

Employees' Provident Fund - 2020

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Employees' Provident Fund for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the statement of income and expenditure, 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 reported to Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the accompanying financial statements give a true and fair view of the financial position of the Fund as at 31 December 2020, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Qualified Opinion

My opinion is qualified 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. 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 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 Audit Scope (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 skepticism 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 Fund'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 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 in relation to the preparation of financial statements

1.5.1 Non-compliance with Sri Lanka Accounting Standards

Non-compliance with Reference to the Relevant Standard	Comments of the Management	Recommendation
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Even though the useful life of non-current assets should be reviewed annually according to paragraph 51 of the Sri Lanka Accounting Standards No. 16, the Fund had not functioned accordingly. As per the schedule for computing the depreciation for the financial statements as at 31 December of the year under review, the value of assets, which had been fully depreciated was Rs.456.31 million. Action had not been taken to identify the assets that are still in use among those assets and to correct the estimation error, occurred due to not reviewing the useful life of non-current assets accurately in accordance with paragraph 51 of Sri Lanka Accounting Standard No. 16, as per Sri Lanka Accounting Standard No. 08 and to properly dispose of the assets that were no longer in use.	I accept that the calculation of depreciation is not accurate at present due to prevalence of shortcomings in the depreciation of non-current assets over several years. Therefore, necessary steps have been taken to revalue the non-current assets from the year 2020 and its proceeding activities have to be delayed due to the prevailing Covid 19 pandemic. It is expected to do rectifications for that as soon as possible.	Action should be taken in relation to the non-current assets in terms of the Standard.

1.5.2 Accounting deficiencies

Audit Observation	Comments of the Management	Recommendation
<p>Although there had been unsettled balances amounting to Rs. 11,838 million, comprised of a total of Rs.11,241 million as dishonored cheques, transactions not recorded in the bank statement, transactions not recorded in the cash book, direct debit / credit and other unidentified balances within a period of 01 year to 19 years according to the bank reconciliation statements prepared as at 31 December 2020 in relation to 08 bank accounts maintained by the Fund and a total of Rs.456 million as money orders deposited but not realized, unrealized cheques and cheques issued but not presented and a sum of Rs.141 million that has been carried forward since 2006 as a defect in the computer accounting system that was being used, action had not been taken to identify these items and to make necessary adjustments.</p>	<p>Transactions amounting to Rs. 11,389 million, out of the unidentified transactions, were the transactions carried out through the main bank account of the Fund during the period of 2006 to 2018. A special project was commenced in January 2020 to settle these balances prevailing continuously. The project was delayed due to the Covid-19 pandemic and action will be taken in the future to settle the ongoing balances prevailing in the bank reconciliation statements by considering the results of this project as well.</p>	<p>Identification of unsettled balances included in Bank Reconciliation Statements and taking appropriate action in that regard.</p>

1.5.3 Unreconciled Control Accounts or Records

Subject	Value according to Financial Statements	Value according to Corresponding Reports.	Difference Rs. Million	Comments of the Management	Recommendation
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	Rs. Million	Rs. Million			
(a) Property, Plant and Equipment	996.2	571.28	424.92	It is anticipated to rectify the fixed assets by revaluation.	Entering accurate numerical data by ensuring the correct value of the fixed assets in accordance with all the relevant schedules.
(b) Balance of 7 accounts included in the members'	78,582	46,287	32,295	Transactions are recorded on cash basis in the 'AS / 400' system and transactions in the	The reasons for the relevant differences should be searched and rectifications

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general ledger are should be made recorded on an accordingly. accrual basis. The general ledger is daily updated by uploading data of the individual member accounts maintained in the 'AS / 400' system to the general ledger via a file. The accounts of these two systems are reconciled daily to ensure the recording of daily transactions occurring in the balances of the member accounts of both the systems. Accordingly, all the transactions in the 'AS / 400' system have been duly recorded in the general ledger during the year 2020.

