

## **Associated Newspapers of Ceylon Limited - 2018**

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### **1.1 Qualified Opinion**

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The audit of the financial statements of the Associated Newspapers of Ceylon Limited (“Company”) and the consolidated financial statements of the Company and its subsidiaries (“Group”) for the year ended 31 December 2018 comprising the statements of financial position as at 31 December 2018 and the statements of comprehensive income, statements of changes in equity and cash flow statements for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, 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 provisions of the National Audit Act No. 19 of 2018 and Finance Act No. 38 of 1971. My comments and observations which I consider should be reported to Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the accompanying financial statements of the Company and Group give a true and fair view of the financial position of the Company and Group as at 31 December 2018, and of their financial performance and their cash flows for the year then ended in accordance with Sri Lanka Accounting Standards for Small and Medium-Sized Entities (SLFRS for SMEs).

### **1.2 Basis for Qualified Opinion**

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My opinion is qualified on the matters described in paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor’s Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

### **1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements**

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Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards for Small and Medium-Sized Entities (SLFRS for SMEs), and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Company.

#### **1.4 Audit Scope**

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My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company;
- Whether the Company has performed according to its powers, functions and duties; and
- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

## 1.5 Financial Statements

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

Non-Compliance with the reference to particular Standard	Management Comment	Recommendation
(a) The actual cash outflow relating to finance expenses was Rs.74,168,000. However, it had been recorded as Rs.75,486,000. As a result, the operational cash flow had been overstated by Rs.1,318,000 in contrary to section 7.14 of the Sri Lanka Accounting standard on Statement of Cash Flows.	Actions will be taken to rectify this in next year.	Cash flow statement should be prepared as per the provisions of the standard.
(b) The fully depreciated property, plant and equipment valued at cost amounting Rs.1,182,000,000 are being continuously utilized by the Company without reviewing the useful economic lifetime of such assets in contrary to section 17.19 of Sri Lanka Accounting standard on Property, Plant and Equipment.	Fixed assets physical verification and reconciliation is in progress and carrying out by, consultant – BDO Consulting (Pvt) Ltd.	When fully depreciated assets are utilized, useful economic lifetime should be reviewed and restate the accounts accordingly.
(c) As per section 28.15(a) of Employee Benefits, Obligations under the defined benefit plans as at 31 December 2018 amounting Rs.583,746,000 had not	As per Section 28.19 Company has used the simplifications in	As per the standard, such obligations should be measured at

been measured at its present value as required by the Standard. measuring the defined benefit obligations. its present value.

## 1.5.2 Unreconciled Control Accounts or Records

----- Audit Issue -----	----- Management Comment -----	----- Recommendation -----
Differences aggregating Rs. 4,061,664 had been observed between the inventory balance shown in the ledger and physically verified stock balance in respect of six (06) items of stocks.	Reasons for the differences have been identified in the reconciliation process and would be rectified during the year 2019.	Reconciliations should be made in order to rectify differences.

## 1.6 Accounts Receivable and Payable

### 1.6.1 Receivables

----- Audit Issue -----	----- Management Comment -----	----- Recommendation -----
(a) The value of trade debtors as at 31 December 2018 was Rs.828,751,000. Although confirmations had been sent to 679 debtors valued at Rs.635,362,202, only 41 debtors valued at Rs.37,144,202 or 06 per cent out of 679 debtors had responded as at 08 April 2019. Out of 41 debtors responded, only 21 debtors valued at Rs.16,440,483 had agreed with the balance of the Company. Trade debtors aggregating Rs.114,375,569 had remained outstanding for more than one year and out of that, an amount of Rs.31,260,774 had been referred to the legal sections considering as unrecoverable.	Even though, there were no responses (agreed or disagreed) to the confirmation letters sent, most of the outstanding balances as at 31st December 2018 have been settled as at 24.04.2019.	A system should be established to tally Company's records with its clients' records.
(b) The outstanding balance appeared in the subscription account as at 31 December 2018 was valued at Rs. 8,279,137. Out of that, an amount of Rs.4,006,615 was outstanding since the period ranging from 2011 to 2015 and no action had been taken to recover this amount even as at the end of year.	Action had been taken in 2017 to submit credit facilities only to Government institutions in order to minimize the bad debt percentage.	When newspapers are delivered on subscription, recoveries should also be monitored.

