

Sri Lanka Handicrafts Board - 2022

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Sri Lanka Handicrafts Board (“Board”) for the year ended 31 December 2022 comprising the statement of financial position as at 31 December 2022 and the statement of financial performance, statement of changes in net assets 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, and Finance Act No. 38 of 1971. 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 Board as at 31 December 2022, 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 Board’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 Board or to cease operations, or has no realistic alternative but to do so.

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

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

1.4 Auditor's Responsibilities for the Audit of the Financial Statements

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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 Board'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 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 Board and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Board has complied with applicable written law, or other general or special directions issued by the governing body of the Board,
- Whether it has performed according to its powers, functions and duties; and
- Whether the resources had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Audit Observations on the preparation of Financial Statements

1.5.1 Non-compliance with Sri Lanka Accounting Standards

Non-compliance with Reference to Relevant Standard	Comments of the Management	Recommendation
(a) Current liabilities should be recognized only for liabilities expected to be settled within the normal operating cycle within 12 months after the period in which the liability is reported in terms of Section 69 of Sri Lanka Accounting Standard No.1. Nevertheless, out of the total trade creditor balance of Rs.255,675,927, a sum of Rs.150,440,727 is inactive outstanding creditor balance for more than 5 years. Similarly, since a debit balance of Rs. 3,821,690 had been included in the creditor balance in the name of Sri Lanka Handicrafts Board the creditor balance was shown in less than that value.	Most of these balances are suppliers who have given gems and jewellery. The suppliers have provided the goods on a cash on sale basis. (Consignment Model) Accordingly, it is confirmed that the goods have not been sold within a period of 5 years. Therefore, it is informed that these balances are not to be settled and cannot be written off.	Actions Should be taken in terms of Sri Lanka Accounting Standards.

<p>(b) Since the actual value is not represented in stock of second quality valued at Rs. 154,646,764 in the stock balance of the Board including stock shortages, stock to be repaired and non-moving stock in terms of Section 28 of Sri Lanka Accounting Standard No. 02, they had not been shown and accounted for in net realizable value.</p>	<p>It has been informed that the net realizable value of stocks will be revaluated and accounted for in the future accounting years.</p>	<p>Actions Should be taken in terms of Sri Lanka Accounting Standards.</p>
<p>(c) Although all losses relating to stock should be recognized and accounted for as expenses in the period in which the loss occurs in terms of Section No. 34 of Sri Lanka Accounting Standard No. 02, it had not been so accounted for regarding the shortage of stock totalled to Rs. 3,425,875 included in first quality stock as at 31 December 2022 .</p>	<p>This is an addition of stock shortages identified for each year over a number of years and as it requires an approval of Board of Directors to be written off as an expense, it has been shown as follows until that approval is given.</p>	<p>Actions Should be taken in terms of Sri Lanka Accounting Standards.</p>
<p>(d) Actions had not been taken to reevaluate the land owned by the Board with a total value of Rs.380,788,639, computer equipment valued at Rs.19,279,453 and software valued at Rs.10,193,250 and to account for the current market value in terms of Sri Lanka Accounting Standard No 16.</p>	<p>Since the organization does not have the capacity to perform this type of a work, due to current financial difficulties, it has been informed that this work will be done after the financial situation improves.</p>	<p>Actions Should be taken in terms of Sri Lanka Accounting Standards.</p>

1.5.2 Accounting Deficiencies

Audit Observation	Comments of the Management	Recommendation
<p>(a) As the renovation works of the Fort Laksala building had been suspended, a sum of</p>	<p>This expenditure has been incurred to demolish certain parts of the building. Since the</p>	<p>Actions should be taken to complete the renovations and</p>