1.5.4 Documentary Evidences not made available for Audit

Subject	Amount	Evidence not made available for Audit	Comments of the Management	Recommendation
	(Rs. Million)			
Fixed Assets	996.2	<ul style="list-style-type: none"> Fixed asset registers containing basic information such as code number, date of purchase, cost, and location of establishing assets. Reports of the Verification of Goods for the Year 2020 	<p>A fixed asset register has not been maintained and instructions have been issued to maintain the register in the future. Arrangements have been made to submit the reports in relation to the verification of goods to the Audit Division of our Department.</p>	<p>Making arrangements to systematically maintain a fixed asset register and to conduct Verification of Goods annually.</p>

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

References to Laws, Rules and Regulations etc.	Non-compliance	Comments of the Management	Recommendation
(a) Section 2 of the Department of Labour Circular No. 2011/06 dated 29 April 2011	Although the actions need to be taken to inquire a complaint within 14 days after receiving it to the Office, action had not been taken to inquire in to and finalize 112 or 394 complaints out of the complaints received in the years 2019 and 2020 respectively to the Colombo South District Labour Office even by the date of the audit in March 2021.	Delays are unavoidable as it is very difficult to obtain accurate information and verify the accuracy of the information during the process of inquiring in to complaints and inquiring in to complaints is a complex process that determines the time taken on employer employee responses. Moreover, a limited number of employees were called for duty in the year 2020 and that had led to delays in inquiring. However, investigations are carried out giving priority to complaints that are urgent and subject to prescription.	Providing optimal service to the members by acting in terms of the Circular in relation to complaints.
(b) Department of Labour Circular No. 01/99 dated 11 February 1999.	It was observed that contributions and surcharges amounting to Rs.146.78 million and Rs.256.12 million in relation to the issuance of 190 and 224 final notices respectively to employers for the recovery of arrears and surcharges in the years 2019 and 2020 had not been recovered by the Colombo South and Colombo West District Labour Offices even by 31 March 2021 and the period of delay was in between 3 months to 2 years.	There were delays in the legal process of recovering arrears and surcharges as requests were made for obtaining instalment reliefs, removal of surcharges, revision of notices, etc. after the issuance of final notices. Furthermore, the delay was also due to the Covid 19 pandemic, which had hampered the continuation of office work.	Action should be taken to collect arrears in contributions and surcharges efficiently.

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| (c) | Department of Labour Circular No. 08/2002 dated 20 May 2002 | Although it is required to maintain an institutional register, containing the registration number, name of the institution, address, nature of the business, number of employees and the date of last inspection, the District Labour Offices in Colombo Central, Colombo West and Colombo South had not taken action to maintain such institutional registers. | Answers had not been submitted. | It is required to estimate the time periods of inspections and measure the efficiency of the officers by maintaining an institutional inspection register as per the provisions of the Circular. |
| (d) | Department of Labour Circular No. 01/99 dated 11 February 1999 | Fifty-one (51) instances of spending 20 to 455 days to issue the first notice for the recovery of surcharges and contributions after conducting institutional inspections in the years 2019 and 2020 and 79 instances of spending 20 to 563 days to issue the final notice were observed during the audit test checks carried out in relation to the Colombo South and Colombo West District Labour Offices. Furthermore, final notices had not been issued in relation to 39 instances and any notice had not been issued in relation to 68 occasions. | Existence of vacancies in the staff, obstructions to office operations due to the prevalence of Covid-19 pandemic and prevailing of instances where the monitoring data system of the Fund was not operating had been the reasons for such delays. Issues in relation to addresses of employer institutions, requirement of employers to pay arrears in instalments after the first notice was sent to them and requesting to remove surcharges had also been the reasons for these delays. | Action should be taken to recover contributions and surcharges by issuing notices in terms of the provisions of the Circulars. |

2. Financial Review

2.1 Financial Results

The operating result for the year under review was a profit of Rs. 283,986 million and the corresponding profit for the preceding year was Rs. 257,741 million. Accordingly, an improvement in the financial result amounting to Rs. 26,245 million was observed. The growth in the interest income earned from the investments made by the Fund during the year under review by Rs.22,728 million was the major reason for this improvement.

