

Lanka Hospitals Corporation PLC - 2020

1. Financial Statements

1.1 Opinion

The audit of the financial statements of The Lanka Hospitals Corporation PLC (“Company”) and the consolidated financial statements of the company and its subsidiaries (“Group”) for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the income statement, statement of profit and loss and other comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with provisions of the National Audit Act No. 19 of 2018. My comments and observations which I consider should be report to Parliament appear in this report.

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

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 Key Audit Matters

Key audit matters are those matters that, in my professional judgement, were of most significance in my audit of the Company Financial Statements and the Consolidated Financial Statements of the current year. These matters were addressed in the context of my audit of the Company Financial Statements and the Consolidated Financial Statements as a whole, and in forming our opinion thereon, and I do not provide a separate opinion on these matters.

- **Revenue recognition** – Refer to Note 4.15 – accounting policy and Note 5 to the Financial Statements. The Revenue of the Group for the year ended 31st December 2020 was Rs.6,804 Million.

Risk Description

The Group’s revenue generated from its healthcare services is disclosed in Note 5 together with the related accounting policy in 4.15. I considered revenue as a focus area due to the complexity of the pricing structure, its high volume, and determination of

Our Response

My audit procedures included the following, among others;

- I carried out audit procedures over revenue measurement by testing on a sample basis, transactional level pricing and applicable

appropriateness of gross or net basis of revenue recognition in certain arrangements, and reliance on IT controls.

- I discussed with management regarding the contractual arrangements where consultant medical personnel are involved, and tested on a sample basis the appropriateness of the recognition of revenue on a gross or net basis.
- I obtained an understanding about the key IT and manual controls over the occurrence of revenue and tested the same on a sample basis.
- I performed specific audit procedures over cash collection related to revenue covering a sample of locations where the Group's business is carried out.
- I assessed the adequacy of the disclosures made in Note 5 in the financial statement.

- **Carrying value of inventories** – Refer to Note 4.8– accounting policy and Note 16 to the Financial Statements. The Group carried inventories of Rs.439 Million as at December 31, 2020, at the lower of cost or net realizable value.

Risk Description

Valuation of inventory involves judgment and estimates due to the nature of products and stringent quality requirements. Due to allocation and sale of inventories within Group operations based on the business model, both existence and valuation of inventories are key areas of focus.

Our Response

- My audit procedures included; assessing adequacy and consistency of provisioning for inventories at the reporting date with the Group's inventory provision policy.
- On a sample basis, comparing the carrying amounts of the Group's inventories with net realisation value of those inventories.
 - Testing the existence of inventories through physical verification as at year end and validating the cost allocation within Group entities.

- **Recoverability of Trade Receivables** – Refer to Note 4.9.1 – accounting policy and Note 17 to the Financial Statements. The Group’s trade receivables as at 31 December 2020 were Rs.444 Million.

Risk Description

Assessment of recoverability of the Group’s trade receivables involves based on management judgment. The historical payment patterns and other information relating to the creditworthiness of customers. Inherent subjectivity is involved in making judgments in relation to credit risk exposures to determine the recoverability of trade receivables.

Our Response

My audit procedures included –

- Testing the Group’s credit control procedures, including the controls around credit terms, and reviewing the payment history and financial information pertaining to the customers.
- Testing the receipt of cash after the year end relating to 31 December 2020 balances; and
- Testing the adequacy of the Group’s impairment provisions against trade receivables by assessing the judgments made and the historical trading experience with the relevant customers.
- Assessing the adequacy of the Group’s disclosures about the degree of estimation involved in arriving at the impairment provision.

1.4 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 Group’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Group 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 Group 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 Group.

1.5 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 skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company and the Group'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 Group'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 Group 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.

1.6 Audit Observations on the preparation of Financial Statements

1.6.1 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.

Audit Issue	Management Comment	Recommendation
(a) Although the entries in the cash book should be consecutively numbered and these numbers affixed to the corresponding vouchers, that had not been done.	Due to inherent limitation in “Tally” accounting system which is used by the Company, payment voucher numbers are not constant. Therefore, the company refers cheque number and the date as a serial for all references.	The entries in the cash book should be consecutively numbered and these numbers affixed to the corresponding vouchers.
(b) Fixed Asset Register of the company had not been updated and facilities had not been provided to adjust periodically adjusted revaluation gain or loss in this register.	The first fixed assets registry prepared with assisting of KPMG in 2012. In this assignment all the assets were identified and tagged with assign asset codes. But we have been able to assign up to 82% value of the assets purchased after 31st December 2007. Due to the unavailability of the documents it was unable to assign value for the sum of the assets and these assets were represents zero value in the fixed assets register. At that time it was decided and agreed to continue fixed assets register there onwards.	Fixed Asset Register need to be updated and upgraded.

