

Airport and Aviation Services (Sri Lanka) (Private) Limited - 2019

1.1 Qualified Opinion

The audit of the financial statements of the Airport and Aviation Services (Sri Lanka) (Private) Limited (“Company”) for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 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 2019, 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 intends 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.

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 Accounting Standards

Non -Compliance with the reference to particular Standard -----	Management Comment -----	Recommendation -----
The statement of financial position includes property, plant and equipment relating to the Mattala Rajapaksha International Airport (MRIA) with a carrying amount of Rs.21 Billion and Capital work in progress of Rs.70 Million as at 31 December 2019. However, this airport has been underutilized from the inception to date.	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 there, there would not have been any flight movement during runway overlay period within that closure time period. Arrangements are making by the new government and to re-develop the Airport with their vision.	Even though there were arrangements making to re-develop the MRJA, those have not yet been implemented. Therefore, indicators for impairment are still there and an

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 the relevant assets of the MRIA may be impaired, on the basis of it being a separate cash generating unit

Thereon, a Cabinet decision was taken on 04 March 2020 to attract Airlines to Mattala Rajapaksha International Airport (MRIA) and Colombo International Airport Ratmalana (CIAR)” by coordinating the discussions with relevant institutions. Further, a proposal for the establishment and operation of the International Pilot Training Academy at MRIA has also been approved by the Cabinet on 04 March 2020.

impairment test should be carried out.

1.5.3. Accounting Policies

Audit issue	Management Comments	Recommendation
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(i) In contrary to the direction of the 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.
(ii) 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 2019 in respect of the above loans was Rs.10,441 Million.	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	Government loans should be transferred to AASL books in a proper manner to avoid the duplication with coordination of the Treasury.

It was further observed these loans are also shown as liabilities in the Republic Account by duplicating of recording the loans.

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 2019 was Rs.24,587 Million which is equivalent to USD 134 Million.

Consolidated Fund. Debt servicing are done out of these revenues.

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.

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

The following non-compliances with Laws, Rules, Regulations and Management decisions etc. were observed.

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 been prepared and got approved from Civil Aviation Authority of Sri Lanka.	AASL has decided to proceeds Master Plan update utilizing AASL own funds and Budget allocation was made for Year 2020 and 2021. Request of Proposal (RFP) document was prepared and awaiting to proceeds procurement of consultancy services for the Master Plan Preparation work. However, all modifications and new construction activities (Apron E, Runway etc.) of aerodrome of BIA were Approved by	Master plan should be prepared and action should be taken to get approved early.

CAA case by case as per the Civil Aviation Act No.14 and in far with the existing Master Plan.

(b) Section 6 of the companies Act, No. 07 of 2007

Name of the Company remains in its all official correspondence including annual financial statements of 2019 without the suffix “(Private) Limited” or the abbreviation “(Pvt) Ltd”, despite the fact that the Company had re-registered with the suffix “(Private) Limited” without considering the legal opinion of Attorney General.

The company is in the process of making the name change as per the application law, with due regard to securing it’s corporate image.

Action should be taken to change the name or use the registered name as it is.

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

(i) paragraph 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 for it from Line Ministry.

The procedure manuals for all divisions and units have been finalized and tabled before the Board in August 2019. Action will be taken to submit a soft copy of the procedure manuals of the company to the line ministry and to the Department of public enterprises, General treasury for its concurrence.

Approvals should be obtained from the Line Ministry & concurrence from General Treasury to all operational manuals.

(ii) Paragraph 9.2

The Organization Chart

The Board has appointed a

Action should be

- (d) and the approved Cadre of the Company had not been registered with the Department of Public Enterprises, General Treasury. Committee on 29th April 2020 to review the Cadre of the company and to submit a report to the Board for its approval, as instructed by MSD. Organization structure also to be included in to this. Before the end of this financial year (2020) that process would be completed. taken to get the approval from General Treasury
- (iii) 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. After getting the approval for the cadre from MSD, the SORPs will be provided for the approval. Action should be taken to register the Schemes of Recruitment and Promotion with the Department of Public Enterprises of General Treasury.
- (iv) Paragraph 9.14 HRM Manual of Procedures had not approved by the Board with the concurrence of the Secretary to the Treasury through the Department of Public Enterprises, General Treasury. The preparation of Human Resources Management Policy and Procedure Manual has been awarded to an external party and the original deadline was end March 2020. However, due to Covid19 situation, both parties could not co-ordinate this matter. Now, we are reviewing the first draft of the HRM Manual and hope to finalize this assignment within the month of July 2020. HRM Manual of Procedures should be approved by the Board and obtain the concurrence of Secretary to the Treasury through the Department of Public Enterprises, General Treasury.

(v) paragraph 7.4.5	Annual board of survey had not been conducted on time to carry out the verification of assets	Annual board of survey of 2019 has been planned to outsource to complete within a period of 3 months. Selection of an audit firm has been approved by Tender board ii on 25/06/2020. Board of survey could not be started as scheduled and tender process has been delayed due to covid-19 epidemic and lock down during March and April 2020.	Annual Board of Survey should be appointed on or before the 15 th of December of each year and Board should report to the Chairman as soon as possible after 31 December of each year.
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1.7 IT General Controls

Audit Issue

Management Comment

Recommendation

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 used in the finance system due to continuous modification requested by the users and there is no integration between the modules and other related systems.

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.

