

## **Sri Lanka Savings Bank Limited - 2018**

### **1.1 Opinion**

The audit of the financial statements of the Sri Lanka Savings Bank Limited (“Bank”) for the year ended 31 December 2018 comprising the statement of financial position as at 31 December 2018 and the income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows 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.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2018, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

### **1.2 Basis for Opinion**

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 opinion.

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

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, 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 Bank’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 intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank’s financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Bank 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 Bank.

### **1.4 Auditor’s Responsibilities for the Audit of the Financial Statements**

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 Bank'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 Bank 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 Bank, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Bank has complied with applicable written law, or other general or special directions issued by the governing body of the Bank ;
- Whether the Bank has performed according to its powers, functions and duties; and
- Whether the resources of the Bank had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

## 1.5 Accounts Receivable and Payable

### 1.5.1 Receivables

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
Five receivable accounts aggregating to Rs.1,989,693 had remained unchanged for more than three years period. The reasons for long outstanding balances were not explained to audit.	Noted	Take necessary actions to clear the long outstanding balances.

### 1.5.2 Payables

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
(i) Actions had not been taken to clear long outstanding suspense account and payable account balances amounting to Rs.6,821,041 and Rs.41,104,200 respectively which are disclosed under other payables in the financial statements as at 31 December 2018.	Agreed. Provision for contingency amounting to Rs.37,032,798, which is made for pending legal cases is included in other payable balance.	Take necessary actions to clear long outstanding payable balances.
(ii) Unusual debit balances aggregating to Rs.768,028 were identified under five payable accounts as at 31 December 2018.	Noted.	Take necessary actions to clear the debit balance in payable accounts.
(iii) The actions had not been taken to transfer the credit balances recorded in error correction saving account and control account for loan saving amounting to Rs.1,975,556 and Rs.1,438,493 respectively to relevant customer saving accounts.	Agreed. The outstanding balances had not transferred to relevant customer's savings accounts.	Take necessary actions to transfer the error correction saving account balance and control account for loan saving to relevant customer's saving account.

### 1.5.3 Advances

<b>Audit Issue</b>	<b>Management Comment</b>	<b>Recommendation</b>
(i) The loan outstanding balance of Rs.99,992,620 which is recoverable from six community based organizations had not been recovered since 2015. These borrowers had not provided any security against these loan balances. Therefore the recoverability is doubtful.	Noted.	Take necessary actions to recover the outstanding loan balances from relevant customers.
(ii) Out of total loan outstanding amount of Rs.55,313,218 granted under the loan scheme of “Rehabilitation of Person, Property, Industries Authority (Reppia)”, a sum of Rs.49,909,789 or 90 per cent was reported as non performing as at 31 December 2018.	Noted.	Take all necessary actions to recover the non-performing loans granted under “Reppia” category.
(iii) The cash receipts of 05 rescheduled customers aggregating to Rs.3,393,428 had been posted to the account called “Termination Over Payment-MF”, since the Bank’s system does not support to post the entries for rescheduled loans. Accordingly, the customers loan accounts in the general ledger did not reflect the actual due amount from the customer.	Noted.	Ensure that the Bank’s system is supported for the correct posting of accounting entries.
(iv) A difference of Rs.1,799,167 and Rs.740,491 in relation to loan and lease and Hire Purchase balances respectively was observed between the General Ledger and application system as at 31 December 2018.	Noted.	Ensure that general ledger balances are tallied with the system generated balances.
(v) Abnormal credit balances aggregating to Rs.698,010 was observed in six loan categories as at 31 December 2018.	Noted.	Take necessary actions to eliminate abnormal credit balances recorded in particular loan accounts.
(vi) Actions had not been taken to clear long outstanding balances remained in six rental due loan accounts aggregating to Rs.900,229 as at 31 December 2018.	Noted.	Take necessary actions to clear long outstanding balances carried forward in particular rental due accounts.

## **2. Financial Review**

### **2.1 Financial Result**

The operating result of the year under review amounted to a profit of Rs.351,266,136 and the corresponding profit in the preceding year amounted to Rs.604,369,273. Therefore a deterioration amounting to Rs.253,103,137 or 42 per cent of the financial result was observed. The reasons for the deterioration are reduction of other operating income, higher personnel and other expense incurred and increase in VAT, NBT and income tax expense.

