**National Insurance Trust Fund – 2020**

## 1. Financial Statements

### 1.1 Disclaimer of Opinion

The audit of the financial statements of the National Insurance Trust Fund ("Fund") for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the statement of comprehensive income, 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 report to Parliament appear in this report.

I do not express an opinion on the accompanying financial statements of the Fund. Because of the significance of the matters discussed in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

### 1.2 Basis for Disclaimer of Opinion

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

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report.

### 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 Accounting Standards, and for such internal control as management determine 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 fund'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 intend to liquidate the fund or to cease operations, or has no realistic alternative but to do so.

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

As per Section 16(1) of the National Audit Act No. 19 of 2018, the fund 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 fund.

## 1.4 Auditor's Responsibility for the Audit of the Financial Statements

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, misrepresentations, 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 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 fund'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 fund 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 fund, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the fund has complied with applicable written law, or other general or special directions issued by the governing body of the fund;
- Whether the fund has performed according to its powers, functions and duties; and
- Whether the resources of the fund had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

**1.5 Audit Observations on the preparation of Financial Statements**
**1.5.1 Internal Control over the preparation of financial statements.**

| Audit Observations | Management Comment | Recommendation |
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| (a.) Weak Control Environment had been observed due to following reasons.<br><br>(i.) There were three (03) vacant positions from four (04) key management positions. The Chief Executive Officer and the Assistant General Manager – Finance positions had been filled on acting basis in addition to their permanent responsibilities. The Assistant General Manager – Operation position is vacant since the carder approved date of 01 November 2016. Further five (05) positions had been vacant out of seven (07) management positions and three (03) Management positions had been filled on acting basis in additions to their permanent responsibilities. Therefore, the possibility of development of internal controls, effective monitoring of implementation of internal control system and developments to strengthen the internal controls is minimized. | However, even though, it is essential to fill those vacancies for the smooth functioning of the organization to achieve organizational goals, the entity has done recruitment processes for the actuarial manager and risk Engineer. These vacancies could not be filled due to the lower remuneration scales offered by NITF compared with the industry, since NITF has to follow the “Management Services Circular No 02/2016”. Further. the government has stopped all recruitments since 2019 onwards. NITF expects to fill those vacancies with the future operational requirements as per the corporate plan and needs to obtain special approval from the Ministry to recruit under the prevailing regulation. | The management should take necessary actions to fill key management positions and strengthen the control environment. |
| (ii.) It was observed that the actuarial function, risk management function, investment function and research | It should be noted that although the actuarial function, risk management function and investment function | The management should take necessary actions to establish those key |

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| | and development function had not been effectively carrying out due to unavailability of responsible divisions and officials with required skills specified in the recruitment procedure to carrying out those functions. Therefore, timely identification of risks and implementing strategies to mitigation of those risks, the provision of accurate information to make actuarial estimations could not be effective. | were not filled with dedicated staff doesn't mean that those functions was not carried out successfully and effectively or not operated at all.<br>With regard to the actuarial function, this function was outsourced to appointed actuary M/s NMG consultants Pvt. Ltd. which is a one of the leading actuarial firm in the local as well as in the global context. They effectively involve in regulatory reporting including IBNR valuations and solvency, RBC and other certifications to IRCSL with the support of finance division. Even IRCSL has not questioned NITF about the effective functioning of the function so far.<br>Investment functions- NITF can only invest in government securities as per the act. Investment functions which is not complex<br>Therefore, NITF deny the fact that "timely identification of risks and implementing strategies to mitigation of those risk, provision of accurate information to make actuarial estimations could not be possible".<br>We are aware of the value of having dedicated staff and have taken necessary actions already to fill vacancies.<br>However, as pointed out above, the current situation of the country and importantly low salary scales of the NITF have adversely affected to delay in attracting suitable human capital. | divisions with required resources for effective running of those functions. |
| (iii.) | An Internal Audit and the Audit Committee had not been functioned for the year 2020. Therefore, the review and evaluate internal control systems on regular basis, review financial statements to ensure compliance with Accounting Standards had not been carried out. | NITF agree that internal audit and audit committee had not been functioning due to the vacant position of the head of the division. Filling the position and functioning of audit committee was delayed due to Covid 19 pandemic situation that prevailed during the year 2020. | The management should ensure the effective functioning of the audit committee. |

