

Canowin Hotels & Spas (Pvt) Ltd - 2021

1. Financial Statements

1.1 Opinion

The audit of the financial statements of the Canowin Hotels & Spas (Pvt) Ltd (“Company”) for the year ended 31 December 2021 comprising the statement of financial position as at 31 December 2021 and the statement of comprehensive income, statement of changes in equity and statement of cash flows 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. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Company as at 31 December 2021, 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

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 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 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 Company’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 Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company’s financial reporting process.

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

1.4 Audit Scope

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 Company'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 Company'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 Company 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 Company, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company;
- Whether the Company has performed according to its powers, functions and duties; and
- Whether the resources of the Company 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 Issue | Management Comment | Recommendation |
|---|---|---|
| (a.) There was no proper procedure to pass non-standard journal entries to the system with the approval of the higher management. | Noted, Necessary actions will be taken to prevent repetition of such incidents in future. | There should be a formal procedure to pass journal entries to the system. |

1.5.2 Accounting Deficiencies

| Audit Issue | Management Comment | Recommendation |
|--|--|--|
| (a.) The advance of Rs. 49,137,764 paid for initial cost of establishment of the arcade, supply of machinery and equipment and civil works in the years 2018 and 2019 had not been identified and capitalized. | Noted, this issue was discussed in the Audit Committee. Further, a valuation has been done by an outsourcing firm with the Audit Committee recommendation. We will take necessary steps to capitalize all assets. | Management should inquire this matter and take necessary actions. |
| (b.) The Economic Service Charge of Rs. 505,327 had been made in the year 2018. However, this balance could not be able to recover from the subsequent income tax payment within next two-year period due to unavailability of income tax liability. This amount had been Carried forward as at 31 December 2021 | Rs.505,327 has been set off against Economic Service Charges (ESC) receivable balance as an Audit Entry in the year 2018 and remaining balance of ESC has been declared as a tax credit in the income tax return for the year of assessment 2019/2020. | The management should take necessary actions to recover the Economic Service Charge. |
| (c.) According to the General Ledger the advance paid to the other supplier's balance was Rs. 5,693,851. However, | Noted, the difference had been reduced from Rs.597,501 to 119,550 and will take the | The management should identify the reasons for difference and make |

according to the age analysis the balance was Rs. 5,813,401. Therefore, the difference of Rs119,550 had been observed between the general ledger and age analysis. The reasons for those differences had not been identified. necessary steps to identify the remaining difference. required adjustments.

1.6 Accounts Receivable and Payable

1.6.1 Receivable

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| (a.) According to Clause 7(6) of the Lease Agreement, Lessee shall pay all dues to the lessor within 14 days of the invoice and in any case not later than 20 th day of the following month. However, it is observed that ten tenants had not paid the balance of Rs. 24,842,365 as at 31 December 2021. | The circumstances of the Covid 19 pandemic have heavily impacted everyone and created a financial crisis for many. Further, Island wide travel restriction was imposed by government as per the instruction issued by Sri Lanka Health Authority. Furthermore, country was lockdown more than three months. During the period tenants have not generated income and some tenants left from business due to losses of their business. Therefore, we did not have opportunity to collect the due amount on time in that circumstance. By considering overdue amount of existing tenants, management of the company has decided and included a specific clause into the new agreement that "If the Lessee fails to make the monthly rental for three months (03) continuously, the rent agreement will be automatically cancelled and forfeited the security deposit and take over possession of the premises without any condition or any notice. | The management should take necessary actions according to the agreements. |

1.6.2 Advances

| Audit Issue | Management Comment | Recommendation |
|--|--|---|
| (a.) According to the age analysis of advances paid to supplier has more than two years balance of Rs.1,413,723. This has occurred due to the suppliers had not provide the goods or services procured by the company. | Noted, the Company has decided to take legal action against those suppliers. | The Company should take necessary actions to recover the advances paid or get the services done from the suppliers. |