An action should be taken to implement the new integrated system early.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs.10,996,009,352 and the corresponding profit in the preceding year amounted to Rs. 5,313,155,819. Therefore, an improvement amounting to Rs. 5,682,853,533 of the financial result was observed. The main reason for the improvement is decreasing of finance cost by Rs.8,028,348,443 due to exchange gain in loan conversion instead of exchange loss occurred in preceding year.

2.2 Trend Analysis of major Income and Expenditure items

	2019	2018	Variance	%
Revenue	-----	-----	-----	-----
Aeronautical Revenue	5,430,766,464	5,234,386,906	196,379,558	4
Non Aeronautical Revenue	20,221,486,743	19,724,793,830	496,692,913	3
Other Income	63,840,889	3,779,811,015	(3,715,970,126)	(98)
Non-Operating Income	4,164,672,412	3,134,442,144	1,030,230,268	33
Total Airport Revenue	29,880,766,508	31,873,433,895	(1,992,667,387)	(6)
Administration & Establishment Expenses				
Staff cost	6,513,810,228	6,051,848,491	461,961,737	8
Defined contribution/benefit plan costs	1,602,849,819	1,406,277,355	196,572,464	14
Depreciation & Amortization	2,856,562,491	2,693,830,019	162,732,472	6
Repairs & Maintenance	462,842,807	397,856,041	64,986,766	16
Provision for debtor's impairment	397,143,394	238,433,748	158,709,646	67
Finance Cost				
Loan Interest	1,325,977,575	1,008,360,931	317,616,644	31
Exchange (gain) /loss (On loans)	(156,729,149)	8,182,292,344	8,025,563,195	98

2.3 Ratio Analysis

Type of Ratio	2019	2018	2017	2016	2015
Current Assets Ratio (number of times)	7.23	3.49	2.78	2.65	2.09
Quick Assets Ratio (number of times)	7.10	3.43	2.71	2.60	2.06
Net Profit Ratio (%)	43	18	42	38	05
Earnings per Share (Rs.)	54,980	26,566	43,574	34,598	4,084
Return on Net Assets (%)	28	19	37	42	07
Revenue per Passenger (Rs.)	2,582	2640	2,085	1,936	1,846

The following observation are made.

- Increase in short-term bank deposit by 27 percent and decrease in trade payable by 74 percent were the main reasons attributed for the increase in Current Ratio and quick Assets Ratio.
- The earning per share had increased by 107 percent during the year mainly due to increase in exchange gain on loan conversion in 2019 instead of exchange loss incurred during 2018.
- The decrease of the other income by 98 percent mainly due to decrease in net exchange gain on transactions in 2019 comparing the exchange gain incurred during 2018.

3. Operational Review

3.1 Performance

The physical performance of the Key Performance Indicators (KPI) of the Company is given below.

Key Performance Indicator	2019	2018	2017	2016	2015
Number of International Flight Movements	62,195	67,351	62,850	61,637	56,156
Number of Total Passenger Movements	9,958,688	10,884,028	9,957,502	9,466,248	8,505,740
Cargo Movements (Metric Tons)	259,089	279,559	274,047	248,347	220,422
Total Cost per Flight Handled (Rs. '000)	236	318	202	216	256

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 -----
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. 5,638.3 Mn as at 31 December 2019 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

3.3 Operational Inefficiencies

Audit Issue -----	Management Comment -----	Recommendation -----
(i) An ERP system compatible with current technology had not been introduced to the Company even as at 31 December 2019.	As decided by AASL management ERP system is being implemented in two stages. As the first stage Finance, Supply Chain and Payroll modules will be implemented and currently running in-house developed peripheral systems will be integrated into this. It is scheduled to go live by 01st of August 2020. Consultancy project initiated by the company (SMD) for Stage 2 of the implementation is currently going on.	It is recommended to introduce and implement the new ERP system as early as possible to meet the company's requirements.
(ii) Assets coding system and properly updated assets register had not been made available for audit.	Instead of 12 digit coding system, a 16 digit coding barcode readable system was introduced. At the time of submission of registers to the Auditor General, Master Fixed Assets Register has not been updated with new codes and currently it is being updated with new codes in order to upload into the ongoing ERP project by 15 th August 2020 as scheduled.	ERP system should be implemented as early as possible and assets register should be updated regularly.

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 74,397 million Japanese Yen for Phase II Stage 02 of Bandaranaike International Airport Development Project on 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 2019. Further the Company had paid a sum of Rs. 290.3 million to the Japan International Cooperation Agency as at 20 April 2020 as commitment fee due to under-utilization of funds. Changing the design had been caused for the delaying of the project.</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. As per Cabinet Decision dated 19/2/2020, it was decided to award Package A to Taisei Corporation. The letter of Acceptance issued on 4/3/2020 and Contract Agreement signed on 13.3.2020. Construction Works is expected to commence within 2 month time and Contractor is in the process of requesting an advance payment. With the release of advance payment from the loan SLP104 there will be a substantial amount of disbursement from the loan and which is expected to complete within 3 years.</p>	<p>Action should be taken to complete the construction of package A as per the contract agreement, review the construction progress periodically to avoid further delays.</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. As an example the Company had taken nine months to complete the procurement of RFID cards during the year 2019.</p>	<p>Not given</p>	<p>Procurement activities should be executed within the time frame and delays should be avoided.</p>

4. **Accountability and Good Governance**

4.1 **Environmental Issues**

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