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| (iv.) | A fraud done by an employee in the Agrahara Insurance Scheme had been discovered accidently in October 2022. This fraud had been committed from the year 2018 and the discovered financial loss as per the internal audit report is Rs. 5,136,000. This was happened due to lack of design and implementation of the sound internal control system with proper supervision and monitoring. Further, this evident that the non-existence of the sound system of control environment for the fund | No answers provided by the management. | The management should ensure sound system of internal control to avoid frauds and minimize the fraud risk. |
| (b.) | An integrated system for handling Agrahara Claims from acceptance of the claim applications to settlement of the claims and to identify the claim liabilities at the year-end for financial reporting process had not been available for the fund. | Agreed with the observation. However, Agrahara claim division is functioning with an integrated system except acceptance and identification of claim liability which is to be done a very first stage of the claim process. These initial stages of claim processing system modifications were considered in the corporate plan 2022- 2025 and it is currently progressing. | The management should take necessary actions to introduce sound system of internal control for the Agrahara insurance scheme. |
| (c.) | The transactions of the Strike, Riot, Civil Commotion and Terrorism Fund (SRCC & Tr Fund) had been recorded in the excel files using source documents and at the end of the year all transactions recorded in the excel files had been updated to a manual ledger and submitted to the audit. Even though, the facility had been provided in the SAGE Accounting System in the year 2019, that facility had not been used for the financial reporting process of the Strike, Riot, Civil Commotion and Terrorism Fund. | Both manual and SAGE accounting system were used simultaneously for accounting by SRCC & TC. SAGE accounting system was fully used in 2020 for accounting by SRCC & TC for the whole year. The system access is available for checking the system via the same user ID and password given to auditors. | The management should ensure that timely update of financial information systems and ensure the information integrity. |
| (d.) | Claims had been recognized as one item of income and expenditure in the financial statements for Agrahara Normal, Silver and Gold Premiums. Since there was no | Agreed with the observation on the basis that unavailability of comprehensive updated data base. However, in the existing system, the Agrahara normal, silver and gold | The management should take necessary actions to ensure effective system for the premium collection and claim |

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| | proper and updated database, it is difficult to obtain evidence for contributions made to the fund and claims incurred from each Agrahara Insurance Schemes and to obtain a detailed record of the monthly contributions made by each institution and by each policy holder to the Fund. | premiums can be provided separately except few institutions. However, a new comprehensive information system has been implemented with the support of the Ministry of Finance and will be in operation in the near future. | processing for Agrahara insurance scheme. |
| (e.) | No proper system in place for handling transactions and keeping records in the reinsurance section while it is maintained in manually. | Agreed with the observation for claim handling process of RI segment. Accounts receivable module of Sage ACCPAC is currently in operation for underwriting processes. Further, NITF is currently in the process of developing system for claim handling of RI division as per corporate plan 2022-2025. | The management should ensure that the effective reporting system in place. |

**1.5.2 Non-Compliance with Sri Lanka Accounting Standards**

| Non-Compliance with the reference to particular Standard | | Management Comment | Recommendation |
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| (a.) | **LKAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors**<br>A re-insurance premium of Rs. 148,380,847 received from Agriculture and Agrarian Insurance Board (AAIB) for agriculture insurance scheme had been recognized for the gross written premium in the year 2019. Further, this revenue had been returned to the Agriculture and Agrarian Insurance Board in the year 2020 on the basis that, the NITF has no any legal authority to accept this payment. This error correction had not been adjusted in the financial statements in the period under review by restating the comparative amounts for the year 2019 presented in which the error occurred in accordance with the paragraph 42 of the standard. | On the request of Secretary to the Ministry of Agriculttue, Rural of economic affairs, Livestock Development, Irrigations and fisheries and Aquatic Resource Development, NITF has accepted reinsurance crop aggregate excess of loss reinsurance cover extension to AAIB. Accordingly, total premium of LKR 148,380,8471- received in 2019.In the meantime, NITF board instructed to get the approval from Ministry of Finance. Board decided onl2l08l2020 to the refund the funds in full. Accordingly, funds were refunded on 2S/0912020 to AAIB. Kindly note that this is not an accounting error to restate the comparative as suggested. | The management should adjust material prior period errors in the financial statements retrospectively. |

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| (b.) | **LKAS 12 – Income Tax**<br>The fund had not recognized the deferred tax liability amounting to Rs. 934,018,739 as at 31 December 2020. Further, no accounting policy had been disclosed for accounting of deferred tax. | Agree with the observation. Deferred tax calculation will be made and disclosed in future reporting. | The management should take necessary actions to accounting for deferred taxation. |

