

Airport and Aviation Services (Sri Lanka) Limited – 2018

1.1 Qualified Opinion

The audit of the financial statements of the Airport and Aviation Services (Sri Lanka) Limited (“Company”) for the year ended 31 December 2018 comprising the statement of financial position as at 31 December 2018 and the statement of comprehensive income, statement of changes in equity and cash flow statement 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. My comments and observations which I consider should be report 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 give a true and fair view of the financial position of the Company 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 Qualified Opinion

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

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 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

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 scepticism 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 Internal Control over the preparation of financial statements.

Audit Issue	Management Comment	Recommendation
Assets coding system and properly updated assets register had not been made available for audit.	As to the date, Fixed Asset database with barcode system is being developed in house. New barcodes are being pasted during the Fixed Assets verifications. Soft copy of the fixed asset register is available for your review.	ERP system should be implemented as early as possible and the assets register should be updated regularly.

1.5.2 Non-Compliance with Sri Lanka Accounting Standards

Non Compliance with the reference to particular Standard	Management Comment	Recommendation
(a) The statement of financial position includes property, plant and equipment relating to the Mattala Rajapaksha International Airport (MRIA) with a carrying amount of Rs.22 Billion as at 31 December 2018. There had been a downturn in the	Not Agreed, AASL Management is of the view that “MRIA Assets have not been impaired” and its maintaining as an alternative airport for emergency requirements. This was experienced during BIA Runway closure for repairs and Overlay period. If it not being	Even though there were discussions held with Government of India (GOI) for creating a joint venture company to commercial operations and

operations of MRIA from commencement and presently there are a few international flight movements and domestic flights.

Considering these to be indicators of impairment in accordance with LKAS 36, Impairment of assets, management has not carried out an impairment assessment to check whether there is any indication that MRIA may be impaired, on the basis of it being a separate cash generating unit

there, there would not have been any flight movement during runway overlay period within that closure time period.

In addition, the negotiation process with Airport Authority of India (AAI) "G2G" private/public partnership in the ratio of 70:30 of MRIA operations as a mode of Joint Venture in order to operate and maintenance of MRIA is being processed. Therefore, it is clearly evident if there is no potential of MRIA, AAI will not going to make an offer to operate the Airport.

maintenance of MRIA, the process has not been finalized.

Therefore, indicators for impairment are still there and an impairment test should be carried out.

(b) An Investment had not been made for the Retirement Benefit Plan as per Paragraph 34 of LKAS 26-Accounting and Reporting by Retirement Benefit Plans.

Investment in long term debentures was done in order to match the gratuity liability. Approval of the board of Directors has also been granted exclusively for this purpose. Company placed debentures amounting to Rs. 4,584 Mn as at 31 December 2018 for creating the dedicated fund to serve the retirement benefit liabilities of the company. Action will be taken to disclose this in Note No 14 to Financial Statements.

The investment for Retirement benefit plan should be clearly identified and disclosed in financial statements.

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

The following instances of non-compliance with laws, rules, regulations and management decisions were observed in audit.

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) Section 14 of the Civil Aviation Act, No.14 of 2010	A Master Plan on establishment or expansion of aerodromes had not	Airport and Aviation Service (AASL) has taken action to Update Master Plan for	Master plan on establishment of aerodromes should be prepared and

been prepared and got approved from Civil Aviation Authority of Sri Lanka. Bandaranaike International Airport. RFA document was prepared. KOICA (Korea International Corporation Agency) pay willingness to provide grant for whole process. obtain approval early.

Action will be taken to obtain the relevant approval after finalizing the above.

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

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| i) Section 7.2 and 7.3 | Operational manuals had not been revised and updated regularly and action had not been taken by the Company to obtain approvals from Line Ministry. | Action will be taken to submit operational manuals to Treasury through the line ministry by the end of June 2019. | Action should be taken to submit operational manuals to Treasury through the line Ministry as early as possible. |
| ii) Section 7.4.5 and Financial Regulation 507 of the Government of the Democratic Socialist Republic of Sri Lanka | Annual board of survey had not been conducted on time to carry out the verification of assets. | Teams were appointed to carry out Annual board of survey for the year 2018 and As at to date almost all teams have done above 60% of their ground work. | Annual board of survey should be carried out as at 31 December and reports should be submitted to Auditor General. |
| iii) Paragraph 9.2 (d) | The Organization Chart and the approved Cadre of the Company had not been registered with the Department of Public Enterprises, | The Company has a cadre approved by the Board and worked within the approved cadre at all times. This has already been sent to the Treasury through the Line-Ministry for | Action should be taken to obtain the approval from General Treasury |

