Employees' Trust Fund Board - 2014

The audit of financial statements of the Employees' Trust Fund Board for the year ended 31 December 2014 comprising the statement of the financial position as at 31 December 2014 and the income statement, 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 10 (1) of the Employees' Trust Fund Board Act, No. 46 of 1980. My comments and observations which I consider should be published with the Annual Report of the Board in terms of Section 10 (7) of the Employees' Trust Fund Board 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 the International Auditing Standards of the 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 misstatement of the financial statements, whether due to fraud or error. In making those risk 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 the financial statements. Section 10 (1) of the Employees' Trust Fund Board Act, No. 46 of 1980 gives 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 Employees’ Trust Fund 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 7

Even though the cash flows during the period under review should be reported in the cash flow statement by classifying under operating, investments and financing activities, disclosures pertaining to the investments and financing activities had not been correctly reported in the cash flow statement of the Board.

(b) Sri Lanka Accounting Standard 8

(i) When retrospective application is required upon introduction of a new accounting policy, change in the accounting policy should be applied retrospectively. Nevertheless, according to the financial statements of the year under review, having classified Rs.341.6 million at the fair value adjusted to profit and loss of the portfolio on the basis of the prices in the share market and Rs.6,638 million as financial assets available for sale while introducing a new accounting policy, accounting had been carried out so as to credit Rs.35 million and Rs.1,468.7 million to the profit and the reserve respectively as changes in the fair value.

(ii) Instead of retrospectively adjusting the overprovision of Income Tax amounting to Rs.59.9 million relating to the preceding year, it had been added to the income of the year under review and shown.

(c) Sri Lanka Accounting Standard 12

Detailed information had not been stated in the financial statements so as to clearly identify the manner in which the income tax commitment valued at Rs.202 million was computed.

(d) Sri Lanka Accounting Standard 16

Even though the assets which are being depreciated under the diminishing balance method but further used over a period of 25 years had existed in the fixed assets costing Rs. 417.9 million as at 31 December 2014, a revaluation had not been carried out to show the fair value thereof.

(e) Sri Lanka Accounting Standard 24

Disclosure of related party information of the Board of Directors and the Management of the Board had not been made in the financial statements.

2.2.2 Going Concern

Percentage of the declared annual benefits had been consistently maintained as 7 per cent from the year 2012 to the year under review except for the compulsory interest of 3 per cent given to the members by the Board. An adequate annual operating surplus was not available with the Board for declaring this dividend benefits and thus, sums of Rs. 746 million, Rs. 2,089 million Rs.473 million and Rs. 492 million had been obtained from the year 2011 to the year 2014 respectively from the Dividend Equalization Reserve and retained profits of the preceding years and the year under review. In addition, unrealized profits of Rs.2,596 million and Rs.2,684 million had been utilized for the payment of dividends in the preceding year and the year under review respectively. Accordingly, it cannot be ruled out that the attempt made for further utilization of the Dividend Equalization Reserve and retained profits for the maintenance of annual dividend percentage at 7 per cent would be adversely affect the going concern of the Board.

2.2.3 Contributions not credited to Members' Accounts

Even though the balance of the Members' Fund Account as at 31 December 2014 had been disclosed in the financial statements as Rs. 193,868 million, the actual amount credited to the Members' Account as at 17 August 2015 amounted to Rs. 173,670 million. Accordingly, a sum of Rs.20,198 million of this amount had not been credited to each member's account even by 17 August 2015. A sum of Rs.11,754 million out of the above amount had been received in the year 2014, whereas membership contributions, interests and dividends had existed but not accounted even by 17 August 2015.

The balance sum of Rs.8,444 million had been received over a period of about 34 preceding years from 1981 to 31 December 2013 and represented members' contributions, interests and dividends not accounted up to now. The balance not credited to the members' accounts during the preceding year amounted to Rs.9,496 million and it had decreased up to Rs.8,118 million or 14.5 per cent during the year under review. Nevertheless, an adequate improvement in the process of accounting members contributions received prior to the current year could not be observed.

2.2.4 Accounting Deficiencies

The following observations are made.

(a) Even though an interest not less than 3 per cent of the total earnings from investments should be credited to the Personal Accounts of the members of the Fund annually in terms of the Fund Act, due to non-accounting of the interest of Rs. 5,287 million equivalent to 3 per cent in the year under review as an operating expenditure, the operating surplus of the year under review had been overstated by that amount. Due to over accounting the interest in the preceding year, the operating surplus in that year as well had overstated by Rs.4,752 million.

(b) The sum of Rs. 772 million shown in the financial statements as capital profits is not a profit computed on the cost of shares as at 01 January 2014 and as a result, the comprehensive income of the year under review had been overstated. The amount which had been excessively credited to the comprehensive income statement in the preceding year as capital profit was Rs.171.9 million.