- Rs.45,451,390 incurred for that works of the building has accurately account had been shown in the financial statements as work in progress from the year 2014 to the year under review. under review. constructing, it has been put under work- in - progress.
- (b) Actions had not been taken to obtain the legal ownership of the properties handed over by the Department of Small Scale Industries in the year 1993 in Nuwara Eliya and Thummulla, where the Board conducts businesses to enter in the financial statements. During the restructuring of the Small Industries Department according to an approval of Cabinet of Ministers in the year 1993, Nuwara Eliya, Katubedda and Tummulla properties have also been handed over in transferring the assets of the Department including employees and buildings to the Sri Lanka Handicrafts Board. Actions should be taken to receive the legal ownership and to enter in the financial statements.
- (c) Even though a bank overdraft which is not actually existing of Rs.986,112 remaining from the year 2015 had been included under current liabilities in the financial statements, actions had not been taken to settle even in the year under review. The bank balance is Rs.99,973 as per the bank balance confirmation letter and the balance related to the above current account was an overdraft of Rs.(986,112) according to the cash book. Accordingly, the amount has been shown as Rs. 986,112 in the financial statements under bank overdraft. Further, since the overdraft value has occurred due to a wrongly accounted amount in 2015, actions will be taken to correct it as well. Actions should be taken to settle if there is a nominal value.
- (d) Even though agreed royalty charge of Rs.9,090,000 had been accounted for as other income in contracting for overseas sales in the year 2022, no overseas sales whatsoever during the year under review had occurred. Since the franchise sales agents contracted in the year 2022 have not commenced businesses, a situation where it is impossible to pay these royalty charges has occurred and actions will be taken to send these values to the Board Only the actual income receive should be accounted for.

of Directors to remove them from the accounts.

- (e) Actions had not been taken to disclose or to account for a shortage of stock with a sales value Rs.2,915,960 belonging to Thummulla Showroom revealed as per Physical Board of Survey Reports and about a stock shortage valued at Rs.876,452 belonging to the Battaramulla showroom at the weighted average cost. It has been informed that the actions will be taken by carrying out a Board of Survey by the Board of Survey Division and by a Board of Survey in the year 2023 to properly assess these deficiencies and make relevant changes in the 2023 accounts. Actions should be taken to disclose the shortage of stock in financial statements or to account for.
- (f) Although no damage whatsoever was reported for the year under review as per physical stock verification records at Thummulla showroom, a stock damage of Rs.1,712,412 had been accounted for as at 31 December 2022, according to the financial statements. . Arrangements are being made to account for stock damage in the relevant year with the approval of the Board of Directors and the Board of Survey Division has been authorized to credit the stock damages to the stock damages account of the respective showroom. Further, the stock shall be removed from the stock remained for sale in the showroom. Nevertheless, total stock including damaged stock is accounted for in stock accounts. The accuracy of stock verification should be verified.

1.5.3 Unreconciled Control Accounts or Records

Item	Value as per Financial Statements Rs.	Value as per corresponding Records Rs.	Difference Rs.	Comments of the Management	Recommendation
Property Plant and Equipment	228,677,799	80,955,189	147,722,610	Actions will be taken to account for the accurate balances after revaluation of assets.	Actions should be taken to identify the differences and to account for.

1.5.4 Lack of Documentary Evidence for Audit

	Item	Amount Rs.	Audit Evidences unavailable	Comments of the Management	Recommendation
(a)	Creditor Balance	37,952,164	Schedules or balance confirmations	Since these are old balances, as the institution does not have the documents related to this, it has been informed that the actions will be taken by a letter of Board letter of Board of Directors to write off from the accounts.	Schedules or balance confirmations should be submitted.
(b)	Trade Debtor Balance	23,562,897	Balance confirmation letters	Receiving balance confirmation letters is a very difficult task. Because trade debtors do not have knowledge of their receivables. Arrangements will be made to obtain balance confirmation letters.	Actions should be taken to get balance confirmation letters
(c)	Accrued Expenses	6,546,541	Payable party	Due to lack of supporting documents, arrangements will be made for disposal in the year 2023 for	Actions should be taken to identify the payable party specifically.

approval of Board
of Directors.