2.2 Trend Analysis of Major Income Items

Particulars	Year 2020	Year 2019	Increase / (Decrease) in Income	
	Rs. Million	Rs. Million	Rs. Million	%
(a) Interest income				
i. Treasury bonds	266,130	244,238	21,892	8.96
ii. Treasury bills	414	2,125	(1,711)	(80.52)
iii. Fixed deposits	5,877	2,104	3,773	179.33
iv. Repurchase Agreements	521	1,171	(650)	(55.51)
(b) Dividend income - unlisted companies	466	3,674	(3,208)	(87.32)

Interest income earned from investments in fixed deposits had increased by 179.33 per cent during the year under review as compared with the preceding year and interest income earned from investments in Treasury bills and repurchase agreements had declined by 80.52 per cent and 55.51 percent respectively. Furthermore, dividend income earned from investing shares of unlisted companies had also declined by 87.32 per cent as compared with the preceding year.

2.3 Ratio analysis

According to the information provided, some of the key ratios of the Fund for the year under review and for the preceding year are mentioned below.

<u>Ratios</u>	<u>2020</u>	<u>2019</u>
Net Profit Ratio (%)	85.8	86.0
Ratio of Returns on Average Investment (%)	10.61	10.69
Ratio of Returns on Member Balance (%)	10.31	10.37

The following matters were observed.

Net profit ratio of the Fund for the year under review had reduced by 0.2 per cent from 86.0 percent to 85.8 per cent as compared with the preceding year. The investment income has increased by 10.18 percent from Rs. 259,039 million to Rs. 285,419 million. The Fund was able to maintain the return on average investment ratio and the return on member balance ratio in parallel level as in the preceding year. Furthermore, the interest distributed among the members during the year under review had increased by Rs. 16,425 million from Rs. 215,197 million to Rs. 231,622 million as compared with the preceding year.

3. Operational review

3.1 Identified losses

Audit Observation	Comments of the Management	Recommendation
<p>Five (05) machines purchased by incurring Rs. 2.75 million in the year 2008 under the first phase of the project of issuing identity cards to the members of the Fund and installing machines for examining balances of the account were underutilized from the date of purchase and 2 machines out of the five machines were disposed on 17 September 2020. A decision had not been taken in relation to the remaining machines even by the date of audit. Fifteen thousand (15,000) cards prepared by incurring an amount of Rs. 12.61 million in the year 2008 for issuing identity cards for the members had been idling in the computer section. Although a period of about 12 years had elapsed since the cards had been stored, they had not been used and that expense was a loss to the Fund. Moreover, 30 machines had been purchased in 2015 by incurring Rs. 14.92 million to check the balance using the fingerprint of the member instead of using the identity card. The fingerprint of the member had to be computerized under the re-registration programme to check the balance using that machine. It had been decided to remove the machines from usage due to the reasons such as the number of members thus registered was only 1,053,342 as at 31 December 2020 and that project too had not been successfully implemented and 13 machines were out of order by 01 March 2019. Although it was decided to dispose of 30 machines, the relevant machines had not been brought to the Head Office even by the date of audit in April 2021. Accordingly, the total cost of the project had been a loss to the Fund owing to the failure in completing the project successfully.</p>	<p>These machines were in working condition after the inclusion of computer software related to their functionality. Later, the machines were kept in warehouse due to malfunctioning of the machines.</p> <p>Since printing of cards for all the members was a costly affair, approval has been obtained to set up computer programmes that could be used to retrieve information using fingerprints instead of the card and an additional fee had not been charged for that purpose by the relevant institutions.</p> <p>The KIOSK machines purchased in 2015 were installed and utilized island wide and after carrying out repairs from time to time it was possible to keep 20 machines in working condition by 31 December 2018. Although it has been decided to utilize the usable parts after carrying these machines back to the Head Office I kindly inform you that it is not possible to deploy the staff for that purpose due to the current outbreak of the Covid-19 pandemic.</p>	<p>It is the responsibility of the Management, which holds the custody of the Fund to function efficiently, effectively and economically according to well-designed plans in incurring expenses from the income of the members' funds.</p>

