe owned by the Mahapola Trust Fund had been vested in the said Company for management for a period of 8 years. An agreement had been again entered into between the Trust Fund and the Sri Lanka Institute of Information Technology (Guaranteed) Limited before the expiry of the said period of agreement, that is on 14 November 2005 and that the following conditions favourable to the Fund and included in the original agreement had been eliminated and revised.

Conditions eliminated

(i) Section 4 (e)- All the assets and income of the Mahapola Campus should not be directly or indirectly used by other branches of the SLIIT or for any other commercial purpose contradictory to the objectives of the Trust Fund.

(ii) Section 4 (h)- All activities meant for the betterment of the University should be done with the concurrence of the Trust Fund.

(iii) Section 4 (i)- Collection of income earned from the conduct of academic courses and incurring necessary expenditure for the betterment of the University shall be a responsibility of the SLIIT.

(iv) Section 4 (j)- The SLIIT should realize that a considerable amount of loan had been obtained by the Trust Fund from the National Development Bank (NDB) for the objective of the establishment of the University and that the SLIIT assures in every effort made for the payment of installments when the institute is steady with financial capacity.

(v) Section 4 (k)- The Board of Trustees shall have the right to appoint an independent group of persons comprising competent managers and auditors for the management, examination of accounts and evaluation of the University and to appoint a team comprising qualified, educated and skilled persons for evaluating new courses likely to be introduced.

(vi) Section 4 (l)- According to the decision of the Board of Trustees, the Malabe University should be named as the Mahapola Campus and the new auditorium should be named as the Lalith Athulathmudali Auditorium and those name boards should be clearly displayed in the premises.

(vii) Section 4 (m)- In case of termination of this agreement due to expiry of its period or any other reason , the assets financed by the Trust Fund should be considered as the assets of the Trust Fund.

Conditions Revised

(viii) According to Section 4 (m) of the legal agreement of 19 March 2003, the surplus of the income generated from the activities of the University after deducting the agreed management fee shall be credited to the Trust Fund prior to 30 June in the ensuing year and other investments shall not be made without prior approval of the Trust Fund. Nevertheless, the Board of Directors of the SLIIT may seek approval of the Board of Trustees of the Trust Fund for the maintenance of a reserve account for future development activities of the University and it had been decided according to the new agreement to lease out the land belonging to the Trust Fund to the SLIIT instead of providing necessary funds for such development activities from the above reserve account by the Trust Fund. Moreover, according to Section 5(a)(i) of the agreement, it has been agreed to pay a sum of Rs.8 million or 20 per cent of the annual net profit of the SLIIT or whichever is more as the annual lease rental.

(ix) According to Section 4(l) of the agreement entered into on 19 March 2003 between the Trust Fund and the SLIIT, the right of recommendation of development activities of the University, is assigned to the Board of Trustees and all activities carried out for the development of the University should be carried out on the concurrence of the Trust Fund. However, according to Sections 4(e) and 4(f) of the second agreement entered into on 14 November 2005 between the Trust Fund and the SLIIT, it had been agreed to carry out operations of this University as per the decision taken by the Board of Directors thereof for achieving the objectives of the SLIIT, prepare circulars accordingly, make arrangements for conducting examinations, enrollment of students, engage the academic staff in the service, carry out management and maintenance activities of infrastructure facilities and to take action under the approval of the Trust Fund only in major constructions.

(b) The Mahapola Higher Education Scholarship Trust Fund had reimbursed a sum of Rs.373,579,392 appropriate to the value of investment, incurred as expenses on behalf of the SLIIT. The Trust Fund had entered into two agreements on 12 May 2015 with the Sri Lanka Institute of Information Technology (Guaranteed) Limited for the establishment of the Sri Lanka Institute of Information Technology (Guaranteed) Limited as an independent institute from the Trust Fund and on behalf of the land on lease basis on which SLIIT has been constructed

Further, by eliminating conditions favourable to the Trust Fund included in the original agreement entered into on 19 March 2003 and the agreement entered into on 14 November 2005, following new conditions had been entered in the agreement by the said two agreements.

