

Development Lotteries Board - 2014

The audit of financial statements of the Development Lotteries Board for the year ended 31 December 2014 comprising the statement of financial position as at 31 December 2014 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Section 13(1) of the Finance Act, No.38 of 1971 and Section 14(3) of the Development Lotteries Board Act, No. 20 of 1997. My comments and observations which I consider should be published with the Annual Report of the Board in terms of Section 14(2)(c) of the Finance Act appear in this report.

1.2 Management’s Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

1.3 Auditor’s Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards consistent with International Standards of Supreme Audit Institutions (ISSAI 1000 – 1810). Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgement, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risks assessments, the auditor considers internal control relevant to the Board’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Board’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements. Sub-sections (3) and (4) of Section 13 of the Finance Act, No. 38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

1.4 Basis for Qualified Opinion

My opinion is qualified based on the matters described in paragraph 2.2 of this report.

2. Financial Statements

2.1 Qualified Opinion

In my opinion, except for the effects of the matters described in paragraph 2.2 of this report, the financial statements give a true and fair view of the financial position of the Development Lotteries Board as at 31 December 2014 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.2 Comments on Financial Statements

2.2.1 Sri Lanka Accounting Standards

The following observations are made.

(a) **Sri Lanka Accounting Standard No. 01**

(i) The main operation of the Board was the sale of lottery tickets and the expenditure incurred for the vehicles deployed for that purpose and the depreciations totalling Rs.19,463,884 had been considered as administration expenditure. As such, the expenditure classification was not properly depicted.

(ii) Although the Nation Building Tax amounting to Rs.198,540,485 should have been shown as selling and distribution expenses in the statement of comprehensive income, the Board had deducted it from the sales income and shown in the financial statements.

(b) **Sri Lanka Accounting Standard No. 36**

An Impairment Test on the studio the net value of which was Rs.30,013,677 as at 31 December of the year under review which was not being utilized for the expected economic objectives of the Board had not been conducted and carrying amount of the asset had not been shown in the financial statements.

2.2.2 Accounting Deficiencies

The following observations are made.

(a) Although prizes of Rs.100,168,320 allocated for draws but not owned by the winners should be adjusted to the profit of the year under review and transferred to the Prizes Reserve Account in the statement of changes in equity, without doing so, it had been adjusted through the Ledger Accounts and as such the profit of the year under review had been understated by that amount.

(b) In accordance with the computation of the Commissioner General of Inland Revenue, the value of Income Tax defaulted by the Board from the year 2001 to 2009 was Rs.3,320,913,232. Although the Board had submitted an assessment report to the

value of Rs.284,896,813 as the Income Tax relating to that period to the Commissioner General of Inland Revenue, concurrence therefore had not been granted even by 17 March 2015. Nevertheless, the Board had not disclosed this matter in the financial statements of the year under review.

- (c) A double cab motor vehicle valued at Rs.8,095,000 ordered by the Board and registered in the name of the Board in the year 2008 had been taken over by the then Chairman from the supplier company, whereas it had not been handed over to the Board even by the end of the year under review. The value of that double cab motor vehicle, the physical existence of which had not been established at the audit had been included in the financial statements under Property, Plant and Equipment and the relevant value had been shown as a liability payable to a private institution.

2.3 Accounts Receivable and Payable

The following observations are made

- (a) A rent advance of Rs.8,685,360 had been paid to the Ministry of Trade on 01 November 2003 for obtaining a building on rent basis for the Head Office of the Board. Subsequently, as the Board had decided not to obtain the said building on rent, a sum of Rs.2,985,360 out of the advance had been received back to the Board and a sum of Rs.5,700,000 further receivable had not been received as yet. Board had not taken a formal course of action for the recovery of this money.
- (b) There was a balance receivable from an outsider amounting to Rs. 2,520,000 on which a court case was pending even as at 31 December of the year under review.

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

The following non-compliances were observed.

