Pradeshiya Sanwardana Bank - 2020

1.1. Opinion

The audit of the financial statements of the Pradeshiya Sanwardana Bank ("Bank") for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 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. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2020, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

Emphasis of Matter

I draw attention to Note 20.2 to the financial statements which discloses the impairment provision is recognized net of the funds available in the Special Reserve Fund created to provide for bad and doubtful debts of the bank as per the Section 23 of Pradeshiya Sanwardana Bank Act No.41 of 2008. My opinion is not qualified in respect of this matter.

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 determines 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

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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 Bank’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. Financial Statements

1.5.1. Documentary Evidences not made available for Audit

Audit Issue	Management Comment	Recommendation
Evidences were not available to verify the stock of Lankaputhra Development Bank amounting to Rs.11,106,023 and minus balance of Rs.952,007 of stock in transit.	Incomplete system generated entries, unusable stationary stock with former Lankaputhra Development Bank (LDB) logo, some outdated stocks are some issues encountered in taking over former LDB stock balances. This matter would be looked in to with the assistance of Administration Department and writing off from the books will take place against already made contingent provisioning by end of this year.	Take necessary actions to check the accuracy of stocks value and make required adjustments.

1.6. Accounts Receivable and Payable

1.6.1 Receivables

Audit Issue	Management Comment	Recommendation
I. 704,048 number of loans amounting to Rs.65,043 million had been disbursed by the bank during the year 2020. Out of that, 569,819 number of loans or 80.9 per cent from the total number of loans disbursed amounting to Rs.26,153.4 million were pawning advances. Further, another 5.1 percent from total number of loans or 35,697 number of loans amounting to	Due to the Covid 19 pandemic situation high demand arises for pawning facilities and loan against deposit. Though the people were facing lot of financial difficulties, there was no demand for other loans, due to uncertainty of investment and their business during that time.	Take necessary actions to diversify the loan portfolio and reduce the NPL levels at least up to industry standards.

Audit Issue	Management Comment	Recommendation
Rs.9,308.6 million had been disbursed as loans against deposits. Therefore, 98,532 number of loans or 14 percent from the total number of loans amounting to Rs.29,580.9 million only had been disbursed as all other types of loans.		
II. Gross NPL ratio of the bank had been continuously increased from Rs.3 billion or 2.85 percent from the year 2016 to Rs.16.7 billion or 10.11 percent as at the end of year 2020. However, the average NPL of Licensed Specialized Banks and Banking sector as at 31 December 2020 was 6.8 percent and 4.9 percent respectively.	Most of the irregular loans were rescheduled and the irregular loans which were to be taken legal actions against at that time were not done due to the Government instructions. And also as a rule, bank took decision to limit granting new loans. The result was NPL ratio raised to high percentage.	
III. 52.6 per cent or Rs.8.8 billion from the total non-performing loans outstanding balance as at 31 December 2020 represents by Industrial loans and Micro Enterprise Loans.	90 percent of the RDB industrial & micro enterprise loans consist of small-scale enterprises. Just after the Easter Sunday attack they were the most affected sector of Covid 19 pandemic time.	

1.6.2 Payables

Audit Issue	Management Comment	Recommendation
I. As per the agreement signed between SME Bank and General Treasury on 27 October 2006 and the letter no LDB/INF/19/035 dated 31 January 2019 of LDB General Manager, Rs. 50 million had been given by Mahaweli Authority to LDB on 12 November 2009 to continue stage III of Mahaweli Loan Scheme. According to the section 2 (a) & (b)of the above agreement, LDB should pay the loan by four annual instalments within 5 years including a one-year grace period with 4 per cent annual	No loan repayment schedule had been provided for the said Rs.50 million loan. Since, no repayments had been made we have accounted correctly showing the amount as payable in the books of RDB. Also, we have noted that said Rs.50 million is not in the books of General Treasury as receivable from former LDB.	Take necessary actions to act as per the conditions of the signed agreements.

interest. However, the bank had not complied in this regard and remained the loan balance of Rs. 50 million as a payable balance in the financial statement more than 11 years with the merger of RDB & LDB effected on 01.04.2019.		
II. Capital outstanding of Rs.117,613,802 and interest outstanding of Rs.72,248, 586 in relation to 12 loan schemes/ revolving funds had been remained over a long period without taking actions to clear.	Capital outstanding of Rs. 48 million and interest outstanding of Rs.44,965,720 had been settled in April 2021 in relation to 2 loan schemes. Other loans are long outstanding and recorded in relation to province offices. Arrangements will be made to refer the issue to the respective provinces and clear the possible balances by end of this year.	Take necessary actions to settle the payables without any further delay.