3.2 Management inefficiencies

Audit Observation	Comments of the Management	Recommendation
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(a) The rate of return on the contributions of the members reduced from 11 percent in 2013 to 10.5 percent in 2014. Although that rate had been maintained continuously from 2014 to 2017, it had been steadily declining since 2018 and the rate had fallen to 9 percent in the year under review.	The interest rate is determined by considering the income of the year, expenses, balance of the members and the behavior of the average interest rate of market in the year. Furthermore, the income tax rate of the Fund was increased from 10 per cent to 14 per cent with the introduction of the new Inland Revenue Act No. 24 of 2017, which was effective from 01 April 2018, and the basis on which the taxable income is calculated was also changed. As a result, the income tax expenditure of the Fund was gradually increased.	Action should be taken to provide higher benefits to the members.
(b) Although the Fund had invested Rs. 83,463 million in 83 listed companies, the market value of those investments had decreased by Rs.12,656 million or 15 percent up to Rs. 70,807 million by 31 December in the year under review.	The market prices of listed stocks fluctuate depending on the performance of the companies and the prevailing economic conditions. It is admitted that the listed shares show an unrealized loss as at the relevant date as compared with the cost. However, Rs.1,890 million has been identified in the income and expenditure statement as a loss occurred due to the changes in the market price of the listed shares in the investment portfolio of the Fund for the year 2019 as compared with the previous year and it has been recorded as a profit amounting to Rs. 5,023 million during the year 2020.	When investments are done, action should be taken to make optimal investments to provide higher returns to the members.
(c) Dividends amounting to Rs. 466 million had been received only from two companies out of the investments in unlisted companies during the year under review. It was	West Coast Power (Pvt) Ltd. represents the majority of the dividends earned from investments in equity of unlisted companies and its payment of dividend	When investments are done, action should be taken to make optimal investments to

a decline of 87 percent as compared with the previous year.

depend mainly on the settlements made by the Ceylon Electricity Board. Therefore, there is a fluctuation in the dividend income earned by investing the unlisted shares of the Fund.

provide higher returns to the members.

(d) Even though Rs. 5,000 million or 56 per cent out of the investments in equity of unlisted companies had been invested for the construction of the Canwill Holdings hotel complex in 2013, it had not commenced its business activities even by the end of the year under review and therefore, any return had not been received for those investments. The Fund had also lost an amount of Rs.205 million during the year under review due to the revocation of the license of the “The Finance Company”.

It has been stated in the Annual Report of the Company that the approval was granted at the meeting of the Cabinet of Ministers held on 07 August 2020 to resume the construction work of the 'Grand Hyatt Colombo' project. Construction of the project has been resumed in 2020 and the Fund has been made aware that the Company plans to inaugurate its first phase by 27 December 2021. It is anticipated that business activities will begin accordingly.

When investments are done, action should be taken to make optimal investments to minimize the risk and thereby, to provide higher returns to the members.

3.3 Operational inefficiencies

Audit Observation	Comments of the Management	Recommendation
<p>Action had not been taken to credit the amount of Rs. 10,486 million recovered by the Department by filing a case against the employers of the account maintained in favor of the Labour Commissioner within the Members’ Fund of the Fund as at 31 December 2020 and the amount of Rs. 453 million retained in the General deposit account until settling after recovering the amount by filing a case in that manner to each members’ account. Further, action had not been taken to identify the relevant members and to settle the balance of Rs.65,865 million existed as at 31 December 2020 in the "Current Year Contribution- No. 01" account maintained separately in favor of the employers. Although retained benefits and unclaimed benefits amounting to Rs. 925 million as at 31 December of the year under review and UP/OP contributions amounting to Rs.1,984 million and UP/OP refunds payments amounting to Rs. 682 million had been stated under the member’s Fund, action had</p>	<p>Delays were occurred in sending "C" reports with shortcomings to relevant employers due to the pandemic situation prevailed island wide. Web based application / Mobile application and a new technological tool for updating automated member’s account have been developed and finalized to expedite the individual member accounting. It is possible to resolve the unclaimed benefit account and the</p>	<p>An efficient programme should be made to settle the unsettled contributions without delay.</p>