## 1.7 Non-compliance with Laws, Rules, Regulations and Management Decisions etc.

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) Section 114 (1) of the Inland Revenue Act No.10 of 2006 or Section 83 of the Inland Revenue Act No.24 of 2017 (from 1 <sup>st</sup> April 2018), 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 tax amounting to Rs.3,894,137 during the period from April 2018 to March 2019 on behalf of the bonus payments made to the employees without deducting it from respective employees.	PAYE tax for bonus has been computed and remitted in accordance with the Inland Revenue Act No. 10 of 2006.	PAYE tax should be deducted from employees and remit to the IRD.
(b) Section 9.3.1 of the Public Enterprises Circular No. PED/12 of 02 June 2003.	The Company had not obtained the required approval of the Board and the appropriate Ministry with the concurrence of the Department of Public Enterprise and General Treasury for the Scheme of Recruitments and Promotions.	ANCL does not come under the supervision of Department of Public Enterprises, Hence, stipulated circulars are not applicable to ANCL.	If Company wants to deviate from Public Enterprises Circulars, a direction should be obtained from the department of Public Enterprises.
(c) Public Enterprises Circular 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. However Company had not obtained any direction to deviate from PED Circulars	ANCL does not come under the supervision of said department. Hence, stipulated circulars are not applicable to ANCL.	If Company wants to deviate from Public Enterprises Circulars, a direction should be obtained from the department of Public Enterprises.
(d) Section 9.4 of Public Enterprises Circular No.12 of 02 June 2003	Eighteen officers including eight Journalists, four Editors, Assistant General Manager (technical), Photographer, Proof Reader, Assistant Manager, General Assistant and an Executive had been released for the services of other Government Institutions during the year under review and the  Company had spent a sum of	the Management has approved to release them with pay.	Company should adhere to Public Enterprises Circular No.12 of 02 June 2003.

Rs.11,962,607 as their salaries, wages and allowances. Further after releasing eight Journalists and four Editors, the Company had been recruited forty five Journalists and twenty seven Editors on contract basis during the year under review.

(e )	Extraordinary Gazette of the Democratic Socialist Republic of Sri Lanka No.162/5 of 14 October 1981 -Code of Ethics for Journalists	Fourteen defamation cases and one intellectual property matter had been filed against the Company by outsiders as at 31 December 2018. After failing from two defamation cases filed against the Company, an amount of Rs.5,193,912 had been paid by the Company for two plaintiffs during the year under review.	Noted.	Defamation cases can be reduced if Journalists follow the "Code of Ethics"
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**2. Financial Review**  
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**2.1 Financial Result**  
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The operating result of the year under review amounted to a loss of Rs.166,227,000 and corresponding profit in the preceding year amounted to Rs.243,660,000. Therefore a deterioration amounting to Rs.409,887,000 of the financial result was observed. The reason for the deterioration is the increase in cost of sales mainly due to high prices of printing materials.

In analyzing the financial results of the Company for last four years and the year under review, the value addition had been fluctuated from 2014 to 2018. However, after taking into account the employee salaries, taxes and depreciation charged for the years (before dividend and fair value adjustment), the value addition for the years 2017 and 2018 was Rs.2,025,767,000 and Rs.1,756,556,000 respectively thus showing a reduction by 13 per cent in the year 2018 as compared with preceding year.

## 2.2 Ratio Analysis

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

	2018 Percentage	2017 Percentage
Gross Profit Margin	44.33	55.32
Profit mark up (Gross profit on cost of sales)	79.63	123.81
Administration Cost on Turnover	38.81	36.96
Selling and Distribution Cost on Turnover	12.25	11.96
Finance Cost on Turnover	2.54	2.29
Current Ratio	1.59	2.46
Acid Test Ratio	0.89	2.05
Return on Capital Employed	(13)	35
Gearing Ratio	14	18

The gross profit margin and the profit mark-up of the Company for the year under review, as compared with the preceding year had decreased by 10.99 percent and 44.18 percent respectively. Administrative cost and selling and distribution cost on turnover had increased slightly with compared to the preceding year. Return on capital employed had reduced by 48 per cent while gearing ratio had reduced from 18 per cent to 14 per cent.

