

The audit of the operating activities of the Lanka Sathosa Ltd for the year ended 31 December 2018 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.

1. Financial Statements

1.1 Responsibilities of the Management and Those Charged with Governance for the Financial Statements

As per Section 16(1) of the National Audit Act, No. 19 of 2018, every auditee entity shall maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared in respect of such entity. In terms of Section 16(2) of the said Act, annual financial statements in respect of every other auditee entity shall be submitted by the Chief Accounting Officer to the Auditor General along with the annual performance reports, within such period as may be provided by rules. As per Section 38(1)(d) of the said Act, timely preparation and submission of annual and other financial statements shall be ensured and in addition, the Chief Accounting Officer shall be required to submit annual reports to Parliament pertaining to the auditee entity.

1.2 Non-submission of Financial Statements for Audit

In accordance with Section 6.5.1 of the Public Enterprises Circular No. PED / 12 dated 02 June 2003 and Section 150 of the Companies Act No. 07 of 2007, the annual financial statements of the companies should be submitted to the Auditor General within 60 days of the end of the financial year, although the financial statements for the year 2018 had not been submitted for audit up to in this report.

2. Report on Other Legal and Regulatory Requirements

The National Audit Act No. 19 of 2018 and the Companies Act No. 7 of 2007 contain special provisions relating to the following requirements.

In terms of Section 150 (1) of the Companies Act No. 07 of 2007, the Board of Directors of the Company shall ensure that the person responsible for preparing the financial statements within six months from the date of the balance sheet.

2.1 Continuity of the Organization

| Audit Observation | Comments of the Management | Recommendation |
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| As a result of losses incurred relating to the stocks including the damages caused to imported rice stocks, the equity had become a minor value of Rs.10,929,943,402 since year 2014 and the unfavorable position of the equity and the existence of current liabilities exceeding current assets had resulted in an uncertainty regarding the going concern of the Company without providing Treasury funds. | The management did not comment. | Attention should be paid to the points outlined in the audit observations and necessary measures should be taken to avoid them. |

2.2 Non-Compliance with Laws, Rules, Regulations and Management Decisions

| Reference to Non-Compliance Laws, Rules, Regulations etc. | Comments of the Management | Recommendation |
|--|---|---|
| Sections 3.1 and 3.2 of the Public Enterprises Circular No. PED 1/2015 dated 25 May 2015 | Contrary to the circular, the vehicle assigned to the Chairman of the Company exceeds the approved limit for the year 2018 and 2019, respectively Rs. 88,589 and Rs. 81,760 had been spent on fuel and the approval of the Secretary of the Ministry with the recommendation of the Board of Directors had not been obtained. | The management did not comment. Action should be taken as per the provisions of the circular. |

2.3 Financial Management

| Audit Observation | Comments of the Management | Recommendation |
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| The bank reconciliations were not made in respect of the 10 bank accounts of the Company during the year under review. | The management did not comment. | Action should be taken to prepare the bank reconciliation statements monthly. |

2.4 Management of Vehicle Fleet

| Audit Observation | Comments of the Management | Recommendation |
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| (a) Attached to the Line Ministry in 2017, two vehicles belonging to the Company, which cost Rs. 5,400,000 and Rs.13,300,000 had been brought to the Company premises in an unhygienic condition without a proper delivery and the vehicle, valued at Rs. 5,400,000 was in bad condition and idle. | The management did not comment. | The vehicle must be repaired or disposed in such a way that it is effective for the Company. |
| (b) Three vehicles owned by the Company and the two vehicles used by the Chairman were purchased under the operating leasing method did not maintain daily running charts and monthly summaries. | The running charts had not been maintained regarding in this vehicles | Action should be taken to maintain running charts and monthly summaries regarding vehicles |

2.5 Operating Inefficiencies

| Audit Observation | Comments of the Management | Recommendation |
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| <p>(a) The Treasury had allocated Rs. 500 million during the year under review for its capital activities such as opening new outlets, installing time machines, upgrading existing outlets, operating a security camera system and opening chartered outlets and Rs. 438.7 million had been utilized. Out of these, Rs. 15 million to Rs. 12.3 million and 100 percent progress had been made regarding installing time machines and a sum of Rs. 80 million allocated for the security camera system, out of this sum of Rs. 48 million had been spent and made a 71 percent improvement. Nevertheless, a sum of Rs. 150 million allocated and in addition Rs. 126.1 million had been spent, for opening new outlets, only 26 percent was achieved, but capital expenditure on upgrading the existing outlets and opening franchised outlets amounted to Rs. 118 million and Rs. 27 million had been allocated respectively, but had not been commenced.</p> | <p>The management did not comment.</p> | <p>Provisions made by the Treasury should be utilized to maximum effect.</p> |
| <p>(b) In relation to the stock management process of the Company which was vested in a private sector company from 2016 to 2019, although it has been discontinued since June 2019, the audit date was 2</p> | <p>The management did not comment.</p> | <p>Action should be taken to recover stock related losses from the relevant parties.</p> |

October 2019 at Rs. 42,764,243 worth of groceries were in the warehouse. The stock was classified as deliverable, expires in a short term and returned from outlets and had a value of Rs. 4,369,485, Rs. 18,744,895 and Rs.19,649,861 respectively. This situation had arisen due to the lack of proper supervision of the Company.