1.6.3 Advances

Audit Issue	Management Comment	Recommendation
I. Audit of Loans granted for closed down garment factories by Lankaputhra Development Bank, Rs. 750,000,000 had been received to the LDB for the disbursement among closed down garment factories as per the cabinet memorandum No. MF/FMAU/TAEL/CM dated 22.01.2007 where the Ministry of Finance is acting as the facilitator to implement a scheme to restructure/ rehabilitate closed factories. Out of these funds Rs. 700,000,000 had been received with related to closed garment factory and Rs. 50,000,000 had been received for other 5 factories. Following observations are made in this regard.		Take necessary actions to recover the loan outstanding balances and remit the collected money to the General Treasury.

(i) Closed garment factory

a) Out of the received amount Rs. 700,000,000 for closed garment factory, LDB had disbursed only Rs. 580,865,369 and therefore, Rs. 119,134,631 had been available with the bank without disbursing or reimbursing to the treasury.	Out of received amount of Rs. 700 million for closed garment factory, former LDB had initially disbursed Rs. 550 million and also arranged a revolving Trade Finance Facility of Rs. 150 million (including Letter of Credit facility) through government bank for which no disbursement involved. The said company had utilized Rs. 30.87 million in the said Trade Finance facility and defaulted when the settlement was due. As a result, said Rs.30.87 million too had been treated as a disbursement to the said company and no further transactions took place through the said facility. Hence, there had not been any requirement to disburse the balance amount of Rs. 119.13 million to the company.
b) Further, contrary to the section 7 of the above Cabinet memorandum, Rs.5,500,000 had been retained by the LDB out of the total collection of Rs. 25,500,000 from closed garment factory without reimbursing to the treasury.	Former LDB had collected Rs. 20 million from closed garment factory and remitted to General Treasury. In addition, further sum of Rs. 5.5 million was also collected from the company by installments over a loan period which too to be remitted to General Treasury. Pending further payments from the company as committed former LDB had retained the said amount temporary since the amount was insignificant and shown in the books as payable to General Treasury.

c) According to the section (iv) of the letter dated 10.09.2007 from the Department of Development Finance, LDB is responsible for recoveries of loans and monitoring of performances. However, no any evidences were available regarding the actions taken by the bank for recoveries of loans.	Former LDB had taken recovery action through visiting the factory, meetings with the officials and meetings at Ministry of Finance as well. Through the said process, LDB was able to recover Rs. 25.5 million and Rs. 20 million has also been remitted to Ministry of Finance. Even though there were several discussions to explore the possibility of filing legal action since there were no other remedy, proceeding further did not take place since Chairman of the company passed away and the balance sheet of the company reflected negative net worth position.
d) The nonperforming loan balance of closed garment factory was Rs.555,365,000 and the above balance had been classified under other assets without categorizing under loans.	For loan facilities made available to closed garment factory, the role of former LDB was to route the funds received from General Treasury to the said company. Former LDB did not hold the credit risk in this regard and therefore classified said loans under other assets. Since, the bank did not hold credit risk of the fund routed through the bank there is no necessity to treat the said facility being a part of the loan portfolio of the bank and therefore treated under other assets.
(ii) Other factories a) Out of the received amount of Rs. 50,000,000 for other factories, Rs.49,000,000 facilities were approved.	Even though, Rs. 49 million was scheduled to be granted out of Rs. 50 million received, only Rs. 25,354,516.92 was granted due to unsatisfactory

	However, only Rs.25,354,516.92 had been disbursed to the companies as per the customer loan statements from the LDB.	creditworthiness of certain proposed facilities.
b)	Contrary to the section 7 of the above Cabinet memorandum, the bank had retained collected money from other factories of Rs.16,000,481.92 without reimbursing to the treasury.	Rs. 16,000,482 had been recovered through recovery action and however recovered amount had not been remitted to the General Treasury. This amount too has been shown in the accounts under payable to General Treasury at RDB and it was revealed that no amount is due from former LDB as per the books of General Treasury with regard to reopening of closed down garment factories.

