National Film Corporation of Sri Lanka – 2017

The audit of financial statements of the National Film Corporation 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 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 31(1) of the National Film Corporation of Sri Lanka Act, No.47 of 1971. My comments and observations which I consider should be published with the Annual Report of the Corporation 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 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 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 Corporation'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 Corporation'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 Going Concern of the Corporation

The commission on film distribution, which was one of the main sources of income, had been deprived to the Corporation with the abolition in the year 1999 of the monopoly of distribution of films which existed with the National Film Corporation. As such, the General Treasury had made arrangements to grant provisions for employees' salaries since the year 2001 on the inadequacy of the Corporation's income in settling expenses.

Further, continuous loss was observed before receiving Treasury Grants by the Corporation during the year under review and 4 preceding years and accordingly, it was observed that the going concern of the Corporation had been uncertain without the financial assistance of the Government.

1.5 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 National Film Corporation as at 31 December 2017 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

The following non-compliances were observed.

(a) Sri Lanka Accounting Standard 1

Contributions for the Employees Trust Fund had been computed from January 2006 to December 2015 without considering the cost of living allowance and due to that, an outstanding sum of Rs.2,763,753 and a surcharge of Rs.1,381,876 had to be paid. Even though, the Board of Directors approval had been granted for that on 27 April 2017, provision had not been made in the accounts in terms of the section 27 of the standard.

(b) Sri Lanka Accounting Standard 7

In terms of paragraph 7 of the standard, in accounting Treasury Bills and Bills repurchasing, investments of 03 months or less should be presented in the cash flow statement as cash and cash equivalents. However, the value of Treasury Bills to be matured within a period of 03 months amounting to Rs.6,863,993 and Bills Repurchasing amounting to Rs.97,461,399 had been presented under the investments in the cash flow statement instead of presenting under the cash and cash equivalents.

(c) Sri Lanka Accounting Standard 16

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(i) Even though, in terms of paragraph 79(a) of the standard, the carrying amount of idle assets should be disclosed, idle assets with outdated technology belonging to the black and white and colour laboratories of the Kelaniya Studio of the Corporation had not been accounted and disclosed.

(ii) Since useful life of non-current assets had not been reviewed annually in terms of paragraph 51 of the standard, fixed assets costing Rs. 69,032,058 had still been in use despite been fully depreciated. Accordingly, action had not been taken to rectified the estimated error in terms of Sri Lanka Accounting Standard 08.

(iii) In terms of paragraph 34 of the Standard, when the fair value of a revalued assest differs materially from its carrying amount, that property should be revalued. Nevertheless, the land bearing assessment number 224 located in Bouddaloka Mawatha and the land of the Kelaniya Studio belonging to the corporation had been valued for the last time in the year 2007. Accordingly, 11 years lapsed as at the end of the year under review, an action had not been taken to revalue these lands and to account the fair value.

(d) Sri Lanka Accounting Standard 19

In terms of paragraph 57 of the standard, provision for post employment benefits should be computed after carrying out an actuarial estimate in terms of Projected Unit Credit Method. However, contrary to that, the Corporation had allocated a gratuity equal to half pay of the monthly salary to every employee for each year of service without identifying an accounting policy for allocating post-employment benefits.

(e) Sri Lanka Accounting Standard 24

No disclosures had been made in terms of 26 (b) of the standard, in relating to the film production loan amounting to Rs.1,732,530 which had been given to the Director of the Board.

(f) Sri Lanka Accounting Standard 38

In terms of paragraph 119 of the standard, the software used for post production activities in the Sarasavi Studio in Kelaniya should be presented under the intangible assets in the financial statements, an action had not been taken thereon.

(g) Sri Lanka Accounting Standard 40

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Even though, investments assets should be recognized and accounted in the financial statements as investment assets in terms of 75(c) of the standard, an appropriate disclosures had not been made to a building rented out by the Corporation to Censor Board, Selacine Institution and SAARC Cultural Centre over a period 16 years.