General Treasury. registration purposes.

iv) 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. However, all recruitment and promotions are carried out as per the Board approved Schemes of Recruitment and Promotion. Action should be taken to register the Schemes of Recruitment and Promotion with the Department of Public Enterprises of General Treasury.

(c) Letter of Deputy Secretary to the Treasury No: PE/COMC/33/02 dated 28 April 2006 The Company had taken over only the liabilities neither valuing the land and buildings and other movable and immovable assets owned by the Government and record in accounts nor issuing shares to the Government of Sri Lanka for the net assets transferring. We're currently in the process of valuing all movable and immovable assets through Government valuation department. However ownership of land used by AASL has not been transferred to the Company. Upon completion of such valuation all immovable properties, will be taken in to accounts subject to clearance of legal ownership and explore the possibility of issuing shares to the Treasury on net assets as stated in the cabinet memorandum. It is recommended to complete the revaluation process as early as possible and issue the shares to GOSL on net assets as directed by the Secretary to the Treasury.

1.7 IT General Controls

Audit Issue

Finance System of the Company has been implemented in 1984 and COBOL which is an outdated programming language has been used to develop the system. High risk is identified in continuity of these modules due to continuous modification requested by the users

Management Comment

Limitations of the current system are the cause for the issue. This has been identified and the management has initiated the procurement of a new system.

Recommendation

Actions should be taken to implement the new integrated finance system early.

and there is no integration between the modules and other related systems.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs. 5,313,155,819 and the corresponding profit in the preceding year amounted to Rs. 8,714,922,195. Therefore a deterioration amounting to Rs.3,401,766,376 of the financial result was observed. The reasons for the deterioration are increasing of finance cost and administration and establishment expenses.

2.2 Ratio Analysis

Type of Ratio	2018	2017	2016	2015	2014
Current Assets Ratio (number of times)	3.49	2.78	2.65	2.09	1.68
Quick Assets Ratio (number of times)	3.43	2.71	2.60	2.06	1.65
Net Profit Ratio (%)	32	43	38	15	40
Earnings per Share (Rs.)	26,566	43,574	34,598	4,084	17,058
Return on Net Assets (%)	19	37	42	7	32
Revenue per Passenger (Rs.)	2640	2,058	1,938	1,846	1,785

The following observation are made

- a) Increase of short-term bank deposit by 40 per cent was the main reason attributed for the increase in Current Ratio and quick Assets Ratio.
- b) The earning per share had decreased by 39 per cent during the year due to increase in exchange loss and income tax expenses in 2018.

3. Operational Review

3.1 Performance

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	2018	2017	2016	2015	2014
Number of International Flight Movements	67,351	62,850	61,637	56,156	54,960
Number of Total Passenger Movements	10,884,028	9,957,502	9,466,248	8,505,740	7,780,724
Cargo Movements (Metric Tons)	279,559	274,047	248,347	220,422	209,607
Total Cost per Flight Handled (Rs.'000)	318	202	216	256	184

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.

3.2 Management Inefficiencies

Audit Issue	Management Comment	Recommendation
(a) Foreign loans obtained by the Government of Sri Lanka relating to Colombo International Airport Development Project and Modernization of Ratmalana Air Traffic Control System had been recorded as liability in the accounts of the Company based on the letter issued by the Secretary to the Treasury on 09 February 2006 without any loan agreement. The total loan outstanding as at 31 December 2018 in respect of the above loans was Rs.11,339 Million. It was further observed these loans are also shown as liabilities in the Republic	As per the letter reference PE/GOCO/1/1 dated 04 th February, 2006 issued by the Secretary to the Treasury, these loans were disclosed in the AASL accounts complying with the Sri Lanka Accounting Standards & International Financial Reporting Standards (SLFRS/IFRS) as per the Cabinet Approval dated 28th April 2006, all revenue generated from government owned assets used by AASL has also retained without remitting to the Consolidated Fund.	It is recommended to transfer the government loans to AASL books in a proper manner to avoid the duplication, with the coordination of the Treasury.