- (d) Stock in Transit 11,014,318 Sufficient information was not submitted to confirm the stock in transit. Making corrections in the balance of this account is a very difficult task and actions will be taken as much as possible to correct it in the coming years. The balance of the stock in Transit account should be annually checked and settled

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

	Reference to Laws, Rules/ Regulations etc.	Non-compliance	Comments of the Management	Recommendation
(a)	Financial Regulations of the Democratic Socialist Republic of Sri Lanka			
(i)	Financial Regulation 371(5)	Although, after issuing an sub-impres, the said impres should be settled again within 10 days of completion of the relevant task, the advances of Rs.2,274,351 given in 58 cases in the year 2022 had been settled with a delay of 20 days to 285 days.	It has been informed to the officers who have been given sub impres to take actions by taking special care about this in terms of Financial Regulations because of the delay is due to day-to-day operational issues of the organization.	Actions should be taken in terms of Financial Regulations.
(ii)	Financial Regulation 371 (2) (b)	Although only staff officers can be given an ad hoc sub - impres up to a maximum of Rs.100,000 at a time for any particular work,	It is an amount of Rs. 500,000/- received under the signature of the Chairman for the purchase of special	Actions should be taken in terms of Financial Regulations.

contrary to that, a sub imprest of Rs.2,360,379 exceeding Rs.100,000 had been issued on 10 occasions.

goods. Further, this special purchase was made because they had to buy the necessary items at the showrooms by giving money due to suppliers not providing Laksha goods on credit.

(b) Establishments Code of Democratic Socialist Republic of Sri Lanka

Sections 21 and 23 of Chapter XLVIII of Volume II of the Establishments Code

Even though two female officers were suspended as per the Decision of the Meeting of Board of Directors held on 19 November 2015, the disciplinary authority of the Board had not issued any disciplinary orders even by the date of audit on 20 May 2023 .

The accused officers have not submitted their answers to the charge sheets submitted by the Board to the suspended officers before a specific period of time and disciplinary investigations have been initiated and conducted accordingly.

Actions should be taken in terms of Chapter XLVIII of the Establishments Code.

(c) Paragraph 6.6 of the Operational Manual for Public Enterprises introduced by Public Enterprises Circular No. 01/2021 dated 16.11.2021

Although the Draft Annual Reports and Financial Statements should be submitted to the Auditor General within 60 days of the end of the accounting year, the financial statements of the year 2022 had been submitted on 18 July 2023, with a delay of 5 months.

It has been delayed for the submission of financial statements to the Auditor General due to the unexpected interruption of SAP ERP system which does accounting and sales of the Board, in December 2022.

Financial statements should be submitted by the due date.

(ii) Although the Annual Report along with the Audit Report should be tabled in Parliament within 05 months after the end of the financial year, the Annual Reports for the years 2020 and 2021 had not been tabled even by 20 August 2023. It has been sent to the Line Ministry to obtain the approval of the Board of Directors and the approval of the Cabinet of Ministers for the Draft Annual Reports of the years 2020 and 2021 . Annual reports should be tabled in Parliament on due date.

2. Financial Review

2.1 Financial Results

The operating result of the year under review was a loss of Rs. 99,040,670 and, the corresponding deficit loss of the preceding year was Rs. 58,546,847. Accordingly, a deterioration of Rs. 40,493,823 was observed in the financial result. Although an increase of Rs.146,127,213 was shown in the income of the Board as compared to the preceding year, increase of administrative expenses, sales and distribution expenses and financial expenses by Rs.68,268,047 as compared to that had mainly attributed for this deterioration.

2.2 Ratio Analysis

The current ratio, which was at 1.14 in the preceding year, had dropped to 1.02 in the year under review. Accordingly, as the amount of current assets owned by the Board is only enough to cover the current liabilities, it was observed that the liquidity of the Board is at a very low level. Similarly, the further decrease of current ratio as compared to the preceding year and representing of 87 per cent of the current assets by stocks and payments in advance had attributed for this.

3. Operating Review

3.1 Uneconomic Transactions

Audit Observation	Comments of the Management	Recommendation
Even though a non-refundable deposit of Rs.5,888,000 was paid to the Urban Development Authority on 30 November 2012 at the time of entering into 10-year contract for the Racecourse Showroom, this sales showroom had been closed on 26 December 2018. Therefore, it was	The Board will conduct a proper feasibility study on acquiring building space on the basis of monthly lease rent payment in the future and a further study of the terms and conditions of the agreement	Proper attention should be made on the terms of the contract.

observed during the audit that, this was an uneconomic transaction.

will be made and decisions will be taken.