## 3. Operational Review

### 3.1 Management Inefficiencies

Audit Issue	Management Comment	Recommendation
(a) Lake House Connect (Pvt) Ltd (formerly known as Business Lanka AN (Pvt) Limited) and Observer Jobs (Pvt) Ltd (formerly known as Info Media (Pvt) Ltd) were two subsidiaries of the Company had sustained a cumulative loss of Rs. 25,884,625 and Rs.13,139,185 respectively as at 31 December 2018. These subsidiaries were fully depended on the Company and therefore, an amount of	Due to its continuous losses, negative working capital and negative solvency margin management decided to cease its business operations of these two subsidiaries.	Management should direct subsidiaries to achieve the expected outcome from the subsidiaries.

Rs.22,534,489 and Rs,10,594,185 respectively were receivable as at 31 December 2018. Furthermore, the Board of Directors had taken a decision on 15 February 2018 to cease operations of these subsidiaries due to continuous business losses, negative working capital and negative solvency margin.

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| (b) | Lake House Property Development (Pvt) Ltd, which was established in 1985 to engage in property development business, had not generated any cash flow from operating activities even up to now.   | Lake House Property Development (Pvt) Ltd is a subsidiary of ANCL and that has been non-operating since 1985.  | A decision should be taken on non-operating entity.               |
| (c) | There were 151 dishonored cheques valued at Rs. 6,748,171 as at 31 December 2018. Out of that 66 cheques valued at Rs. 1,981,878 and 27 cheques valued at Rs. 1,279,588 had remained outstanding for more than 5 years and 3 years respectively.   | Noted. We are in the process of tightening the credit controls and recovery processes to minimize the dishonored cheques and constantly maintains pertinent procedures to recover the balance outstanding due to dishonored cheques. | Prevailing system should be carefully monitored.                  |
| (d) | Although the Company had paid an amount of Rs. 1.2 million as an interim payment to purchase 1200 shares of Lanka Puvath Ltd – National News Agencies of Sri Lanka in December 2008, no return had been received even as at 31 December 2018. Further, a sum of Rs.2,151,146 paid as salaries and wages for three employees relating to Lanka Puvath Ltd in 2017 had been shown as receivable even as at 31 December 2018. | Based on the Board Decision LKPB 202.17, ANCL had invested in 1200 shares of Lanka Puvath (Pvt) Ltd. Two employees have already been resigned and one employee has been joined to ANCL cadre in year 2018.                           | Investments should be made to generate a return.                  |
| (e) | The actions against four debtors amounting to Rs.4,552,559 which were outstanding for more than 720 days could not be taken by the Company due to misplace of relevant supporting documents with regard to transactions made with them.  | Noted. Steps have been taken to rectify the same and avoid such issues in future.  | Responsibilities should be established over custody of documents. |
| (f) | Company had issued 192,665 copies of “Budusarana” periodical to a government institute in 2014. The value of these copies were amounted to Rs.2,209,560. However, without taking any recovery action, a full provision for doubtful trade debts had been made by the Company since 2015 and balance was remained outstanding till 31 December  | Action will be taken to rectify and recover same.  | Attempts should be made to recover the outstanding regularly.     |



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| (g) | Closing stock amounted to Rs.656,115,000 had been valued at cost without valuing them at cost or net realizable value whichever is lower.   | All stocks are consumable items and not trading stocks. Therefore, we do not consider estimated selling price. Company value's the stock based on cost price. | Even for consumable items, valuation has to be done at cost or net realizable value whichever is lower.         |
| (h) | Without being measured at the best estimate that can rationally pay to settle the obligation, constant provision of Rs.20,000,000 had been made every year for legal cases filed against the Company. | Best estimate measured and applied in providing for the legal cases.  | Amount claimed relating to pending cases should be evaluated case by case before arriving into a best estimate. |

