Associated Newspapers of Ceylon Limited - 2016

The audit of consolidated financial statements of the Associated Newspapers of Ceylon Limited ("the Company") and its Subsidiaries for the year ended 31 December 2016 comprising the statements of financial position as at 31 December 2016 and the statements of comprehensive income, statements of changes in equity and statement of cash flows 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 16 of the Associated Newspapers of Ceylon Limited (Special Provision) Law, No.28 of 1973. My comments and observations which I consider should be published with the Annual Report of the Company 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 consolidated financial statements in accordance with Sri Lanka Accounting Standards for Small and Medium- sized Entities (SLFRS for SMEs) and for such internal control as the management determines is necessary to enable the preparation of consolidated 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 consolidated financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards, consistent with International Auditing Standard of Supreme Audit Institution (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 consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the consolidated 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 Company'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 consolidated 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 Opinions

(a) Qualified Opinion – The Company

In my opinion, except for the effects of the adjustments arising from the matters described in paragraph 2.2.2 of this report, the financial statements give a true and fair view of the financial position of the Associated Newspapers of Ceylon Limited (the Company) as at 31 December 2016 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards for Small and Medium – sized Entities.

(b) Qualified Opinion – The Group

In my opinion, except for the effects of the adjustments arising from the matters described in paragraph 2.2 of this report, the consolidated financial statements give a true and fair view of the financial position of the Associated Newspapers of Ceylon Limited (the Company) and its Subsidiaries as at 31 December 2016 and their financial performances and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards for Small and Medium – sized Entities.

2.2 Comments on Financial Statements

2.2.1 Comments on Group Financial Statements

Audited financial statements of the Lake House Property Development (Pvt) Limited, Observer Jobs (Pvt) Limited and Lake House Connect (Pvt) Limited, which are fully owned Subsidiaries of the Company had been taken for preparing the consolidated financial statements. The qualified opinions based on the following matters had been expressed by me on the financial statements submitted by these Subsidiaries for the year under review.

Lake House Connect (Pvt) Limited

(i) Proper records of prime entries and supporting documents relating to first six months of the year under review had not been maintained to scrutinize those transactions. Further, the general ledger accounts had also not been properly balanced for the same period.

(ii) Fully depreciated property, plant and equipment costing Rs.782,574 as at 31 December 2016 are being continuously used by the Company without reviewing its useful life as prescribed by Section 17.19 of SLFRS for SMEs.

(iii) A loss of Rs. 4,374,033 incurred by way of printing magazines through a discontinued operation since March 2016 had not been separately disclosed in the financial statements for the year under review.

Lake House Property Development (Pvt) Limited

(i) Proper records of prime entries, supporting documents, and payment vouchers for administrative expenses amounted to Rs.136,648 had not been maintained to scrutinize those transactions.

(ii) Maintenance fee, water bills, electricity bills and salaries aggregating Rs. 661,649 paid on behalf of the Parent Company had been recorded as expenses of the Company without being recovered from the Parent Company.

(iii) A loan amounted to Rs.3,500,000 given to the Parent Company which was not expected to realize within twelve months after the reporting date had been shown as current asset without considering its nature in terms of Section 4.4 of the Sri Lanka Accounting Standards for Small and Medium- sized Entities (SLFRS for SMEs).

Observer Jobs (Pvt) Limited

(i) A Board decision was taken on 08 February 2016 to write off the payable amount of Rs. 4,496,257 appeared as at 01 January 2016 in the account of Parent Company. Although this balance had been credited to retained earnings during the year under review, proper disclosures had not been made as per Section 3.2 (a) of the Sri Lanka Accounting Standard for Small and Medium- sized Entities (SLFRS for SMEs).

(ii) As per Section 10.21 of the Sri Lanka Accounting Standard for Small and Medium-sized Entities (SLFRS for SMEs), salaries and wages amounted to Rs. 120,746 with respect to the month of December 2015, but paid in the month of February 2016 had not been restated retrospectively.

2.2.2 Comments on Financial Statements of the Company

2.2.2.1 Compliance with Sri Lanka Accounting Standards for Small and Medium-Sized Entities (SLFRS for SMEs)

The following observations are made.