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

	Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
I.	Procurement Guideline reference 2.1.1 and Public Finance circular PF/429 (i)	Bank has used their own developed procurement manual without obtaining approvals from Director General of Public Finance.	The procurement manual of PSB has been prepared in line with the Procurement Guideline by obtaining the approval of the Board of Directors. However, actions are being taking to obtaining the approval of the Director General of the Department of Public Finance as pointed out in the audit report.	Take necessary actions to adhere with the cited direction.
II.	Section 3.1 of PED 1/2015 dated 25.05.2015	200 liters of fuel limit per month had been offered by the Bank for the special grade II officers including newly appointed	As per the Management Services Department letter dated 25 March 2015, the authority to approve the cadre of the bank and determining the applicable	Take necessary actions to adhere with the cited direction.

		corporate managerial positions contrary to fuel allocation limit of 140 liters as per the related circular.	allowances is vested with Board of Directors. As such, granting fuel and drivers allowances for the grade II officers has been done as per the approval of the Board of Directors.	
III.	Section 3.3 of PED 1/2015 dated 25.05.2015	Contrary to the circular, a driver allowance amounting to Rs.25,000 per month had been paid by the bank for the officers in special grade II including newly appointed corporate managerial positions.	As per the Management Services Department letter dated 25 March 2015, the authority to approve the cadre of the bank and determining the applicable allowances is vested with Board of Directors. As such, granting fuel and drivers allowances for the grade II officers has been done as per the approval of the Board of Directors.	Take necessary actions to adhere with the cited direction.
IV.	Chapter – 9.2 (C) of the PED – 12	Any changes to the approved cadre could be implemented at the time of reviewing the corporate plan. However, no such action had been carried out by the bank. Approved cadre of the bank had been changed in each year, contrary to this requirement.	As per the Management Services Department letter dated 25 March 2015, the authority to approve the cadre of the bank and determining the applicable allowances is vested with Board of Directors. Hence, cadre creation for each year is implemented considering the action plan and budget of the year.	Take necessary actions to adhere with the cited direction.
V.	Chapter – 9.2 (D) of the PED – 12	Organization chart and the approved cadre should be registered with the Department of Public Enterprises of the Treasury. Those had only been forwarded to the Board of Directors of the bank.	As per the Management Services Department letter dated 25 March 2015, the authority to approve the cadre of the bank and determining the applicable allowances is vested with Board of Directors. Hence, cadre creation for each year is implemented considering the action plan and budget of the year.	Take necessary actions to adhere with the cited direction.

VI.	Section 9.2 (a), (c) and 9.3.1 (IV) of PED 12 dated 02.06.2003	Head of special projects & policy implementation had been appointed by the bank internally. However, no such position was included in organizational structure and even applications had not been called specifying the position internally or externally. Further, as per the committee paper no. 2020/BHRRC/M01/P02 of 31.01.2020, no provisions had been made for special project and policy implementation division.	Creation of carder position and appointment of Head of special projects and policy implementation had been done as per Board of Directors approval dated 17 June 2021.	Take necessary actions to adhere with the cited direction.
VII.	Section 4 of CBSL Direction No.05 of 2020 dated 27.03.2020	50 per cent or 25 per cent of the accumulated and unpaid interest of the defaulted installments shall be deferred and balance capital outstanding, balance portion of defaulted installments and the future interest shall be rescheduled over a 3 year period. Deferred interest shall be waived by the bank, after the borrower settles the rescheduled loans accordingly. Contrary to the above, bank had opened new reschedule loan account using total arrears interest amount.	As per the instructions given by the circular no 2020/214, loan accounts have been rescheduled.	Take necessary actions to adhere with the cited direction.

VIII.	Section 4(8) of the Banking Act Direction No 4 of 2008	Bank shall not grant new credit facilities for repayment of NPL in the name of the same borrower, unless the credit facility so created is also classified as NPL and categorized into the same category of the repaid NPL had been categorized under direction 4(6). However, bank had classified rescheduled capital and interest accounts in the performing category contradictory to the above direction. Ex: 128059700305 134055900006	128059700305 & 134055900006 Loan Accounts have been rescheduled and those are remained Under D0 Category as at 31.12.2020. The relevant receivable interests of particular loan accounts have been capitalized as 128073200101 & 134073200430 as respectively. According to the CBS system those are remained as Performing category.	Take necessary actions to adhere with the cited direction.
IX.	Section 4 (ii) (f) of CBSL Direction No.05 of 2020 dated 27.03.2020	Contrary to the direction, bank had reclassified NPLs as performing loans without servicing interest for six consecutive months during the debt moratorium period. Ex: 104059600409 802054800043 802059600020	Those loan accounts have been rescheduled several times and those are remained as (A0) Performing Category. The reason for it is, as per request of customer, if the particular loan account has been rescheduled in two times and if the customer depositing even one installments of the particular loan, then the CBS System is transferring the particular loan as the performing loan category. Therefore, after identifying the issue of the system of the particular matter, the Circular of 2021-11 & the Circular of 2021-12 have been advised to correct this matter at the end of each & every month.	Take necessary actions to adhere with the cited direction.