**1.5.3 Accounting Deficiencies**

| | Audit Observation | Management Comment | Recommendation |
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| (a.) | According to the accounting policy of the fund for Proportional Treaty Re-Insurance Agreements, the insurance premium shall be recognized when the periodic advice received from cedants with the leader confirmation. However, contrary to the accounting policy the re-insurance premium relevant prior to 2020 of Rs. 628,756,431 had been recognized for the year under review. Further re-insurance premium of Rs. 718,436,154 relevant for the period had been recognized for the year 2021, due to the leader confirmation and periodic advice had been received in delay. Therefore, the reinsurance revenue for the year had been understated by Rs.89,679,723. | The policy for the recognition of reinsurance premium was disclosed in the financial statements and it is in line with the policy and not contrary as mentioned in the query. The amount invoiced Rs 628,756,431 and, Rs. 718,436,154 have been issued in 2019 and 2020 respectively by the reinsurance division as they received leader confirmation on the year in which it is recognized as premiums. Therefore, in light of the policy disclosed, this is not a violation of the policy at all. | The management should recognize the revenue in compliance with relevant accounting policy. |
| (b.) | According to the accounting policy for Non-Proportional Treaty Re-Insurance Agreement the insurance premium has been recognized based on the contractual premium already established at the start of the treaty Gross Written Premium (GWP) for the year. However, contrary to the accounting policy re-insurance premium relevant prior to 2020 of Rs. 78,341,182 had been recognized for the year under review. Further re-insurance of Rs. 639,615 relevant for the year had been identified in the year 2021. This was occurred due to required adjustments had not been made by reviewing the agreements with available additional information and developments at the end of the accounting period. Therefore, the revenue for the year under | The policy for the recognition of reinsurance premium was disclosed in the ' financial statements and it is in line with the policy and not contrary as mentioned in the query. The amount invoiced have been issued in 2019 and 2020 by the reinsurance division as they received leader confirmation on the year in which it is recognized as premiums. Therefore, in light of the policy disclosed, this is not violation of the policy at all. | The management should recognize the revenue in compliance with relevant accounting policy. |

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| | review had been overstated by Rs.77,701,567 | | |
| (c.) | According to the accounting policy for Facultative Re-insurance Agreement the insurance premium had been recognized after receiving the leader confirmation. Therefore, the re-insurance premiums of Rs.211,129,506 relevant for the prior periods had been recognized for the year under review. Further, re-insurance premium of Rs. 50,279,153 relevant for the period had been recognized in the year 2021. Therefore, the revenue for the year had been overstated by Rs.160,850,353. | The policy for the recognition of reinsurance premium was disclosed in the financial statements and it is in line with the policy and not contrary as mentioned in the query. The amount invoiced have been issued in20I9 and2020 by the reinsurance division as they received leader confirmation on the year in which it is recognized as premiums. Therefore, in light of the policy disclosed, this is not a violation of the policy at all. | The management should recognize the revenue in compliance with relevant accounting policy. |
| (d.) | Premium receivable from Inward Reinsurance as per the financial statement and the Control General Ledger account is Rs. 1,267,806,451. However, as per the age analysis the balance is Rs. 1,258,772,697. Therefore, a difference of Rs. 9,033,754 had been observed. | Agreed with the observation. | The management should identify the differences in timely manner and take appropriate actions to rectify those differences. |
| (e.) | A difference of Rs. 3,537,190 had been observed between staff distress loan balance in the financial statements and the detailed schedule submitted for the audit. | We agreed with the observation.<br>This difference is mainly due to long outstanding opening balance errors. These differences will be submitted to the board for further actions. | The management should identify the differences in timely manner and take appropriate actions to rectify those differences. |
| (f.) | The carrying value of treasury bonds has been overstated by Rs. 139 Mn as of 31 December 2020. The differences have been occurred due to the error in market price used by the fund for fair value calculation | The NITF has calculated fair value on Treasury bond using average price published by public debt department of the Central Bank in arriving at the market value. However, as per the detailed audit conducted by a consultancy firm on Investment, they recommend NITF to use selling price published by Public Debt Department of the Central Bank in arriving at the market price. Therefore, NITF has changed the rate use for the fair valuation. This difference is due to application of average price by NAO<br>Agreed to change the policy | The management should take necessary actions to disclose valuation method used and use that valuation technique consistently. |