Reference to Laws, Rules, Regulations and Management Decisions	Non-compliance
(a) Development Lotteries Board Act, No. 20 of 1997 (i) Section 18(3)	In the event of introduction of new lotteries and lack of adequate amount of money for awarding lottery winnings, the balance of the Prize Reserve Account can be utilized. Contrary to that, a sum of Rs.405,000,000 out of the balance of Rs.874,670,557 existed in the Prize Reserve Account as at 31 December of the year under review had been utilized for the acquisition of the land and the building in which the office of the Board is situated on the decision of the Board of Directors. Accordingly, only a sum of

Rs.469,670,557 was available with the Board relating to the Prize Reserve Account to utilize according to the provisions of the Act.

(ii) Sections 19 (1),(2) and (3)

The Board had earned a sales income of Rs.9,728,586,929 by conducting scratch-and-win lotteries and drawing lotteries even in the year under review as in the preceding years without formulating rules on lotteries in accordance with provisions, obtaining the approval of the Minister in charge of the subject and publishing in the Gazette on the decisions taken by the Board of Directors on each occasion. Out of that amount, the Board had allocated Rs.6,211,302,790 for prizes and granted sales agents commission of Rs.2,063,639,652.

(b) Establishments Code of the Democratic Socialist Republic of Sri Lanka
Section 11.5.1 of Chapter XXIV

Without being complied with the Section, the Board of Directors had decided to incur 50 per cent of the interest of the employees' property loan by the Board. Accordingly, having done the computation, a sum of Rs. 5,836,164 had been paid as interests of the property loans of the officers during the year under review.

(c) Public Enterprises Circular No.PED/12
dated 02 June 2003

(i) Section 6.5.1

A copy of the draft Annual Report of the Board pertaining to the year under review had not been furnished to the Auditor General along with the financial statements.

(ii) Section 8.3.5 (b)

Official motor vehicles had been assigned to 05 Assistant General Managers of the Board who are not entitled to the official vehicles according to the Section and fuel expenses of Rs.1,248,390 had been reimbursed in the year under review.

(iii) Sections 9.7 and 9.12

Without obtaining the approval of the Treasury, the Board had paid Medical assistance amounting to Rs.25,141,298 to the employees on the decision of the Board of Directors during the year under review and a sum of Rs.9,225,519 which had been paid in cash without obtaining any medical bills had been included in that amount.

- (c) Sections 2,6 (iii) and 6 (iv) of the Public Enterprises Circular No.PED-57 dated 11 February 2011.

Having approved a sum of Rs.434,846,000 by the Annual Budget, the Board had spent Rs 306,981,876 for marketing publicity during the year under review. However, the annual publicity programme had not been forwarded to the Department of Public Enterprises for the approval as required by the provisions of Circular and the approval of the Minister of Finance and Planning had not been obtained for the sponsorship exceeding Rs.100,000 awarded to the parties outside the Government and the sponsorship exceeding Rs.2 million awarded to any party.

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the operation of the Board for the year under review had resulted in a surplus of Rs.2,353,246,339 as compared with the corresponding surplus of Rs.2,126,438,341 for the preceding year, thus indicating an improvement of Rs.226,807,998 or 10.6 per cent as compared with the preceding year. Although the adverse variation of the items such as lottery income, expenditure for draws, administrative expenditure, financial expenditure and Income Tax was Rs.246,758,679, the favourable variation of the items such as expenditure for lottery tickets, allocations for prizes, other income, distribution expenditure and taking over of prizes back amounting to Rs.473,566,677 had attributed to this improvement.

3.2 Analytical Financial Review

The following observations are made

- (a) Although the lottery sales income of the year under review had decreased by Rs.212,788,222 or 2.1 per cent as compared with the preceding year, the decrease in cost of sales by Rs.284,492,622 or 3.9 per cent had given rise to increase the gross profit ratio from 28 per cent to 29 per cent.
- (b) Increase in the other income by Rs.8,188,886 and taking over of un-wined prizes amounting to Rs.62,004,480 and decrease in the distribution expenditure by Rs.93,853,621 had attributed to increase the net profit from 21 per cent to 24 per cent.
- (c) The current liabilities of the Board exceeded its current assets and the current and quick ratios were not at an optimum level. The Board had not focused attention on the working capital management during the year under review. The investment of only Rs. 12,274,776 out of the provisions for gratuity of Rs.22,950,330 as at 31 December of the year under review in fixed deposits had further established the afore said matter.

