Insurance Regulatory Commission of Sri Lanka - 2019

1.1 Qualified Opinion

The audit of the financial statements of the of Insurance Regulatory Commission of Sri Lanka for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 and the statement of financial performance, statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, 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 provisions of the National Audit Act, No. 19 of 2018 and Finance Act, No.38 of 1971. My comments and observations which I consider should be presented in Parliament appear in this report.

In my opinion, except for the effects of the matters described in Paragraph 1.5 of this report, the financial statements give a true and fair view of the financial position of the Commission as at 31 December 2019, and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

1.2 Basis for Qualified Opinion

My opinion is qualified based on the matters described in paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAS). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Public Sector Accounting Standards and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Commission's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Commission or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Commission's financial reporting process.

As per Sub-section 16 (1) of the National Audit Act, No. 19 of 2018, the Commission is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Commission.

1.4 Scope of Audit

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.

- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Commission's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Commission to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Commission, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Commission has complied with applicable written law, or other general or special directions issued by the governing body of the Commission*;*

- Whether the Commission has performed according to its powers, functions and duties; and

- Whether the resources of the Commission had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Financial Statements

1.5.1 Non-compliance with Sri Lanka Public Sector Accounting Standards

Non-compliance with reference to the particular Standard	Comments of the Management	Recommendation
(i) A sum of Rs.2,674,746 out of Rs.12,280,195 which was deposited in a private institution so as to recover within 05 years, had been indicated as current assets in the statement of financial position contrary to Sri Lanka Public Sector Accounting Standard 1.	According to deposits paid as per the lease agreement, the deposit of Rs.9,607,449 had been paid before a period of one year and accounting it as non-current assets is accurate. The deposit of Rs.2,674,946 had been paid in the year 2019 and as it is a period less than a year, it is brought to account as non-current assets. The value relating to non-current assets is transferred in the year 2020.	Taking action in terms of requirements of the Standard.
(ii) Useful life of assets should be reviewed annually and the estimated error revealed accordingly should be revised in terms of Sri Lanka Public Sector Accounting Standard 3. However, action had not been taken accordingly in respect of fully depreciated assets costing Rs.36,147,267 but still in use.	In terms of Sri Lanka Public Sector Accounting Standard 7, the useful life of motor vehicles has been examined in the year 2018 and the re-valued profit has been brought to account accurately in the year 2018. Even though the Audit Committee has not approved the revaluation of other assets,	Taking action in terms of requirements of the Standard.

	approval has been given by the said Committee only for revaluation of motor vehicles once in 03 years.	
(iii) Action had not been taken to recognize a computer software valued at Rs.4,723,000 purchased in the year 2019 as an intangible asset of the institute and to bring it to account and to amortize it according to Sri Lanka Accounting Standard 20. Moreover, a payment of Rs.844,167 made for this software in the year 2019, had been indicated under pre-payments. Moreover, a written agreement entered into with the supplier relating to this software had not been made available to Audit.	A sum of Rs.844,167 paid for this software indicated as pre-payments, is debited monthly to the Income and Expenditure Account. As this is a licence fee paid annually, the sum of Rs.4,723,000 indicates the licence fees payable for 05 years. This cannot be brought to account as an intangible asset due to payment being made annually and the benefit thereof is not received for more than one year. As such, this will be debited to the Income and Expenditure Account.	Taking action in terms of requirements of the Standard.

1.5.2 Non-compliance with Laws, Rules, Regulations, Management Decisions etc.

Reference to Laws, Rules, Regulations etc.	Non-compliance	Comments of the Management	Recommendation
(i) Section 6(2)(d) of the Regulation of Insurance Industry Act, No.43 of 2000	All sums of money as may be received by the Commission in the exercise, performance and discharge of its powers, duties and functions, shall be identified as income thereof. However, a sum of Rs.493,068,161 received in the year 2019 as CESS and the interest income of Rs.574,313,018 relating to the Protection Fund of insurance trustees of the year 2019 had not been identified as income of the Commission for the year under review and it was observed that this situation existed in the preceding year as well.	According to Note 7 in the annual financial statements of the year 2019, all income received are separately recorded in PPF. Income of the Commission is clearly recorded in the income statement and income received to the Policyholder Protection Fund is separately recorded as income of Insurance Policyholder Fund.	Action should be taken to identify and account the income accurately.