### 3.2 Operational Inefficiencies

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Audit Issue -----	Management Comment -----	Recommendation -----
(a) The Company had published 07 kinds of newspapers and 10 kinds of periodicals during the year under review and had published 06 kinds of newspapers and 12 kinds of periodicals during the preceding year. A newspaper named as "Resa" had been newly introduced by the Company in 2018 and three periodicals named as "Sithmina", "Mihithura" and "Denamuthu" had been discontinued due to low reader attraction. Further, a periodical named as "Sathmadala" had been newly introduced in 2018.	"Resa" daily newspaper was launched in January 2018 on a recommendation made by the Lake House Corporate Strategic Plan in place for the next three years. The paper was launched also to attract younger readership towards the publication as the readership of newspapers are declining. "Sathmadala" magazine was introduced under a sponsorship package with Sri Lanka Telecom.	Company should evaluate possibilities of attracting more readers.
(b) 1,419,821 copies from main six newspapers and 126,772 copies from newly introduced newspaper "Rasa" had been issued in free aggregating to total copies issued in free as 1,546,593 in 2018. Further, 88,090 copies had been issued in free basis from 10 periodicals in 2018. Overall free copies issued in 2018 with compared to the preceding	Initial distribution of free copies of "Resa" newspaper was to promote the paper in the market. Changes were also made in all main newspapers of Lake House, making the news coverage more independent and improving the quality of the content. Therefore, more promotional activities were organized by distributing papers to corporate sector and prospective	The parties who receive free copies should be periodically updated and should try to reduce.

year had been increased by 187,681 or 13 per cent. The cost involved with these copies was amounted to Rs.109,142,884.

advertisers to create awareness of the changes.

- (c) Overall returned copies from 7 newspapers and 10 periodicals were amounted to 4,433,869 during the year under review and it was a 40 per cent increase with compared to the preceding year. The highest return was recorded from “Rasa” newspaper which was introduced in 2018 representing 27 per cent of return from the production.
- During the first few months after the launch of “Resa”, additional copies were sent to News Agents make the paper available at all selling points. This is the standard practice during the launch of any newspaper as the exact demand for the paper cannot be estimated accurately. 50% returns at the initial stages have now come down to about 17% - 18%.
- Measures should be taken to reduce returned copies.
- (d) Number of copies sold relating to Sunday Observer, Daily News, Dinamina and Silumina had been reduced ranging from 5 percent to 12 per cent during the year 2018. However, Thinakaran and Varamanjaree have shown an increase of copies sold by 3 per cent and 4 per cent respectively. Periodicals named as “Tharunee”, “Manchu” and “Subasetha” have also been shown a considerable decline in sold copies ranging from 9 per cent to 11 per cent.
- There is an overall decline in newspaper sales in the industry. Printing delays during the last quarter of 2018 also resulted in the papers reaching the market late and hence decline in sales.
- Company should evaluate possible opportunities to attract more readers.
- Increase in selling price of three periodicals also contributed to a slight decline in sales.
- (e) Income from all 6 newspapers have been reduced by 3 per cent during the year with compared to the preceding year ignoring the sales income received from newly introduced newspaper “Rasa”. However, sale price of 4 newspapers had been increased by the Company in 2018.
- In order to increase the print quality of the newspapers and to increase the advertising revenue, the management has decided to print main newspapers on Goss Magnum press. To facilitate this it is decided to increase the capacity of the Goss Magnum press for newspaper printing and stopped commercial printing jobs as there were no any other alternative or purchasing a new web press.
- Company should evaluate possible opportunities to attract more readers.
- (f) The revenue from commercial printings, special publications and digital printings had been reduced by 13 per cent, 21 per cent and 63 per cent respectively in 2018 with compared to preceding year.
- The management has decided to print main newspapers on Goss Magnum press. To facilitate this it is decided to increase the capacity of the Goss Magnum press for newspaper printing and stopped commercial printing jobs as there were no any other alternative or purchasing a new web press.
- Projects which give a maximum return should be evaluated rationally.

