

National Housing Development Authority – 2015

The audit of consolidated financial statements of the National Housing Development Authority and its Subsidiary for the year ended 31 December 2015 comprising the statement of financial position as at 31 December 2015 and the statement of financial performance, 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 29.1 of the Housing Development Authority Act, No. 17 of 1979. My comments and observations which I consider should be published with the Annual Report of the Authority 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 Public Sector 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 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 Authority'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 Authority'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 paragraphs 2.2 and 2.3 of this report.

2. Financial Statements

2.1 Qualified Opinion – Group

In my opinion, except for the effects of the matters described in paragraphs 2.2 and 2.3 of this report, the consolidated financial statements give a true and fair view of the financial position of the National Housing Development Authority and its Subsidiary as at 31 December 2015 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

Qualified Opinion – Authority

In my opinion, except for the effects of the matters described in paragraph 2.3 of this report, the financial statements give a true and fair view of the financial position of the National Housing Development Authority as at 31 December 2015 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

2.2 Comments on Financial Statements – Group

The following observations are made.

- (a) Even though the National Housing Development Authority owned 49 per cent of the total share capital of the Sri Lanka Housing Development Finance Corporation Bank, the financial statements of the Bank had not been consolidated with the accounts of the Authority as the Authority could not exert adequate influence in the affairs of the Bank.
- (b) The consolidated financial statements had been prepared based on unaudited financial statements for the year ended 31 December 2015 of the Ocean View Development Ltd., which is the Subsidiary of the National Housing Development Authority and the net assets of the Subsidiary represented about 18 per cent of the net assets of the Authority.
- (c) The ownership of the minority shareholders of the Ocean view Development Company Limited, the subsidiary company of the National Housing Development Authority, had been understated by a sum of Rs. 526,096 in the accounts.

2.3 Comments on Financial Statements – Authority

2.3.1 Sri Lanka Public Sector Accounting Standards

The instances of non-compliance with the Sri Lanka Public Sector Accounting Standards, are as follows.

(a) Sri Lanka Public Sector Accounting Standard 03.

- (i) In case of the unavailability of a specific Sri Lanka Public Sector Accounting Standard that govern a transaction, other incident or an affair, the management should formulate an accounting policy relating thereto. Nevertheless, the accounting policy applied in connection with the accounting of Property, Plant and Equipment purchased on the Government grants, had not been disclosed in the financial statements.
- (ii) As an accounting policy had not been formulated for accounting the financial assets, the financial assets representing 74 per cent of the assets belonging to the Authority, had not been shown to its fair value in the financial statements.

(b) Sri Lanka Public Sector Accounting Standard 09

Although it was stated in accordance with the Accounting Policy 4.3 that the stocks would be accounted at cost or the net realizable value, whichever is lower, the stock of houses costing Rs. 69.57 million had been accounted at cost without computing and reconciling the net realizable value.

2.3.2 Accounting Deficiencies

The following observations are made.

- (a) The value of the plots of land further remained at the housing schemes, lands of 445.2 hectares in extent vested for housing schemes, and 29 plots of land belonging to the Authority where office buildings had been permanently built at, had not been assessed and shown in the financial statements.
- (b) The balance sum of Rs. 13.31 million from the grants of the National Livestock Development Board for constructing houses, had been shown under other aids instead of being shown as accounts payable in the financial statements.
- (c) The gratuity provision for the year under review, had been overstated by a sum of Rs. 929,302 in the accounts.

- (d.) Although provisions for doubtful debts in respect of the housing loans under the debtors in the year under review, had been shown in the financial statements as Rs. 1,947,138,813, according to the computations of the audit, the provision for doubtful debts amounted to Rs. 1,952,023,561. Accordingly, provision for doubtful debts had been understated by a sum of Rs. 4,884,748 in the accounts.
- (e.) The contribution from the lottery income receivable to the Sevna Fund had not been identified on accrual basis. Instead, a sum of Rs. 112.7 million received during the year under review, had been accounted on cash basis.

2.3.3 Unexplained Differences

The following observations are made.

- (a.) A difference of Rs. 6,723,299 had existed between the current accounts maintained by the Head Office for the District Offices and the current accounts maintained at the District Offices for the Head Office.
- (b.) According to the financial statements, the value of the bank loans obtained by the Authority amounted to Rs. 3,249,996,938, but according to the letters of confirmation of balances, the value of the loans payable amounted to Rs. 3,256,226,641. Accordingly, a difference of Rs. 6,229,703 existed between the balances shown in the financial statements, and the balances confirmed by the banks.