(i) Granting a sum of Rs.373,579,392 as the value of investments made by the Trust Fund and a sum of Rs.408,500,000 to cover the value of scholarships awarded by the Mahapola Trust Fund and other incidental expenses to the Trust Fund and non-existence of a financial commitment between the Mahapola Trust Fund and the SLIIT and function of the Sri Lanka Institute of Information Technology (Guaranteed) Limited as an independent institute from the Trust Fund.

(ii) The SLIIT is not subject to the Sri Lanka Accounting Standards, Sri Lanka Financial Reporting Standards and the International Accounting Standards and it is not necessary to furnish accounting records to the Mahapola Trust Fund or amalgamate accounts from the year 2015/2016.

(iii) Leasing out the land on which the SLIIT is located at Malabe on the basis of increasing the annual lease rental every once in 5 years for a period of 60 years from 15 May 2015 to 14 May 2075 and accordingly, liability of paying the lease rental at the rate of Rs.20 million annually for 5 years ending 14 May 2020 and at a rate of Rs.40 million annually for 5 years from 15 March 2070 to 14 March 2075.

(iv) No written permission of the Mahapola Trust is required for sub-lease and mortgage the land or part thereof owned by the Mahapola Trust Fund, leased out to the SLIIT, Malabe.

(v) The SLIIT has been granted permission to construct buildings, install machinery and equipment within the relevant premises or carry out rehabilitation, improvement activities of the relevant land at their cost.

(c) According to the agreement entered into on 14 November 2005, irrespective of outstanding lease rent of Rs.98,642,356 recoverable by 12 May 2015, the Trust Fund had entered into a new agreement on 12 May 2015 with the Company. According to the original agreement of 14 November, the lease rental of Rs.45,358,379 relating to the year under review, receivable to the Trust Fund had decreased up to Rs.20,000,000 according to the conditions of the new agreement.

(d) All rights relating to buildings had been abolished by the agreement entered into between the Trust Fund and the Sri Lanka Institute of Information Technology on 12 May 2015. Nevertheless, a sum of Rs.1,038,092,883 of the profit retained in the said Company had been brought to account as investments of the Trust Fund in the year 2015 stating that the said amount had been spent for development of buildings. Moreover, a sum totalling Rs.1,064,520,695 comprising the said sum (Rs.1,038,092,883) and the sum of Rs.26,427,812 receivable from the Institute of Information Technology had been brought to account as buildings.

5. Accountability and Good Governance

5.1 Presentation of Financial Statements

In terms of Section 6.5.1 of Public Enterprises Circular No. PED/12 of 02 June 2003, the Draft Annual Report should be presented to the Auditor General along with the financial statements within 60 days after the closure of the year of accounts. However, the financial statements of the Trust Fund for the year 2015 had been presented to Audit only on 08 May 2018.

5.2 Internal Audit

An Internal Audit Unit had not been established for the Fund in terms of Financial Regulation 133 of the Democratic Socialist Republic of Sri Lanka and the Management Audit Circular No. DMA/2009/(1) of 09 June 2009 and an internal audit had not been carried out even by the Internal Audit Unit of the Ministry.

5.3 Procurement and Contract Process

5.3.1 Procurements

The following observstions are made.

In terms of Section 6(2) (d) of the Mahapola Higher Education Scholarship Trust Fund Act, No.66 of 1981, the "Online Lottery" had been reintroduced on 30 July 2013 on the Cabinet Approval No.13/0773/54/008 dated 11 July 2013 with the objective of collecting moneys for the achievement of the objectives of the Fund. The following observations are made in this connection.

(a) On the implementation of Mangatha Lottery the possibility of maintaining the online lottery through the National Lotteries Board and the Development Lotteries Board established under 02 Acts of Parliament, had not been looked into.

