Lanka Rest Houses Limited - 2017

The audit of financial statements of the Lanka Rest Houses Limited ("the Company") for the year ended 31 December 2017 comprising the statement of financial position as at 31 December 2017 and the statement of profit or loss and other 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. In pursuance of Provisions in Article 154(6) of the constitution this report is issued.

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 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) According to the Financial statements of the Company as at 31 December 2017, the creditors balance amounted to Rs.3,416,055 and according to the balance confirmations furnish to audit that balance amounted to Rs.15,826,805. Thus, a difference of Rs.12,410,752 was observed.

(b) According to the financial statements of the Company, the fixed deposit balance as at 31 December 2017 amounted Rs.28,071,771 and according to the information provided to audit that balance amounted to Rs.29,583,945. Hence, the fixed deposit balance had been under stated by Rs.1,512,175.

(c) Due to not made provision of income tax on interest income of Rs.3,112,648 at the rate of 28 per cent, the provision for income tax and the profit for the year had been over and under stated by Rs.871,541 respectively.

(d) The incentive allowance that had been paid in the year 2016 amounting to Rs.135,000 had been adjusted to the profit of the year 2017, instead of being adjusted to the profit of the preceding year. Hence, the profit of the year 2017 had been understated by that amount.

(e) When provisions made for bad and doubtful debts, the provision for doubtful debts amounting to Rs.107,776 had been provided in twice for the same debtor and as a result, the debtors and the profit for the year had been understated by that amount.

(f) A deference of Rs.689,450 was observed between the income shown in the financial statements and the income shown in the Value Added Tax statement.

(g) Due to non – collection of management service fees according to the agreements, the management service income of the year had been under stated by Rs.241,129.

(h) According to the financial statements of the Company the interest income amounted to Rs.3,112,648. Nevertheless, as per the computations made by audit that value amounted to Rs.3,241,919. Hence, a defference of Rs.129,271 was observed.

(i) The accuracy and the existence of debtors and creditors amounting to Rs.2,562,429 and Rs.4,952,679 respectively could not be verified due ti unavailability of direct confirmations.

(j) As per the financial statements of the Company the balance payable to the Urban Development Authority (UDA) as at 31 December 2017 was Rs.60,488,725. However, according to the financial statements of the UA it was shown as Rs.59,968,658. No action had been taken to rectify the difference Rs.520,067 observed between these two balances.

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 Lanka Rest Houses Limited as at 31 December 2017, and its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

2.1.1 Report on Other Legal and Regulatory Requirements

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) Except for the effects of the matters described in the Basis for Qualified Opinion paragraph, I have obtained all the information and explanation that 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 requirement of Section 151 of the Companies Act No. 07 of 2007.

(c) The Board of Directors of the Company had failed to comply with section 220 of the company act.

2.2 Non Compliance with Law, Rules, Regulation and Management Decisions

The following non – compliances were observed.

	Reference of Laws, Rules and Regulations	Non – Compliance
(a)	Financial Regulation of the Democratic Socialist Republic of Sri Lanka	

	(i)	Financial Regulation 177	Action had not been taken to bank the daily receipts to the Mahiyanganaya Rest House. Further, 58 instances were observed during the year under review relating to the incurring of expenditure out of the receipts.
	(ii)	Financial Regulation 225 (1)	Even though the format of the all payment vouchers should be filled accurately, action had not been taken accordingly.
	(iii)	Financial Regulation 225 (2)	Even though General 177 format should be used for the payment of travelling expenditure, action had not been taken accordingly.
	(iv)	Financial Regulation 225 (4)	Even though every payment vouchers should be examined and endorsed with the initial, action had not been taken accordingly.
	(v)	Financial Regulation 371 (2)(b)	Even though the ad-hoc advance should not be exceded Rs.20,000, exceding that limit the ad-hoc advance amounting to Rs.303,000 had been paid to a non – staff officer in a clerk post.
	(vi)	Financial Regulation 394(b)(iii)	Even though notes should be put in the cash book before relevant cancelled cheques, action had not been taken accordingly.
	(vii)	Financial Regulation 396 (d)	Even though the chques lapsed of 6 months should be credited to the income, action had not been taken relating to the cheque No.367760 amounting to Rs.18,500.
	(viii)	Financial Regulation 46 (2)	The receipt and payment cash books should be maintained separately and they should be balanced daily, monthly or annualy. However, separate cash books had not been maintained at the Miyanganaya Rest House.
(b)	Paragraph 7.3 of the Department of public Enterprises Good Governance Circular No.PED/12 dated 02 June 2003		The instructions given in the Government Procurement Guidelines should be followed by the Public Enterprises and if other procedures and rules are prepared, according the requirement of the institutions, the approval of the Line Ministry and the Department of Public Enterprises should be obtained. However, such approvals had not been obtained relating to the procedures and rules so prepared by the Company.