(c) It was revealed in the examination of several investment registers made available to audit that due to the sale of shares of 15 companies at less than the cost price in the share market without any approval, a loss of Rs.213.5 million had been incurred. Having made a share classification in the year 2014 without being complied with the Sri Lanka Accounting Standard 39, the cost of the shares that was sold at a loss had been written off against the share price of the share market and as a result, the loss amounting to Rs.213 million had been stated in the financial statements as a profit of Rs.64 million earned from the share transactions. Further, a profit of Rs.191 million earned from the sale of shares of 24 companies had been overstated in the financial statements as a profit of Rs.381.6 million.

2.2.5 Transactions not supported by Adequate Authority

Dividends should have been declared from the profits earned from investments of the Fund in terms of Section 14 of the Employees Trust Fund Act, No.46 of 1980. However, instead of utilizing the actual interest income of Rs. 12,445.8 million receivable for the year under review for a sum of Rs. 155,280 million invested in the Treasury Bonds of the Central Bank of Sri Lanka as at 31 December 2014, to pay members' dividends of the year under review, unrealized profit amounting to Rs. 2,684 million had been utilized to pay members dividends by using effective interest amounting to Rs. 15,130 million contrary to the provisions of the Act.

2.2.6 Lack of Evidence for Audit

Evidence required for the establishment of following each item had not been made available for audit.

(a) Boards of Survey Reports relating to fixed assets valued at Rs. 417.9 million as at 31 December 2014 to verify their physical existence.

(b) Approval of the Cabinet of Ministers obtained in terms of Section 9 of the Employees Trust Fund Act, No.46 of 1980 for the Investment Policy Statement of the Board.

2.3 Accounts Receivable and Payable

The following observations are made.

(a) The Board had not taken action even by the end of the year under review to settle the members contributions totalling Rs. 29.2 million comprising the unclaimed death benefits of Rs. 9 million increasing continuously since the year 1995, the retained benefits of Rs. 14 million brought forward since the year 2001, unclaimed benefits of Rs. 4.8 million and the contributions received from Money Orders from the Postal Department amounting to Rs. 1.4 million.

(b) Necessary steps had not been taken to recover a loan totalling Rs.1.5 million receivable from 9 officers.

(c) Action had not been taken to settle unrealized money orders brought forward since a period of nearly 8 years in 2 bank accounts and value of cheques not produced for payments amounting to Rs.1,091,284 and unidentified difference of 07 bank accounts amounting to Rs.130,305 even by the end of the year under review.

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

Instances of non-compliance with the following laws, rules, regulations and management decisions were observed in audit.

Reference to Laws, Rules, Regulations and Management Decisions	Non-compliance
(a) Sections 8 (g) and (h) of the Employees Trust Fund Act No.46 of 1980	Although a statement of investment indicating declared value of the investment, purchasing price and market value for each year should be prepared and forwarded to the Minister before 30 September of the year following, action had not been taken accordingly.
(b) Paragraph 02 of the Letter No. DMS/C2/2/42 of 05 February 2013 of the Department of Management Services	New salary scales approved by the Board of Directors had been implemented with effect from 01 May 2013 contrary to the Scheme of Recruitments and Promotions approved by the Department of Management Services
(c) Treasury Circular No. 1024/600/29 CD of 12 December 1963	The approval of the General Treasury had not been obtained for the Financial Code of the Board .
(d) Circular No.2013/03 dated 15 February 2013 of the Administration and Human Resources Division	Although an officer who obtained a vehicle loan cannot be granted a loan for vehicles until the expiry of 5 years, 18 officers of the Board had been granted vehicle loans amounting to Rs.15 million before the expiry of the period of 05 years.

3. Financial Review

3.1 Financial Results

Operations of the Board for the year under review had resulted in a surplus of Rs.17,132 million as compared with the corresponding surplus of Rs. 15,368 million for the preceding year thus indicating an increase of Rs. 1,764 million in the financial result of the year under review

3.2 Analytical Financial Review

The total entitlement of the members during the 07 preceding years and the manner of distribution of such total entitlement as the total contributions and the accumulated interest are given below.

Year	Total Contribution	Accumulated Interest	Members' Entitlement as at 31 December
	Rs.Million	Rs.Million	Rs.Million
2008	42,735	46,134	88,869
2009	48,396	54,661	103,057
2010	55,242	64,610	119,852
2011	62,758	72,728	135,486
2012	71,563	82,068	153,631
2013	81,347	92,905	174,252
2014	90,587	103,281	193,868

According to the above information, 46.73 per cent and 53.27 per cent of the total entitlement of the members represented contributions and the accumulated interest respectively by the year 2014. The total members' entitlement and the total contributions had increased by 11.26 per cent and 11.36 per cent respectively in the year 2014 as compared with the year 2013.