3.3 Legal Action Instituted by or Against the Board

A private company had filed a court case against the Board claiming a compensation of Rs.8,095,000 relating to a purchasing of a motor vehicle and the Board had filed a case in a court against an outside person for the recovery of a building rental of Rs.2,520,000.

4. Operating Review

4.1 Management Inefficiencies

The following matters are observed.

- (a) The Board had failed to settle the issue on the arrears of Income Tax, Economic Service Charges and the Value Added Tax over Rs.3, 540 million which had been stated as payable by the Board from the year 2001 to 2009 and thereupon the Department of Inland Revenue had taken action to cease all the bank accounts of the Board temporarily from 28 August to 5 September of the year under review. Having decided to obtain the service of a tax consultant under a contract charge of Rs.4,825,000 to resolve this tax arrears issue, the Board had paid a sum of Rs.2,485,000 to the tax consultant in the year under review. Although a sum of Rs. 284,896,813 had been paid to the Commissioner General of Inland Revenue as arrears in the income tax according to the computation of the tax consultant, the issue had not come to an end. Subsequently, the board had agreed to pay the balance of the tax arrears of Rs. 1,807 million after eliminating the fine, in 83 installments in the year 2015.
- (b) In terms of the letter of implementation of provision 30 of the Management Services Circular No.DMS/E1/04/4/015 dated 17 November 2009, the post of Marketing Consultant had been approved as personal to the holder of that post and with the leaving of the respective officer from the service that post should be abolished. Contrary to that, an officer had been recruited to the post of Marketing Consultant on 01 July 2013 on contract basis without the approval of the Department of Management Services. Although an allowance of Rs.1,710,000 had been paid to that officer from 01 July 2013 to 28 February 2015, the objectives expected by the Board by creating that post had not been achieved.
- (c) Even though high quality and accurate tickets should be supplied in accordance with the agreement entered into with the contractor for the printing of instant lottery tickets, the contractor had not taken action accordingly even in the year under review as in the previous year. Further, it had not been possible to scratch 3,000,000 lottery tickets valued at Rs.3,135,000 even in the year under review, but the Board had not taken action against the contractor in terms of the Guideline 8.11.4(a) and (b) of the Procurement Guidelines. The instant lottery income for the year under review had decreased by Rs.153,204,680 or 37 per cent as compared with the preceding year. According to the complains of the sales agents, the absence of lottery tickets in the due standard had been the main reason for this situation.

4.2 Operating Inefficiencies

The following observations are made.

- (a) Out of the weekly drawn Super Ball Lottery tickets, 40 per cent had been sold on credit basis by the Board in the year 2014 and the value of the lottery tickets thus sold on credit basis in the year under review amounted to Rs.951,792,000 In this connection, either the approval of the Board of Directors or a security had not been obtained.
- (b) Without appointing a Technical Evaluation Committee under the responsibility of the procurement entity in accordance with the paragraph 2.3 of the Government Procurement Guidelines and obtaining its recommendations, the Board had purchased 6107 T-shirts valued at Rs.3,205,200 and 17,000 caps valued at Rs.2,127,500 totalling Rs.5,332,700 in 13 instances in order to distribute for sales promotion activities. A quantitative benefit could have been gained if the requirement of T-shirts and caps for the year 2014 had been pre-determined and the purchase had been effected at a time, whereas the Board had deprived of that benefit as a result of this irregular purchase.
- (c) Out of the 706,891,400 lottery tickets costing Rs.346,407,503 printed for draws in the year under review, the number of unsold lottery tickets was 68,748,179 and the cost thereof amounted to Rs.33, 689,595. It represented 9.7 per cent of the total cost of the lottery tickets.