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| (g.) | The carrying value of Treasury Bills had been overstated by Rs. 1.08 Mn as of 31 December 2020. The differences have been occurred due to the error in coupon rate used by the fund for fair value calculation. | The NITF has calculated fair value on Treasury bill using average price published by Public Debt Department of the Central Bank in arriving at the market value. However, as per the detailed audit conducted by consultancy firm on Investment, they recommend NITF to use selling price published by Public Debt Department of the Central Bank in arriving at the market price. Therefore, NITF has changed the rate use for the fair valuation. This difference is due to application of average price by NAO. | The management should take necessary actions to disclose valuation method used and use that valuation technique consistently. |
| (h.) | The expenses amounting to Rs 1,598,006 for the year 2019 had been accounted in the year 2020. Therefore, the expenses for the year had been overstated and the profit for the year had been understated by the same amount | These accrued expenses which are relating to 2019, should have been recorded as expenditure in 2019 have erroneously recorded in 2020. However, as per the paragraph 06 of LKAS 08, Accounting Policies, Changes in Accounting Estimates and Errors, as this misstatement could not influence economic decisions of users (immaterial), this error is not required to be restated in 2019. | The management should ensure that appropriate processes in place to prepare financial statements on accrued basis. |
| (i.) | The re-insurance liabilities arised from the reinsurance agreements due to adjustment premium of National Natural Disaster Insurance Scheme (NNDIS) for the years 2017/2018 amounting to Rs. 123,387,679 and Adjustment premium of Retrocession Re-insurance for the year 2018/2019 amounting to Rs. 466,292,684 had not been recognized in the financial statements | Minimum deposit premium of LKR 401,153,424/- for extended period of NNDIS for the year 2018/19 which was approved by the Cabinet was recognized in 2019. However, Adjustment premium of retrocession and NNDIS for the 2018/2019 amounting to LKR 589,680,363/- which was not approved by the Cabinet was not provided in financial statements up to 2021 since the acceptance of this liability is questionable. Subsequently, after receiving the Attorney General's opinion in December 2021, NITF liability is probable subject to the concurrence and approval of IRCSL and special cabinet approval. However, there is no impact to the financial results for the period under review. | The management should review the existing agreements at the end of each reporting period to identify the liabilities arise from provisions of those agreements and account accordingly. |

### 1.5.4 Inappropriate Valuation or Estimation

| | Audit Observation | Management Comment | Recommendation |
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| (a.) | Since the fund had not carried out proper evaluation for the long outstanding provisions for non-flood claims existed as at the balance sheet date the accuracy of the provision cannot be ascertain. The provision for non-flood claims of Rs.427,550,703 had been outstanding for more than two to five years and provisions amounting to Rs.156,589,534 were outstanding for more than five years. | However, subsequently, by getting the confirmations by relevant insurance companies, a significant amount of long outstanding was removed from the provision for non-flood claims. | Management should evaluate the long outstanding balances and take necessary actions to clear those balances. |
| (b.) | According to the gazette No. 1791/4 of 21 December 2012, the mandatory cession is 30 per cent for general (non-life) reinsurance. However, the fund had allocated 100 per cent loss as a provision. Therefore, the reinsurance provision had been overstated by Rs. 7,210,000 for the year under review | Agreed with the observation. However, those errors were rectified subsequently. | The management should properly review the appropriateness of the provisions. |
| (c.) | Reinsurance payable amounting to Rs. 801,513 is still in the financial statements even though the insurer has informed that there was no liability as of 05 October 2016. | Agreed with the observation. This claim was removed during the financial year 2021. | The management should assess the reinsurance of liabilities at the end of each reporting period and made adjustments accordingly. |
| (d.) | No evidence such as board approval, actuary valuation or any other documents had been provided to prove the reasonability of estimated provision for Agrahara claims provision amounting to Rs.510,530,810 for the year ended 2020. | Estimation of claim provisioning for Agrahara was obtained from the head of Agrahara claim. Therefore, the claim department experience and judgment has been based on the provision made in the year end 2020.This is an additional provision made in financial statements in regard of the backlog of claims built up over a period of time due to the effect of COVID 19. Kindly | The management should assess the reasonability of provisions at each reporting period, account accordingly and provide information for the audit. |

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| | | note that these claim provisioning is in relation to reported claims and therefore, no need actuarial valuations. In fact, the actuary has considered this provisioning figure when they are doing valuations of IBNR. It is not practical to submitted to the board each divisional provisions figures, instead Agrahara claim provisioning was discussed and agreed at the board meeting when the financial statements for year 2020 were approved. | |
| (e.) | No assessment had been made for the Motor Claims payable balance amounting to Rs. 10,323,235 for the year 2020 which had been continued from the year 2019 without any assessment for the year under review. | These SRCC long outstanding claims are intimated in previous years and approved by the relevant committees. However, since documents are pending for settlement, these balances are long outstanding balances. After getting confirmation for the requirement for settlement and necessary approval, we will reverse the provision | The management should assess the reasonability of liabilities at each reporting period and account accordingly. |