3.3 Legal Action Instituted Against/ by the Institution

The following observations are made.

(a) A sum of Rs.21 million had been paid as a compensation to a private company on an unfavourable judgement delivered against the Board for breach of an agreement entered into without consulting the Attorney General . As a result of an appeal made to the Commercial Courts by the Board against this judgement, a bank guarantee equal to the above value had been handed over to the Court by the plaintiff company. Even though this money had been brought to account as a receivable amount to the

Board, the payment of this money had been made on an unfavourable judgement and as such, there was an uncertainty in getting back this money. However, this judicial process had not been finalized even by 30 June 2015.

(b) A sum of Rs.13 million was receivable to the Board by the end of the year under review in respect of the investment properties leased out to 2 companies since the year 2011 without being reassessed. In order to recover only Rs. 5 million of the above amount, legal action had been instituted against one of the above companies.

4. Operating Review

4.1 Performance

The following observations are made.

(a) The position of the performance of the Board as at the end of the year 2014 is given below.

Particulars	Actual Number	Number relating to the operation of the Board
Employment in the Private Sector and Semi-Government Sector	3,723,947	2,400,000
Employers	235,872	74,276
Number of Accounts of the Members of the Fund (Million)	12.00	2.4

Source:- Report of the Central Bank of Sri Lanka-2014

In terms of the amendment made by Section 7 of the Employees Trust Fund (Amendment) Act, No 47 of 1988 to the Section 20 (1) of the Employees Trust Fund Act No.46 of 1980, the Employees Trust Fund had been granted permission to enroll self-employees. Nevertheless, out of 2,687,257 self-employees reported in Sri Lanka as at 31 December 2014, only 36,912 or 1.37 of the total self-employees could have been able to enroll as the members of the Fund. The contribution received as at 30 June 2015 was Rs.148 million in this connection.

(b) Information relating to the scheme of awarding scholarships implemented by the Board during the period of 07 preceding years is given below.

Year	Active number of members contributed to the Fund	Number of members whose children obtained Scholarships	Cost of Grade Five Scholarships	Cost of Advanced Level Scholarships	Total cost of Scholarships
			Rs.	Rs.	Rs.
2008	2,100,000	2,497	26,084,760	-	26,084,760
2009	2,100,000	3,000	46,811,006	-	46,811,006
2010	2,100,000	3,000	45,385,680	-	45,385,680
2011	2,100,000	6,669	74,051,599	23,640,000	97,691,599
2012	2,200,000	6,962	75,775,685	23,604,000	99,379,685
2013	2,200,000	6,982	84,124,844	17,888,234	102,013,078
2014	2,400,000	7,301	84,975,000	19,632,000	104,607,000
			434,208,574	84,764,234	521,972,808

Out of the overall membership of 2,400,000, the scholarships had been awarded to 7,301 members during the year under review. The Board had not paid attention even by the end of the year under review to improve the education level of members' children who had not passed the scholarship examination and who are unable to continue their education and to make proper arrangement to make them aware of it.

(c) The active statistical data such as the overall number of members, number of Active Accounts and employers of the Employees' Trust Fund as at 31 December 2014 as compared with the data of the Employees' Provident Fund are given below.

	According to the Employees' Provident Fund	**According to the Employees' Trust Fund**
Total Number of Members' Accounts	15,400,000	12,000,000
Number of Active Accounts for which contributions are sent.	2,400,000	2,400,000
Number of Employers	71,000	74,276

Percentage of Benefits paid in the year 2014 (with the interest)	10.5	10.0

Source:- Report of the Central Bank of Sri Lanka - 2014

According to the above information, the Employees Trust Fund with the capacity and opportunities for the members of the approved provident funds and the self-employees to make their contribution was inadequate to reach the targets as compared with the Employees Provident Fund.

4.2 Management Inefficiencies

The following observations are made.

(a) The increase in the value of the share price of 18 companies as at 31 December 2014 stated as the investment portfolio available for sale up on the value in the share market brought forward by writing off the cost as at 01 January 2014 had been indicated as Rs.723 million, whereas according to the average purchasing cost of those 18 companies as at 01 January 2014, the increase in the value of the share market was Rs.123.9 million. Accordingly, share price had been brought to account on the market value by writing off unfavourable purchasing cost and as a result, the benefit of the increase in the share market value had been over stated by 83 per cent in the financial statements.

(b) Despite being informed by the Circular No.01/2008 dated 03 March 2008 of the Treasury Operation that investment of funds with direct or indirect involvement to the Government in any financial institute other than the state banks should be suspended with immediate effect, Treasury Bonds, the face value of which amounted to Rs.250,000,000 and Rs.462,549,361 had been purchased from 2 financial institutions in the secondary market on 24 December 2014 and 21 May 2015 by paying Rs.292,504,500 and Rs.578,158,948 respectively.