2.3.4 Lack of Evidence for Audit

The loan agreements, and the supporting documents for the confirmation of balances in respect of the loan balance of Rs. 220,091,573 payable to the Ministry of Rehabilitation, and the Ministry of Fisheries had not been made available to audit.

2.4 Accounts Receivable and Payable

The following observations are made.

- (a.) Surplus money amounting to Rs. 47.46 million owned by the Authority had been credited to the Consolidated Fund in the year 2010 with the intention of getting it back for housing loans and future construction works of houses under the Millennium Housing Programmes on a Cabinet Decision. Although the Treasury had not confirmed that the money would be given back to the Authority, the Authority had shown this amount in the financial statements continuously as a value receivable from the Consolidated Fund.
- (b.) According to the information made available, the total of the loan balances receivable as at 31 December of the year under review amounted to Rs. 4,186 million. The loan balances included therein that had been brought forward over a period of 05 years, totalled Rs. 2,505 million representing 60 per cent of the total value. The progress in the recovery of those monies had been at a very low level.

- (c.) Out of the advances paid to contractors, stores advances, travelling advances, stores advances and sundry advances as at the end of the year under review, the Authority had not taken action to settle the sum of Rs. 20.74 million brought forward for over a period of 02 years.
- (d.) A sum of Rs. 77.83 million had remained recoverable by the Authority in respect of the employees of the Authority who had been deployed in the other Government institutions. A sum of Rs. 71.82 million thereof, had not been recovered for a period of over 05 years.
- (e.) Action had not been taken to recover a sum of Rs. 1,882,604 receivable to the Authority in respect of a land of 726.35 perches in extent granted by the Authority in the year 1998 from Athnawala Estate to a private social welfare organization for a housing project consisting of 60 houses.
- (f.) Although a sum of Rs. 21.52 million had been provided on the tax in arrears amounting to Rs. 15.33 million and the fine of Rs. 7.12 million relating thereto that remained payable to the Inland Revenue Department on behalf of **National Institute of Machinery**, action had not been taken to settle those liabilities up to the end of the year under review.
- (g.) The total of the loan balances that remained payable as at the end of the year under review amounted to Rs. 1,822.54 million, and action had not been taken for a period of over 05 years to settle a sum of Rs. 644.43 million therefrom.
- (h.) The outstanding loan installments amounting to Rs. 718.23 million and the interest in arrears amounting to Rs. 264.45 million payable for loans obtained from 07 private and public institutions for projects, had remained unsettled over a long period of time.
- (i.) Land compensation amounting to Rs. 293.27 million that had existed for a period of over 05 years as at 31 December 2015, had not been settled.

2.5 **Non-compliances with Laws, Rules, Regulations, and Management Decisions**

 The following non-compliances were observed.

Reference to Laws, Rules, and Non-compliances Regulations

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| (a) | Section 11 (b) of the Finance Act, No.38 of 1971 | Concurrence of the Minister of Finance had not been obtained in connection with investments of Rs. 1,068.63 million. |
| (b) | Financial Regulation of the Democratic Socialist Republic of Sri Lanka | |
| (i) | Financial Regulation 104(2) | Losses relating to 27 vehicle accidents had not been reported to the Auditor General . |

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| (ii) | Financial Regulation 371(2) | Advances should be settled immediately after the completion of the intended purpose. Nevertheless, advances amounting to Rs. 294,430 obtained in 10 instances, had been settled after a period of over one month. |
| (iii) | Financial Regulation 396 | Cheques that had exceeded 06 months from the date of issue and not presented to the bank, should be credited to the income, but action had not been taken in that manner on 10 cheques valued at Rs. 162,243 relating to the Head Office of the Authority and 04 District Offices. |
| (c) | Paragraph 3.3 of the Public Enterprises Circular, No.02/2013, dated 11 September 2013. | The PAYE tax amounting to Rs. 320,349 that should have been paid by deducting from the salaries of the relevant officers, had been paid by the Authority. |
| (d) | Internal Circular of Property Management No. 02 dated 22 December 2011 | In case that the first lessee had not made a transfer, and several heirs claimed rights for lease, the property should be transferred with the concurrence of all the heirs. Nevertheless, the lease rights of a house claimed by several heirs, had been transferred to a single heir without concurrence of all the heirs. |

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the deficit of the Group and the Authority for the year ended 31 December 2015 had been Rs. 1,010 million and Rs. 1,028 million respectively as compared with the corresponding deficit of Rs. 591 million and Rs. 633 million for the preceding year, thus indicating an increase of Rs. 419 million and Rs. 395 million respectively in the deficit for the year under review as compared with the preceding year. As compared with the preceding year, the increase in the deficit had mainly been attributed by the decrease in the other income of the Group and the Authority by Rs. 523 million and Rs. 462 million respectively.