### 1.5.5 Documentary Evidences not made available for Audit

| Item | | Amount Rs. | Evidence not available | Management Comment | Recommendation |
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| (a.) | Staff loan receivable | 54,274,121 | Loan Register | Staff loan register has already been emailed on 30th June 2022 | The management should ensure the availability of information timely for effective audit function. |
| (b.) | Income tax receivable | 22,465,243 | Tax computation and confirmations | We have provided the total income tax calculation which is amounting to Rs. 1,220,442,752. Therefore, it cannot be stated that Rs. 22,465,243 is an understatement. However, when intersegments are concerned, only SRCC segment has income tax liability and the other segment has tax losses carried forward. | |
| (c.) | Re-insurance premium for agriculture insurance scheme | 148,380,847 | Receipt and payment details | The unavailability of the file is due to handing over the file to the former CEO to reply a Finance Ministry request who is | |

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| | | currently interdicted. On 16/12/20I9 the interdiction letter has been issued against CEO and he was restricted from entering the NITF premises.<br>Therefore, NITF Management has no access to the files he has in his custody. Even though, the initial he was missing, please note that NITF is in a position to provide requested evidences as well as any other information as and when required. | |

**1.6 Accounts Receivable**

| Audit Issue | Management Comment | Recommendation |
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| The reinsurance premium receivable amounting to Rs.142,595,979 was outstanding for over one (01) year which represent 11.3% from the total Reinsurance Premium Receivable and an amount of Rs. 148,466,031 was outstanding over two (02) years which represent 11.8% from total receivable amount. The amount of Rs. 151,033,057 was outstanding over three (03) years which represent 12% from the total outstanding balance. It was observed that adequate actions had not been taken to recover long outstanding reinsurance receivables. | The states of the ageing of outstanding balance 31/12/2021 is as follows. Therefore, above 3 years' balances were recovered 89% and stood at 16Mn. | The management should take necessary actions to recover outstanding balances. |

**1.7 Non-compliance with Laws, Rules, Regulations and Management Decisions etc.**

| Reference to Laws, Rules Regulations etc. | Non-compliance | Management Comment | Recommendation |
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| (a.) Sections 7, 31(2) and 49 (b) of Regulation of Insurance Industry Act No.43 of 2000 | Sixty-one (61) quarterly returns containing information as rules made in that behalf should be submitted to the Insurance Regulatory Commission. However, 16 quarterly returns had been submitted with delay | Please note that there are only 04 quarterly returns need to be submitted to IRCSL for a year. All these delays were due to the Covid 19 pandemic impacts such as travel restrictions, lock downs, cases of tested positive number of | The management should take necessary actions to avoid future delays in submission of regulatory returns. |

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| | of 38 to 285 days after considering the extensions granted by the Insurance Regulatory Commission due to COVID 19 pandemic. | staff etc. Further please note that since existing systems are not web based, reporting to work for preparation of accounts was required. However, it was informed to IRCSL about these delays periodically with reasons and possible date of submissions. Steps have already been taken to overcome these delays. | |
| (b.) Section 13(e) of the National Insurance Trust Fund Act No 28 of 2006 | According to the provisions of the act a general account in respect of the Fund and separate Individual accounts in respect of each member needed to be maintained. However separate accounts for individual members had not been maintained by the fund. | Individual accounts details are maintained in the information system; it is possible to access them using clients NIC. | The fund should comply with the applicable provisions of the Act. |
| (c.) Paragraph 23 of the National Insurance Trust Fund Act, No.28 of 2006 | According to the provisions of the act, the fund had not taken necessary actions to inspect records of the insurance companies to verify whether such insurance companies have invoiced and remitted amount accrued to the fund accurately. | Usually, Internal Audit division is carrying out income verification of insurance companies. However, due to the Covid pandemic, this verification was not executed. | The fund should comply with the applicable provisions of the Act. |
| (d.) F.R. 261(1) | The sequential order of the payment vouchers had not been properly maintained. | We noted the observation. Since the deadline for the financial statements were 28th February, we took the cutoff for the accrued expenses around 15th January 2020. All attached expenses were made at the end of January 2022. | The management should take necessary actions to maintain the payment vouchers in serial order. |
| (e.) F.R. 386(7) | Even though the cancelled cheques must be affixed to the counterfoil and retained in the cheque book. The fund has attached cheque counterfoils with the payment voucher. As a result, in the case of any misplacement of the voucher all the details related to cancelled cheques may get lost | As NITF is using continuous cheque roll for printing purposes it is not practically possible to file cheque counterfoil separately. Therefore, Cheque counterfoil is attached and filed along with the payment Voucher. In case of any misplacement of the voucher, all the details are available in the ACCPAC system where any voucher details cannot be changed after posting. However Cancelled | The management should adhere to the requirements in the financial regulations. |