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

| Reference to Laws, Rules Regulations etc. | Non-compliance | Management Comment | Recommendation |
|--|--|---|--|
| (a.) Clause 7(6) and clause 8(e) of the Lease Agreement | According to Lease Agreement lessee shall pay all dues to the lessor within 14 days of the invoice and in any case not later than 20th day of the following month. Further, any delayed payments from the date specified in this agreement shall attract a charge of interest calculated at the prevailing bank lending rates for the number of days delayed from the date of the relevant invoice. However, entity has not charged interest payment for the delayed payments. | The circumstances of the Covid 19 pandemic have heavily impacted everyone and created a financial crisis for many. Further Island wide travel restriction was imposed by government as per the instruction issued by Sri Lanka Health Authority. Furthermore, country was lockdown more than three months. During the period tenants have not generated income and some tenants left from business due to losses of their business. Therefore, we did not have opportunity to charge the interest in that circumstance. In addition to that we had to grant concessions to tenants by considering pandemic situation and income were declining. | Management should comply with the clauses of the Agreement. |
| (b.) Public Enterprises Department Circular No.01/2015(i) dated 27 October 2016. | According to the Circular, an officer who is entitled to an official vehicle has the option either to use the official vehicle or to avail a monthly transport allowance of Rs.50,000. However contrary to the above circular the company paid monthly transport allowance of Rs.100,000 to the Chairman from April 2020 without obtaining approval of the General Treasury. | Noted, Transport Allowance has been paid with board approval and subsequently, Manager Special Project has just informed board decision to Treasury instead obtaining the approval. Canowin Hotels and Spas (Pvt) Ltd (Canowin) involves in managing the highway service area "Canowin Arcade" at Welipanna on the Southern Expressway. The chairman has to visit the Arcade and Head office to ensure the effectiveness and efficiently in managing the service area. Due to the non-availability of a vehicle within the Company for the Chairman's usage, the Chairman has been used his personal vehicle for the purpose of official travelling of the company. | The Management should comply with the provisions of the circular and if there is any deviation the approval of the relevant authority shall be obtained. |

1.8 Non-compliance with Tax Regulations

| Audit Issue | Management Comment | Recommendation |
|---|--|---|
| (a.) According to the paragraph 7(2) of the Inland Revenue Act of the No 24 of 2017, the company had not considered investment income for income tax computation. Therefore, the income tax liability had been understated by Rs.1,978,853 for the year under review. | Noted, it will be corrected when submitting the income tax return for the year 2021/2022 and make the necessary adjustments in year 2022 to eliminate the impact of the income tax calculation for the year 2021. Further we hereby confirm that company has no income tax liability to pay to Inland Revenue Department (IRD) when consider the accumulated taxable losses. | The management should compute and pay income tax the income tax according to the provisions of the tax law. |

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs. 58,865,666 and the corresponding profit in the preceding year amounted to Rs. 37,014,719 Therefore an improvement amounting to Rs. 21,850,947 of the financial result was observed. The reasons for the improvement was increase of revenue by Rs. 7,404,021, increase of other operating income by Rs.1,543,364 , increase of Net Gain from Change in Fair value of Investment Property by Rs.10,510,375 , reduction of administrative expense by Rs.16,563,499 when compared to the previous year.

2.2 Trend Analysis of major Income and Expenditure items

| Financial Statement Line Item | 2021 | 2020 | 2019 | 2018 | 2017 |
|---|---------|---------|---------|---------|--------|
| Revenue (Rs.000) | 137,556 | 130,152 | 137,630 | 97,836 | 99,807 |
| Increase/ (Decrease) of Revenue (Rs.000) | 7,404 | -7,478 | 39,794 | -1,971 | 16,467 |
| Revenue Growth/ (Reduction) % | 5.7% | 5.4% | 40.7% | -1.8% | 19.8% |
| Gross profit (Rs.000) | 109,856 | 109,179 | 102,946 | 63,933 | 61,761 |
| Increase/ (Decrease) of Gross Profit (Rs.000) | 677 | 6,233 | 39,013 | 2,172 | 27,273 |
| Gross Profit Growth/ (Reduction) % | .06% | 6.05% | 61.02% | 3.52% | 79.08% |
| Other Operating Income (Rs.000) | 2,290 | 747 | 5,303 | 17,266 | 5,610 |
| Increase/ (Decrease) of Other Operating Income (Rs.000) | 1,543 | -4,556 | -11,963 | 11,656 | 895 |
| Other Operating Income Growth/ (Reduction) % | 206.56% | -85.91% | -69.29% | 207.77% | 18.98% |