2.2.2 Accounting Deficiencies

Government Grant amounting to Rs.33 millions which had been received for the Presidential Award Ceremony in the year under review had been set off against the expenses of the ceremony without recognizing as an income.

2.2.3 Unexplained Differences

The following observations are made.

(a) An unexplained difference of Rs.5,763,596 was observed in Inter Department current account according to the books of the Corporation and books of the Ridma Circuit.

(b) Even though according to the bank confirmation, the balance of the Treasury Bills Repurchasing amounting to Rs.171,078,340 and according to the financial statements the balance was Rs.171,694,038. Therefore unexplained difference of Rs.615,698 was observed.

(c) Even though as per financial statements as at 31 December 2017, value of closing stock of films was Rs. 5,253,875, only 3 local films and 9 foreign films worth of Rs.718 included in the film stock according to the records of Finance Division.

2.2.4 Non Evidence for Audit

Even though, independent confirmation had been called for the debtor balance amounting to Rs.58,466,046, the letters amounting to Rs.11,088,220 had been returned due to wrong addresses and no confirmations had been received for letters amounting to Rs.47,377,826. Thus it was unable to get the above debtor balances confirmed during the audit.

2.3 Accounts Receivables and Payables

The following observations are made.

(a) Action had not been taken even by the date of this report to recover the film rental of Rs.12,343,433 recoverable from the year 2003 up to 31 May 2016 from the Cine City Cinema Hall in Maradana. Moreover, as the daily report had not been obtained after 31 May 2016, the income from film rental had been unable to compute and account.

(b) Legal actions had not been taken to recover the loan of Rs.1,009,548 and Rs.19,332,544 had not been paid as at 31 December 2017, which were consists of film rental and corporation levy interest and debit notes, from Cineworld Cinema Complex in Kotahena.

(c) Out of the compensation received in 1997 from the Treasury for voluntary retirement of employees, remaining sum of Rs.5,000,000 had not been remitted to the Treasury.

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

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

Reference to Laws, Rules, Regulations etc.	Non-compliances
(a) Sections 10(5) and 11 of the Finance Act, No.38 of 1971 and Section 27 of the Film Corporation Act, No.47 of 1971	An income over expenditure amounting to Rs.140,531,882 from the year 2014 to the year 2017 had not been remitted to the Treasury and Rs.100,117,116 and Rs.173,097,656 had been invested in Treasury Bills and Treasury Bills Repurchasing respectively as at 31 December 2017 without approval of the Minister of Finance and the Line Minister.
(b) Financial Regulation 381(1)of the Financial Regulations of the Democratic Socialist Republic of Sri Lanka	Even though, an approval to open the official bank accounts should have been obtained from the Treasury through the Chief Accounting Officer, there was no assurance obtained from the General Treasury regarding the approval for the 8 current accounts totaling Rs.90,549,292 which have been maintained by the Corporation as at 31 December 2017.
(c)Cabinet Decision No.මප/05/0741/041/012 dated 22 July 2015.	Non-ironic metals such as copper, brass, aluminum, lead etc. and the special type iron, cast iron and steel scraps discarded by Government institutions could have been sold to the Industrial Development Board of Ceylon. Nevertheless, action had not been taken in respect with the iron, scraps and script covers that had been stacked in an old building of the Sarasavi Studio.
(d) Section 9 of National Film Policies and Guidelines of 17 June 1999.	Even though, a Film Preservation Unit should be established and managed by the Film Corporation, 273 old films belonging to the Corporation had been preserved in a repository in the Department of National Archives. However, no arrangement had been made to preserve 962 films screened and copies of new films from the year 1947 to the year 2018.
(e) Sections (a) and (c) of Schedule 111 of the Excise Notification No.902	Liquor permits should not be issued if a religious place or school is located within 500 meters and if the area of the place of selling liquor is less than 500 square feet. However, recommendations had been granted for liquor permits in 47 cinema halls without carrying out inspections thereon.
(f) Paragraph 6 of lease agreement No.4711 of 23 January 2017 entered with the Censor Board	No changes and additions should be done to the building given on lease without the written approval of the Corporation. However additions had been done to the building that had been leased to the Censor Board without the approval.