(a)	Section 4.4	Outstanding staff loan balances amounted to Rs.130,597,000 had not been categorized and shown separately as current and non-current assets, while the deposits made by newspaper agents, regular advertiser and others aggregating Rs.171,159,000 had been shown as non-current liabilities irrespective of its nature.

(b)	Section 7.8 (a), (b) and (c)	The effect of changes in the provision for doubtful debts on other debtors and other receivables amounting to Rs.6,015,000 and Rs.4,527,000 respectively and a loss on disposal of assets valued at Rs. 3,969,452 had not been properly adjusted in arriving the cash flow from operating activities.
(c)	Section 13.4	The closing stocks such as newsprint, commercial printing materials, machinery spare parts etc. had been measured at cost as Rs.327,509,000 without computing the net realizable value of them.
(d)	Section 17.19	Fully depreciated assets costing Rs.984,000,000 are being continuously used by the Company without reviewing its useful life.
(e)	Section 21.14	A brief description about the nature of the obligation and expected amount and timing of any resulting payments had not been disclosed with regard to 31 legal cases pending against the Company.
(f)	Section 28.41	The Company had not disclosed the required information as requested by this Section.

2.2.2.2 Accounting Deficiencies

The following observations are made.

(a) The deductions from salaries of employees due to late attendance prior to the year 2016 amounted to Rs.12,338,537 had been credited to the salary account during the year under review instead of adjusting to the retained earnings. As such, the profit for the year under review had been overstated by that amount.

(b) The sales proceeds of old newspapers and the cost of those newspapers amounting to Rs.32,114,000 and Rs.181,327,666 respectively had been treated as other income and cost of sales respectively without being separately shown the loss of Rs.149,213,666 in the financial statements.

(c) The plan asset and plan liability amounted to Rs.264,877,000 and Rs. 285,688,000 respectively held in the Gratuity Trust Fund related to the retirement benefit obligation of the Company had not been brought to the financial statements for the year under review.

2.2.2.3 Un-reconciled Accounts

The following observations are made.

(a) A difference of Rs.8,513,049 was observed between the debtor balances as at 31 December 2016 shown in the financial statements and the registers maintained by Circulation Department of the Company.

(b) Differences aggregating Rs.2,412,971 were observed between the revenue shown in the register maintained by Commercial Printing Department of the Company and the revenue recognized in the financial statements for the year under review.

(c) Differences aggregating Rs.19,207,312 were observed between the value of ledger balance, and the value of physically verified stock balances relating to 16 items of stocks which reconciliations had been made. However, a further difference of Rs.1,314,480 had been observed even after the reconciliations. Further, prior year errors aggregating Rs.3,534,051 relating to 10 items of stocks had not been adjusted even in the year under review.

(d) According to the individual customer ledger accounts, the interest paid for news agencies was Rs.2,977,811. However, it was shown as Rs.2,297,074 in the financial statements for the year under review. Hence, a difference of Rs. 680,737 was observed in audit.

2.3 Accounts Receivable and Payable

The following observations are made.

(a) Eighty eight money orders to the total value of Rs.326,366 received to a bank account of the Company were still outstanding for the period ranging from one to five years and more than five years without realization.

(b) Out of trade debtors of Rs.796,711,000 as 31 December 2016, a sum of Rs.101,547,882 had been outstanding for more than one year. Further, an amount of Rs.28,061,903 or 28 per cent of this balance had been referred to the Legal Section in order to take legal actions. However, considerable delays ranging from 05 years to 18 years had been observed in performing legal actions against those debtors which referred to Legal Section. Moreover, the legal actions against the news agencies which terminated and defaulted the outstanding balances of Rs.6,266,419 for more than two years had not been taken even up to the end of the year under review.

(c) A sum of Rs. 1,610,430 spent for “Mihinthale Aloka Poojawa” by the Company during the year under review had been recorded as receivable instead of being recognized as expenses.

(d) The Company had issued newspapers valued at Rs. 8,548,322 as at 31 December 2016 to the customers who had not continued their subscriptions with the Company. Out of that amount, a sum of Rs.4,065,309 was outstanding since 2011 to 2015. However, the total outstanding balance had been reduced to Rs.5,775,258 by 31 August 2017.

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

The following instances of non-compliance were observed in audit.

