

## **Airport and Aviation Services (Sri Lanka) Limited – 2016**

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The audit of financial statements of the Airport and Aviation Services (Sri Lanka) 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. My comments and observations which I consider should be published with the Annual Report of the Company appear in this report.

### **1.2 Board’s Responsibility for the Financial Statements**

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The Board of Directors (“Board”) 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 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**

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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**

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

## 2. Financial Statements

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### 2.1 Qualified Opinion

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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 Airport and Aviation Services (Sri Lanka) 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.

#### 2.1.1 Report on Other Legal and Regulatory Requirements

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As required by Section 163 (2) of the Companies Act, No.07 of 2007, I state the followings:

- a. The basis of opinion and scope and limitations of the audit are as stated above.
- b. In my opinion :
  - I have obtained all the information and explanations that were required for the audit and as far as appears from my examination, proper accounting records have been kept by the Company.
  - The financial statements of the Company comply with the requirements of Section 151 of the Companies Act, No. 07 of 2007.

### 2.2 Comments on Financial Statements

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#### 2.2.1 Compliance with Sri Lanka Accounting Standards.

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The following observations are made.

- (a) **LKAS 16 – Property, Plant and Equipment:** Fully depreciated non-current assets costing Rs.16,061 million are being used by the Company without reviewing the useful life of them in terms of Section 51 of the Standard.
- (b) **LKAS 36 - Impairment of Assets:** There was a downturn in the operations of Mattala Rajapaksa International Airport (MRIA) since its commencement and presently flight movements are limited to one international airline. However, an impairment assessment relating to the assets valued at Rs.25,123 million belonging the MRJA had not been carried out even in the year under review.

### 2.3 Accounts Receivable and Payable

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Receivable balances which exceeding the credit periods aggregating Rs.1,027 million were outstanding for more than one year as at the end of the year under review. Details are given below.

Description -----	Amount ----- Rs. Million	Maximum Credit Period -----
Landing , Parking and Over Flying Charges	693	59 days
Aero Bridge Charges	134	30 days
Rental	200	03 days
Total	----- 1,027 =====	

### 2.4 Non – compliance with Laws, Rules, Regulations and Management Decisions etc.

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The following Instances of non-compliance with Laws, Rules, Regulations and Management Decisions were observed in audit.

#### Reference to Laws, Rules, Regulations and Management Decisions

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#### Non- compliance

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a) Section 6 of the Companies Act, No. 07 of 2007

The Company required to publish its name in public documents by adding the suffix “(Private) Limited” or the abbreviation “(Pvt) Ltd”, after re-registration under the new Companies Act. However, the Company still remains in the same name in its publications without suffix “(Private)/(Pvt)”.

b) Section 14 of the Civil Aviation Act, No.14 of 2010 and the Examination Report issued by the Civil Aviation Authority of Sri Lanka in the year 2015.

A Master Plan on establishment or expansion of aerodromes had neither been prepared nor approval obtained from the Civil Aviation Authority of Sri Lanka up to 31 March 2017.

- c) International Civil Aviation Organization (ICAO) Standards and the Examination Report issued by Civil Aviation Authority of Sri Lanka in the year 2015
  - A Head of Security Services had not been appointed permanently.
  - As per National Civil Aviation Security Programme, a specialized security programme had not been implemented although the technical advices given by the Civil Aviation Authority of Sri Lanka.
- d) The letter of Deputy Secretary to the Treasury No: PE/COMC/33/02 dated 28 April 2006
  - Land and buildings and other movable and immovable assets owned by the Government had not been valued and brought to accounts.
  - Shares to the Government of Sri Lanka for the net assets those transferred had not been issued.

e) Public Enterprises Circular No. PED/12 of 02 June 2003 on Public Enterprises Guidelines for Good Governance

(i) Paragraph 7.4.5

Annual Boards of Survey and Special Boards of Survey had not been appointed to carry out the verification of assets.

(ii) Paragraph 9.2 (d)

The Organization Chart and the approved Cadre of the Company had not been registered with the Department of Public Enterprises, General Treasury.

(iii) Paragraph 9.3.1 (i)

The Scheme of Recruitments and Promotions (SOR) of the Company had not been approved by the Ministry concerned with the concurrence of the General Treasury.

### **3. Financial Review**

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#### **3.1 Financial Result**

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According to the financial statements presented for audit the operations of the Company had resulted in a pre-tax net profit of Rs.6,909 million as compared with the corresponding pre-tax net profit of Rs.2,378 million for the preceding year, thus indicating an improvement of Rs.4,531million in the financial result of the year under review. The reasons for the improvement are mainly due to the increase of revenue by Rs.2,808 million and decrease of finance cost by Rs.1,570 million during the year under review.

### 3.2 Value Addition

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The value addition of the Company had increased gradually from the year 2012 to 2014. Although there was a deterioration in the preceding year, in the year under review the value addition had increased by Rs.5,813 million or 50 per cent as compared with the preceding year.

### 3.3 Analytical Financial Review

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#### 3.3.1 Significant Accounting Ratios

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According to the information made available some of the important accounting ratios of the Company for the year under review and preceding four years are given below.

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Current Assets Ratio (Number of times)	2.65	2.09	1.68	1.29	1.78
Quick Assets Ratio ( Number of times)	2.60	2.06	1.65	1.23	1.72
Net Profit Ratio (%)	38	15	40	39	35
Earnings per Share (Rs.)	34,598	4,084	17,058	17,768	13,688
Return on Net Assets (%)	42	7	32	48	65
Revenue per Passenger (Rs.)	1,938	1,846	1,785	1,652	1,570

The following observations are made in this connection.