3.2 Management Inefficiencies

Audit Observation	Comments of the Management	Recommendation
(a) Any legal action had not been taken to recover the amount of Rs.1,182,386 receivable from 8 buyers for the credit sales made by the Katubedda Project which had been closed by the Board in the year 2018 .	Arrangements will be made to consider the buyers to be charged through the Katubedda Project in the year 2023 and get those charges to the Board.	Actions should be taken to collect receivables without delay.
(b) Even though the land on which the Galle Sales Showroom is located and the two-storied building had been handed over to the Board by Gazette No. 670 dated 05 July 1991, actions had not been taken even by the date of audit to receive the legal ownership.	It has been informed that the actions will be taken to receive the legal ownership.	Actions should be taken to take legal ownership.
(c) A sum of Rs.9,589,919 to be charged in the period from 2018 to 2020 was still outstanding as at 31 December 2022 as Rs.456,770 from Thummulla Barista Restaurant, Rs.4,243,949 from Barista Coffee Lanka Institute, Rs.20,000 from Tharumila Flower Association and Rs.4,869,200 from 8 Super Band business locations and actions had not been taken to recover the arrears.	Arrangements have been made by now to collect the amount receivable from Barista Restaurant and it was agreed in the management meeting not to collect the amount receivable from Tharumila Flower Association. Accordingly, steps will be taken to remove this value from the accounts. Further, arrangements will be made to write off the receivables from Super Brands from the accounts considering the Corona epidemic period.	Actions should be taken to collect the receivables immediately.
(d) The Board had mortgaged the Fort Laksala building and obtained a	It was also difficult to settle the bank loans due to the	Management of bank loans should be

loan of Rs.849,481,500 from the Bank of Ceylon on 12 occasions during the period from 2011 to 2017. Due to non-payment of loan installments and interest, the interest accrued from time to time had been also capitalized and the bank had registered as 14 new loans and, the total value of 8 such loans amounted to Rs.332,607,065 had to be paid furthermore as at 31 December of the year under review.

collapse of tourism in the view of the Easter attack in 2019 and the complete suspension of tourist arrivals due to the Covid epidemic in 2020/2021. Hence the loan was restructure.

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| (e) | A loan amount of Rs.200 million had been given to the Board in the year 2013 through the refinancing loan facility provided to the Regional Development Bank under the Saubhagya Loan Scheme implemented by the Central Bank of Sri Lanka. Due to non-payment of loan interest as per stipulated, the accumulated balance of Rs.12,909,761 had also been capitalized as a new loan amount. Accordingly, the outstanding loan balance as at 31 December 2022 was Rs.171,009,585 and the accrued interest for the years 2021 and 2022 was Rs.33,721,736. Although the bank had proposed a new loan repayment plan by letter No. RDB/HO/RE/122/4 dated 14 October 2022, the Board had not agreed for that due to failure of payment of loans and interest continuously. | Due to the 2019 Easter attack and the 2020/2021 Covid outbreak, as the sales revenue had faced a collapse, the Board was unable to pay the loan installments. Accordingly, although a plan has been given to pay in 10 years with interest accrued in the years 2020/2021, since the Board was not satisfied with that interest which is Rs.33 million because of the economic collapse of the entire country, arrangements will be made to make discussions with the bank in the future to reduce the interest on this amount fairly. | Actions should be taken to settle the debt balances. |
| (f) | Gems and jewellery with a sales value of Rs.340,069,730 included in the stock have discoloured for a long time according to stock verification reports, actions had | Arrangements have been made to return the discoloured jewellery to the suppliers. | Arrangements should be made to adopt a more effective method on stock. |

not been taken to sell them by offering special discounts or by using appropriate marketing strategies.