3. Financial Review

3.1 Financial Results

According to the financial statement presented, the operation of the Company as at 31 December 2017 had resulted pre tax profit of Rs.10,986,542. As compared with the corresponding pre tax profit of 9,779,652 for the preceding year, thus indicating improvement in the financial result by Rs.1,206,890 of the company. Improvement of interest on fixed deposits by Rs.970,879 and Rest Houses income by Rs.420,424 were mainly attributed to the improvement in the financial result.

3.2 Analytical Review

(a) Compared to the preceding year, increase of interest on fixed deposits by Rs.970.79 million had been attributed to increase of income of the Company by Rs.1.7 million and due to decrease of direct purchase of the Company by Rs.237,882 the gross profit ratio of the company had increased to 90.36 per cent in the year under review, from 87.28 per cent in the preceding year. Compared to the preceding year, the net profit ratio of the Company for the year under review had decreased up to 30.16 per cent, from 31.08 per cent for the preceding year, due to the increase of administration and financial expenditure by Rs.1,306,477.

(b) The Current ratio of the Company for the year under review was slightly increased to 053:1 from 0.41:1 for the preceding year. However, the Company had failed to maintained for the current ratio at optimal level.

04. Operational Review

4.1 Performance

The main functions of the Company is to providing of quality, ethical and deticated service to the Tourists, Gests and Partners. Nevertheless, an Action Plan indicating the physical and financial targets that expected to be achieved, had not prepared. As well, the key performance indicators (KPI) relating to the main functions of the Company had not been prepared for the year under review. Hence, the performance of the Company for the year under review could not be evaluated in audit.

4.2 Management Activities

4.2.1 Rest House Management

The following observations are made.

(a) The rest houses which had been runed by the Local Government Authorities in the various regions in the country, had been vested to the Urban Development Authority (UDA) since the year 1980 and subsequently the Rest house Management had been given to the external parties. Although actions had been taken to streamline the Rest House Management functions by the Lanka Rest House Private Limited, establish under the UDA, the long term leasing activities of the Rest Houses had not been conducted based on a formal policy. The Rest Houses had not been leased out after being called quotations in order to selection of experienced and financially strength bidders. Instead, based on the letters given by the external parties, based on their private connections, stating that their consent to lease out the rest houses and agreeing in writing to carry out the reconstruction works of the Rest Houses by incurring a huge expenditure.

(b) When leasing out the Rest Houses, a permanent policy for leasing out them for a specific period of years had not been followed. The agreed leasing out period of each of Rest House differed from 4 years to 30 years. Further, the specification applied for leasing out the Rest Houses had not been furnished to audit.

(c) Actions had not been taken to carried out essential reperbisment works and correct the deficiencies by the Management Authority. Instead of that it was observed that the instructions had been given to the external parties to carring out the reperbisment works and modification activities of the Rest Houses.

(d) The many leaseholders of the Rest Houses had agreed to make renovations by investing Rs.05 million to Rs.120 million to the leasehold Rest Houses during the leasehold periods and by stating that they had leased out premises lower values. However, none of the Leaseholder had taken action to carryout the renovation and modification activities.

(e) Even though the related expenditure estimates should be furnished before starting the renovation and collection activities, only 09 Rest Houses had been furnished the expenditure estimates out of 30 Rest Houses.

