

## **Lanka Rest House Limited - 2019**

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### **1.1 Disclaimer of Opinion**

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The audit of the financial statements of the Lanka Rest House Limited for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 and the statement of profit and loss and other 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 reported to Parliament appear in this report.

I do not express an opinion on the accompanying financial statements of the Lanka Rest House Limited. Because of the significance of the matters discussed in the Basis for disclaimer of opinion section my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

### **1.2 Basis for Disclaimer of Opinion**

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

### **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, 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 (Auditor's Responsibility for the Audit of financial statements)**

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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 Internal Controls over perpetration of financial statements**

Entities are required to “devise and maintain” a system of internal accounting controls sufficient to provide reasonable assurance that, transactions are executed in accordance with management’s general or specific authorization, transactions are recorded as necessary to permit preparation of financial statements in conformity with the applicable reporting standards, and to maintain accountability for assets, access to assets is permitted only in accordance with management’s general or specific authorization, and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

### **1.5.2 Non – Compliance with Sri Lanka Financial Reporting Standards for medium and small sized entities (SLFRS for SMEs)**

| <b>Non compliance with reference to the relevant standard</b>   | <b>Management Comment</b>   | <b>Recommendation</b>   |
|---|---|---|
| (a) According to paragraph 60 of LKAS 1, the assets and liabilities as at 31 December 2019 should be stated in the statement of financial position in liquidity order. However, the statement of financial position had not been prepared accordingly.  | Comment had not been given.   | The statement of financial position should be prepared according to the Accounting Standards.   |
| (b) According to paragraph 81 of Sri Lanka Financial Reporting Standard – 16, the revenue received on operational lease should be identified on the Stateline method or any other systematic basis. However, the key money received from 3 rented Rest Houses, given on 10 years period, on 10 July 2019 amounting to Rs.2,787,000 had been identified as a income of the year under review instead of being identified them on systematic basis though out the rented period. As a result, the profit for the year under review had been overstated. | As this amototerised over 10 years period, the Journal entries put for only 2019, and it will be corrected. | According to the Sri Lanka financial reporting standard, the lease income should be identified. |

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|---|---|---|
| <p>(c) Contrary to LKAS – 7, when preparing the cash flow statement, the fixed deposit amounting to Rs.39,498,342, which is not realized within a year had been shown under the cash and cash equivalents. In addition, instead of being shown the purchase cost of the property plant and equipment as cash out flow, the net amount after deducting of depreciation had been adjusted to the cash flow statement. As a result, the new cash out flow shown in the cash flow statement had been understated by Rs.631,893.</p>         | <p>Only the actual cash flows should be shown under the investment activities, Hence variances should be adjusted. Purchase of fixed assets should be shown under the investment activities. It had been showed the net amount after deducting of depreciation, it will be corrected.</p> | <p>According to the relevant standard, the cash flow statement should be prepared.</p>  |
| <p>(d) The details relating to the depreciation for fixed assets amounting to Rs.631,893 had not been furnished to audit in order to prove the provisions were compliance with LKAS - 16.</p>   | <p>The asset schedule and the register were not available. Hence, the details could not be furnished to audit.</p>  | <p>In order to prove the correctness of calculation of depreciation, the details should be furnished to audit.</p>  |
| <p>(e) According to LKAS – 37, initiated legal proceedings by the Company and the legal cases filed against the Company should be disclosed in the financial statements. However, the legal case filed against the renter of the Weligama Rest House for the period of November 2009 to November 2017 by the Company and the legal case filed against the Company by the renter of the Negambo (old) Rest Houses that rented for the period from November 2009 to November 2017, had not been disclosed in the financial statement.</p> | <p>Comment had not been given.</p>  | <p>According to the requirement of the standard, the legal responsibilities should be disclosed as required and action should be taken to make necessary adjustments.</p> |

### 1.5.3 Accounting Deficiencies

| Audit Observation  | Management Comment  | Recommendation   |
|--|---|--|
| <p>(a) Even though the property, Plant and Equipment amounting to Rs.10,289,128 had been shown in the financial statements, the assets purchased subsequent to the</p> | <p>The Company had not been maintained an asset register and information related to prior to the year before 2011, cannot be furnished.</p> | <p>Actions should be taken to verify all assets belonging to the Company and they should be included to an asset register and those information should be maintained comprehensive and</p> |

year 2011 had only been represented that amount. The management of the Company had accepted that the assets acquired before the year 2011 are also owned by the Company and other assets including Rest Houses are already existed. However, action had not been taken to revalue those assets and brought to the accounts. An assets register had not been maintained comprehensive and updated manner relating to the assets owned by the Company as at 31 December 2019.

updated manner.