4.3 Transactions of Contentious Nature

The following observations are made.

- (a) For the exhibition of Trade Name and Logo of the Board in a private website, a sum of Rs.1,200,000 had been paid without a proper selection procedure and entering into an agreement with both parties during the year under review.
- (b) The Board had granted Rs.36,807,205 to District Secretariats in respect of Deyatakirula Development Project during the year under review and it had been shown under selling and distribution expenses.
- (c) Five minutes documentary programmes prepared by an institution selected by the Publicity Committee of the Board by calling for quotations from 3 institutions without following the Government Procurement Guidelines had been telecast via Government electronic media and a sum aggregating to Rs. 30,498,000 comprising Rs.13, 958,000 and Rs.16,540,000 had been paid in the years 2013 and 2014 respectively for that purpose.
- (d) For the use of the Working Director of the Board, motor vehicles had been obtained on hire basis on two occasions without following procurement procedure during the year under review and a sum of Rs.1,111,060 had been paid as rental for the period from January to July and November to December 2014.

- (e) For the purpose of carrying out a promotional activity on the lotteries within the internal and external premises of the Bandaranayake International Air Port using Digital Advertisement Boards for a period of one year from 01 June 2014, the Board had paid the total amount of Rs.23,986,561 to the supplier as a lump sum without following any guideline of the Government Procurement Guidelines at a request of an advertising firm and on the recommendation of the Publicity Committee of the Board. The advertising firm had not introduced an electronic mechanism to ensure that the advertisements are published as agreed manner and the Board had not taken action to ensure whether the advertisements were properly published through the examination of a Transmission Report certified by a third party.
- (f) In accordance with the Guideline 3.6.1 of the Government Procurement Guidelines, if a period of six months from the date of award of the original contract had not elapsed, the relevant goods can be procured from the same Government supplier. Nevertheless, despite the elapse of a period of six months from the date of award of the original contract, the Board had purchased 138 bicycles valued at Rs.1,488,642 and 11 wheel-chairs valued at Rs.333,380 from the former supplier without calling for quotations contrary to the Procurement Guidelines.
- (g) In the selection of items for giving sponsorship under the sales promotion expenditure and in the determination of the amount to be paid for the selected item, the Board had not introduced an evaluation procedure for the benefits thus received by the Board through the sponsorship. As revealed at the audit test check, a sum of Rs.24,427,000 had been spent on 07 sponsorships thus given without carrying out a proper evaluation during the year under review and those had ranged between Rs.2,000,000 and Rs.5,355,000. Further, expenditure of Rs.9,331,800 incurred on sponsorships and had been brought to account as lottery publicity production charges.
- (h) In order to obtain computer operating system service for the lottery draws of the Board, a supplier had been selected in the year 2009 without following the procurement procedure and a sum of Rs.71,348,976 had been paid from the year 2009 up to 31 December 2014. Although a Consultant had been recruited on contract basis for the creation of a combined computer information system for the Board without a formal scheme of recruitment and allowances amounting to Rs.2,055,000 had been paid from December 2012 to 28 February 2015, the Board had failed to establish a combined computer information system or create a computer system for the lottery draws even up to 31 May 2015.
- (i) A driver of a Jeep owned by the Board had stated to the audit in writing that the said Jeep had been used for running for the political functions and meetings from February 2012 up to November 2014 with the outsiders of the Board and the Running Charts were got signed by the Confidential Secretary of the Board and other two officers after writing Running Charts to the effect that the vehicle was used for the promotional activities according to the instructions of the Chairman. Further, in order to get the subsistence allowances, the driver had submitted letters including false information indicating that the vehicle was used for the promotional activities, though the vehicle was actually used for the running outside the Colombo as mentioned

above. Those letters had been recommended by the Deputy General Manager (Marketing) and arrangements had been made to obtain allowances of Rs.249,750 to the driver. Accordingly, having utilized the Jeep for the extraneous activities during the above period, the Board had paid a sum of Rs.3,170,017 for the salary and allowances of the driver and for the fuel.