| | | | | | |
|---|---------|---------|---------|---------|---------|
| Finance Income (Rs.000) | 12,455 | 15,511 | 17,801 | 15,913 | 14,114 |
| Increase/ (Decrease) of Finance Income (Rs.000) | -3,056 | -2,290 | 1,888 | 1,799 | 3,110 |
| Finance Income Growth/ (Reduction) % | -19.70% | -12.86% | 11.86% | 12.75% | 28.26% |
| Administration Expenses (Rs.000) | 43,506 | 60,070 | 64,069 | 44,289 | 35,394 |
| Increase/ (Decrease) of Administration Expenses (Rs.000) | -16,564 | -3,999 | 19,780 | 8,895 | 13,709 |
| Administration Expenses Growth/ (Reduction) % | -27.57% | -6.24% | 44.66% | 25.13% | 63.22% |
| Selling & Distribution Expenses (Rs.000) | 13,639 | 13,581 | 2,129 | 8,759 | 1,918 |
| Increase/ (Decrease) of Selling & Distribution Expenses (Rs.000) | 58 | 11,452 | -6,630 | 6,841 | 1,918 |
| Selling & Distribution Expenses Growth/ (Reduction) % | 4.27% | 537.90% | -75.69% | 356.67% | 100% |
| Profit After Tax (Rs.000) | 58,865 | 36,015 | 41,751 | 54,595 | 49,370 |
| Increase/ (Decrease) of Profit After Tax (Rs.000) | 22,850 | -5,736 | -12,844 | 5,225 | 36,579 |
| Profit After Tax Growth/ (Reduction) % | 63.45% | -13.74% | -23.53% | 142.84% | 285.97% |

2.3 Ratio Analysis

| Ratios | 2021 | 2020 | 2019 | 2018 | 2017 |
|--------------------------------|-------------|-------------|-------------|-------------|-------------|
| Gross profit ratio (%) | 79.9% | 83.9% | 76.9% | 65.3% | 61.9% |
| Return on capital employed (%) | 6.0% | 4.2% | 7.0% | 4.3% | 6.9% |
| Current Ratio | 8.32:1 | 8.6:1 | 7.2:1 | 6.9:1 | 4.4 |
| Quick Ratio | 8.26:1 | 8.6:1 | 6.9:1 | 6.6:1 | 4.4 |
| Gearing Ratio % | 10.4% | 9.9% | 6.7% | 8.5% | 7.3% |
| Earnings Per Share (EPS) | 0.68 | 0.43 | 0.48 | 0.63 | 0.57 |

3. Operational Review

3.1 Operational Inefficiencies

| Audit Issue | Management Comment | Recommendation |
|--|---|--|
| (a.) The entity had purchased water on hiring basis for consumption of arcade A & B due to lack of water flow in the tube wells. As per the financial statements a sum of Rs. 3,929,440 had been incurred additionally by the entity during the year 2021 for supplying of water to the premises. The lack of water supply to the premises will severely impact to the effective functioning of the arcade and service provided by the arcade. | Noted, we have two tube wells to get water, but the capacity is not sufficient for the daily consumption. Currently the consumption is nearly 150,000 liters of water per day, but nearly 100,000 liters of water drained out from two tube wells. Therefore, we should purchase for the shortage of water on hiring basis. Further, a request has been made to the National Water Supply and Drainage Board to obtain pipe borne water to the Welipenna service zone, which is under processing. | The management should ensure the fixed and continued water supply to the premises for continuing and effective functioning of the service. |

3.2 Procurement Management

| Audit Issue | Management Comment | Recommendation |
|--|---|---|
| (a.) A Master procurement plan had not been prepared in accordance with the paragraph 4.2.1 of the procurement Guideline. | Noted, we will ensure to follow the Procurement Guidelines in order that would prevent such misses in future. | The management should comply with the requirement of the procurement guideline. |
| (b.) According to the paragraph 2.7.5 of the procurement Guideline a Procurement Committee had not been established. | Noted, considering the nature and the capacity of our organization, each and every procurement is to be evaluated by Technical Evaluation Committee (TEC). Thereafter payments are approved according to the delegations of Financial Authority of the company. | The management should comply with the requirement of the procurement guideline. |
| (c.) Even though, the 5.4.4 of the procurement guidelines restricted to paid a maximum of twenty percent (20%) of the contract sum as an acceptable advance payment guarantee the company paid 60% advance payment amounting to Rs.4,350,000 to a supplier without taking an advance guarantee and enter in to an agreement. Further, the agreed tasks had not been completed yet. | The Company has decided to take legal action against the supplier as per the board approval while Legal department will take it forward. | The management should take necessary actions to get the supplies and services from the supplier or take appropriate actions against the supplier. |