	Reference to Laws, Rules, Regulations and Management Decisions etc.	Non-compliance
(a)	Section 114 (1) of the Inland Revenue Act, No.10 of 2006 and Section 8.7 of the Public Enterprises Circular No. PED/12 dated 02 June 2003.	The Company had paid the Pay As You Earn (PAYE) tax amounting to Rs. 5,163,583 on bonus payment made to its employees during the year under review without deducting from the bonus payments of the employees.
(b)	Public Enterprises Circulars	
	(i) No. PED/12 of 02 June 2003 - Section 9.2 (a)	The approved Cadre of the Company should be included in the Corporate Plan. Instead, the actual Cadre as at 31 July 2006 and 30 November 2013 had been included in the Corporate Plan prepared for the period of 2013 - 2016.
	- Section 9.3.1	Every public enterprise should have prepared a Scheme of Recruitments and Promotions for each post and the schemes should be approved by the Board and the appropriate Ministry with the concurrence of the Department of Public Enterprises and the General Treasury. However, the Company had not prepared a Scheme of Recruitments and Promotions as requested.
	(ii) No. PED 3/2015 of 17 June 2015	Although the Company has been categorized as a state owned enterprise, it has not followed any directions laid down by the Ministry of Finance or Department of Public Enterprises up to now. In this connection the Director Finance in his letter dated 29 June 2017 had informed me “that the management had a discussion with the Minister of Finance to obtain a waiver to deviate from PED Circulars. However, such approval has not yet been received”.

(iv) No. PED 05/2016 of 16 December 2016	The Companies which had earned profits and paid incentives based on attendance, performance or any other form of incentives, could pay only a bonus of Rs.13,500 for the year 2016. However, sums aggregating Rs.168.8 million had been paid by the Company as bonus for the year under review on the basis of 4 ½ months basic salary.

3. Financial Review

3.1 Financial Results

According to the financial statements of the Company and the consolidated financial statements of the Group, the operations of the Company and the Group for the year ended 31 December 2016 had resulted in a pre-tax net profit of Rs.40,631,000 and Rs. 29,008,000 respectively as compared with the corresponding pre-tax net profit of Rs. 26,111,000 and Rs.16,204,000 respectively for the preceding year, thus indicating an improvement of Rs.14,520,000 and Rs.12,804,000 respectively in the financial results. Increase of advertising income by Rs.2,548,682,715 was the main reason attributed for the improvement in financial results of the Company for the year under review.

After taking into account the salaries, taxes and depreciation charged for the years (before dividend and fair value adjustment) 2015 and 2016, the value addition of the Company was Rs. 1,784,471,000 and Rs. 2,153,741,000 respectively showing an increase of 20.7 per cent in the value addition.

3.2 Analytical Financial Review

3.2.1 Significant Accounting Ratios

According to the financial statements presented, some important accounting ratios of the Company are given below.

	2016 Percentage	**2015 Percentage**
Gross Profit Margin	53.69	53.20
Profit mark up (Gross profit on cost of sales)	115.92	113.68
Administration Cost on Turnover	43.85	43.43
Selling and Distribution Cost on Turnover	10.86	11.10
Finance Cost on Turnover	1.64	2.00
Current Ratio	2.12	2.05
Acid Test Ratio	1.60	1.58

The gross profit margin and the profit markup of the Company for the year under review, as compared with the preceding year had increased only by 0.49 per cent and 2.24 per cent respectively.

4 Operating Review

4.1 Performance

In terms of Sections 2 and 17 of the Associated Newspapers of Ceylon Ltd (Special Provision) Law No. 28 of 1973, published in the Extraordinary Gazette of the Republic of Sri Lanka No: 71/1 of 04 August 1973, the main objectives of the Company are (i) to establish, acquire, print, publish and circulate any newspaper or other publications and carry on all or any of the business of printers, stationers, machines rulers, numerical printers, lithographers, type founders etc. (ii) to carry on the business of manufactures of distributers of and dealers in engravings, prints, pictures, drawings and, advertising agents, advertisement contractors and designers of advertisements. (iii) to carry on the business of manufacturers of films and other apparatuses and machines in connection with mechanical reproduction or transmission of pictures, amusements, music and sounds (iv) to carry on the business as tourist agents

The following observations are made in performing the above objectives during the year under review.