X.	Section 04 of CBSL Direction No. 05 of 2020 (dated 27.03.2020) and section 05 of CBSL Direction No. 10 of 2020 (dated 09.11.2020)	Maximum repayment period of converted loans shall be 36 months. However, some rescheduled loans had been issued contrary to the above direction.	As per the instructions given by the circular no 2020/214, loan accounts have been rescheduled.	Take necessary actions to adhere with the cited direction.
XI.	Section 1.(i), 3.(i) c & d of CBSL Direction No.05 of 2020 dated 27.03.2020	As per the concessions for existing performing loans as at 25.03.2020, debt moratorium includes capital and interest and three months debt moratorium for personal loans, leases and six months debt moratorium for all other eligible businesses had been allowed. However, 3 months and 4 months respectively for capital repayment had been allowed by the bank as per the addendum VI of Office Instructions Circular(Development Loan) No.2020-211 dated 29.05.2020.	According to the Debt moratorium directions monthly salaried customers were allowed for 3 months moratorium only. But the most in this category requested to extend the period though the most were not full salaried at that time some of them not having OT payment. Therefore the bank has taken the decision to extend the grace period as per the request made by customers only.	Take necessary actions to adhere with the cited direction.

1.8. Non -compliance with Tax Regulations

Audit Issue	Management Comment	Recommendation
PAYE tax /APIT Every Employer is required to deduct income tax from the gains and profits from employment of each employee who is liable to pay income tax with his consent. Contrary to Public Enterprises Circular No. PED	Before merging in to one entity in 2010 permanent employees in the six provincial banks had been enjoying the benefit of bearing the PAYE tax component by the employer. Further, Section 45 (2) (d) of	Take necessary actions to adhere with the cited circular.

03/2016 of 29 April 2016, the Bank had paid APIT tax amounting to Rs.10,064,824.89 for the year 2020 out of its own funds on behalf of its employees instead of being deducted from the salaries of the respective employees.	Pradeshiya Sanwardana Bank Act No. 41 of 2008 states offering of employment on terms and conditions not less favorable than the terms and conditions which were previously enjoyed by them with the acquiring bank. On this basis RDB has been continuing bearing of PAYE tax liability of employees as an expense of the Bank. In addition, under the provisions of collective agreement with Ceylon Bank Employees' Union, the bank has paying PAYE tax liability of the employees like other state own banks following the same practice. Further, this is not a prohibited practice by the Inland Revenue Act.

2. Financial Review

2.1. Financial Result

The operating result of the year under review amounted to a profit of Rs.1,013,448,401 and the corresponding profit in the preceding year amounted to Rs. 1,222,160,409. Therefore, a deterioration amounting to Rs. 208,712,008 or 17.1 percent of the financial result was observed. The main reasons for the deterioration are decrease of interest income and higher impairment charges.

2.2. Trend Analysis of major Income and Expenditure items

Analysis of major income and expenditure items of the year under review compared with the preceding year is as follows.

Description	Variance Increase/ (Decrease) (Rs.Million)	Variance Percentage	Reason for the Variance
Interest Income on loans and advances	(2,605)	(11.9)	Decrease of interest rates
Interest expense on customer deposits	(1,544)	(12.4)	Decrease of interest rates
Impairment charges	(397.8)	(16.5)	Impairment provision was recognized net of the funds available in the Special Reserve Fund created to provide for Bad & Doubtful Debts.

2.3. Ratio Analysis

According to the information made available, some of the important ratios of the bank for the year under review and the preceding year together with the sector ratios is as follows.