(ii) Section 48 (1) of the Regulation of Insurance Industry Act, No.43 of 2000.	Every insurer shall, in respect of insurance business transacted by the insurer, cause an investigation to be made by an actuary at the end of each financial year into the financial condition of such insurance business, including a valuation of its assets and liabilities in respect of that business, and shall cause an abstract to be made in accordance with rules made in that behalf by the Board. Nevertheless, the post of Actuary of the Commission remained continuously vacant and accordingly, the Commission had failed to put in place a well-established methodology to review actuarial report presented by the insurer per year.	An Actuarial Consultant has been appointed by the Finance Sector Modernization Project implemented under the World Bank assistance and these activities are being carried out by the said Consultant at present.	Action should be taken to expedite the reviewing of actuarial reports.
(iii) Section 9.14 of Public Enterprises Circular No. PED/12 dated 02 June 2003	A Manual of Procedure should be prepared and thereafter with the approval of the Board of Directors the concurrence of the Secretary to the Treasury should be obtained therefor. Nevertheless, the concurrence of the Secretary to the Treasury had not been received for the Manual used by the Commission even by 31 July 2020. However, it was observed that activities such as payment of advances, granting vehicle loans were being in progress in accordance with the unapproved Manual of Procedure.	Manual of Procedure has been forwarded for Treasury approval on 30.03.2017. By the Letter No.PE/REG/IRCSL/PR dated 05.04.2018, the Public Enterprises Department has informed us that there is a delay in granting relevant approval due to issues found in the existing system for the evaluation of Manual of Procedure. Likely, Insurance Regulatory Commission of Sri Lanka follows the Manual of Procedure in its institutional activities in terms of the provisions of Regulation of Insurance Industry Act under the approval of the Commission.	Action should be taken to obtain concurrence to be obtained to the Manual of Procedure in terms of relevant circular provisions.

(iv) Section 07 of the Inland Revenue Act No.24 of 2017.	It was observed that the Income Tax totalling Rs.1,067,381,178 pertaining to the year under review to be liable to Income Tax of the assessment year of the Commission had not been taken into account in the computation of liabilities	In terms of Inland Revenue Act No.24 of 2017, Income Tax value for the surplus of the Insurance Regulatory Commission of Sri Lanka has been paid to the Inland Revenue Department. The requests relating to exemption of tax for Cess and interest income received by the Policyholder Protection Fund (PPF) have been forwarded to the Ministry of Finance in writing and several discussions thereon have been conducted. A decision in that connection is expected. We have furnished the copies of letters sent by the Insurance Regulatory Commission of Sri Lanka to the Ministry of Finance on that matter to the Audit.	Action should be taken to compute Income Tax in accordance with the provisions of Inland Revenue Act No.24 of 2017.

2. Financial Review

2.1 Financial Results

The operating result for the year under review had been a surplus of Rs.129,218,719 as compared with the corresponding surplus of Rs.41,337,937 for the preceding year, thus observing an improvement of Rs.87,880,782 in the financial result. The increase in the income had been the main reason for the said improvement.

2.2 Trend Analysis of major Income and Expenditure items

Income of the year under review showed an increase of 82 per cent, while staff cost and finance and other expenses increased by 42 per cent and 909 per cent, respectively. However, an increase of Rs. 108,021,452 of the Surplus Before Tax was shown as compared with the preceding year, and it was an increase of 250 per cent as compared with the preceding year.

3. Operational Review

3.1 Management Inefficiencies

Following observations are made.

Audit Observation	Comments of the Management	Recommendation
(i) Insurance companies applying for registration shall deposit to the Treasury such amount as may be determined by the Board as per the Section 13 (1) (c) of the Regulation of Insurance Industry Act. A difference of Rs. 3,700,000 was observed between the schedule of such deposits maintained by the Department of Treasury Operations and the schedule maintained by the Commission. As such, it was observed that the reasons for the relevant difference were not compared and the deposit registers were not maintained in an updated manner.	Names or other details of payers are not mentioned in the relevant deposit report of the Department of Treasury Operations. Therefore, it is impossible to ensure whether these deposits have been received for this purpose. However, since names and all information is available in the report maintained by the Commission, we consider that the report maintained by us is accurate.	Actions should be taken to update and maintain the relevant details.
(ii) Commission had not taken action to maintain information on deposits mentioned in paragraph (a) above relevant to the 11 insurers that had been registered prior to the year 2007.	It has been informed that it is expected to update.	Relevant information should be maintained properly and completely.
(iii) Action had not been taken by the Commission even by the end of the year under review to settle the balance of Withholding tax amounting to Rs.1,208,602 mentioned as receivables in the financial statements from prior to the year 2016.	The reason for existence of a tax burden of Rs. 1,208,602 not set off in the years prior to the year 2016 was that the Insurance Regulatory Commission had no income tax paying liability during that period. In terms of Inland Revenue Act, No.10 of 2006, Insurance Regulatory Commission of Sri Lanka had been exempted from income tax.	Action should be taken to settle the balances.

	Income tax should be paid in terms of the new Act, No.24 of 2017 and it was not possible to set off the Withholding tax in the years prior to 2016.	

3.2 Human Resources Management

Audit Observation	Comments of the Management	Recommendation
As the Commission shifted towards a surveillance system based on Risk Based Capital (RBC) method introduced in place of the solvent legal framework of the insurance companies from the beginning of the year 2016, five executive level posts approved in year 2016 for establishment of an Actuary Unit were remained vacant.	Recruitments have been made for the two executive posts, and action is being taken to publish newspaper advertisements and to make recruitments for the vacant posts of Actuary and Assistant Actuary.	The vacancies in the staff that may affect the performance of the Commission should be filled promptly.