Sri Lanka Insurance Corporation Ltd - 2020

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Sri Lanka Insurance Corporation Limited (the "Company") and the consolidated financial statements of the company and its subsidiaries (the "Group") for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the statement of profit or loss and other 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 report to Parliament in pursuance of provisions in Article 154 (6) of the Constitution will be tabled in due course. To carry out this audit I was assisted by a firm of Chartered Accountants in public practice.

In my opinion, except for the effects of the matters described in the basis for Qualified Opinion section of my report, 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 its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Qualified Opinion

My opinion is qualified on the matters described in paragraph 1.5 of this report.

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

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

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Company.

1.4 Audit Scope

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.

- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company*;*

- Whether the Company has performed according to its powers, functions and duties; and

- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Audit Observations on the preparation of Financial Statements

1.5.1 Accounting Deficiencies

Audit Issue	Management Comment	Recommendation
According to the judgment delivered by Supreme Court of Sri Lanka on 04 June 2009, the Secretary to the Treasury was directed to cause profits of the Company during the period of private ownership, be computed and the profits attributable to the previous parent be settled. No adjustments have been made in the Financial Statements pending determination of the aforesaid attributable profits.	The Supreme Court directed Secretary to the Treasury to compute and pay the profits attributable to the previous parent be settled. Hence the Company does not have any direct involvement to compute the profit.	It is recommended to adhere to the Supreme Court Decision.
Contrary to the article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka and the National Audit Act No.19 of 2018 Litro Gas Lanka Limited (LGLL) and Litro Gas Terminal Lanka (Pvt) Limited (LGTLL) appointed a private auditor as their auditor at the Annual General Meeting held on 07 December 2020. The financial statements of the Group include the financial position, performance and cash flows of LGLL and LGTLL. The total assets of these companies as at 31 December 2020 amounted to Rs.43,277,102,671, and the total profit for the year ended 31 December 2020 amounted to Rs.1,103,301,494. Because of the matters stated above, I am unable to confirm the transactions, balances, cash flows and events of LGLL and LGTLL, which are incorporated in the consolidated financial statements of the Group.	Board of Directors of SLIC has instructed LGLL and LGTLL to follow the correct procedure when appointing their Auditors.	It is recommended to follow the Articles 154(1) of the constitution of the Democratic Socialist Republic of Sri Lanka and the National Audit Act No.19 of 2018 and the relevant guidelines governing the Group in making crucial decisions and take appropriate steps to monitor the compliance activities of the Group.

1.5.2 Documentary Evidences not made available for Audit

Item	Amount Rs.	Evidence not available	Management Comment	Recommendation
Amounts receivables from Distilleries Company of Sri Lanka PLC	168,763,399	Confirmation of balances	This balance includes receivable balance from Distilleries Group of Companies. This amount will be adjusted upon the finalization of the payment as per the court decision given on 04 June 2009.	It is recommended to take necessary action to recover the balances.

1.6 Accounts Receivable and Payable

1.6.1 Receivables

	Audit Issue	Management Comment	Recommendation
(a)	According to the reinsurance aging as at 31 December 2020, balances of Rs.28,176,762 are overdue for more than two years.	Due to the closely follow up and monitoring process, more than 90% of the total dues had been recovered within two years. Our strategy is to set off these claims against due premiums. We have reduced the outstanding amount of Rs 28 mn to Rs. 26.8 Mn as at July 2021 and another Rs.16.5 Mn will be settled within one-month period. Target is to clear all dues over three years with in the year 2021.	The company should take appropriate steps to recover the long outstanding reinsurance receivables.
(b)	Long-outstanding other receivable balances of Rs.236,818,088 from 15 debtor accounts have been noted as at 31 December 2021.	This balance includes receivable balance from Distilleries Group of Companies. This amount will be adjusted upon the finalization of the payment as per the court decision given on 04 June 2009.	It is recommended to take necessary action to recover the above balances.