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|-----|---|---|---|
| (b) | The payable expenditure for renovation of the Maiyanganaya Rest House during the year under review amounted to Rs.3,194,655 had not been accounted for as an expenditure of the year under review and as a payable expenditure.                             | The expenditure will be capitalized through a Journal entry in order to make the corrections stating it as work-in-progress of the year 2019. | The expenditure and liabilities related to the year under review should be shown in the financial statements. |
| (c) | The receivable interests as at 31 December 2019 from fixed deposits had been understated by Rs.745,519. As a result, the profit for the year had also been under stated by that amount in the financial statements.   | Based on the confirmation given by the bank, this will be changed.  | The receivable income should be correctly identified.   |
| (d) | The income receivable from the Rest Houses had been overstated by Rs.1,499,047 in the financial statements of the year under review. As a result, the profit for the year and trade debtors had been overstated in the financial statements by that amount. | The Company had not maintained a debtor's ledger. However, in order to provide real information, action has been taken.                       | - do -  |

- (e) The value added tax payable to the Local Authorities amounting to Rs.3,668,269, on the income generated by the Company by managing the Rest Houses owned by the Local Authorities, had not been shown in the financial statements.
- This had been totally omitted from the accounts and action to be taken to make the corrections.
- After deducting related liabilities from the received income, only the net income should be identified as the income.
- (f) Even though the Receivable Value Added Tax (VAT) as at 31 December 2019 amounted to Rs.1,205,798, only a sum of Rs.739,971 had been shown in the financial statements. Hence, VAT amounting to Rs.467,821 had been under stated in the financial statements.
- Comment had not been given.
- Action should be taken to include the correct receivable income in the financial statements.

#### 1.5.4 Reconciled Control Accounts or Reports

| Item   | Amount as per financial statements | Amount as per corresponding records | Difference | Management Comment  | Recommendation  |
|--|------------------------------------|-------------------------------------|------------|---|---|
|  | (Rs.)                              | (Rs.)                               | (Rs.)      |   |   |
| Current account with the Parent Company of Urban Development Authority | 57,637,911                         | 61,686,503                          | 4,054,592  | Even though that reconciliation statement had not been furnished to audit in 2019, corrections to be taken in order to give real picture. | Action should be taken to reconcile the current account balances with corresponding balances, in order to make the corrections before furnish the accounts. |

#### 1.5.5 Unauthorized Transactions

| Audit Observation  | Management Comment  | Recommendation  |
|--|---|---|
| (a) Even though it had been informed that disposal of fixed assets at the Kataragama Rest House during the year under review, a Board of | Most of the assets had been formally handed over to the Maiyanganaya Rest House and subsequently, those | The required system and control procedures should be introduced by the management in order to get |

survey had not been appointed to obtain the authority for the disposal (The particulars of the disposed assets had not been furnished to audit). The relevant adjustments had also not been made in the financial statements.

assets had been auctioned.

the maximum benefits to the Company from the disposals.

### 1.5.6 Lack of Written Evidence for Audit

| Item                          | Amount<br>(Rs.million) | Evidence not made available                | Management Comment   | Recommendation  |
|-------------------------------|------------------------|--|--|---|
| (a) Written-off of bad debts. | 4,152,161              | Details of bad debt calculations.          | Even though a register for the calculation particulars had not been maintained, action to be taken to maintain it for the year 2019. | Action should be taken to provide the particulars to audit. |
| (b) Income tax calculations   | -                      | Detailed schedules and calculation details | Comment had not been given   | - do -  |

## 1.6 Accounts Receivable and Payable

### 1.6.1 Accounts Receivable

#### Audit Observation

Action had not been taken to recover the trade debtors amounting to Rs.10,352,823 and other debtors amounting to Rs.6,673,529 for a period ranging from 1 to 5 years.

#### Management Comment

Comment had not been given.

#### Recommendation

Prompt action should be taken to recover the receivables.

### 1.6.2 Account Payables

#### Audit Observation

(a) It was observed that the payables as at 31 December 2019 amounting to Rs.21,545,403 to the Local Authorities had not been paid within the stipulated time period.

#### Management Comment

Comment had not been given.

#### Recommendation

The payables to the Local Authorities should be paid according to the law.

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|-----|---|-----------------------------|---|
| (b) | The confirmations relating to trade creditors amounting to Rs.21,125,835 and other creditors amounting to Rs.7,154,819 had not been received. Therefore, existence of those creditors could not be confirmed in audit | Comment had not been given. | Existence of the creditors should be confirmed. |
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**1.7 Financial Management**  
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**Audit Observation**  
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The procedures relating to payment by cheques had not been introduced. As a result, action had not been taken to cancel 10 issued cheques which were validity period exceeded by 6 month amounting to Rs.1,006,380 and credit to the income or to make necessary adjustments.