	Sector Ratios (Licensed Specialized Banks) Percentage	2020 Percentage	2019 Percentage
Profitability Ratios			
Net Profit Ratio (PAT)	8.44	1.66	1.81
Net Interest Margin	3.84	5.39	6.85
Net Interest Income on Interest Income	32.94	46.97	47.25
Non-Interest Income to Total Income	3.70	4.81	4.18
Interest Cost to Interest Income	67.06	53.03	52.75
Staff Cost to Operating Expenses	55.01	77.54	74.55
Return on Average Assets (PAT)	0.90	0.19	0.26
Return on Equity	16.70	2.67	3.33
Earnings Per Share		0.74	0.91
Asset Quality			
Non Performing Advance Ratio	6.88	10.11	9.63
Capital Adequacy Ratios	**Minimum Requirement**		
Common Equity Tier I Capital Ratio	7	9.998	10.90
Total Tier I Capital Ratio	8.5	9.998	10.90
Total Capital Ratio	12.5	14.440	16.27
Liquidity Ratios			
Statutory Liquidity Assets Ratio	20	29.3	32.38

3. Operational Review

3.1. Management Inefficiencies

Audit Issue	Management Comment	Recommendation
I. Appointment of General Manager		
(i) As per the letter No. MF1/BOD/PSB dated 26.10.2020 issued by secretary to the Ministry of Finance, Director of Treasury Operations Department had been appointed as acting General Manager of the bank and informed	Applications for the post of General Manager were called internally and externally on 15 November 2020 and due to non-availability of a proper/suitable candidate for the above post it was decided	Select a suitable person for the post of General Manager without any further delay.

	the chairman regarding the recruitment of permanent employee in accordance with the PSB Act with a copy of above letter. Further, the Board has the responsibility to appoint the General Manager as per the section 26.1 of PSB Act. However, suitable employee had not been recruited for the post of General Manager though 10 months lapsed with the above acting appointment.	by the Board of Directors to head-hunt a suitable candidate to fill the General Manager position of PSB. However, since that attempt was also failed actions were taken to call for application by publishing an advertisement for the post of General Manager/CEO on 12 September and accordingly, the recruitment process is in progress at present.	
(ii)	Director or CEO shall not be appointed as a Director or a CEO of another Licensed Bank operating in Sri Lanka prior to expiry of 6 months cooling off period from the date of cessation of his/her office at a Licensed Bank as per the CBSL Direction No.09 of 2019 dated 19.12.2019. However, the above Acting General Manager had been appointed contrary to this.	The appointment of Actg. General Manager/CEO of PSB was done by the Ministry of Finance due to unexpected vacancy arose in the position. The appointed Actg. General Manager/CEO was meant to be a temporary appointment and therefore, Fit and Propriety for the above temporary position had not been submitted to CBSL. Having considered the scope of responsibility of the bank and the prevailing situation several initiatives were taken to fill up the post of General Manager/ CEO immediately though delays and postponements were occurred time to time due to Covid-19 pandemic situation.	Take every step to adhere with the applicable directions.
(iii)	As per the Banking Act Determination No.01 of 2019 dated 19.12.2019 issued by CBSL, CEO and such other officers performing executive functions of licensed banks shall be fit and proper persons. However, Acting General Manager's fitness & propriety had not been submitted to CBSL as at the audited date. Further, above Acting General Manager's appointment is contradictory with the Section 26 of the PSB Act No.41 of 2008.		
(iv)	As per the Section 12.5.4 of Chapter VII of Establishment Code, 25 per cent of basic salary of acting post should be paid to an officer performing duties of both	As per the Management Services Department letter dated 25 March 2015 the authority to determining the applicable allowances is	Take every step to adhere with the applicable rules and regulations.