1.6.2 Payables

Audit Issue	Management Comment	Recommendation
According to the reinsurance payable aging as at 31 December 2020, the overdue reinsurance payable is Rs.49,310,165 and it was outstanding for more than two years. However, the company has not taken appropriate actions on these balances.	Our strategy is to set off any premium payable against claim receivable. If the parties are not responding or no longer doing business, it will transfer from payable to write back. This Rs 49 mn has reduced to Rs 13.3 mn as at 30th June 2021.	The company should take appropriate steps to reconcile reinsurance receivable and payable and settle payable on a timely basis to avoid discontinuation of service.

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

	Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a.)	Section 53 of Regulation of Insurance Industry (Amendment) Act No. 03 of 2011	As discussed in Note 48 to the financial statements, the company has not segregated the long-term insurance business and the general insurance business being carried on by it into two separate companies	As per the section 53 of Regulation of Insurance Industry (Amendment) Act, No. 3 of 2011 on the Segregation of Insurance Business, IRCSL has granted us an extension by their letter dated 15th June 2020, in order to meet the requirement for the segregation of business up to 31st December 2020 upon our request. Further we as a responsible organization have done the following internal developments to entrust the operational efficiency even though the said segregation has been legitimately extended.	It is recommended to follow the IRCSL regulations and requirements.
(b.)	Section 31(1) of the Regulation of Insurance Industry Act, No. 43 of 2000	Insurers shall place reinsurance only with a reinsurance company which has Minimum credit and financial strength ratings. However, It was observed that the company has placed facultative reinsurance arrangements with the reinsurer the rating of the reinsurer is not in line with the rating requirements stated in the terms and conditions for reinsurance placements.	Due to the global pandemic, it is becoming increasingly difficult to find reinsurance for risks with very large values from reinsurers with a higher rating as many reinsurers have either stopped writing business from certain regions or are having very strict guidelines for acceptance. For that reason, we were compelled to place a very small share of 3% with this reinsurer. At the next renewal we will do our best to replace this reinsurer with another reinsurer**.**	It is recommended to follow the IRCSL guidelines on selecting the reinsurer.

1.8 Cash Management

	Audit Issue	Management Comment	Recommendation
(a)	There were differences of Rs.1,230,257 had been observed between General Ledger (GL) balances and the 09 Bank Reconciliation Reports.	The above differences were due to the entries passed after the BRS preparation and those have been corrected in following month BRS, during January 2021. Further, we will make sure to avoid this kind of issues from 2021 onwards.	Bank reconciliation is an important part of the internal control system and recommend that the person reviewing these reconciliations should ensure that unreconciled items are cleared on a timely basis.
(b)	42 non-operating bank accounts had been identified for the year under review.	During 2020 company has implemented a pilot project to cluster some bank accounts to reduce the unnecessary increasing of Bank Accounts reconciliations and Bank charges. Accordingly, theses bank accounts are non-operating at present and not closed until to evaluation of success of the project. Further, we will be able to utilize them for newly opened branches.	The management must review those non-operating accounts and if thought fit, must take necessary steps to close those non-operating bank accounts.

1.9 IT General Controls

	Audit Issue	Management Comment	Recommendation
(a)	Periodical reviews for user access rights were not carried out for the systems during the period under concerned to ensure that the access rights are based on their job roles and insufficient or excessive access rights are not granted to employees.	User access review had been started during 2020. This activity was completed during 1st Quarter 2021 with necessary sign offs from HODs.	It is recommended to review user profile/ access rights periodically on all available systems to ensure that none of the users are having excessive privileges and any inactive user accounts are disabled without delay.
(b)	It was observed that the company had not performed periodic reviews of the super user activities in the SAP ERP, Life, General, HRIS and Claims One system.	Currently super user activities are logged as standalone logs in related system. There is no efficient way to centrally manage these logs for monitoring purpose. As a solution to this issue ICT is planning to purchase a SIEM system which is capable of monitoring all user activities including Super user activities in the applications.	Recommend implementing a feature to generate audit trail reports in the systems to track user activities and periodic reviews of super user activities should be performed.