(g)	Section 7(2) (a) (i) of the National Film Corporation Act, No 47 of 1971	Even though after inquiring the Subject in charge of the Minister of Education or the Line Minister, two members representing Universities had to be appointed as Board of Directors of the Corporation, such appointments had not been made.

2.5 Transaction not Supported by Adequate Authority

Journals worth of Rs.14,736,803 had been included in the financial statements as impairment loss of doubtful debtors on the approval of the Accounts Clerks without proper authorization.

3. Financial Review

3.1. Financial Results

The financial result of the corporation for the year under review had been a loss of Rs. 51,970,405 before receiving Treasury Grants as compared with the corresponding loss of Rs.34,638,806 for the preceding year, thus indicating a deterioration of Rs.17,331,599 in the financial result for the year under review as compared with the preceding year. Decrease in commission income from distribution of foreign films by Rs.9,157,132 and increase in impairment adjustment for bad debts by Rs.11,926,984 had mainly attributed to the above deterioration.

In analyzing the financial results of the year under review and 04 preceding years revealed a continuous loss in the financial results before receiving Treasury Grants and in the year 2013 it had been Rs.58,337,827 while as at the end of the year under review it had been Rs.51,970,405. However, in re-adjusting the employees' remuneration and depreciation for non-current assets to the financial result, the contribution of the Corporation which was Rs.19,157,095 in the year 2013 had increased to Rs.52,207,037 as at the end of the year under review.

4. Operating Review

4.1 Performance

4.1.1. Planning

The following observations are made.

(a) Even though an action plan had been prepared for the year under review, that plan had not been prepared based on the objectives of the Corporate Plan. Moreover, the targeted activities had been identified quarterly in the Action Plan, the performance reports had not been prepared in a manner to enable the evaluation of its performance.

(b) Even though, Rs.25 millions had been allocated for the improvements of production facilities of Sarasavi Studio in Kelaniya and Rs.50 millions for the establishment of film preservation unit and film restoration, that amount had not been utilized during the year under review. Moreover, Rs. 50 millions had been allocated for the establishment of National School for the Capacity Building of Film Artist and Technicians, out of that only Rs. 500,000 had been spent for the soil test and rest of the project had not been carried out.

4.1.2 Activity and Review

Even though it had been planned to inspect at least 1500 shows as a whole ensuring a cinema hall is subjected to an inspection at least once a month ,only 850 shows had been inspected during the year under review.

4.2 Management Activities

The following observations are made.

(a) In terms of letter No.PE/ME/NFC/GEN/2015 of August 2015 of the Director General of the Department of Public Enterprises, as a reply to the letter of requesting approval for writing off outstanding money recoverable from Cinema Halls and the loan of Rs,192 million granted for production of films, it was observed that the following activities had not been done in connection with the recovery of outstanding income.

(i) As per the recommendation by the Parliamentary Committee on Public Enterprises, (COPE) it had been instructed to appoint a committee at Ministerial level and formulate a proper methodology for collecting outstanding monies. However, there had been no representation from the Ministry for the appointed committee.

(ii) Failure in investigating on the legal ability for recovery of the relevant loans and not taking legal action to recover the relevant outstanding amounts from debtors identified through such investigations.

(iii) Non-presentation of a proper procedure by the above mentioned committee to collect the loans granted at least from the cinema halls which are functioning at present, in installments or on long term basis.

(iv) Despite of having informed earlier, failure in obtaining the approval from the Cabinet by submitting a Cabinet Paper to write off the remaining amounts except for the loan amount that could be recovered as mentioned in (ii) and (iii) above.

(b) Action had not been taken even by the end of the year under review to obtain legal ownership and account the value of the land bearing assessment No.303 at Bauddaloka Mawatha on which the building of the Corporation is located.

(c) The value of Treasury Bills and Treasury Bills Repurchasing was amounted to Rs.273,214,772 and investments had been made in the same bank continuously. However, the attention of the Management had not been given for investing on more beneficial interest rates by calling for quotations from the State Banks in the Primary Market.