(a) The Company had published 06 kinds of newspapers and 09 kinds of periodicals during the year under review and 06 kinds of newspapers and 25 kinds of periodicals during the preceding year. However, 11 periodicals published in 2015 had been discontinued while another 05 periodicals published had been issued as supplementary together with "Dinamina" and "Silumina" Newspapers in order to attracting the readers during the year under review. Further, the marketing expenses related to sales of newspapers for the year under review had also increased by Rs.14 million or 49 per cent with compared to the preceding year. Nevertheless, the overall sales income received from all 06 newspapers and 07 periodicals published in the year under review had decreased by Rs.67.9 million with compared to the preceding year.

(b) The number of copies sold out of 06 newspapers and 08 periodicals had reduced by 2,369,491 or 10 per cent during the year under review. However, the periodical calling "Mihira" had only shown an increasing trend in sales volume in the year 2016. Number copies printed in 06 newspapers and 07 periodicals had also been decreased in 2016 and the overall decline was 1,972,647 copies or by 7 per cent with compared to the preceding year.

(c) Income earned from commercial printings and annual publications had been declined from Rs.315.8 million in 2015 to Rs.51.4 million or by 84 per cent in 2016 mainly due to closure of Annual Publication Department and stoppage of printing of government school text books and telephone directories.

(d) The overall advertisement income had been increased by Rs.459 million or 22 per cent as compared with the preceding year as a result of increase of advertisement rates and introducing an incentive scheme to the advertising/sales managers in order to attract more advertisements to the Company during the year under review.

(e) The Company had entered into two lease agreements with the People's Bank and the Bank of Ceylon to lease out two premises in the Head Office building and a sum of Rs.33.4 million had been earned as rent income for the year under review. However, there would have been a net loss of Rs.1.04 million for the year under review if not earned this rent income during the year 2016.

4.2 Management Activities

The following observations are made.

(a) Lake House Connect (Pvt) Ltd (formerly known as Business Lanka AN (Pvt) Limited) which commenced its operational activities during the year 2013, had been incurred a cumulative loss of Rs. 19,433,501 as at 31 December 2016. In the absence of a proper recovery policy, the doubtful debts had been increased significantly and therefore, the balance of the trade debtors as at the end of the year under review was amounted to Rs.15,542,704 and provision for bad debts was Rs. 14,456,255.

(b) Observer Jobs (Pvt) Ltd (formerly known as Info Media (Pvt) Ltd), had been incurred a cumulative loss of Rs. 11,615,486 as at 31 December 2016. An amount of Rs. 5,437,267 or 322 per cent had been paid as salaries and wages with compared to its revenue of Rs. 1,686,480 earned during the year under review. As a result of continuous losses, the Board of the Company had decided on 08 of February 2016 to write off the amount of Rs. 4,496,257 to be received from this Subsidiary.

(c) Lake House Property Development (Pvt) Ltd, established in 1985 in order to engage in property development business had not generated any cash flow from operating activities even up to the end of the year under review.

(d) Total value of the dishonoured cheques as at December 2016 was amounted to Rs.10,585,138. Out of this, 82 cheques valued at Rs.5,018,153 had been outstanding for more than one year. However, legal actions had been taken only against 31 dishonoured cheques valued at Rs. 2,501,495.

(e) Although the Company had paid an amount of Rs. 1.2 million as an interim payment for the purchase of 2400 shares from Lanka Puvath Ltd (National News Agencies of Sri Lanka) in December 2008, no return had been received from this investment even up to the end of the year under review.

4.3 Transactions of Contentious Nature

The Company had paid 10 per cent interest per annum to the news agents on their deposits kept with the Company when they entered into agreements. However, the approval of the Board of Directors for the limits of deposit, decision to pay such interest and the rate of interest had not been obtained. Although an amount of Rs. 2,977,811 had been paid for 460 news agents as interest during the year under review, no investment plan had been introduced in this regard. Subsequently, these news agents had been allowed 50 days credit period to settle their dues to the Company.

4.4 Idle or Under-utilized Assets

A land with an extent of 8 acres located at Hokandara, purchased for constructing a housing scheme had remained idle since the year 1985.

4.5 Identified Losses

A penalty of Rs.642,908 had to be paid to the Department of Education Publication during the year under review due to delayed in submission of printed books for the period from 2012 to 2015.