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| | | | cheques are affixed to the counterfoil. | |
| (f.) | F.R. 395(b) | Bank Reconciliation Statements should be certified by the Paying Officer concerned, and made available to Audit for inspection. However, the Bank Reconciliation Statements prepared for eleven (11) bank accounts had been certified without name, designation and date. | The bank reconciliation statements will be amended to include responsible officer with name, designation and date for the current signing space given in the bank reconciliation for prepared by, checked by, certified by and approved by. | The management should adhere to the requirements in the financial regulations. |
| (g.) | F.R.396 | The procedure stipulated in the Financial Regulations had not been followed for the cheque remains un-cashed for more than six months from the date of issue. The sixty-one (61) lapsed cheques amounting to Rs. 3,501,599 in two (02) Bank Accounts had been observed as at 31 January 2021. | These unpresented cheques are related to Agrahara and Motor claim payments. NITF is currently sending reminders to customers by registered post. Based on their response, we will take unpresented amounts to the income or extend the validity period. | The management should adhere to the requirements in the financial regulations. |
| (h.) | Section 04 of Public Enterprises Circular No. PED 2/2015 dated 25 May 2015. | According to the provisions of the circular the cost of purchasing mobile phones should be personally born by the officers. However, the fund has purchased mobile phones for employees by incurring Rs. 2,432,371 for the years 2016 to 2020. | Please note that to meet business requirements NITF has purchased mobile phones and recorded as its assets (taken to the inventory) and allocated to staff for the use and when resign from the job or at the end of period the mobile phone allocated has to be returned to NITF. Therefore, this is not a reimbursement of private mobile phone referred in the circular. | The management should adhere to the requirements in the circular. |

**1.8 Investment Activities**

| | Audit Observation | Management Comment | Recommendation |
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| (a.) | Even though the investment manager's role has been defined in the paragraph 13 of the Investment Policy this position had been vacant since 30 August 2020. | We have recognized importance of employing an investment Manager. However, according to the Ministry of Finance circular issued on 20.11.2019 the vacancy of Investment manager cannot be filled as recruitments are temporarily stopped. | The management should ensure that effective functioning of the investment of funds. |
| (b.) | Even though as per the paragraph 17 of the Investment | With the vacancy of the Investment Manager position and with the Covid | The management should take necessary actions for |

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| | Policy the Investment Committee should meet at periodically and the responsibilities of the Investment Committee had been defined. However, the Investment Committee had not been met for the year under review | pandemic in 2020 investment committee had not been met. However, as per the Operational Manual for state owned enterprises issued by the Department of Public Enterprises Boards of SOEs with a consistent revenue of at least Rs. 30 billion per annum in the last two years must establish an Investment Committee (IC) in line with the investment policy established by the Board of Directors. However, NITF does not fallen under that requirement. | effective functioning of investment committee. |
| (c.) | There is no provision in the Investment Policy to review the Investment Policy on regular basis. Further, the Investment Policy had not been reviewed by the board after its implementation and incorporate required improvements to the policy on timely basis | Investment policy will be reviewed in the future after incorporating Investment Committee. | The management should take necessary actions to review the investment policy on regular basis. |
| (d.) | According to the investment policy, selection of investments is based on evaluation of economic conditions, interest rates behavior, future trends, and the operational cash flow requirement of the fund. However, there was no cash flow forecasts had been prepared to identify the excess cash flows and timing of those cash flows to take investment decisions in prudent manner | Cash flows are not prepared for a particular period. Depending on the nature of NITF business, liquidity requirement and fund availability is monitored daily before making investment decision about the tenner and amount. Therefore, decisions are taken based on actual figures not on cash flow forecast. Daily cash availability and excess funds are identified based on Daily balances and investment report. | The management should take action to prepare cash flow forecast to identify future cash flows and its timing to take investment decisions in prudent manner. |
| (e.) | The financial assets of the fund (Investments) amounting to Rs. 21,666,072,511 and which represented 79% of the total assets of the fund. However, the delegation of financial authority for investment decisions had not been defined in the Investment Policy based on the value of the investments and the sources of investments. All investments were approved only by the Investment | Since the daily investment decisions need to be taken, under delegation of Financial Authority, The Board had delegated its authority to relevant officials and Investment Committee | The management should delegate the financial authority based on the value of the investment and the sources of investment for effective functioning of the investment activities. |

Committee irrespective of the value and the sources of the investments.