1.6.2 Accounting Deficiencies

Audit Issue	Management Comment	Recommendation
As at 31 December 2020, the deferred tax liability was under provided by sum of Rs.3,220,000.	This under provision has been updated in the books of accounts in March 2021.	Necessary actions should be taken to make necessary adjustments in 2021 Financial Statements.

1.6.3 Unreconciled Control Accounts or Records

Item	As per Financial Statements	As per corresponding Record	Difference	Management Comment	Recommendation
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	Rs. million	Rs. million	Rs. million		
Amount Due to Sri Lanka Insurance Corporation Limited	4.76	8.59	3.83	Differences was carried forward from the time that both entities under private ownership. In 2012 we have gone through the SLIC information and they were unable to provide documentary evidence to prove that above mentioned balance directly related to Lanka hospitals.	Action should be taken to clear the difference.

1.7 Accounts Receivable and Payable

1.7.1 Receivables

Audit Issue	Management Comment	Recommendation
A total amount of Debit Notes raised amounting to Rs.1,097,817 had been brought forward over long period without being cleared.	We will consider clearing up above provision during this year.	Action should be taken to clear the balances.

1.7.2 Payables

Audit Issue	Management Comment	Recommendation
(a) Trade and Other payables amounting to Rs.952 million including a sum of Rs.31.7 Million representing over 5 years, the company had not taken any action in this regard.	We have analyzed and identified which can be write back to the financial statement from above listed payables. This write back will be done soon after obtaining necessary management approval.	Necessary actions should be taken to clear the balance.

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| (b) | Although the value of cheques issued as at 31st December 2020 but not submitted within six months is Rs.113,031,563, no action had been taken to re-validate or recognize as an income after reasonable period of time. | As per control mechanism cheques not realized within six months transferred to stale cheque accounts further we have analyzed and identified which can be write back to the financial statement from above balances. This write back will be done soon after obtaining necessary management approval ones its exceed more than 5 years. | Necessary actions should be taken to clear the balance. |
| (c) | A sum of amount due to Related Party (Sri Lanka Insurance Corporation Ltd) amounting Rs.4,769,076 had been brought forward over a long period without taking actions to settle this balance or recognize as an income. | We will do necessary actions to write back with required approval. | Necessary actions should be taken to clear the balance. |

1.7.3 Advances

Audit Issue

The ledger account balance of provision for refundable deposit amounting to Rs.1,414,401 had been brought forward more than five years without being taking actions to clear this balance and no documentary evidence pertaining to this amount.

Management Comment

We will do necessary actions to write back this provision.

Recommendation

Action should be taken to clear the balances.

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

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
Public Enterprise Department circular PED 1/2015	Fuel allowances had been granted to the Chief Executive Officer and Chief Operating Officer / Chief Financial Officer exceeding the limits by 50L and 35L respectively.	The Lanka Hospitals Corporation PLC is a public listed company and fuel allowance is part of remuneration of the employees. Fuel limits have been defined as per the organization practice which has been therefrom the known history. The company fuel entitlement has been decided at the time of recruitment as a part of remuneration package. The total remuneration is negotiated with the candidates including the fuel which should par with the amounts of similar categories and those offered by other public listed companies.	Action should be taken to get approval for the practice of the company from the Public Enterprise Department.

2 Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs.443,578,902 and the corresponding profit in the preceding year amounted to Rs.420,196,802 Therefore an improvement amounting to Rs.23,382,100 of the financial result was observed.

2.2 Ratio Analysis

Ratio	2020	2019
Current Assets Ratio	3.87 times	3.77 times
Quick Assets Ratio	3.50 times	3.41 times
Gross Profit Ratio	42%	44%
Return on Capital Employed	3%	9%
Gearing Ratio	N/A	N/A

2.3 Key Performance Indicators

The Company Key Performance Indicators and its achievement are as follows.