4.3 Transactions of Contentions Nature

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The following Observations are made.

(a) According to the financial Statements, an expense of Rs.44,394,717 had been accounted for the Presidential Film Festival held on 31 March 2017 and following observations were made in this regard.

(i) Even though, an institution should be selected for this festival by competitive bidding in terms of 3.2.1 of the Procument Guidelines, deviating from that and contrary to the Cabinet Decision No.08/2253/338/043 dated 2 December 2008 of allowing only advertising activities and advertising programs to the Selacine Institution, stage decoration, lighting and artistic activities had been given to the Selacine Institution.

(ii) For this award ceremony, the total cost estimate had been prepared by the Corporation amounted to Rs.38,170,000 and approval from the Board of Directors had been obtained. Even though only a sum of Rs.19,400,000 had been allocated for the Event Management in the estimate, the Corporation had entered in to a contract with Selacine Institution on 23 February 2017 for the amount of Rs.27,682,469 (without taxes). Hence Rs.8,282,469 had been contracted and paid against the approval of the board of directors.

(iii) Six reports had been submitted by the Technical Evaluation Committee regarding this activity and out of that, 2 reports dated were 30 March 2017. The ceremony had been held on 31 March 2017 and another 2 reports had also been submitted after the ceremony. Therefore, it was observed that the role of the Evaluation Committee had not been done in proper manner.

(iv) An unusual sum of Rs.7,654,750 which was consist of Rs.3,103,750 for stage decoration of the Bandaranayaka Memorial Hall, a sum of Rs.1,943,500 for the stage lighting system and Rs.2,587,500 for the other artistic activities had been included in the above (ii) contracted amount of Rs.27,682,469.

(v) Even though only Rs.1,955,500 included for food and beverages in the contracted amount of Rs.27,682,469 with the Selacine Institution, Rs .6,250,000 had been paid to the Selacine Institution at the time of audititing. Therefore, Rs 4,294,500 had been paid contrary to the agreement.

(vi) According to the accounts presented, Rs. 44,394,717 had been shown as total expenditure for the award ceremony and Rs.9,854,285 had been identified as payable to Selacine Institution and accounted as an accrued expenditure in the accounts exceeding the contracted amount. However, the Board of Director's approval had not been obtained for the above accrued expenditure and Journal vouchers had been certified by the accounting officer. Further, no bills and other evidence had submitted to the audit to prove the above accrued expenditure.

(vii) Even though, contracted amount with the Selacine Institution was Rs. 27,682,489 for the Presidential Award Ceremony, Rs. 27,000,000 had been paid as at audited date and according to the financial statements, further Rs. 9,854,285 had been accounted as accrued expenditure for the year ended 31 December 2017. Accordingly, it was observed during the audit that it had been planned to pay in excess of contracted amount.

(b) (i) The liquor permits had been issued in the year under review to 18 cinema halls of the Ridma Circuit since many years and 29 cinema halls of the other circuits during the year without any connection whatsoever with the objective of the Corporation and without being based on legal provision. In terms of permits issued, liquor should be sold only to viewers. However, during the physical inspection of 02 theaters in Sabaragamuwa Province in November 2017, the tickets issued for the nine days were 04 ,while the income from liquor sales was Rs.405,690.Therefore, it was observed that liquor had been sold to people who were not viewers.

(ii) The issue of liquor permits under state patronage is an action against the "Mathata Thitha" policy of the Government of Sri Lanka and even in instances of screening family films and children's films, the recommendation of liquor permits for cinema halls to enable intake of liquor observed as a contentious matter.

4.4 Operating Activities

According to the Financial Statements presented, the total recoverable amount as at end of the year under review was Rs.578, 661,380 consisting of film producers, other loans and staff advances. Out of that, Rs.161,470,386 for impairment adjustment, Rs.119,490,277 for provision for surcharge and Rs. 4,618,805 for provision for interest for production loans had been made. However, it was observed during the audit that, the recoverability of Rs. 285,579,469 which is 49 per cent are doubtful.