4.6 Release of Human Resources to Other Institutions

Nine officers including two Journalists, an Associate Editor, Managing Editor, Assistant General Manager- Technical, Photographer, Proofreader, Assistant Manager and a General Assistant had been released for services of other Government Institutions during the year under review contrary to the provisions in PED Circular No.12 of 02 June 2003. The Company had spent a sum of Rs.9,512,682 as salaries, wages and allowances on behalf of them. Although two Journalists released, six Journalists had been newly recruited during the year under review.

4.7 Personnel Management

The following observations are made.

(a) Policies and procedures for personal management to be followed by the Company had not been prepared.

(b) Although the Company had obtained service of several consultants in the field of human resources, information technology and internal audit by paying Rs. 8,041,274 during the year 2016, their contribution for the improvement of Company's performance had not been ascertained and furnished to audit.

(c) As per the Action Plan of the Company, it was planned to improve skills of employees by carrying out job analysis and assessing knowledge, skills and competency levels of employees. However, no such program had been implemented during the year under review. Only 25 per cent of local trainings and 50 per cent of overseas training had been provided as planned. Further, name of the officers, cost incurred therein, purpose of the visits and value addition to the Company etc. related to overseas training had not been furnished to audit.

(d) Ninety eight employees were in excess and 181 employees were in vacant as per the approved cadre prepared by the Company itself for Editorial Department and General Administration Department respectively as at 31 December 2016. Although 177 employees from different positions had been left from the Company under a Voluntary Retirement Scheme (VRS) introduced during the year under review after paying Rs.163,513,000 as compensation, 05 employees on permanent basis and 105 employees on contract basis had been newly recruited in 2016.

5. Accountability and Good Governance

5.1 Corporate Plan

A Corporate Plan for the period of 2013 – 2016 had been prepared by the Company in terms of Section 5 of the Public Enterprises Circular No. PED/12 of 02 June 2003. However, the salient features such as available current resources, organizational structure, proceeding three year operating results were not included in it and achievement of corporate objectives, particularly formulating strategy to become market leader in newspaper industry, implementation of the operational and marketing plan, improving product quality had not been evaluated by the management.

5.2 Annual Action Plan

Even though, An Annul Action Plan had been prepared for the year under review in line with the Corporate Plan, the activities planned to be implemented during the year under review such as exploration and establishment of a marketing plan for web and social media, expansion of product themes to create advertising opportunities, offering value addition to existing client base, acquisition of latest state of the art web printing press and upgrading human resources policies, procedures and skills of employees had not been achieved as targeted.

5.3 Audit Committees

The Audit Committee should comprise at least three non-executive board members, chaired preferably by a treasury representative or person possessing financial management skills. However, neither of the directors was no non-executives or treasury representative had been participated for such meetings.

5.4 Budgetary Control

The following observations are made.

(a) According to Section 5.2.3 of Department Public Enterprises Circular No. PED/12 of 02 June 2003, the time target for preparing budget and submission it to the Line Ministry, Department of Public Enterprises, General Treasury and Auditor General had not been followed.

(b) Considerable deviations ranging from 25 per cent to 256 per cent had been observed between the budgeted and the actual figures, thus indicating that the budget had not been made use of as an effective instrument in management control.

5.5 Unresolved Audit Matters

Due consideration had not been paid for the following matters which were pointed out in the audit report issued in preceding years.

(i) Un-received of received any return from the investment made at Lake House Property Development (Pvt) Ltd and Observer Jobs (Pvt) Ltd amounting to Rs.7,500,000 and Rs.2,500,000 respectively.

(ii) Appearance of differences between ledger balances and corresponding registers maintained by individual Departments of the Company.

(iii) Continuous decrease in sales of 06 newspapers which was discussed at the meeting of the Committee on Public Enterprise held on 09 December 2013.

6. Systems and Controls

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

	Control Area	Observations
(a)	Debtors Management	Non-reviewing the un-confirmed debtor balances.
(b)	Stock Control	- Differences were existed between ledger balances and physically verified stock balances - Existences of unidentified amounts in the ledger even after the reconciliations were made.
(c)	Circulation Revenue	Decrease in sales income of newspapers and discontinuation of 11 periodicals.
(d)	Human Resources Management	- No training programmes for improvement of skills of the employees. - Un-availability of approved Scheme of Recruitment and Promotion - None evaluation on the contributions of the consultants provided to uplift the Company's performance
(e)	Post-employment Benefits	None disclosure of plan asset and plan liability held in the Gratuity Trust Fund