	Actual	Budget	Budget
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Average length of Stay (Days- Total beds)	2.21	2.24	(0.03)
Average Occupancy Rate	61%	67%	(6%)
Average daily admissions	61	70	9
Total Admissions	22,192	26,320	(4,128)
Foreign patient admissions	625	1,120	(495)
OP Consultations	264,164	290,500	(26,336)
No of Surgeries	9,631	10,151	(520)

3. Operational Review

3.1 Operational Inefficiencies

Audit Issue

In year 2017 the Company started a Medical Center by investing Rs.42,127,193 in Seychelles. The Seychelles Medical Center has reported net loss of Rs.11,193,820 and Rs.2,473,850 in year 2019 & 2018 respectively. The board decided to discontinue the operations on 12 May 2020 as the medical center continuously reporting losses. Further, total loss of investment had not been assessed by the management.

Management Comment

The main objective of opening Seychelles medical center is to get referral patients from Seychelles. After the Easter bomb attack it was adversely affected the getting referral patients from Seychelles and it has contributed to the loss from Seychelles medical center operations. Currently COVID-19 situation also affected the operations in Seychelles adversely. Especially we were unable to continue the essential supplies to the center in Seychelles. Considering the adverse trends and safety of our staff, we discontinued the operation from 31st July 2020.

Recommendation

Proper evaluation should be done before made an investment.

3.2 Transactions of Contentious Nature

Audit Issue

The company had paid separately for the services obtained from 21 consultants hired for some

Management Comment

Sri Lanka is a country having consultant driven market rather than hospital driven market. Majority of Sri Lankan patients

Recommendation

Proper evaluation should be made to check whether the payment is economical.

specialized areas, but in addition paid them Rs.110,381,165 during the year under review for retention of those consultants.

are consulting their preferred consultants by their names not by the hospitals names. This industry nature will also apply to Lanka hospital as well. To be in the industry leader Lanka hospital need to have a partnership with key highly reputed consultants. Patients coming to the hospital around the clock and some patients require specialized medical assistance in urgent basis not like in other business the delaying medical assistance may cost of human life therefore hospital require to have a partnership with industry leading consultants in different specialties. It is not possible to having these leading consultants in hospital staff carder because they are not willing to join as a full time employee. If hospital wants to recruit them as a full time employee it will cost even much more to the organization.

3.3 Procurement Management

Audit Issue

Management Comment

Recommendation

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| (a) | As per the paragraph 2.4 of government procurement guideline, primary responsibility of procurement is bearing by the head of the company and he may delegate the authority to their subordinators. However, no evidence pertaining to appointment of procurement committee by delegating authority to the respective procurement. | Board of Directors (BOD) who is the prime authority of Lanka Hospitals has approved authority limits for procurement and financial approvals (MOFA – Memorandum of Financial Authorities) based on the requirement. As per MOFA, BOD has delegated authority limits for PC and Company officials as required. | Need to take actions to comply with government procurement guideline. |
| (b) | As per the paragraph 2.12 in government procurement guidelines, all members of Procurement Committee are required to sign a declaration in the prescribed format at its first meeting. We observed that there is no any | LHC prime authority; BOD has appointed and approved PC and Approval matrix based on the value and nature of the product. Also BOD has instructed to initiate own procurement manual for LHC instead of NPA guideline. Accordingly each approval body has declared one time to the BOD. | -do- |