In analyzing the financial results of the year under review and the 04 preceding years, a continuous deficit in the financial result of the Authority was observed. The deficit of the year 2011 amounting to Rs. 518,293,152 had increased up to Rs. 1,027,969,195 by the year under review. However, by taking into account of employee remuneration, tax paid to the Government, and the depreciation on non-current assets, the contribution of the Authority that had amounted to Rs. 324,193,053 in the year 2011, had reached to Rs. 445,636,668 by the end of the year under review.

4. Operating Review

4.1 Performance

The National Housing Development Authority had been established in terms of National Housing Development Authority Act, No. 17 of 1979 to execute the functions such as : to directly engage itself in the construction of flats, houses and other living accommodation or buildings ; to formulate schemes to establish housing development projects in order to alleviate the housing shortage, and to make land available for housing development. In addition to the Head Office, the Authority functions island wide with 26 District Offices and 03 Urban Offices.

- (a.) According to the Annual Action Plan, it had been planned to build 101,797 housing units during the year under review. Nevertheless, only 78,426 housing units representing 77 per cent , had been completed by the end of the year under review. Particulars are as follows.
- (i) Despite being planned to build 679 housing units at 05 housing schemes under the Public Private Contribution Project, no housing unit whatsoever had been built by the end of the year under review.
 - (ii) Despite being planned to repair 6,349 houses under the programme “Nagamu Purawara”, only 1,305 houses had been repaired. Furthermore, it had been planned to commence the repair of 40 houses under the Rehabilitation of new houses Programme, repairs had been commenced only on 20 houses by the end of the year.
 - (iii) Although it had been planned to grant aids for 2,500 housing units under the Sevana special aid programme, aids had been granted only for 08 housing units by the end of the year under review indicating a progress of 0.32 per cent.
 - (iv) Although a sum of Rs. 2.67 million had been incurred during the period from 1998 – 2001 by the District Office in Kandy for the construction of 16 housing units under the Galaha Housing Scheme, the construction of those houses had not been completed even by the end of the year under review.

4.2 Management Activities

The following observations are made.

- (a.) Even though the Authority had taken over the tenure of lands under Section 38(a) of the Land Acquisition Act, various parties had filed cases versus the Authority against for taking over of certain lands. However, a long period had been taken to acquire the tenure of certain lands due to the problems such as a duration of 11-38 years had been taken by the trials. Accordingly, the compensation that remained payable as at 31

December 2015, amounted to Rs. 233,315,880, whilst the interest in arrears payable thereon amounted to Rs. 47,132,014. The following observations are further made in this connection.

- (i) The Authority had taken over the tenure of 58 plots of land 159.93 hectares in extent by the end of the year under review for which compensation had either been paid or scheduled to be paid. As the process of acquiring lands had taken a long period of time, those lands had been encroached.
 - (ii) Due to failure in taking action to pay compensation in a timely manner for lands 165.20 hectares in extent taken over during the period from 1979-2015, the value of compensation that remained payable as at 31 December 2015 for private lands, amounted to Rs. 276.5 million.
 - (iii) Although a sum of Rs. 60 million had been allocated for the year under review by the Treasury to acquire lands, the Authority had incurred only a sum of Rs. 32.9 million on acquiring lands. Furthermore, a sum of Rs. 11.15 million therefrom had been incurred for paying the interest resulted in due to delay in paying compensation.
- (b.) The approval for the building plans should be obtained from the relevant Local Authorities prior to the implementation of the housing schemes. However, as houses had been built without doing so, problems had arisen by the end of the year under review in obtaining Certificates of Conformity for 2,247 houses in 39 housing schemes. Accordingly, due to failure in establishing management Corporations by vesting the houses of the housing schemes in the owners, the Authority itself further had to carry out the maintenance and repairs of those housing schemes, and the Authority had to incur sums of Rs. 16.43 million and Rs. 167.64 million respectively in the year under review.
- (c.) Of the loan amounting to Rs. 4,097,171 granted during the years 1989-1994 in order to purchase solar panels for 526 families in Kurunegala district, any amount had not been recovered in the year under review, and a specific methodology had not been implemented as well to recover those monies.
- (d.) Although the Authority had incurred a construction cost of Rs. 20 million on the Mahaiyawa Housing Project consisting of 32 houses implemented by the Authority on a land belonging to the Kandy Municipal Council, the monies relating thereto had not been recovered from the Kandy Municipal Council even by the end of the year under review.
- (e.) According to the report of the land survey conducted on the lands taken over/owned by the Authority in the year 2015, lands of 445.2 hectares in extent had been identified, but 111.52 hectares of land therefrom had been encroached by the end of the year under review. The survey on the lands in 04 districts pertaining to the Northern Province, had not been conducted even up to the end of the year under review.