### **2.2 Trend Analysis of major Income and Expenditure items**

- (i) The interest expense of the Bank had decreased by Rs.49 million or 34 per cent as compared with the previous year. Non-accruing the interest expense on debentures issued to PSDB customers due to maturity is the main reasons affected for the reduction.
- (ii) The other operating income had also declined by Rs.30 million or 62 per cent due to reduction of write off loans recovered from customers and unavailability of gain on sale of property, plant and equipment during the year under review.
- (iii) Personal expenses of the Bank had increased by Rs.48 million or 40 per cent due to making provision for salary and bonuses as per the proposed collective agreement.
- (iv) Other expenses had increased by Rs.65 million or 70 per cent due to imposition of tax penalty, paying the debt repayment levy and incurring losses on selling seized tractors.
- (v) Tax on financial service had increased by Rs.26 million or 25 per cent due to increase on total value addition based on the increased personal cost.
- (vi) The income tax expense also increased by Rs.137 million or 100 per cent due to imposition of income tax under new Inland Revenue Act No. 24 of 2017.

### **2.3 Ratio Analysis**

Following observations are made on some important accounting ratios of the Bank for the year under review as compared with sector ratios.

- i) Return on Equity (ROE) and Return on Assets (ROA) had been decreased up to 6.52 per cent and 5.22 per cent respectively as at 31 December 2018 when compared with the preceding year mainly due to low profitability in 2018.
- ii) High net interest margin of 11 per cent was observed for the year 2018 as compared with the Licensed Specialized Bank ratio of 3.2 per cent.
- iii) Total Capital Adequacy Ratio of the Bank reported as 90 per cent as at the 31 December 2018 which is much higher than the minimum statutory requirement of 12.5 per cent.
- iv) The gross non performing advance ratio excluding Pramuka Savings and Development Bank (PSDB) non-performing loans as at the end of year 2018 was 11 per cent which is higher than Licensed Specialized Bank average ratio of 4.8 per cent. Increase of non-performing loans of rehabilitation of persons, properties and industries authority (RAPPIA – 90%) category and

individual & corporate loan (25%) category had mainly caused to increase the NPL ratio. However, the gross non - performing advance ratio including PSDB non-performing loans as at the end of year 2018 was 36 per cent.

### 3. Operational Review

#### 3.1 Management Inefficiencies

Audit Issue	Management Comment	Recommendation
(i) The Bank had maintained nearly 66 per cent of its total assets in different investments such as repo, fixed deposits, debentures and equity instruments and only 26 per cent on loans and advances which is opposed to main objective of the Bank of identify, develop, promote, catalyze and support sustainable income generating opportunities and a higher quality of life for the poor through a range of activities including productive self-employment micro enterprises and rural work by the provision of financial assistance and services.	Noted.	Ensure that more focus is given on the main objective of the Bank.
(ii) Out of the Pramuka Savings and Development Bank non-performing loan outstanding amount of Rs.1,035,391,453 as at 31 December 2017, the Bank was able to recover only an amount of Rs.15,289,016 or 2 percent during the year under review.	Noted.	Take necessary actions to recover the outstanding loan balance from PSDB customers.
(iii) The Bank recorded a growth rate of 6 per cent of its asset base since 2014 to 2018 which is far below the growth rate of 31 per cent of Licensed Specialized Banking sector for the same period.	Noted.	Take necessary actions to increase the growth rate of Bank's asset base as par with the industry growth rate.
(iv) The market share of the Bank in terms of total deposit base and total assets base of Licensed Specialized Banks had declined by 0.071 per cent and 0.15 per cent respectively since 2014 to 2018.	Noted.	Take necessary actions to increase the deposit based and assets based market share of the Bank.
(v) Out of the total loan portfolio of the bank, a sum of Rs.1,319 million or 33.3 percent represented the micro finance loans as at 31 December 2018. Out of total outstanding amount of micro finance loans, a sum of Rs.568 million or 43 per cent represents the loans granted to six	Noted.	Take necessary actions to reduce the dependency on few community based organizations when granting micro finance loans.

community based organizations and outstanding balance of each organization exceeds Rs.50 million. It was further observed that the securities provided covered only up to 13 per cent to 45 per cent of the outstanding loan balances.

Aggregated outstanding loan balance of another 10 community based organizations represents 28 per cent of the total micro finance loan balance as at 31 December 2018 and individual loan balance of each organization lies between Rs.20 million to Rs.50 million which brings considerable risk to the Bank.

**3.2 Human Resources Management**

**Audit Issue**

The approved cadre of the Bank for the year under review was 183 and the Bank had deployed 109 employees as at the end of the year 2018. Accordingly, 74 vacancies remained as at 31 December 2018. It was further observed that 28 or 15 Per cent of executive level positions are remained vacant as at 31 December 2018.

**Management Comment**

Noted.

**Recommendation**

Take necessary actions to fill the vacancies after obtaining relevant approval.