4.5 Underutilization of Funds

The monthly average balance of 8 bank current accounts of the corporation amounted to Rs.50,503,509 and an attention had not been paid to invest surplus funds in short term investments.

4.6 Idle and Underutilized Assets

The following observations are made.

(a) The stock of negative films and chemicals sum of Rs.870,659 had been unused since the year 2014.

(b) Over 500 library books provided to the library by the welfare society of the Head Office were being decayed due to stacking them in an unprotected manner in the Sarasawi Studio in Kelaniya.

4.7 Staff Administration

The following observations are made.

(a) The number of vacancies of the Corporation as at 31 December 2017 stood at 71 and the approved cadre had not been reviewed, according to the present requirements. Hence, 02 Essential posts staff grade had been vacant from long period and due to that, it was observed that there was no proper guidance and monitoring, when preparing plans ,setting up targets and monitoring in order to achieve those targets.

(b) An officer with at least 10 years experience at senior management level after obtaining a post graduate, should have been appointed as General Manager in terms of 4.1.1 of Scheme of recruitment of the Corporation, an officer with no qualifications had been recruited on contract basis and sum of Rs.1,671,808 had been paid as salaries and allowances during the year under review without approval of the Department of Management Services.

(c) Deviating from the Scheme of recruitment and without the approval of the Board of directors or approval of the Department of Management Services with the recommendations of the secretory to the Ministry, a driver had been requited and Rs.738,000 had been paid as monthly allowances and overtime.

5. Sustainable Development

5.1 Achieving Sustainable Development Goals

Every public institution should act in compliance with the United Nations “agenda” for the year 2030 for the sustainable development. and the corporation was aware about how to act in respect of the functions coming under own scope relating to the year under review. The following observations are made thereon.

(a) Although the existence of an accurate data base for the measurement of performance was essential, the corporation had failed to create an accurate data base for the measurement of achieving of sustainable Development Goals.

(b) As a result of not performing a proper coordination with the other institutions while being prepared to achieve Sustainable Development Goals, it was observed that the pre-preparation of plans to achieve targeted objectives and the status of pre-preparation process was at a very slow condition.

6. Accountability and Good Governance

6.1 Procument

Even though, according to section 4.2.1(b) and 4.2.2 of Procument Guidelines, a Master Procument Plan including expected procument activities at least for a period of 3 years and a procument time table should be prepared, it had been prepared only for the year under review.

6.2 Internal Audit

Even though according to the approved cadre, an Internal Audit Division should have 3 permanent Audit Assistant posts, non-had been employed as at 31 December 2017. Accordingly, it was observed the corporation had not paid sufficient attention over internal audit activities.

6.3 Tabling of Annual Reports

Annual Reports for the years 2015 and 2016 had not been tabled in Parliament even as at 24 August 2018 in terms of 6.5.3 of the Public Enterprises Circular No.PED/12 dated 02 June 2003.

7. Systems and Controls

Deficiencies in systems and controls observed during the course of audit were brought to the notice of the Chairman of the Corporation from time to time. Special attention is needed in respect of the following areas of control.

Areas of Systems and Control	Observations
(a) Assets Control	(i) Failure to take necessary actions with regard to the idle assets of the Studio. (ii) Failure to maintain library books in protected manner. (iii) The inventory had not been properly maintained to identify receipts and issues an easy manner.

(b) Debtors Control	(i) Failure to take necessary actions against the outstanding loan balances of over 10 years. (ii) Lack of proper supervision over loan agreements. (iii) Non establishment of a system or division to recover loans.
(c) Revenue Control	(i) Lack of supervision in recovery of film rentals and annual taxes. (ii) Payments of Producer's rent income without confirming the proceeds from the cinema halls.
(d) Credit Control	In terms of agreements, film promotion loan had not been recovered from first income.
(e) Control of Computer Software Systems.	(i) Password had not been given to the each post of the Staff. (ii) Changing date in main file by the non staff officers and lack of supervision. (iii) Backups have been at the same place. (iv) Risk of accessing to the Pay Processing System through the Team viewer software and internet facilities.