not been taken to identify those balances and to settle them. retained benefit account after receiving accurate determination letters in relation to those accounts, which had not been credited to the aforesaid accounts. member's accounts.

3.4 Procurement Management

Audit Observation -----	Comments of the Management -----	Recommendation -----
<p>The total cost estimate amounting to Rs.135.3 million obtained from the Department of Buildings without following the Government Procurement Guidelines for the preparation of the Interior Partitions of the “Mehewara Piyasa” office premises had been approved and the entire amount had been paid to the Department of Buildings on 31 December 2020. Furthermore, the approval of the Chief Accounting Officer had not been obtained for the total cost estimate as per Guidelines Nos. 4.3.1 and 4.3.2 of the Government Procurement Guidelines and for the recommendations of the relevant departmental procurement committees as per Guideline No. 2.14.1 and a formal contract had not been entered in to in terms of Guideline No. 8.9.3. Moreover, the full contract value had been paid prior to the commencement of the activities in contrary to Guideline No. 5.4.4 (i) and retention amount had not been retained in accordance with Guideline No. 5.4.6 (b). Furthermore, the interior partitions work had not been commenced even by 31 March 2021.</p>	<p>As the Department of Buildings is a Government Institution and our Department had used to pay the entire amount to the Department of Buildings prior to this occasion when carrying out construction work of our Department by the Department of Buildings, the entire amount was paid to the Department of Buildings.</p> <p>It was decided to get this work done by the Department of Buildings without calling for bids as there were obstacles to formally report for duty owing to Covid -19 pandemic and as time was not sufficient. The Technical Evaluation Committee appointed to prepare the specifications had not performed the task and as a result, cost estimate had not been submitted to the Technical Evaluation Committee and approval for the estimate had not been obtained from the Technical Evaluation Committee. This estimate had been prepared by a team of qualified officers in the Department of Buildings. It was difficult to submit the total cost estimate, which exceeded Rs. 100 million to the Secretary of the Line Ministry and to obtain his approval for the estimate and action will be taken to rectify this in carrying out future activities.</p>	<p>Procurement should be carried out by following the Procurement Guidelines and utilizing the funds efficiently and effectively.</p>

4. Accountability and good governance

4.1 Internal Audit

Audit Observation	Comments of the Management	Recommendation
<p>An independent internal audit division has not been established for the Employees' Provident Fund and the task is being carried out by the Internal Audit Division of the Central Bank of Sri Lanka. Although the approved staff of the Internal Audit Division of the Department of Labour, which administers the Fund, was 14, the actual number was limited to 09. It is observed that the Internal Audit Unit needs to be strengthened as the Fund manages a Members' Fund of about Rs. 2.8 trillion. Although the Committee on Public Accounts had directed continuously from 2013 to strengthen the internal audit of the Department, action had not been taken to carry out an audit by attaching an adequate staff. The approved internal audit plan prepared for the year under review by the Fund and the internal audit reports issued in relation to the year under review were not submitted to audit.</p>	<p>The internal audit activities of the Employees' Provident Fund Department of the Central Bank of Sri Lanka come under the purview of the Internal Audit Department of the Central Bank of Sri Lanka and those audit activities are reviewed by the Audit Advisory Committee with the participation of a member of the Monetary Board.</p>	<p>Internal audit should be strengthened to carry out an adequate internal audit.</p>