permanent post and acting post. Contradictory to the above, 1/3 of the basic salary and 50 per cent of the entertainment allowances of the post of General Manager had been paid by the Bank as per the decision of the BHRRC paper No.BHRRC/2020/M-06/P10 dated 25.11.2020.	vested with Board of Directors. As such payment of acting allowances to the Actg. General Manager position has been determined by the BHRRC and approved by the Board of PSB.	
II. The inquiry against the Employee No.1906 had been conducted over 6 years. Following observations are made.		Take necessary actions to use bank funds effectively and efficiently.
III.		
(i) Cost of Rs.357,580 (approximately) had been incurred for the inquiries of the above employee. Out of the total 43 callings, 19 was postponed due to the absenteeism of the officers and deferment.	The disciplinary officer was unable to prevent unnecessary delays and postponements in the mentioned inquiry due to the circumstances beyond his control.	
(ii) The bank had spent Rs. 2,203,940 (approximately) with related to the writ application presented by above employee. However, it was dismissed by the Court of Appeal ordering to pay the expenses made by the bank and only Rs.40,000 had been recovered based on the scale of fees to be paid to counsel and registered attorneys in Court of Appeal. Further, the board had decided to withdraw the ongoing inquiry based on the request made by the employee and special board approval received from Wayamba Sanwardana Bank for private practice as a Chartered Accountant excluding normal office hours. Therefore, the cost incurred haven't any value addition in this regard.	Although an estimate of Rs. 2,203,940 (approximately) had been provided in relation to the writ application in Court of Appeal regarding the appeal made by related employee an actual payment of only Rs. 40,000 has been incurred for counsel and registered Attorney in Court of Appeal.	

3.2. Transactions of Contentious Nature

Audit Issue	Management Comment	Recommendation
I. Staff motor vehicle loan of Rs.4,750,000 and staff housing loan of Rs. 1,536,858.79 had been disbursed by the bank on 23.04.2020 and 18.02.2020 respectively to a Key Management Personnel responsible for granting loans at 5 percent rate of interest. Following observations are made.		
(i) As per the Section 8 of Office Instructions Circular (Development Loan) No.2010/40 dated 27.12.2010, loan should be repaid by equal monthly installments. However, as per the loan agreement dated 23.04.2020, motor vehicle loan should be repaid through 39 installments each amounting to Rs.76,498.43 and one installment of Rs.2,430,507.77 at the end. However, the monthly installment should be Rs.129,167 (approximately) as per the aforesaid circular.	Related conditions regarding the setoff of loan outstanding balance up to 50 percent of the gratuity fund had been mentioned in the Chapter II of the Circular No.2013-84.	Chapter II of the Circular No.2013-84 had been cancelled by the Chapter VI of the Circular No.2013-84 dated 29.11.2017. Therefore, take necessary actions against responsible parties and recover loan instalments as per the applicable circulars. Further, actions should be taken to strengthen the internal control of the bank.
(ii) As per the Section 4 Chapter II of Office Instructions Circular (Development Loan) No.2013-84 dated 06.04.2015, the special condition of outstanding loan and related interest should be recovered at the retirement of the employee. However, the above condition was not mentioned in the motor vehicle loan agreement and the special condition of changing interest from 5 to 20 percent was only mentioned.	Above officer had informed that he had not involved for the preparation of the loan or approval and not check the conditions of the loan. Therefore, he does not have any responsibility regarding the loan file.	
(iii) A staff housing loan amounting to Rs. 1,536,858.79 had been	The purpose of obtaining a housing loan is to living in that	

granted on 18.02.2020 for the purchase of a new property at a rate of 5 percent referring to the Section 5 of Chapter II Circular No.2013/84 and Section 2-II of Chapter IV Circular No.2011/51. However, those refers granting of loan for residence changed due to merger of provincial banks and residencies become inappropriate due to floods, earthquakes. Prior to the merger of provincial banks three housing loans amounting to Rs. 1000,000 and after the merger another housing loan of Rs. 500,000 had been obtained by the above employee. As per the circulars of the bank, an additional loan can be assessed for completing the remaining work of the firstly built house only.	house and not any other purpose. He is living in the house purchased using the loan obtained. He can’t live close to the office if the additional loan obtained for repairs of the firstly built house. This is humanity matter and circulars provide only guidelines.	
(iv) Further, the registered mortgage bond of the above property was not available.	Related mortgage bond is included in the loan file maintained in the branch and he is not able to check the above.	However, related registered mortgage bond had not been provided.
II. A payment of Rs.3,720,000 being the salary arrears and reinstatement in the service with effect from 15.08.2019 had been ordered by the Labor Tribunal on 09.08.2019 for case filed by an employee against the bank. Petition of appeal against the order of the Labor Tribunal had been made by the bank on 12.09.2019 and deposited Rs. 5,115,000 as a Bond. Following observations are made.		
(i) Legal department is of the view that above order could be challenged in appeal and accordingly, Board of Directors had granted approval to appeal against the order of Labor	The observation of the Legal department was based on the LT Order. A thorough study of all the documents submitted as evidence and the proceedings of the LT case which	The merger of RDB and LDB had been taken place with effect from 01.04.2019 and therefore, legal division has the access

