

Securities and Exchange Commission of Sri Lanka - 2017

The audit of financial statements of the Securities and Exchange Commission (“the Commission”) of Sri Lanka for the year ended 31 December 2017 comprising the statement of financial position as at 31 December 2017 and the statement of financial performance, statement of changes in reserves and statement of cash flows 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 the Sri Lanka read in conjunction with Section 13(1) of the Finance Act, No. 38 of 1971 and Section 37(2) of the Securities and Exchange Commission of Sri Lanka Act, No.36 of 1987.

My comments and observations which I consider should be reported to Parliament in terms of Article 154 (6) of the Constitutions of the Democratic Socialist Republic of Sri Lanka 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 the Sri Lanka Public Sector 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 Auditing 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 judgement, 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 the 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.

2. Financial Statements

2.1 Opinion

In my opinion, the financial statements give a true and fair view of the financial position of the Securities and Exchange Commission of Sri Lanka as at 31 December 2017, and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the operations of the Commission for the year ended 31 December 2017 had resulted in a net deficit of Rs.391,794,822 before taking into account the transfers from the Cess Fund for operational expenses and it was reported the net deficit of Rs. 331,278,495 for the preceding year. The net surplus for the year under review after taking into account the transfers from the Cess Fund for the year was Rs.3,835,003 and it was reported the net surplus of Rs.38,313,564 in the preceding year which was also as a result of an additional sum of Rs. 22 million transferred from the Cess Fund in the preceding year.

3.2 Analytical Financial review

The following observations are made.

- (a) The revenue of the Commission for the year under review and the preceding year was Rs. 427 million and Rs. 401 million respectively including transfers from the Cess Fund to meet operational expenses amounting to Rs. 396 million and Rs. 370 million respectively and it representing an increase of 6.5 per cent in the total income as compared with the previous year. However, the expenditure incurred for capital market development activities during the year under review was only Rs. 72 million as compared with Rs. 42 million in the preceding year, thus showing that only 17 per cent of the total expenditure had been utilized for the capital market development activities during the year under review. Further, out of the total expenditure an amount equivalent to 46.5 per cent had been spent for personnel costs during the year under review as compared with that of 49 per cent in the preceding year.
- (b) A sum Rs.12,866,350 had been incurred as professional fee during the year under review on behalf of obtaining services for various purposes such as obtaining the services for temporary assignments, legal consultancy services and other consultancy services etc. and it had been increased by 46.3 per cent and 894 per cent as compared with the preceding year and the year 2015 respectively.

- (c) Capital Market and Product Development expenditure for the year under review was Rs. 46.7 million. It was mainly included an amount of Rs.25.4 million spent for Broker Back Office systems (BBO) and Order Management System (OMS). Further, an amount of Rs. 17.4 million was incurred for expenditure relating to the Annual Meeting and Conference of the IOSCO Growth and Emerging Markets Committee and Asia Pacific Regional Committee.

4. Operating Review

4.1 Performance

According to the information made available for audit, the performance of the Commission as a regulator of capital market in Sri Lanka is summarized below.

- (a) There were 93 entities under the supervision of the Supervision Division as at 31 December 2017 and this Division had completed on-site inspections relating to 55 entities excluding 4 special on-site inspections conducted in the year under review as compared with 53 inspections conducted excluding 2 special on-site inspections in the preceding year. It was further observed that the on-site inspections are conducted pursuant to an assessment of risks posed by regulated and licensed entities.
- (b) The performance of the Corporate Affairs Division of the Commission during the year under review as compared with previous year is shown in the following table.

Activity -----	Actual Performance -----	
	2017 -----	2016 -----
Resolve of Complaints	36 out of 38 complaints resolved	50 out of 52 complaints resolved
Approval of Exceptional Private Transfers under Section 28 of the SEC Act	525	469
Approval of Off the Floor Transfers under Section 28 of the SEC Act	175	146
Review of Annual Reports	Completed 57 out of 111 annual reports	Completed 75 out of 113 annual reports

- (c) Out of 31 cases handled by the Investigations Division, two cases had been completed as at the end of the year under review and one case was referred to the Department of Criminal Investigations and another case was referred to the Financial Intelligence Unit of the Central Bank of Sri Lanka and the investigations of 27 other cases were in progress.

4.2 Operating Inefficiencies

The following observations are made.

- (a) As per the terms and conditions applicable to the disbursement of funds for Broker Back Office systems (BBO) and Order Management System (OMS), the date of Go Live of the BBO and OMS should be on or before 31 March 2016 and if any delay, the total grant will be reduced from 25 per cent to 100 per cent. Even though 05 Stockbrokers had not met this requirement, the Commission had given approval to disburse full amount to the above Stockbrokers.
- (b) A Consultant was appointed during the month of January 2015 for obtaining Consultancy and Project Management Services to implement the Central Counter Party Mechanism (CCP) in order to mitigate the settlement risk and strengthen the clearing and settlement process in the financial market. According to the tripartite agreement entered into between the Colombo Stock Exchange (CSE), Central Bank of Sri Lanka (CBSL) and the Commission, the cost of the project including the consultancy fee will be equally shared among them. Accordingly, the Commission has spent Rs.22.2 million for the consultancy fee of the first phase of the project as a share of the Commission during the year under review. However, the CBSL had withdrawn from this tripartite agreement in 2015 and the tripartite agreement was terminated without completing other four phases of the project.

4.3 Human Resources (HR) Management

The following observations are made.

- (a) According to the letter dated 31 March 1992 of the Secretary to the Ministry of Finance and Planning, the Commission is privileged to recruit its staff and fix their salaries and other emoluments without considering other Government regulations. However, the Commission had not obtained required clearance from the National Salaries and Cadre Commission in this regard.
- (b) An officer attached to the Commission had been interdicted from service with effect from 19 April 2016. However, an amount equivalent to half of his monthly gross salary excluding transport allowances and other benefits is being paid contrary to Sub-section 31.11 of the Establishment Code of the Democratic Socialist Republic of Sri Lanka. The total amount so paid to him during the period of April 2016 to December 2017 was Rs.3,397,364.
- (c) As per the Administrative Manual of the Commission, the Director General may employ the persons on casual basis for a period not exceeding 3 months at a time. However, at the audit test checks it was revealed that six persons had been appointed on the above basis since the month of October 2015 and service of the two persons had been continued over one year for the similar assignments. Further, no recruitment procedure had been followed to recruit those persons.

- (d) It was observed that the post of Director Surveillance, Director Capital Market Development, Director Investigations, Director Human Resources and Director Capital Market Education and Training were still vacant.

5. Accountability and Good Governance

5.1 Budgetary Control

Significant variances ranging from 32 per cent to 97 per cent were observed between the budgeted and actual expenditure thus, indicating that the budget had not been made use of as an effective instrument of management control.

6. Systems and Controls

Deficiencies observed in systems and controls 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 incurring the expenditure within the budgeted limits and prepares the budget in rational manner.