- (f.) Although a sum of Rs. 8,686,000 had been paid to the Urban Development Authority on 20 March 2012 for taking over the land in Ratnapura, named as Galkaduwwawatta on an assessment obtained on 19 April 2000, the Authority had decided not to take over the land on 07 July 2014. However, action had not been taken up to the end of the year under review to recover that amount paid.
- (g.) The stock of houses had comprised of reserved houses valued at Rs. 43,823,559, the remaining houses, and shops for a period of over 05 years. Action had not properly been taken by the Authority to recover the dues in arrears receivable with respect to the reserved houses, and sell the remaining houses and shops in the stock promptly.
- (h.) The Authority had not taken proper action to recover or settle the housing loans amounting to Rs. 5,965,000 granted under the Thrift and Credit Co-operative Societies (TCCS) Loan Scheme by the Jaffna District Office as 1,468 housing loan files had been misplaced.
- (i.) Two motor vehicles costing Rs. 1,765,000 existed in the pool of vehicles of the Authority had remained misplaced since the year 2008, but action had not been taken by the Authority to conduct a formal inquiry and recover the loss from the officers responsible.
- (j.) A sum of Rs. 5,459,920 had been spent by the Authority for printing diaries and calendars for the year 2015. However, the Authority had received diaries and calendars valued only at Rs. 2,877,920. Action had not been taken by the Authority to recover the sum of Rs. 2,582,000 paid for the diaries and calendars that had not been received by the Authority.
- (k.) The total of the loans granted to the Housing Loan Programme amounted to Rs. 19,410 million by the end of the year under review, and it comprised 340,880 debtors. Of the said loan balance, a sum of Rs. 3,103 million had reached maturity, and the sum scheduled to reach maturity amounted to Rs. 16,307 million. A sum of Rs. 54.75 million had been incurred in the year on loan recovery commissions, but the progress in the recovery of loans had increased only by 2 per cent. The percentage of the dormant debtors had been 75 per cent by the end of the year under review.

4.3 Transactions of Contentious Nature

Despite a separate Engineering Division comprising 93 personnel had functioned under the Authority and the possibility of executing the relevant constructions through the subcontractors, the repairs on condominiums valued at Rs. 167.64 million had been assigned to the State Engineering Corporation.

4.4 Uneconomic Transactions

Even though a period of 18 years had elapsed after the investment of Rs. 120 million in the Subsidiary Company by the Authority, the Authority had not received any returns whatsoever therefrom in the other years except the years 2011 and 2013.

4.5 Identified Losses

The following observations are made.

- (a.) Several floors of the National Housing Development Authority Building had been leased out to the Housing Development Finance Corporation Bank. As the lease rents had been decreased without any justifiable reason in accordance with a new assessment made on 01 January 2008, a cumulative lease rent income amounting to Rs. 37,249,606 had been deprived of by the end of the year under review.
- (b.) It had been stated that the valuation of the immediate year should be obtained in disposing properties to the encroachers in terms of the Cabinet Decision No.140/98 of 17 December 1998. However, contrary to it, the loss sustained by the Authority amounted to Rs.10.3 million due to the basis of the valuation of the year 1998 had been applied in disposing the house No. D/V/2/2/L of the Manning Town Housing Scheme.
- (c.) Despite having the methodologies approved by the Cabinet of Ministers for the regularization of encroachers, three encroachers of the Gampaha, Wewalduwa Housing Scheme had been regularized contrary to it, and a loss of Rs.3,772,499 had been sustained by the Authority.
- (d.) As competitive bidding had not been followed by the Authority for printing calendars for the year 2015 contrary to Guideline 2.7.5 of the Procurement Guidelines, the Authority had sustained a loss of about Rs. 1.18 million as a calendar had been printed for Rs. 190 of which the printing cost at the open market would have been Rs. 85.
- (e.) As the car parks C and D, and A and B of the Housing Scheme in Maligawatta had been closed without any justifiable reason for periods of 12 months and 06 months respectively, the income that the Authority had been deprived of in the year under review, amounted to Rs. 925,200.
- (f.) Construction and disposal of flats should be carried out in accordance with Property Management Circular, No. 2011/ 07. Nevertheless, buyers had been selected on the approval of the Chairman of the Authority without transparency by considering only the requests directly made by the buyers. The housing scheme that had been planned by the Authority to sell on the pre sales basis, had been sold on installment basis. As the remaining 04 houses of the said scheme the estimated selling price of which had been Rs. 58,650,000 had been sold for a sum of Rs. 47,359,000 on the Decision No. 16/2013, of the Board of Directors, dated 10 September 2013, a loss of Rs. 11,291,000 had been sustained by the Authority.