Account by duplicating of Debt servicing are done recording the loans. out of these revenues.

Further, foreign loan obtained for Mattala Rajapakshe International Airport (MRIA) had also been transferred to the Company by General Treasury through a Memorandum of Understanding (MOU) without any valid loan agreement or transfer. The outstanding loan balance as at 31 December 2018 was Rs.27,001 Million which is equivalent to USD 146 Million.

Mattala Rajapakshe International Airport loan has been transferred to AASL as per the Cabinet approval granted on 24th October 2013. In addition a MOU has been signed with the treasury to affect the above loan transfer.

3.3 Operational Inefficiencies

Audit Issue

A properly designed computerized finance system which is compatible with current requirement had not been introduced. Further, implementation of Enterprise Recourse Planning (ERP) System had failed in the year 2016 and action had not been taken to introduce a new system to date.

Management Comment

A cabinet decision taken Considering the directive of the COPE, AASL terminated the contract for the implementation of the ERP system on 27/12/2016 due to poor performance and inability to meet AASL requirements. The Contract is to be signed with IFS upon completion of the Proof of Concept (POC) Test to change the scope of original ERP and phase out to two modules; finance and supply/stores.

Recommendation

It is recommended to introduce and implement the new ERP system as early as possible to meet the AASL requirements.

3.4 Under -utilization of Funds

Audit Issue	Management Comment	Recommendation
<p>The Company had entered into two agreements with Japan International Cooperation Agency for funding of Japanese Yen 74,397 million for Phase II Stage 02 of Bandaranaike International Airport Development Project on the dates of 28 March 2012 and 24 March 2016. However, the contract value equivalent to the 92 percent of the funding value, had not been awarded even up to the 31 December 2018. Further the Company had paid a sum of Rs. 245.7 million to the Japan International Cooperation Agency as at 20 April 2019 as commitment fee for under-utilization of funds.</p>	<p>JICA review and concurrence due to direction by the cabinet of Ministers to Re-design and construct a new terminal building at BIA, the utilization of the above loan is at a low level. As per the loan agreement a commitment fee of 0.1% to be paid on the total unutilized loan balance until the loan amount is fully for SL-P104.</p> <p>Action will be taken to expedite the bidding process of the package A contract.</p>	<p>Action should be taken to award the contract and meet the objective under the agreement.</p>

3.5 Procurement Management

Audit Issue	Management Comment	Recommendation
<p>Most of the procurement activities had not been executed within the time scheduled and it was observed a huge delay in procurement. Further, as per the Master procurement plan of the Company, 16 no of procurement activities which were estimated at a total cost of Rs.4,174,332,000 had not been commenced even though they were planned to be completed in the year 2018 and 8 No of those procurements were recognized as urgent.</p>	<p>Not given</p>	<p>Procurement activities should be executed within the stipulated time frame in-order to avoid delay.</p>

3.6 Defects in Contract Administration

Audit Issue	Management Comment	Recommendation
Due to extra work and fluctuation of exchange rate, an amount of Rs. 5,386,493,321 was identified as excess payment for construction of Mattala Airport Stage II Project. Due to the delay on settlement, it had been agreed with contractor of China Harbour Engineering Company to be paid Rs. 6,012,045,000 with additional payment of Rs. 625,551,678.	Not given	Actions should be taken to settle outstanding payments within due dates in future to avoid additional payments and contract administration should be maintained properly to minimize losses to the Company.

4. Accountability and Good Governance

4.1 Environmental Issues

Audit Issue	Management Comment	Recommendation
There was no any formalized disposal procedure to dispose confiscated items and thereon it is adversely impact to the environment	Not Given	A formal disposal procedure for confiscated items Should be introduced.

4.2 Sustainable Development Goals

Audit Issue	Management Comment	Recommendation
The sustainable goals as per the United Nations Sustainable Development Agenda had not been identified and included in to the Corporate plan/Annual Action plan of the Company.	Not given	Sustainable development goals should be identified by the Company as instruction early.