- (g) The overall advertisement income had been decreased by Rs.6,357,000 except the advertising income received from “Resa” compared with the preceding year even though Company had introduced an incentive scheme for advertising/sales managers in order to attract more advertisements. Further, Company had increased rates of casual advertisements of “Daily News”, “Dinamina”, “Thinakaran” and “Varamanjari” with effect from 01 June 2018.
- Overall Advertising Revenue up to September 2018 were more than the revenue of the same period of the preceding year, hence we were confident that we could achieve at least 5% increase at the end of the year compared to previous year as advertising trend in the later quarter of the year is usually very high. However, the Advertising revenue in the months of October, November and December 2018 were badly affected due to unsettled political situation in the country, hence the shortfall.
- Management should look into the ways of increasing the market share for newspapers and periodicals and increase the ways of advertising income.

### 3.3 Idle or underutilized Property, Plant and Equipment

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Audit Issue -----	Management Comment -----	Recommendation -----
A land with an extent of 8 acres located at Hokandara purchased for constructing a housing scheme had remained idle since the year 1985.	Accepted. Ownership of the Hokandara Land transferred to ANCL in year 2013 and mortgage to Commercial Bank for obtaining loan for VRS in year 2016 and working capital.	No restrictions are made once a property is kept as a security. Company has to utilize this asset to generate a return.

### 3.4 Human Resources Management

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Audit Issue -----	Management Comment -----	Recommendation -----
(a) The Company had prepared a cadre on 06 June 2017 instead of the cadre which had been prepared on 01 July 2012. However, Board approval had not been obtained for the cadre even up to the date of 13 May 2019. Further, as per the cadre prepared in 2017, the General and Editorial cadre was 658 and 327 respectively. However, General and Editorial actual cadre (including 468 contract basis employees) as at 31 December 2018	Proposed cadre has been prepared by the Management as at 06/06/2017 based on the strategic plan that is being developed for Lake House and taken in to consideration the efficiencies that will arise from the automation and systems that are planned or are in progress (ERP, Sales, IT System, Network upgrades, HRIS Systems, etc.) Editorial – 327, General Admin – 658. It will take Lake House two years or more to reach this headcount through reduction in a sustainable manner. This cadre position has	Board approval should be obtained.

was 1088 and 558 respectively.

been approved by the Chairman.

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| (b) | Although seven policies such as talent acquisition, promotion, leave policy, performance management etc. had been prepared by the Company for better personal administration, the Board approval had been received only for the performance management policy as at 31 December 2018. | Out of the 7 HR policies Board approval was granted only for the “Performance Management” policy. Further, the HR Department is reviewing the unapproved policies and wishes to submit to the Board for approval.  | Board approval should be obtained for all the policies.   |
| (c) | Recruitment and promotions should be affected systematically in line with the realistic cadre position of the enterprise. However, company was unable to categorize actual employees which stood as at 31 December 2018 according to their job positions.                             | Some employees have been appointed on contract basis based on the requirement of some departments especially Editorial to maintain the higher standard in our publications.  | The Company should introduce system to categorize actual number of employees according to their job categories. |
| (d) | Age limit for the post, mode of recruitment (external advertisement/ internal notice and written assessment/ interview) had not been incorporated in the schemes of recruitment of the company.   | Age limit has mentioned in the advertisement when a position is advertised externally and also interviews are conducted for each and every position and written tests are held for some positions on need basis  | Schemes of recruitment should consist with required details.  |
| (e) | Although the Voluntary Retirement Schemes (VRS) had been introduced in 2008, 2010, and 2016 to reduce overstaff of the Company and 991 employees left the Company under these schemes, 598 employees had been newly recruited by 31 December 2018 from 01 September 2008.             | Some employees have been appointed on contract basis specially for Editorial Departments at the discretion of the Management with the introduction of new publications (Resa, Tabloids published with Ministries), to maintain the higher standards in English Newspapers and to cater to new technological innovations in social media. | The VRS should be adopted on a rational basis, since staff recruiting regularly after the VRS.                  |

#### **4. Accountability and Good Governance**

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##### **4.1 Audit Committee**

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<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
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Although the Audit Committee should comprise at least three non-executive Board members, chaired preferably by a Treasury representative or person possessing financial management skills, no treasury representative had been participated for the meetings and an executive director had chaired the meetings.	Noted	Audit Committee should comprise with relevant personnel.