(f) Due to not giving the approval from the Local Authorities to carry out the development activities of the Gampha, Kurunegala and Bandarawela Rest Houses, it was observed that the development activities had been abandoned without being completed.

(g) According to the letter of the Director of Rest Houses No.29/05/18 dated 14 February 2017, the renovation activities of the Rest Houses had not been commenced even at the date of that letter although the renovation activities of the Rest Houses should be commenced since the agreement date. However, any follow up action had not been taken, by the Executive officer and other officers relating to the not commencement of renovation activities as per the agreements.

4.2.2 Management of Miyanganaya Rest House

The following observations were made by the Internal Audit Division relating to management of the Miyanganaya Rest House by the Lanka Rest House Limited.

(a) A sum of Rs.7,050,977 to be receivable from the Rest House Manager for his service period from 2009 to 10 September 2016. Out of that a sum of Rs.5,978,273 was unbanked balance from the daily collections.

(b) Further, the total income of the Rest House for that period amounted Rs.45,260,369 and it was confirmed that instead of being banked the entire income, a sum of Rs.16,948,699 had been incurred for the direct expenditure. Even though the instructions had been given relating to the actions to be taken in a such a situation by the letter of the Director of Rest House Management (Rest House Management) dated 19 October 2011, actions had been taken contrary to that instructions.

(c) Even though a sum of Rs.110,410 should be receivable from the credit sales made during the period of 2009-2012. It was revealed that the receipts relating to that period had been destored by the Manager.

(d) Without being taken actions to sellect a suitable persons to rent out the Rest House, the Rest House had been runed by the then Manager of the Rest House with the support of the UDA employees, from the period of 01 November 2015 to 30 January 2016, a three months period, according to the action taken by the Director of the Rest House Management Division. A sum of Rs.620,000 to be receivable to the Lanka Rest House Ltd, relating to that 03 month period.

(e) A sum of Rs.142,294 collected from 04 receipts for the period of February 2016 to March, had not been handed over to the Lanka Rest House Limited up to date of audit.

(f) The receipts submitted by the Ex – Manager totalling Rs.1,703,660 had been included a receipt relating to purchase of building material for Rs.29,120 older than a year and purchased without having the approval of the Divisional Head, and the material purchased for the requirement of the Rest House from Kurunegala Region for Rs.44,014.

4.3 Operational Weakness

Even though the Company had made the payments for 5 telephones of the Company only the particulars relating 2 telephones had been included to the Register. Further that Register had not been checked by a responsible officer and the monthly bills had not been paid in certain months. Furthermore, in some instances, the payment shad been made in twice per month and made the over payments than the value of the bill.

4.4 Human Resources Management

A separate staff had not been recruited to the Lanka Rest House Limited and functions of the Company had been carried out by the staff of the UDA.

5. Accountability and Good Governance

5.1 Submission of Financial Statements

Even though according to the Public Enterprises Circular No.PED/12 dated 02 June 2003, the financial statements of the Company for the year 2017 should be furnished for audit before 28 February 2018, the financial statements had been furnished for audit only on 21 march 2018.

5.2 Action Plan

An Action plan had not been prepared for the year under review.

5.3 Annual Budget

According the paragraph 5.2.4 of the Pubic Enterprises Circular No.PED/12 dated 02 June 2003, the annual budget should be approved before 3 months prior to the forth coming financial year, the annual budget for the year under review had been approved only on 11 February 2017.

6. Systems and Controls

The deficiencies observed during the course of audit had informed to the Chairman of the Company in time to time. Special attention is needed for the following areas of control.

	Areas of Control	Observations
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(a)	The Rest Houses manage by the Company	Action had not been taken to prepare a formal procedure to controlling and supervision activities of the Rest Houses.
(b)	Rented Rest Houses	Action had not been taken to formalize the development activities of these Rest Houses and to strength the monitoring and supervision functions.
(c)	Renting of Rest Houses	A specific and acceptable procedure had not been prepared thereto.
(d)	Debtor Control	A considerable delays were observed in the process of collection of debtors and other receivables.
(e)	Human Resource Management	Actions had not been taken according to the instructions in the Public Enterprises Circulars relating to the staff.