3.3 Human Resources Management

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| (a.) An approved organization chart with an approved cadre had not been available for the company in accordance with the section 3.3 Operational Manual for State Owned Enterprises issued on 16 November 2021 by the Department of Public Enterprises, General Treasury. | Noted, the proposed cadre (organizational chart) and the recruitment policy presented to the Audit Committee held on 27 June 2022 for comments further the management of the company decided at the board meeting held on 28 July 2022 to outsource the policy preparation. The parent company, Sri Lanka Insurance Corporation prepared an organizational structure for the company while conducting an internal audit in the company. Nevertheless, the structure still requires some alterations. The structure will be completed after a proper work study. Noted, there is a difference between proposed cadre and the existing employees as there was no any proper structure from the very beginning, there is a variance between the required number of staff and replacements. The current Board of Directors already attended on above to sort out the issue. | The Company should have an approved organization chart with an approved cadre in accordance with the provisions of the Guidelines on Corporate Governance and Operational Manual for State Owned Enterprises. |

4. Accountability and Good Governance

4.1 Corporate Plan

| Audit Issue | Management Comment | Recommendation |
|--|--|--|
| (a.) A Corporate Plan had not been available for the Company in accordance with the Annexure 1 of the chapter 5 of the Guideline on Corporate Governance for State Owned Enterprises issued on 16 November 2021. | Noted, Management of the company decided at the board meeting held on 28 th July 2022 to outsource the policy preparation. Quotations are called from companies to prepare and improve company policies after necessary work studies. Management decided to prepare and improve Organizational Structure, Recruitment policy with pay structure, Action Plan and Corporate Plan with the help of expertise knowledge. | The Company should have a Corporate Plan in accordance with the provisions of the guideline. |

4.2 Internal Audit

| Audit Issue | Management Comment | Recommendation |
|---|---|---|
| (a.) An internal audit had not been carried out since April 2018. | Internal audit functions of the Company have been handed over to the auditing staff of Sri Lanka Insurance Cooperation. Audit Department of SLIC will perform the audit periodically in future. | The board of directors should ensure that effective internal audit function in place for the Company. |

4.3 Audit Committee

| Audit Issue | Management Comment | Recommendation |
|--|---|--|
| (a.) According to the section 4.2(h) of the Guideline on Corporate Governance and Operational Manual for State Owned Enterprises issued on 16 November 2021 by the Department of Public Enterprises, General Treasury this committee should meet on least once in three months. However, during the period of 2019, 2020 and 2021, the Company had not facilitated to conduct the Audit Committee. | Company has appointed members for the Audit Committee (AC) and currently, AC meeting is holding periodically as required. | The board should ensure that, the effective functioning of audit committee and oversight the affairs of the company. |

4.4 Budgetary Control

| Audit Issue | Management Comment | Recommendation |
|---|--|--|
| (a.) According to the Annexure I of the Chapter 5 of Guideline on Corporate Governance for State Owned Enterprises issued on 16 November 2021 by the Department of Public Enterprises, General Treasury, the Company should have one master budget and separate budget for main activities. However, the company had not prepared Budgeted Income Statement, Budgeted Statement of Financial Position and Budgeted Cash Flow Statement for the year under review. | Noted, we have prepared budget including Budgeted Cash Flow, Budgeted Income and Expenditure and Budgeted Capital Expenditure as per the practice. Budget for the year 2023 will be prepared according to the chapter 5 of the guideline on Corporate Governance for the State-Owned Enterprises issued on 16 November 2021. | The board should ensure that the effective budgetary control is in place within the company for enabling management to proper control over expenditure of the company. |