3.3 Transactions in Contentious Nature

Audit Observation	Comments of the Management	Recommendation
(a) Although the trade debtor balance as at 31 December 2022 was Rs.23,562,897, thus the total of the debtor balances of more than Rs.50,000 to be collected from various government agencies in that balance was Rs.10,560,711, the goods had been sold again to the same debtors without following a formal system to recover the balances.	These balances are very old debtor balances and actions will be taken to check files related to this and to recover .	Actions should be taken to collect receivables from debtors promptly.
(b) A sum of Rs.2,010,000 had been deposited in the current account without being deposited the securities collected from officers in a savings account in the name of respective officers and it had been indicated that an interest of Rs. 1,261,533 had to be paid to the said officers at the rate of 6 per cent per annum.	According to the approval of the Board of Directors, arrangements will be made to transfer the deposits obtained for the securities in the year 2023 into a fixed deposit or to open individual savings accounts for the relevant employees.	Actions should be taken to start saving accounts immediately.

3.4 Underutilization of Funds

Audit Observation	Comments of the Management	Recommendation
Actions had not been taken even in the year under review to get settled the project retention of Rs.12,502,564 over the several years and the balance of Rs.3,838,357 included in the refundable deposit balance and the advance balance of Rs.16,026,936 given for the purchase	Instructions have been given to be settled with special attention in the year 2023.	Actions should be taken to settle the old balances.

of trade items and non-trade items and administrative activities.

3.5 Idle or Underutilized Property, Plant and Equipment

Audit Observation	Comments of the Management	Recommendation
<p>(a) The land and buildings of 01 acres 30.6 perches that belonged to Galle Unawatuna Salusala Institution had been handed over to the Board by Cabinet Decision No. 12/1523/553/020 dated 11 October 2012. Accordingly, although the Board had paid Rs. 15,248,575 on 12 December 2012, considering it as purchase, it had failed to obtain legal ownership and usable rights of the property in the year under review also. Further, actions had not been taken to obtain the legal ownership of the properties situated in Katubedda as well.</p>	<p>Although written requests have been made from Lanka Salusala Limited to transfer the ownership of this property to the Sri Lanka Handicrafts Board through a regular deed, Lanka Salusala Limited has not done the transferring activities.</p> <p>It has been mentioned that currently, there is a case in the court regarding the relevant property.</p> <p>However, further actions are being taken to get the above property to the Industrial Development Board on payment of money to the Sri Lanka Handicrafts Board on the recommendations of the said Ministry for a Southern Province tourism promotion project expected to be implemented under the Ministry of Industry.</p>	<p>Arrangements should be made to take over the legal ownership and right of use of property or to recover the amount paid.</p>
<p>(b) The sales showroom was sealed by the National Museum Department on 01 January 2023 due to the failure of agreeing of the two parties to the terms of the contract related to the renovated museum building from 2013 to 2015 at the cost of Rs.175,118,237 on the approval of the Cabinet. Nevertheless, even though 06</p>	<p>Discussions are currently being made with the Honourable Ministers and Secretaries of the Ministry of Industry and State Ministries of Small and Medium-sized Enterprise Development in respect of the necessary arrangements to re-open the Museum Laksala Showroom</p>	<p>Actions should be taken to re-possess the showroom or to take over the stock.</p>

months had elapsed since the date of seal on 10 June 2023, the Board had failed to recover the showroom and the value of stock totalled to Rs.99,777,436 had remained in idle in the showroom.

as soon as possible or to recover the money spent by the Board for its modernization and development works.

- (c) Since only a very small space of 1200 square feet is used in the fort sales showroom building, it was also observed that the building premises of about 40830 square feet has been idle for a long time.
- Actions are being taken by now for the renovation and conservation of this building under the supervision of the Department of Archaeology and to repair and modernization work will be done at the expense of the investor in order to generate additional income and the building will be put to use and reservation of 2,000 square feet of space for a showroom, settlement of the bank loan obtained by Laksala Institute by mortgaging the building and Inviting “proposals with business ambitions” from “Sri Lankan Investors and Institutions” willing and able to make sufficient investment to settle other liabilities related to this building and selecting a suitable party.
- Actions should be taken to make the most use of the idle building.