(b) The Trust Fund had taken action to implement the said lottery through a private institution and the following matters were observed in that connection.

(i) In order to select an investor for the implementation of the lottery by investing Rs.6 billion under the first and second stages, a special committee called "Mahapola Lottery Committee" consisting of five members had been appointed on 12 July 2012 by the Board of Trustees as per a proposal made by the Minister of Co-operative and Internal Trade. However, in terms of Guideline 2.7.2 (b) of the Procurement Guidelines, a Procurement Evaluation Committee had not been appointed.

(ii) Standard bidding documents had not been used for calling for bids contrary to Guideline 5.3.1 of the Procurement Guideline and a Technical Evaluation Committee as well had not been appointed. As such, the bidding documents used had not been checked and approved by a Technical Evaluation Committee.

(iii) A period of at least 21 days should be allowed for submission of the bids in terms of Guideline 6.2.2 of the Procurement Guidelines. However, only 3 bids had been received as only 10 days had been given.

(iv) As a Bid Evaluation Committee had not been appointed, an extensive bid evaluation had not been carried out; instead, the Lottery Committee had only compared the bids. In accordance with Guideline 5.3.2 of the Procurement Guidelines, the eligibility and qualification requirements should be included in the request for calling for bids. However, with that requirement not included, one out of the 03 bids submitted had been rejected stating that information furnished had not been clear.

(v) Rejection of all bids received can be justified when lack of effective competition is clearly evident in terms of Section 7.12 of the Procurement Guidelines. However, without doing so and contrary to Section 7.10 of the Procurement Guidelines, a foreigner being a main investor of a company who had submitted a bid valued at Rs.6 billion had been evaluated instead of evaluating a bidder that had made an investment irrespective of other resources, financial position, and experience. Furthermore, maintaining the lottery had not been mentioned as an objective at the registration of the Company.

(vi) A formal contract agreement should be prepared by the procuring entity in terms of Section 8.9.1 of the Procurement Guidelines. However, the bidder selected had prepared the agreement. Hence, the matters mentioned in 6, 8, 9, 14, 15, 16, 17, and 20 of the "Guidelines for preliminary operations to execute the Mahapola lottery" had been eliminated from the agreement. As such, there had been no transparency in the operations of the lottery and the performance.

(vii) In terms of Section 7.1 (b) of the contract agreement, the contractor should pay the premium to the Trust Fund on or before the first date of the quarter. In the event of failing to do so, the contractor should be informed in that connection in writing within a period of 90 days and the agreement should be cancelled within 14 days from that date. Even though the payments had been defaulted from 05 May 2015, the Trust Fund had not informed the contractor in writing. Accordingly, the said agreement had been cancelled on 15 September 2016 without terminating it on 17 August 2015 on which the agreement should be terminated. As such, a private company had been allowed to earn excessive profits for a period of over one year by using the concept of "Mahapola". Moreover, the outstanding amount as that date had been Rs.673,913,043.

(c) A newspaper advertisement had been published in the English Medium by spending a sum of Rs.38,761, notifying that the closing date for submitting bids as 14 May 2016, for selecting a place fit for operating the office of the Trust Fund without giving details on the nature of requirement. However, according to the written request of the Trust Fund made on 09 May 2016, the bid with the monthly rental of Rs.274,500 submitted on 18 May 2016 by the J.R.Jayawardene Centre, had been accepted. As such, an overpayment of Rs.294,000 as well had to be made annually than the bid received according to the newspaper advertisement and rejected. Moreover, it was observed that the decisions to be taken by the Board of Trustees are taken by the Director and one Trustee and the members are notified thereafter.

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

	Areas of Systems and Controls	Observations
(a)	Internal Audit	Non-recruitment of an officer for the post of Accountant.
(b)	Investment of Funds	Failure in obtaining proper approval for investments and evaluating investment benefits.
(c)	Procurement	Failure in taking action in accordance with Procurement Guidelines, Procurement Manual and Procurement Plans.