

Lake House Connect (Private) Limited - 2016

The audit of the financial statements of the Lake House Connect (Private) Limited (“the Company”) for the year ended 31 December 2016 comprising the statement of financial position as at 31 December 2016 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.

This report is issued in terms of provisions in Article 154(6) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

1.2 Board’s Responsibility for the Financial Statements

The Board of Directors (“Board”) is responsible for the preparation and fair presentation of these 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 Board 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. 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 judgment, 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 Company’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 Company’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Board, as well as evaluating the overall presentation of the financial statements.

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

- (a) 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.
- (b) 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 in Section 17.19 of SLFRS for SMEs.
- (c) 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.

2. Financial Statements

2.1 Qualified Opinion

In my opinion, except for the effects of the matters described in the Basis for Qualified Opinion paragraph, the financial statements give a true and fair view of the financial position of the Lake House Connect (Private) Limited 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 (SLFRS for SMEs).

2.2. Non-Compliance with Laws, Rules, Regulations and Management Decisions

An extraordinary general meeting of shareholders had not been called within twenty working days when the net assets of the Company were less than half of its stated capital as per the requirements of Section 220 of the Companies Act, No. 07 of 2007.

2.3. Going Concern of the Company

The Company's name has been changed from "Business Lanka AN (Pvt) Ltd to "Lake House Connect (Pvt) Ltd" with effect from 29 July 2016 and simultaneously its objectives have also been newly designed as to organizing indoor and outdoor events of the Parent Company and carrying on the business of outdoor advertising instead of printing magazines. However, the Company has been experiencing continuous business losses, negative working capital and negative solvency margin. Details of the Company's working capital and the solvency margin since the year 2014 are as follows.

Details	2016	2015	2014
	Rs.	Rs.	Rs.
Current Assets	1,395,833	5,420,500	10,801,514
<u>Less</u>			
Current Liabilities	(17,981,100)	(15,839,148)	(11,171,273)
Working Capital	(16,585,267)	(10,418,648)	(369,759)
Net Assets	(16,433,502)	(9,740,116)	835,542
<u>Less:</u>			
Stated Capital	(3,000,000)	(3,000,000)	(3,000,000)
Solvency Margin	(19,433,502)	(12,740,116)	(2,164,458)

However, the Chairman of the Company from his letter dated 16 November 2017 has informed me, that the management has no such plan either to liquidate or to cease trading and also Parent Company would continuously provide financial supports to the Company.

2.4. Financial Management

The Parent Company had given an extra amount of Rs.1,500,000 for the period from August to December 2016 in order to cover-up the Company's expenses. However, a sum of Rs. 485,595 of that amount had been kept idle in a current account during the same period without being utilized for any purpose. Subsequently, of that, an amount of Rs.467,000 had been transferred to the Parent Company on 31 December 2016.

3. Financial Review

3.1 Financial Results

According to the financial statements of the Company, the operations of the Company for the year ended 31 December 2016 had resulted in a pre-tax net loss of Rs.6,693,385 as compared with the corresponding pre-tax net loss of Rs.10,575,658 for the preceding year, thus indicating an improvement of Rs.3,882,273 in the financial results for the year under review. Decrease of administration and distribution expenses by Rs.2,861,985 and Rs.2,923,885 respectively was the main reason attributed for the improvement in the financial results of the Company for the year under review.

Even after taking into account the salaries, taxes and depreciation charged for the year 2015 and 2016, the value addition of the Company was reported as negative figures of Rs.5,194,890 and Rs.2,850,944 respectively. However, it was shown an increase of 45 per cent in value addition for the year under review as compared with the previous year.

4. Operating Review

4.1 Operating Weaknesses

The following observations are made.

- (a) Even though the revenue earned during the year under review was Rs. 1,588,259, an amount of Rs. 3,453,643 had been paid as salaries and wages and it was represented 217 per cent of the revenue for the year under review.
- (b) The doubtful trade debts as at 31 December 2016 had been significantly increased due to unavailability of proper debt recovery policy. The balance of the trade debtors as at 31 December 2016 was amounted to Rs. 15,542,704 and out of that a sum of Rs.14,456,255 or 93 per cent had been made as provision for bad and doubtful debts.
- (c) The Company had been financially supported by the parent company in order to cover-up its expenditure. Hence, the Company's outstanding expenditure of Rs.17,297,969 as at 31 December 2016 had been settled by the parent company.

5. Accountability and Good Governance

5.1 Corporate Plan

A Corporate Plan is a reflection of the commitment by the Board of Directors and senior management in the future prospects of the entity. However, in terms of Section 5 of the Public Enterprises Circular No. PED/12 of 02 June 2003, a Corporate Plan had not been prepared by the Company since its inception.

5.2 Audit Committee

It is the responsibility of the management to set up committees, with a team of appropriate persons to deal with matters, which have a material impact on the entity. However an audit committee had not been appointed to meet on a regular basis at least once in three months in order to submit its observation to the Board of Directors with recommendation for necessary action.

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) Accounting	- Maintenance of proper books of prime entries and supporting documents. - Balancing the ledger accounts.
(b) Debtor Management	Introduce a proper debt recovery policy.
(c) Control over Expenditure	Increase the income or reduce the salaries and wages.
(d) Working Capital Management	Increase the operating cash inflow in order to meet the short term liabilities.