- declaration given by the members of PC in any procurement file.
- (c) As per the paragraph 2.12 in government procurement guidelines, all members of TEC's are required to sign a declaration in the prescribed format at its first meeting. We observed that there is no any declaration given by the members of TEC in any procurement file.
- (d) Some members of the bid opening committee were not present at the committee meeting and representatives were present on their behalf. However, written evidence pertaining to the appointment of such agents had not submitted for audit.
- (e) (i) The company's procurement committee had estimated the cost of an air sample at Rs.60,000. However, the bids received at Rs.695,000 and Rs.1,452,995 respectively were evaluated without considering that they were unusually higher than the estimated cost.
- (ii) Further the Company had awarded the contract to bidder with the highest price and had rejected the lowest
- Since the TEC has been consists by the LHC internal employees including Executive members, they already declared to the LHC for each and every action in the sense of fair, un-bias and transparent.
- According to the approval received from the BOD, initial Bid opening committee consist of Two EXCO (Executive Committee) member, Manager Procurement and independent member. But, they are nominated a person time to time due to their tied working schedule. However their representatives attending for bid opening committees on behalf of them due to unavoidable circumstances with related to tied schedule but responsibility will be taken by the appointed members.
- LHC has called direct quotations by e-mail for this requirement giving 3 days grace period to quote and also to get more price competitiveness, quotations were called from all the LHC registered supplier base. Even though two bidders quoted their prices within the given time period and due to the urgency of the requirement, received quotations were accepted and tender has been closed. However hospital main goal is to obtain and fulfill the most suitable and cost effective solution/requirements when comparing the market situation.
- Since this is a medical related requirement, professionals of the medical field especially the medical doctors needs to recommend the product and it should be most suitable for the
- Need to take actions to comply with government procurement guideline.
- Need to take actions to make appointments of representatives in proper way and keep documentary evidences.
- Need to take actions to attract more suppliers.
- Need to keep documentary evidence.

- quoted bidder by stating reason as bad experience with another machine supplied by the respective supplier previously. But no written evidence of that bad experience was presented for audit.
- (iii) Although it is the company's policy to charge a penalty of 1% of the value of the order for delay, the delay charges could not be charged for a delay of about 4 weeks.
- (f) At the time of calling to quotation for purchase of spare parts for 40 Kg Washing Machine, requested to provide the details of availability, registration (If applicable), earliest delivery date, warrantee/guarantee, catalogue, after sales services, other terms & conditions. However two bidders were submitted and they submitted only Performa invoice. But entity continues procurement without calling above information.
- (g) As per the invitation for quotation for procurement for Urodynamic System the quotation calling email state that 'If the bidder act as an agent, sub-agent, representative or nominee for
- users and must be user friendly as those are medically critical items in the hospital. Accordingly medical doctor panel has given their recommendation to procure the highest price product based on their own past experience.
- As per the general format there is a penalty clause as a control tool. But, normally we are charger penalties from procurement which are under contract agreements. According to the nature of the business, LH placing large numbers of POs/Work Orders quarterly and it is not possible to follow up each and every delay of each PO/Work order.
- Regular tender invitation was sent to prospective bidders requesting to provide mentioned details in order to cover all the aspects. Bidders may provide the details which are applicable for the particular requirement and received bids contained such details which are applicable for the Washing Machine spare parts. Received quotations contained specific cat/article No to identification purpose and also mentioned delivery date and other terms and conditions which were adequate to select a bid. At the time of evaluation of bids, end-user/subject specialist has been accepted the bid based on the given details which are adequate to proceed the order to get down the spare parts to fulfill the requirement to maintain uninterrupted operation of the hospital.
- The above particular procurement is under Shopping method and once we open the bids we do not know whether the bidder is registered with the register of companies for contract. Nevertheless, we unable to interrupt the process due to unavailability of such document as item
- Need to take actions to comply with Company Policy of delivery if not change the Company Policy of Delivery.
- Regular tender invitation should be customized by nature of the procurement.
- Regular Documents should be customized by nature of procurement.

and on behalf of any tenderer has to be supplied at earliest to fulfill the requirement. a copy of PCA 3 certificate issued by the registrar of public contracts should be submitted along with the quotation and should get contract registered after the each bid is awarded if the bid value is exceeding 5mn Rupees. Value of this contract is Rs.6,323,940, however the selected bidder had not furnished PCA 3 form for this contract.

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| (h) | <p>In the Procurement to Purchase of HD-Laparoscopy System, 6 bidders bid for this procurement. Among them highest price quoted bidder was selected to award the contract and others rejected by stating that the surgeons are unhappy with image quality. However, considering the specification details provided by the bidder regarding camera system and monitor system, all the bidders' specifications are in line with the company requirement. As well as there is no any documents to prove the surgeons recommendation.</p> | <p>Two doctors who are main user for this particular laparoscopy systems and they have stated their signatory in the TEC report as well.</p> | <p>Keep Documentary evidence for Doctors' recommendations.</p> |
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3.4 Human Resources Management

Audit Issue

The actual cadre exceeded the approved cadre by 12 numbers for 09 positions.

Management Comment

The excesses had been adjusted and no excesses in year 2021.

Recommendation

Approved carder should be reviewed periodically and should make necessary amendments.