**Management Comment**  
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Comment had not been given.

**Recommendation**  
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Action should be taken relating to the cheques outstanding over 6 months.

**1.8 Non – Compliance with Tax Regulations**  
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**Audit Observation**  
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According to Section 83 of the Inland Revenue Act No.24 of 2007, the payee tax should be paid before the 15<sup>th</sup> of next month. However, payee tax amounting to Rs.550,236 had not been so paid by the Company. Further, the payee tax return had not been furnished to the Department of Inland Revenue on or before 30 April.

**Management Comment**  
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Even though the payee tax had been deducted, the tax had not been remitted to the Department of Inland Revenue. That should be shown in the financial statements as tax payable, it will be corrected in future. After been made the required adjustment to the profit and loss account, tax calculation details can be provided. Until obtain the correct financial position, the tax cannot be calculated.

**Recommendation**  
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According to requirement of the Inland Revenue Act, the tax should be paid.



## 2. Financial Review

### 2.1 Financial Results

The operating result of the year under review amounted to a pre tax profit of Rs.10,206,977 and the corresponding profit in the preceding year amounted to Rs.8,375,861. Therefore, an improvement amounting to Rs.1,465,261 of the financial result was observed. The reasons for the improvement were decrease of administration cost by Rs.323,793 and increase of other income by Rs.2,944,939.

## 3. Operational Review

### 3.1 Identified Losses

| <b>Audit Observation</b>  | <b>Management Comment</b>   | <b>Recommendation</b>  |
|---|-----------------------------|--|
| (a) The agreements entered into between the UDA Rest House Ltd, the Lanka Rest House Ltd and respective Local Authorities had not been furnished to audit. It had been agreed to pay 65 per cent of income to the Local Authorities for the rest houses belonging to them. However, due to the management weaknesses, out of such 40 Rest Houses, 10 and 14 Rest Houses were in idle in the years 2018 and 2019 respectively. It had not been obtained consent of the Local Authorities relating to recovering of losses occurred due to not renting of Rest Houses and not proper maintenance. | Comment had not been given. | The operating activities should be conducted based on the agreements.  |
| (b) Even though an Action Plan had been prepared for the year 2019, a performance report had not been prepared. Hence, the Company had filed identify, whether the conducted activities were related to the year or not, the results achieved in the year, none – implemented activities, reasons for such none implementations and reasons for the low progress achieved in the year etc.  | Comment had not been given. | The corrective actions should be taken relating to unfavorable results, after being prepared an action plan. |

### 3.2 Management Inefficiencies

| Audit Observation  | Management Comment                 | Recommendation  |
|--|------------------------------------|---|
| <p>(a) Based on the Gazette notifications issued on 09 September 1980 and 11 December 1981, 38 Circuit Bungalows and Rest Houses owned by the Local Authorities had been acquired by the UDA. As well, based on the decision made by the Cabinet of Ministers on 17 July 2006, the administration functions of the Rest Houses had been vested to the Company. The Cabinet of Ministers had decided that the assets including rented assets and good will to brought to the first balance sheet, to appoint a private management Agent and to issue 49 per cent shares to that Agent and to revalue all the assets including good will. However, those decisions had not been implemented.</p> | <p>Comment had not been given.</p> | <p>According to the decisions made by the Cabinet of Ministers, all functions should be carried out.</p>                                |
| <p>(b) Even though in order to manage the Rest Houses, a Company namely Lanka Rest House Ltd had been established under the UDA, the Company had not taken action to rent out the Rest Houses on long term basis applying a specific policy. Particularly, the Rest Houses had not been rented out after being called quotations for select the highest bidders while evaluating rest house management experiences and the financial capacities.</p>   | <p>Comment had not been given.</p> | <p>Introducing required systems and controls, the management should take actions to enhance efficiency of the operating activities.</p> |
| <p>(c) When renting the Rest Houses on long term basis, specific rent period had not been applied. The agreed renting periods for each Rest House were varied.</p>   | <p>Comment had not been given.</p> | <p>A specific policy should be introduced for renting the Rest Houses.</p>  |

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

| Audit Observation   | Management Comment                 | Recommendation  |
|---|------------------------------------|---|
| <p>According to the information submitted by the Director (Rest House Management) of the UDA on 26 September 2011, 43 Rest Houses were under the Management of the Company. Out of 40 Rest Houses</p> | <p>Comment had not been given.</p> | <p>Proper registers should be maintained relating to the Rest Houses and the responsibilities of those Rest Houses.</p> |

come under the preview of the Lanka Rest House Ltd, the profit earning Rest Houses were 30 and 26 in the years 2018 and 2019 respectively and 10 and 14 Rest Houses were also in idle.