(c)	Vulnerability assessments and penetration tests on the entire network have not been carried out by an independent third party.	ICT department do periodic vulnerability assessment internally using a Vulnerability assessment tool and we have provided sample assessment reports to the auditors. Apart from that we are already in the process to perform Vulnerability assessment by an independent third party in 2021.	It is recommended to perform periodic vulnerability assessments and penetration tests on the entire network by an independent third party.
(d)	It was identified that audit logs cannot be generated from front end for the applications of Core insurance system and HRIS.	This will be addressed by SIEM implementation. All the log data can be viewed from SIEM system once implemented.	The management should consider implement a feature to generate the audit trail and monitoring key activities for applications.
(e)	The Company does not maintain a system for reinsurance data bases in General Insurance. Instead the company maintains its bordereaux database and facultative register in the manual excel versions.	This requirement had already been identified and added to the required features of the proposed new core system for general insurance side.	An accounting system for re-insurance be implemented.

2. Financial Review

2.1 Financial Result

Company

The operating result of the year under review amounted to a profit of Rs. 5,788.5 million and the corresponding profit in the preceding year amounted to Rs.7,028.9 million. Therefore a deterioration amounting to Rs. 1,240.4 million of the financial result was observed. The reasons for the deterioration are reduction of investment income and increase of change in contract liabilities – life fund and increase of tax expense.

Group

The operating result of the year under review amounted to a profit of Rs. 6,930.3 million and the corresponding profit in the preceding year amounted to Rs.4,513.8 million. Therefore an improvement amounting to Rs. 2,416.5 million of the financial result was observed. The reasons for the improvement are increase of investment income, reduction of net benefits and claims and reduction of other operating and administrative expenses.

2.2 Trend Analysis of major Income and Expenditure items

Line Item	2020	2019	Variance	Increase/ (Decrease)
	Rs. Million	Rs. Million	Rs. Million	%
Company				
Gross Written Premium	39,421.3	33,794.3	5,627.0	17%
Net Earned Premium	34,206.5	29,772.0	4,434.5	15%
Investment income	16,511.3	17,671.5	(1,160.2)	(7%)
Other income	1,469.0	1,132.1	336.9	30%
Total Income	52,614.5	48,608.6	4,005.9	8%
Net benefits and claims	(15,772.3)	(16,623.7)	(851.4)	(5%)
Underwriting and net acquisition costs (including reinsurance)	(2,996.8)	(2,986.2)	10.6	0.4%
Change in contract liabilities - life fund	(16,118.7)	(11,659.8)	4,458.9	38%
Other operating and administrative expenses	(9,754.9)	(9,133.8)	621.1	7%
Income tax expense	(2,183.2)	(1,176.0)	1,007.2	86%
Net Profit for the year	5,788.5	7,028.9	(1,240.4)	(18%)
				Group
Revenue from other group operations	46,505.7	50,685.2	(4,179.5)	(8%)
Investment income	17,754.9	16,954.6	800.3	5%
Other income	1,540.8	1,835.5	(294.7)	(16%)
Total Income	99,849.8	98,779.2	1,070.6	1%
Other operating and administrative expenses	(15,417.4)	(20,154.1)	(4,736.7)	(24%)
Cost of services of subsidiaries	(40,053.7)	(38,992.5)	1,061.2	3%
Income tax expense	(2,560.5)	(3,849.0)	(1,288.5)	(33%)
Net Profit for the year	6,930.3	4,513.8	2,416.5	54%

2.3 Ratio Analysis

Company Specific Ratios	2020	2019	2018
Retention Ratio	87%	88%	88%
Claim Ratio - Long Term	42%	51%	60%
Claim Ratio - Non Life	51%	61%	66%
Total Claim ratio	46%	56%	63%
Expense Ratio	84%	80%	70%
Combined ratio	131%	136%	133%
Profitability Ratio	15%	17%	16%
ROA	3%	4%	4%
ROE	13%	13%	12%
Investment Yield	8%	9%	7%
Liquidity Ratio	1.08	1.11	1.11
Financial Assets to Total Assets	0.84	0.82	0.81
Capital to technical reserves ratio	3.71	4.14	2.16