## 2. Financial Review

### 2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs. 7,526,099,442 and the corresponding profit in the preceding year amounted to Rs3, 114,086,727. Therefore, an improvement amounting to Rs 4,412,012,715 of the financial result was observed. The reasons for the improvement were increase of net earned premium from amount of Rs. 1,027,001,050 , decrease of net benefits and claim expenses from amount of Rs. 4,124,801,551 and decrease of underwriting and acquisition cost from amount of Rs.440,830,904 when compared to preceding year.

### 2.2 Trend Analysis of major Income and Expenditure items

| Year | 2020 | 2019 | Variance Rs. | Variance as a percentage |
|---|---|---|---|---|
| Net earned premium | 17,475,027,816 | 16,448,026,766 | 1,027,001,050 | 6% |
| Other revenue | 1,387,023,110 | 1,269,216,686 | 117,806,424 | 9% |
| Net benefits and claims | (7,954,516,263) | (12,079,317,814) | (4,124,801,551) | -34% |
| Underwriting and acquisition cost | (1,614,860,946) | (2,055,691,850) | 440,830,904 | -21% |
| Other operating and administrative expenses | (409,175,576) | (552,685,117) | 143,509,541 | -26% |
| Income tax | (1,339,826,929) | 105,600,661 | -1,445,427,590 | -1,369% |
| Profit for the year | 7,526,099,442 | 3,114,086,727 | 4,412,012,715 | 142% |

### 2.3 Ratio Analysis

According to the financial statements and information's made available to the audit, some important ratios for the last three years were as follows.

| Ratio | 2020 | 2019 | 2018 |
|---|---|---|---|
| Retention ratio | 161% | 143% | 138% |
| Total claim ratio | 46% | 60% | 72% |
| Expenses ratio | 12% | 16% | 16% |
| Combine ratio | 57% | 76% | 87% |
| Revenue growth | 6% | 18% | 18% |
| Profitability ratio | 90% | 24% | 34% |
| Net profit | 40% | 18% | 21% |
| Return on Asset | 37% | 17% | 19% |
| Return on Equity | 83% | 43% | 47% |
| Liquidity ratio | 1.2 | 0.68 | 0.74 |
| Current ratio | 6.26 | 8.92 | 9.34 |
| Financial assets to total assets | 82% | 77% | 76% |
| Assets turnover | 1.34 | 2.46 | 2.17 |

## 3. Operational Review

### 3.1 Operational Inefficiencies

| Audit Observation | | Management Comment | Recommendation |
|---|---|---|---|
| (a.) | The recommendations made by the actuary in relation to data capturing, splitting major class of business, provide claim counts and claim handling expenses had not been discussed at the board level or the appropriate level of management to make required improvements to increase the data confidence level of the fund. | At present, keeping OS values are consistent with audited numbers. Further, from 2021 onwards, NITF followed a NITF experience for providing its claim handling expenses to estimate the Company specific indirect claims costs and no more use of industry experience. Most of the other recommendations are found difficult since its nature of the businesses of NITF, for example, Reinsurance and SRCC matters. However, IBNR results have been discussed at the time of submitting financial statements at the board level. | The management should take necessary actions to implement recommendations made by the actuary to improve data confidence level of the fund. |
| (b.) | An Actuarial Division was not established by the fund to collect, retain and provide required actuarial information | An actuarial division had not been established in NITF. Therefore, relevant data are being provided by finance division | The management should ensure the effective functioning of actuarial function. |
| (c.) | A documented policy for handling reinsurance claim process and to identify payable obligation had not been available for the fund. Hence, the fund identified and record reinsurance obligation from the primary intimation document. | There is no specific document set for the settlement of claims, it depends on nature of the policy, claim and class. Normally RI department assure that the mentioned documents before settle the claim. However, accordingly leader reinsurer terms and conditions are being used to settle claims. | The management should ensure availability of policies for major functions of the fund. |
| (d.) | The fund does not have an Approved Overtime Policy nor follow the provisions in the E-Code for processing overtime payments. | According to the delegation of authority, approved by the board of directors. It is mentioned that the limits of OT approvals. Accordingly, the entity has paid overtime payments based on the authority limits. Further, entity has not taken the approval for the board of directors to practice the provisions of OT in the E Code. | |