### 3.4 Procurement Management

#### Audit Observation

In terms of section 7.3 of the Public Enterprises Circular No.PED/12 dated 02 June 2003, state companies also should follow the Government Procurement Guidelines equally. However, though the Company had procured goods and services valued at Rs.8,761,999 in the year 2019, a procurement plan had not been prepared for the year 2019.

#### Management Comment

Comment had not been given.

#### Recommendation

The circulars issued by the Public Enterprises Department of the Treasury should be followed by the Company.

### 3.5 Human Resource Management

#### Audit Observation

In terms of section 9.2 of the Public Enterprises Circular No.PED/12 dated 02 June 2003, after being prepared the cadre, it should be registered in Public Enterprises Department of the Treasury. As well, even though the approval of the Ministry and the Department of Public Enterprises should be obtained for the recruitment and promotion procedure, as per section 9.3.1 of the circular, those approvals had not been obtained. Further, the approval for the cadre had not been obtained from the Department of Management services in terms of Department of Management Services Circular No.30 dated 22 September 2006.

#### Management Comment

Comment had not been given.

#### Recommendation

After being prepared the cadre of the Company and recruitment and promotion procedure, the required approvals should be obtained as per the circular instructions.

#### **4. Accounting and Good Governance**

##### **4.1 submission of financial statements**

###### **Audit Observation**

According to the Public Enterprises Circular No.PED/12 dated 02 June 2003, the financial statements for the year 2019, should be furnished for audit on or before 28 February 2020. However, the financial statements had been furnished for audit on 07 September 2020 after delaying 06 months.

###### **Management Comment**

Comment had not been given.

###### **Recommendation**

Action should be taken to furnish the financial statements according to the circular instructions.

##### **4.2 Furnishing of Annual Reports**

###### **Audit Observation**

According to section 6.5.1 of the Public Enterprises Circular No.PED/12 dated 02 June 2003, the drafted Annual Report should be furnished to audit within 60 days after the closer of the financial year. However, action had not been taken accordingly.

###### **Management Comment**

Comment had not been given.

###### **Recommendation**

Action should be taken to furnish the annual report on stipulated time period.

##### **4.3 Corporate Plan**

###### **Audit Observation**

According to section 12 of Enterprises Circular No. PED/12 dated 02 June 2003, a Corporate plan had not been prepared for the year 2019.

###### **Management Comment**

Comment had not been given.

###### **Recommendation**

A Corporate plan should be prepared.

##### **4.4 Annual Action plan**

###### **Audit Observation**

According to paragraph 5(2) of the Public Finance Circular No.01/2014 dated 11 February 2014, an Action Plan should be prepared by the Company based on the Corporate Plan. As well, as per section 5.1.3 of the Public Enterprises Circular

###### **Management Comment**

Comment had not been given.

###### **Recommendation**

After being prepared the Annual Action Plan, relating to the activities of the Company, the approvals should be obtained.

No.PED/12 dated 02 June 2003, the Action Plan should be furnished to the Line Ministry, the Department of Public Enterprises, Treasury and Auditor General, before 3 months beginning of the respective financial year, after being obtained the approval from the Board of Directors. However, the Action Plan prepared for the year 2019, had not been approved by the Board of Directors.

**4.5 Internal Audit**  
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**Audit Observation**  
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An Internal Audit Division had not been established for the Company and action had not been taken to get done the Internal Audit functions of the Company through the UDA internal audit division.

**Management Comment**  
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Comment had not been given.

**Recommendation**  
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As there is no internal audit division in Company, action should be taken to cover the internal audit functions of Company through the UDA's internal audit division.

**4.6 Audit Committee**  
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**Audit Observation**  
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Audit Committees had not been conducted by the Company in the year under review.

**Management Comment**  
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Comment had not been given.

**Recommendation**  
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Action should be taken to conduct the Audit Committees.

**4.7 Budgetary Control**  
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**Audit Observation**  
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According to section 5.2.4 of the Public Enterprises Circular No.PED/12 dated 02 June 2003, the budget of the Company should be approved before 3 months beginning of the respective financial year, the budget for the year under review had not been so approved.

**Management Comment**  
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Comment had not been given.

**Recommendation**  
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After being prepared the annual budget, the approval of the Board of Directors should be obtained for the budget.