- a) Increase of short term bank deposits and investments in treasury bills under repurchase agreements by 140 per cent and 17 per cent respectively were the main reasons attributed for the increase in current ratio and quick assets ratio.
- b) The net profit ratio had increased by 23 per cent during the year under review due to increase in revenue by 18 per cent and decrease in finance cost by 37 per cent. As a result the earnings per share had also been increased by 745 per cent.

#### 4. Operating Review

##### 4.1 Performance

(a) The physical performance of the Company as compared with the Key Performance Indicators (KPI) which mentioned in the Corporate Plan of the Company is given below.

Key Performance Indicator	Actual Achievements				
	2016	2015	2014	2013	2012
Number of International Flight Movements	61,637	56,156	54,960	51,972	48,416
Number of Total Passenger Movements	9,466,248	8,505,740	7,780,724	7,330,421	7,079,920
Number of Transit Passengers	1,285,756	1,227,451	1,273,037	1,370,266	1,296,495
Transit Passengers to Total Passengers Ratio	1:7.4	1:6.9	1:6.1	1:5.3	1:5.5
Cargo Movements (Metric Tons)	248,347	220,422	209,607	194,020	186,618
Total Cost per Flight Handled (Rs.'000)	216	256	171	177	164

The following observations are made in this connection.

- (i) Annual Targets on Key Performance Indicators (KPI's) had not been set out by the Company. Therefore, it was unable to compare the actual performance with the expected targets in audit.
  - (ii) The target of 10 million passenger movements and transit passengers to total passengers ratio of 1:7 to be expected to achieve in the year 2018 had already been achieved in the year under review. Hence, it was observed that the Company had set inefficient targets in its Corporate Plan.
- (a) Performance of the Mattala Rajapaksa International Airport (MRIA) built under a foreign loan of US\$190 million as a separate unit is summarized and shown below.

Key Performance Indicator -----	2016 -----	2015 -----	2014 -----
Number of Passengers	6,207	6,291	40,386
Action on International Aircraft (Number)	1,317	1,044	2,890
Action on loading of Air Cargo (Metric Tons)	Nil	19	221.9

The following observations are made in this connection.

- (i) Annual Targets on Key Performance Indicators (KPI's) had not been set out. Therefore, it was unable to compare the actual performance with the expected targets.
- (ii) Due to weak performance of the MRIA, the contracts for running the duty free shops have been terminated. Hence, the rental income had been decreased by Rs.18 million in the year under review.
- (iii) Assessment of damage caused to the Cargo Building valued at Rs.891 million due to paddy storage in the year 2015 had not been carried out even up to 31 March 2017.
- (iv) Financial performance of the MRIA had also been deteriorated as follows.

(v) F Description -----	Rs. in million		
	2016 -----	2015 -----	2014 -----
Total Income <sup>a</sup>	49	71	136
Total Operating Expenditure <sup>c</sup>	2,339	2,289	2,228
Operational Loss <sup>a</sup>	2,290	2,218	2,092
Finance Expenditure	701	882	637

## 4.2 Management Weaknesses -----

The following observations are made.

- (a) Adjustments valued at Rs.227 million had been made through 53 journal entries after submission of the draft financial statements to audit. Therefore, the possibility of prevailing further such deficiencies in the accounts could not be ruled out in audit.

- (b) The contract for implementation of an Enterprise Resource Planning (ERP) System had been awarded to a private company on 29 June 2012 for an amount of Rs.248.6 million to complete within a period of 08 months. The Company had paid a sum of Rs.27 million to the contractor and the contract period had also been extended in four instances up to 31 October 2016. Even though the period exceeding 04 years had elapsed since the award of the contract, the contractor had failed to complete the contract even up to 31 October 2016. Therefore, the performance bond of Rs.24.86 million had been claimed on 03 January 2017. However, the contractor had filed a case against the recovery of performance bond by the Company. Nevertheless, the Company had not taken any legal action against the contractor in this regard.
- (c) A land had been purchased from a private party by spending a sum of Rs.7 million in the year 2012 for the purpose of constructing a circuit bungalow. Subsequently, Divisional Secretariat, Katharagama had informed that this land is belonging to the Government. Nevertheless, the Company had failed to recover Rs.7 million paid to the private party. Further, the Company had filed a case against the private party in this connection.

#### **4.3 Transactions of Contentious Nature**

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The Company had paid a compensation of Rs.2.5 million in the year 2012 to an employee who had resigned voluntarily from the service in the year 2011.

#### **4.4 Human Resources Management**

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The following observations are made.

- (a) As per the Finance Circular No.124 of 24 October 1997 of the Ministry of Finance and Planning, covering up duties of a vacant post should be limited to a period of 03 months. However, four Deputy Divisional Heads had been appointed for cover up duties in the vacant posts in Heads of Divisions for a period ranging 01 to 05 years.
- (b) Staff cost per employee per annum had increased from the year 2012 to the year under review from Rs.1,020,000 to Rs.1,577,000 without the approval from Department of Management Services, General Treasury.

#### **5. Systems and Controls**

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Deficiencies observed in the systems and controls of the Company 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.

<b>Control Area</b> -----	<b>Observations</b> -----
(a) Human Resources Management	Cadre and Scheme of Recruitment and Promotions had not approved.
(b) Accounting	There was no an aggregated comprehensive accounting system in the Company.
(c) Receivables and Payables	Long outstanding balances remained in the accounts without being recovered / settled.
(d) Asset Management	<ul style="list-style-type: none"> <li>- Board of Survey not performed.</li> <li>- Non availability of assets coding and properly updated assets register.</li> </ul>