### 3.2 Transactions of Contentious Nature

| Audit Issue | | Management Comment | Recommendation |
|---|---|---|---|
| (a.) | According to the paragraph 3(1) of the Extraordinary Gazette No. 1542/11 dated 25 March 2008, the premium collected from the issuance of policies for strike, riot, civil commotion and terrorism shall be credited to the account maintained in a State Bank. However, the premium charged on non-motor policies had been credited to the fund after allowing 20% commission to the insurance companies without proper legal provisions to do so. The amount allowed from non-motor policies as commission for the year under review is Rs. 1,228,933,582. | Non-Motor gross premium (100%) are invoiced and recorded as premium income. However, 20% commission is need to be paid by NITF to cover the primary insurer's marketing and administration cost. The credit notes are received from general companies for 20% commission and supposed to be settled by NITF. Instead NITF allow to deduct the credit note commission payable from the invoice in the settlement. | The company should evaluate and take necessary actions for the legality of paying commission for premium collected from the issuance of non-motor policies for strike, riot, civil commotion and terrorism cover. |
| (b.) | According to the paragraph 3(1) of the Extraordinary Gazette No. 1542/11 dated 25 March 2008, the premium collected from the issuance of policies for strike, riot, civil commotion and terrorism shall also be credited to the account maintained in a State Bank. However, the fund has recovered only 12% of the total premium collected by the insurance companies for strike, riot, civil commotion and terrorism cover from motor policies without proper legal provision to do so. Therefore, the reduction of premium to the fund for the year under review is Rs.10,155,796,304. | As per the Motor XOL arrangement implemented for motor class from the inception of the SRCC & Fund was continued to practice by NITF, accordingly time to time the percentage of premium charged under the motor class Excess of Loss arrangement (XOL) was determined and thus the board decision no. 53-16 the money obtained as premium is 12% of the total premium collected by insurance companies. However, before deciding 12%, 15% of the total premium was requested in the same year as industry was opposed to that decision it was finally come down to 12%. In 2021 as management of NITF noted the opportunity to discontinue the present practice of XOL arrangement, it was decided to change the present practice of the Motor premium collection and accept 100% as per the Board Paper No. 172-03 liability in the motor insurance class with 100% premium with effect from | The company should evaluate and take necessary actions for the legality of paying commission for premium collected from the issuance of motor policies for strike, riot, civil commotion and terrorism cover. |

| | | | |
|---|---|---|---|
| | | 01.04.2022. in implementing this decision as industry was opposed the implementation was postponed. | |
| (c.) | According to the National Insurance Trust Fund (amended) Act No 28 of 2007 and Extraordinary Gazette Notification No 1791/4 dated 21 December 2012, the fund has the mandatory cession of 30% of general (non-life) reinsurance in Sri Lanka. However, it was observed that, the fund had paid a commission to reinsurers who reinsure the mandatory portion. The fund had paid Rs. 6,720,273,899 as reinsurance commissions for 13 general insurance companies for the years 2017 to 2020 for the aforesaid mandatory portion without proper legal provisions to do so. | According to the nature and practice of the reinsurance business, the primary insurance companies in Sri Lanka are arranging their reinsurance covers with the foreign panel of reinsurers and NITF under the mandatory 30% cession become only one reinsurer to the panel. However, the reinsurance agreement initially agreed and signed with the lead reinsurer who accept the high percentage of risk. As per the reinsurance norms, all the other reinsurers in the panel are following the same terms and conditions. Therefore, percentage of the commission is originally agreed by the leader has to be accepted by NITF. | The company should evaluate and take necessary actions for the legality of paying commission for premium collected from the mandatory 30 percent reinsurance cover. |

### 3.3 Procurement Management

| Audit Observation | Management Comment | Recommendation |
|---|---|---|
| A delay of eleven (11) months had been observed for obtaining re-insurance agreement to cover whole account excess of loss re-insurance contract (Risk Catastrophe) during this period the fund had proceed with 30% compulsory cession without any reinsurance cover. If there is any claim occurred during this period it will directly effect to the operations of the fund. The reason for this delay is delay in procurement procedure for reinsurance retro cession | The procurement process was started on 18th July 2018 to obtain the reinsurance cover for 30% compulsory reinsurance cession for a period of one year commencing from 15th March 2019. At that time the National Insurance Trust Fund was under the Ministry of Youth Affairs, Project Management, and Southern Development. | The management should obtain reinsurance covers on timely basis to manage the risk undertaken by the fund. |