Tribunal and to handover the appeal of the case to a Senior Counsel based on the recommendation of the Legal Consultant. However, later Chief Legal Officer and Legal Consultant mentioned that since the bank cannot adduce new evidence the chances of success are either marginal or probability of success in favor of the applicant may be more. Therefore, it is questionable of providing separate opinions by the legal division from time to time.	commenced in the year 2017 were in the custody of the counsel of the LDB and as such, the RDB Legal Officers were not able to study the documents and the proceedings that were in the brief due to time constrains. The appeal petition has to be filed before 16-09-2019 and the Board approval was to be obtained before that date.	for all documents. Therefore, issuing of different opinions from time to time may mislead the Board. Further investigation regarding the legal background and taking actions against responsible parties needed in this regard.
(ii) The letter submitted by Legal Consultant to the Senior Counsel, mentioned that the above employee had met the new chairman and the Chairman discussed with the Legal Department very confidentially with regard to any possibility of settlement of this case and Chairman informed Legal Consultant to submit a letter. As a reply to the above-mentioned letter, reaching a settlement had been mentioned by the Senior Counsel.	The letter of the Legal Consultant to Senior counsel had been sent on 27.01.2020 (erroneously dated as 27.01.2019) after the appeal had been filed. The counsel, after studying these cases and also the proceedings of the LT, had concluded in this letter of 25.02.2020 that the bank had failed to adduce evidence to prove the charges, especially the failure to lead the evidence of the most important witness, the Internal Auditor of the LDB and the evidence of the Acting GM/CEO of the LDB.	
(iii) A complaint had been made to the Bribery Commission regarding the transaction related to the aforesaid case at wennappuwa branch under the no.BC/685/2016 and advised by the board to obtain a clearance certificate from the Bribery Commission to avoid unnecessary issues. However, evidence of such clearance obtained were not made available.	A complaint had been made by the LDB to the Bribery Commission in the year 2016. Most of the officers who are complainant as well as the accused are not available in the RDB now. The complaint involves a number of employees at the Wennappuwa Branch. Action against those employees who are now in the RDB can be taken only if the Bribery Commission acts on	Board instructed to obtain the clearance from the bribery commission prior to any settlement with the related employee. Therefore, further investigation and taking actions against the responsible parties is needed.

	the complaint and only if any indictments are served on such employees. The Bank cannot ignore the LT order of the LT President. Any noncompliance or any deviation of the order without the consent of related employee would amount to a contempt of Court.	

3.3. Human Resources Management

Audit Issue	Management Comment	Recommendation
I. Salary revisions of other state banks had been considered when deciding the salary revision of the bank. However, the salary revisions of those banks cannot be applied directly with RDB since the asset base, profit levels, number of employees and number of branches are not similar. (i) It was observed that though the bank had incurred Rs.2.25 million per employee per year, the profit generated per employee was only Rs.0.15 million for the year 2020. However, other government banks had reported profit per employee amounting to Rs.1.12 million to Rs.2.1 million. (ii) Personnel expenses as a percentage of net operating income of the bank was 61 per cent for the year 2020 representing highest value and other government banks reported personnel expenses as a percentage of net operating income ranging from 28.56 per cent to 34.72 percent.	The collective agreement for 2018-2020 between the PSB Management and the Trade Union was based on the request made by Trade Union and was as in line with the other state banks. This Collective agreement which the salary revision was embedded was approved by the Board of PSB and the Ministry of Finance by taking in to consideration the possible cost increment.	Take necessary actions to effectively use the bank funds while increasing the efficiency of employees.
II. Succession plan had not been reviewed and updated properly and as a result, senior managerial posts	Succession Plan has been done but Compliance Department advised to do certain changes	Take necessary actions to prepare updated succession plan

are remained vacant.	which are being done.	considering the competencies of employees.

4. Accountability and Good Governance

4.1. Corporate Plan

Audit Issue	**Management Comment**	**Recommendation**
Board approved Corporate Plan for the period 2016-2020 was in place. However, bank is in the process of preparing new Corporate Plan for the year 2021 as at the audited date on July 2021.	Corporate Plan for the year 2021 has been prepared.	However, Board Approved Corporate Plan is not available. Therefore, take necessary actions to prepare Board approved Corporate Plan without any further delay.