2.6 Resources Released to Other Organizations

| Audit Observation | Comments of the Management | Recommendation |
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| <p>Contrary to Section 8.3.9 of the Public Enterprises Circular No. PED / 12 dated 2 June 2003, a vehicle owned by the Company is attached to the Line Ministry and amounting of Rs. 346,704 was paid in the year under review, but it was not reimbursed.</p> | <p>The management did not comment.</p> | <p>Action should be taken as per the circular.</p> |

2.7 Transactions of Contentious Nature

| Audit Observation | Comments of the Management | Recommendation |
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| <p>In addition to the fees paid to a company that provides security services on behalf of the Company, the fees and allowances paid to a consultant assigned to the Company by the Lanka Sathosa have been reimbursed to the company without proper approval and the officer was allowed to use the vehicles of the Company. Accordingly, the reimbursement amounting to</p> | <p>The management did not comment.</p> | <p>In addition to the services rendered in accordance with the agreement, must obtain approval from the Board of Directors for fees paid.</p> |

Rs.65,000 per month from June 2018 to September 2019 was Rs.1,040,000.

2.8 Human Resource Management

| Audit Observation | Comments of the Management | Recommendation |
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| (a) The approved cadre of the Company was 4,246, but the existing staff for the year under review was 3,859 with a shortage of 990 and a surplus of 603. Although with the growth of the outlets, there has been a corresponding recruitment to the approved positions, it was observed that the staff excesses and shortages was mainly due to delay in promotions related to the posts in the shops staff reductions and shortages. | The management did not comment. | Recruitment should be done according to the approved staff. |
| (b) Although the Scheme of Recruitment of the Company which was prepared in 2017 had not been approved by the Department of Management Services, the recruitment had been done according to that Scheme of Recruitment | The management did not comment. | The scheme of recruitment should be approved. |
| (c) Recruitment and promotions had been carried out without the authentication of the bogus educational and professional certificates submitted by six management level officials including the Chief Executive Officer. Although it was revealed that the officers had been suspended and | The management did not comment. | Necessary action should be taken with regard to the parties concerned. |

investigations have commenced as of the date of this report, no action has been taken to conclude the investigation and take appropriate action. The Company had paid the total amount of Rs 23,143,170 as salaries and allowances of the that officers during the period.

2.9 Delays in Capital Works

| Audit Observation | Comments of the Management | Recommendation |
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| <p>Enterprises Resource Planning Project</p> <p>(i) The project, which was awarded at a cost of Rs. 198,175,784, had to be completed within 15 months, but the deadline had been extended without formal approval.</p> <p>(ii) The information technology division of the Company had carried out the work due to the failure of certain parts of the project and Although 29 months had elapsed since the commencement of the project, 30% of the contract money had been paid to the contractor when the project had not been completed.</p> <p>(iii) The contractor shall be liable for any loss or damage equaling to 1 percent from the contract value incurred by the contract or any part thereof or any other</p> | <p>The management did not comment.</p> <p>The management did not comment.</p> <p>The management did not comment.</p> | <p>Work should be completed soon.</p> <p>Once the work of the project is completed as per the agreement, the relevant amount should be paid.</p> <p>Action should be taken as per the agreement.</p> |

party without the written consent of the purchaser. However, due to the transfer of certain parts of the project to another institute, the contract was delay, but the loss of 1 percent of the contract value of Rs. 19,817,578 had not been recovered from the contractor.

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| (iv) | Although it is stated that if the contract is delayed for delivery it should be deducted 1 percent from the contract amount, but the late charges was not fixed. As a result of the delay of 574 days beyond the due date of the contract, only 1 percent of the amount of the contract had been deducted and the payments have been made as mentioned in (ii) above. | The management did not comment. | Demurrages should be charged according to the number of late days |
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2.10 Procurement Management

| Audit observation | Comments of the Management | Recommendation |
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| (a) The company had purchased 12,800 plastic crates amounting to Rs. 24,382,509, at two prices on three occasions from the same supplier without calling national bids, according to the 3.2 of Procurement Manual. | The management did not comment. | Action should be taken as per the provisions of Procurement Guidelines |
| (b) The Procurement and Technical Evaluation Committees were not appointed in accordance with the Procurement Guidelines 2.8.4 relating to this procurement | The management did not comment. | Action should be taken as per the provisions of Procurement Guidelines |

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| <p>(c) A physical inspection on 02 January 2019, revealed that out of the 12,800 crates purchased in 2017, and by the end of 2019, 1975 of those crates remained idle. When assessed at a minimum price of Rs. 1,904.48 for a crate that was purchased at two prices, the value of the crate which was underutilized was Rs. 3,761,348.</p> | <p>The management did not comment.</p> | <p>Purchasing should be done with due diligence and to meet the requirements</p> |
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3. Accountability and good governance

3.1 Corporate Plan

| Audit Observation | Comments of the Management | Recommendation |
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| <p>Although a Corporate Plan had been prepared for the year under review, the approval of the Board of Directors and the Secretary of the Ministry had not been obtained in terms of Section 5 of the Public Finance Circular No. 1/2014 dated 17 February 2014.</p> | <p>The management did not comment.</p> | <p>Action should be taken as per the provisions of the circular.</p> |

3.2 Annual Action Plan

| Audit Observation | Comments of the Management | Recommendation |
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| <p>In terms of section 2 of paragraph 5 of the above circular, an action plan had not been prepared incorporating the commercial activities expected to be implemented in the next financial year.</p> | <p>The management did not comment.</p> | <p>Action should be taken as per the provisions of the circular.</p> |

3.3 Audit Committee

| Audit observation | Comments of the Management | Recommendation |
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In terms of Section 7.4.1 of the Public Enterprises Circular No. PED / 12 of 2 June 2003, the Audit and Management Committee must meet at least once in three months, but the Audit Committee met twice in the year under review.

The management did not comment.

Action should be taken as per the provisions of the circular.