4.6 Contract Administration

It had been decided to build 560 housing units of the Mihindupura Housing Scheme for the duration 2014-2015 at a cost of Rs. 6,300 million under the Public Private contribution Project. The works thereon had been halted when the progress of the construction had been 2 per cent due to the delay of the contractor in taking action to renew the performance bond of the project.

4.7 Resources of the Authority Released to other Public Institutions

Salaries amounting to Rs. 2,540,836 had been paid by the end of the year under review to 07 officers released to the Line Ministry contrary to the provisions of Paragraph 9.4 of the Public Enterprises Circular, No. PED/12, dated 02 June 2003.

4.8 Personnel Administration

According to the Human Resources Plan of the Authority, the number of approved cadre had been 1,376, but the actual cadre had been 2,180 as at 31 December of the year under review, thus observing an excess cadre of 804. Particulars are as follows.

- (a.) Although 47 vacancies had existed in the executive, middle, and junior management levels, the cadre of the Management Assistant and the primary level comprised of 851 employees in excess of the cadre approved by the Department of Management Services.
- (b.) Contrary to the provisions in Section 9.3.1 of the Public Enterprises Circular No. PED/12 of 02 June 2003, thirty five officers had been deployed in acting capacity and to covering up duties over periods ranging from 03 months to 09 years.
- (c.) According to the Scheme of Recruitment of the Authority, a public notice should be published in the newspapers when making recruitments for the post of Deputy General Manager (Human Resource Management, and Administration), but this recruitment had been made without doing so. In recruiting for the said post, it was necessary to have obtained minimum educational qualifications stated in the Scheme of Recruitment of the Authority – a degree in the relevant field and a postgraduate degree together with a service period of at least 15 years at a post in managerial level of a Public institution. However, the officer recruited had not fulfilled the said educational qualifications and the service experience, but 15 salary increments had been granted to him.

5. Accountability and Good Governance

5.1 Corporate Plan

Although one million houses should have been built according to the One Million House Programme introduced by the Government under the Janasevana Housing Programme in the year 2011, the number of houses expected to be built by the Authority for the period 2015-2019 for achieving those targets, represented only 34.32 of the total number of houses.

5.2 Internal Audit

Although the approved cadre for the Internal Audit Unit had been 47, only 31 had been employed therein by the end of the year under review. Emphasis had not adequately been placed on the performance audit through the functions included in the Annual Audit Programme. Some of the District Offices had not been audited by the Internal Audit Unit over several years.

5.3 Budgetary Control

As significant variances were observed between the budgeted and the actual expenditure, the budget had not been made use of as an effective instrument of financial control.

5.4 Tabling of Annual Reports

Reports for the years 2012 and 2013 had not been tabled in Parliament even up to 30 July 2016 by the Authority.

5.5 Unresolved Audit Paragraphs

Only the Valuation of the Valuer of the Authority had been obtained for the sale of the Liberty Plaza Circuit Bungalow owned by the Authority to the Ocean View Development Pvt. Ltd. without obtaining the valuation of Government Valuer. However, the value of the valuation of the Government Valuer obtained later relating to the said property had been Rs. 11,520,000, whereas the selling price had been Rs. 9,000,000. This situation had been discussed at the COPE meeting held on 23 November 2012, and in accordance with the Directive therein, it was ordered to take disciplinary action against the officers responsible for the said irregular transaction. Nevertheless, action had not been taken in that connection even up to 30 June 2016.

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 Authority from time to time. Special attention is needed in respect of the following areas of control.

Areas of Systems and
Controls

Observations

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| (a.) Control of Advances | (i) Failure to maintain a Register for the advances granted for purchasing spare parts. |
| | (ii) Granting advances again even when the advances obtained had remained unsettled. |
| | (iii) When obtaining advances an estimate prepared properly, had not been presented, making it possible for the officer obtaining advances to retain an extensive amount of balance money in hand. |
| (b.) Procurement Procedure | Failure to follow the National Competitive Bidding method |
| (c.) Human Resource Management | Making recruitments contrary to the Scheme of Recruitment, and for the posts not included therein. |
| (d.) Budgetary Control | (i) Failure to prepare the budget in a realistic manner. |
| | (ii) Failure to follow a proper methodology to control expenses. |