Group Ratios	Group			Company		
	2020	**2019**	**2018**	**2020**	**2019**	**2018**
Profitability and Return						
Revenue Growth	**0.33%**	8.63%	18.61%	**15%**	6%	8%
Return on Equity	**7%**	5%	9%	**9%**	11%	9%
Asset Turnover	**0.86**	0.88	0.84	**0.54**	0.48	0.46
Net Profit Ratio	**8.6%**	**5.6%**	**10.3%**	**11.0%**	**14.5%**	**11.8%**
Liquidity						
Current Ratio	**0.28**	0.24	0.22	**0.18**	0.10	0.10
Investor Return						
Earnings Per Share	**11.56**	7.53	12.67	**9.65**	11.72	8.74
Dividend Per Share	**1.50**	3.25	3.06	**1.50**	3.25	3.06
Dividend Cover	**7.70**	2.32	4.14	**6.43**	3.61	2.86
Net Assets Per Share	**155.43**	151.91	147.19	**105.25**	103.83	101.81

	2020	2019	2018
Technical reserve ratio	2.01	1.98	0.99
Market Share (Total)	19%	17%	17%
Market Share (Long Term)	19%	17%	16%
Market Share (Non-Life)	18%	14%	13%

Industry Comparison	Industry 2020	Industry 2019	Industry 2018	Company 2020	Company 2019	Company 2018
Growth Rate (Total)	**6%**	8%	12%	**8%**	10%	13%
Growth Rate (Long Term)	**16%**	11%	12%	**30%**	12%	6%
Growth Rate (Non-Life)	**-2%**	6%	9%	**6%**	2%	-2%

3. Operational Review

3.1 Operational Inefficiencies

	Audit Issue	Management Comment	Recommendation
(a)	For the Life insurance business the SLIC has dealt with only one reinsurer.	The reinsurer has been our reinsurer for many decades and has been very accommodative for SLIC. Further that reinsurer is very large and stable reinsurer having AA- (Standard & Poor's Ratings Services) rating and presence in all Insurance companies in Sri Lanka. Therefore, the risk at termination is very minimal. The cover granted by reinsurer is until the portfolio is ended.	It is recommended to be highly concerned regarding the above matter.
(b)	The company did not make any timely payments to the reinsurer since the company had not received any acknowledgement from the reinsurer for quarterly statements. Non-payment may result in discontinuation of services and may result in operational and reputation risk.	Following quarterly Payments are outstanding • Individual life and Group Life: 4th quarter 2019 to 4th quarter 2020. • Health Life: 1st quarter 2019 to 4th quarter 2020 The payments are delay due to reinsurer has not provided their confirmation to RI accounts provided by SLIC. We have reminded the situation to reinsurer through E-mails and over the phone. Also we have made every effort to finalize same.	It is recommended to make the necessary decision to get the acknowledgement from the reinsurer to make payments for payable balance to reinsurer.

3.2 Idle or underutilized Property, Plant and Equipment

Audit Issue	Management Comment	Recommendation
The Helanco Hotels and Spas (Pvt) Ltd, a subsidiary of Sri Lanka Insurance Corporation has acquired a land of 3.8 Hectare by investing Rs. 177.97 million from Urban Development Authority on lease basis to construct Hyatt Regency Hambanthota Hotel. However, it has not commenced any operations and the land purchased for this purpose had not been used for any other useful purpose.	The management of the company seeks necessary directions from the line Ministry on way forward of the company.	Prompt actions should be taken to utilize the asset by considering the strategic decisions and thereby obtain positive results as expected.

3.3 Delays in Projects or Capital Work

Audit Issue	Management Comment	Recommendation
The Group had invested Rs. 13.5 billion in Grand Hyatt Franchise Hotel project implemented through Canwill Holdings (Pvt) Ltd and its Subsidiary, Sinolanka Hotels & Spa (Pvt) Ltd. The project had been initially planned to be completed in the year 2014 at project cost of Rs. 20 billion, whereas the constructions of the project was partially ceased from 2018 and fully ceased in 2019. Further, at present the estimated cost to complete project is Rs.60 Billion.	The management of the company seeks necessary directions from the line Ministry on way forward of the company.	Prompt actions should be taken to execute and complete the project by considering the strategic decisions and thereby obtain positive results as expected in the cash flow forecast.