(c) The Employees Trust Fund which is considered as one of the main institutions engaging in the purchasing of Treasury Bonds in Sri Lanka had purchased Treasury Bonds valued at Rs.173,573.8 million as at 31 December 2014, whereas necessary action has not been taken to register for the purchase of Treasury Bonds directly from the Treasury Bonds auctions of the Sri Lanka Central Bank even by 30 June 2015.

(d) The Board had maintained an average bank balance of approximately Rs. 500 million in a savings accounts during the first part of the year under review and a balance of Rs. 700 million to Rs.1,933 million from August 2014 to January 2015. The Board had received an interest income of Rs.27 million from this bank account during the year 2014. If the Board had invested this money in a fixed deposit account during that period, a gross interest income of Rs.49 million could have been earned.

(e) A sum of Rs.4 million invested in the purchase of 178,700 shares of a dormant textile company had been written off from the books stating that there was no any course of action to be taken in that connection. This company had been eliminated from the official list for over a period of 5 years and the Board had not received any benefit from the aforesaid investment.

(f) Although a sum of Rs. 12 million invested in promissory notes and Rs.7 million invested in debentures of a group of companies should have been realized in the year 2002 and 2007 respectively, the Board had failed to get this money realized even by 30 June 2015.

(g) Debenture interest amounting to Rs.12 million due from an estate company had not been recovered even by 30 June 2015.

(h) Shares in 15 companies had been sold at a price less than the cost in the year under review thus incurring a loss of Rs. 213.5 million. The loss incurred by the sale of shares of 6 companies in the preceding year was Rs.22 million.

(i) The Board had invested a sum of Rs. 10 million for the purchase of 1,000,000 units in a Unit Trust Fund in the year 1997. However, any return whatsoever on this investment had not been received by the Board during the period of 18 years from the date of commencement of the investment up to the end of the year under review. However, had this money been invested even at a minimum interest rate of 5 per cent during the relevant period, the estimated gross income of approximately Rs. 14 million could have been earned. Nevertheless, having determined the market value of a unit as Rs.137.72 though the cost of which was Rs.10 per unit of this Unit Trust Fund which has not generated any benefit for a number of years , financial statements had been prepared by adjusting Rs.127.7 million to the accounts.

(j) The Board had not received any income from the investment of Rs.775 million in 7,740,783 shares of 12 companies made in the year 2014 on the basis of share market value. This investment had included a sum of Rs. 2 million invested in a computer company, the going concern of which was uncertain and Rs.2 million invested in a Finance Company which was continuously sustaining losses. Details on the invested companies from which no such income was received during the past 5 years are given below.

Year	**Number of Companies**	**Number of Invested Shares**	**Amount Invested**
			Rs.
2010	17	4,111,468	119,083,880
2011	18	7,683,979	163,867,080
2012	25	13,046,750	226,125,038
2013	24	18,817,090	700,560,142
2014	12	7,740,783	775,039,968

(k) Details on investment made in the share market, income received from the investment and the percentage of income in the years 2011 and 2012 are given below.

Year	Number of Companies	Number of Shares	Amount invested as at 01 January 2014	Investment income received	Percentage of income
			Rs.	Rs.	
2011	130	78,211,481	5,204,377,279	703,052,274	13.5
2012	107	101,999,123	7,713,939,116	324,179,030	4.2

The Board had not furnished a detailed investment statement and as such investment income received from the share market transactions and percentage of the income and the matters relevant to the profitability in the years 2013 and 2014 could not been included in this report.

4.3 Transactions of Contentious Nature

Overtime had been computed at the rate of 1 ½ hours for one hour and added a day's pay after completing 08 hours of work on Saturdays/Sundays and Public Holidays stating that the Board is operated under Shop and Office Employees Ordinance and as a result, the overtime cost of Rs.21 million had been incurred during the year under review. According to the above Ordinance, an Officer should serve 5 ½ days a week to obtain overtime and the annual leave is limited to 21 days. Contrary to that, officers had been allowed an annual leave of 42 days and 5 days service per week.

4.4 Identified Losses

A loss amounting to Rs.2 million had been incurred from the sale of 3 vehicles of the Board during the year under review.

5. Accountability and Good Governance

5.1 Internal Audit

The internal audit had not been planned and implemented so as to cover the significant areas such as investments, purchasing and adherence to the laws and rules of the Board in terms of Financial Regulation 133(2).

5.2 Budgetary Control

Significant variances were observed between the budgeted and actual income and expenditure, 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) Accounts Receivable and Payable
(c) Investments
(d) Maintenance of Members' Accounts