4.4 Idle and Underutilized Assets

The following observations are made.

- (a) Even though the Board had constructed a studio in the year 2010 at a cost of Rs.38,752,448 for filming the lottery draws, that studio had not been used for filming. Further, the Board had not taken action to implement the recommendations made by the Rupavahinee Corporation in June 2012 which was made after conducting a study on the existing deficiencies in the studio. Since the lottery draws had been filmed at the Rupavahinee Corporation without being utilized the studio owned by the Board, a sum of Rs.35,800,000 had been paid during the year under review for that purpose.
- (b) Six hundred and sixteen units of goods valued at Rs.1,801,310 relevant to 14 categories of sales promotion goods remained idle in the stores over periods ranging from 4 to 10 years.

4.5 Identified Losses

Although it was established by the Marketing Division of the Board according to the documents that the Board had implemented a publicity programme relating to 06 lotteries using 600,000 posters and 3,000 banners by spending Rs.20,850,000 (exclusive of tax) in November of the year under review, according to the reports and statements of the Security Division and statements of the Storekeeper and the Stores Assistant of the Board, it was confirmed to the audit that the stores had received only 60,000 posters and 60 banners. A total amount of Rs.1,425,000 comprising Rs.1,260,000 and Rs.165,000 for 60,000 posters and 60 banners respectively only had to be paid to 03 advertising firms, whereas the Board had paid Rs.20,850,000 based on the documents submitted by the Marketing Division stating that 600,000 posters and 3,000 banners had been received by the Board and thereby the publicity programme was properly implemented. As a result, the Board had incurred a financial loss of Rs.19,425,000.

4.6 Uneconomical Transactions

Although the Board had obtained a Certificate of Quality Management System in conformity with the ISO 9001:2008 by obtaining consultation service of a private institution on payment of Rs.1,295,000 in the year under review, since the officers of the Board had not followed the quality manuals and quality procedures in the discharge of their duties and functions, it was observed as an uneconomical transaction in audit.

4.7 Personnel Administration

The following observations are made.

- (a) Even though the approved cadre stood at 201, the actual cadre stood at 225. The vacancies in the approved cadre of the Board as at 31 December 2014 stood at 15 and the excess cadre stood at 39.
- (b) Without obtaining the approval of the Department of Management Services in terms of the letter No DMS/E/04/04/015 dated 17 November 2009 of the Department of Management Services and Public Administration Circular No.25/2014 dated 12 November 2014, twelve employees had been recruited on contract basis.

4.8 Resources of the Board given to other Government Institutions

In terms of Section 8.3.9 of the Public Enterprises Circular No.PED12 dated 02 June 2003, the resources of the Board (inclusive of human resources) cannot be deployed for the use of the Line Ministry or the other Government institution, whereas a junior security officer had been released to an external institution from 13 August 2010 contrary to the above condition. Without obtaining any service to the Board during the relevant period, the Board had paid Rs.2, 228,435 as salary and allowances to the said officer from August 2010 to December 2014.

5. Accountability and Good Governance

5.1 Internal Audit

A separate Internal Audit Unit had not been established up to 31 December of the year under review and the Board had taken action to obtain the service of a private audit firm on a monthly payment of Rs.70,000 up to October of the year under review.

5.2 Procurement Plan

Although the Procurement entity had prepared a Procurement Plan in accordance with the Guideline 4.2 of the Government Procurement Guidelines, all the procurements had not been covered by that Plan.

5.3 Budgetary Control

A significant variance ranging from 6 per cent to 209 per cent was observed between 07 Objects and the other item of revenue, thus indicating that the Budget had not been made use of as an effective instrument of management control.

6. Systems and Controls

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

- (a) Accounting
- (b) Human Resources Management
- (c) Assets Management
- (d) Expenditure Management
- (e) Stores Control