

Sri Lanka Savings Bank - 2019

1.1 Opinion

The audit of the financial statements of the Sri Lanka Savings Bank Limited (“Bank”) for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 and the income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with provisions of the National Audit Act No. 19 of 2018.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2019, 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 Opinion

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

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

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, and for such internal control as management 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 Bank’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

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

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

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

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an

audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

- Whether the Bank has complied with applicable written law, or other general or special directions issued by the governing body of the Bank ;
- Whether the Bank has performed according to its powers, functions and duties; and
- Whether the resources of the Bank had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Financial Statements

1.5.1 Suspense Accounts

Audit Issue	Management Comment	Recommendation
. There were suspense account balances aggregating to Rs.10,523,919 disclosed under other payables as at 31 December 2019. It was further observed that a negative balance of Rs. 92,577 was included in the suspense accounts loan and a balance of Rs.113,839 in suspense account debtors under the sundry debtors as at the year end.	Agreed This will be Rectified in year 2020. An extensive exercise being carried out for the reconciliation work with the support from Scier System. Almost completed the unreconciled items (As per the Management Committee decision, Special Committee has been appointed to identify unreconciled account balances and report to be submitted.)	Actions should be taken to clear the suspend accounts balances.

1.5.2 Internal Control over the preparation of financial statements.

Audit Issue	Management Comment	Recommendation
a. A net difference of Rs.5,438,669 was observed in lease, hire purchases and other loan balances as at 31 December 2019 between general ledger and application system.	Agreed and will be Rectified in year 2020. An extensive exercise being carried out for the reconciliation work with the support from Scier System. Almost completed the unreconciled items (As per the Management Committee decision, Special Committee has been appointed to identify unreconciled account balances and report to be submitted.)	Take necessary actions to reconcile the balances.

<p>b. Bank's system does not support to update the rescheduled loans by posting entries. Accordingly, received cash from customers for rescheduled loan cannot be set off against their loan balance in the system. Hence the bank had maintained an account called "Termination Over Payment- MF" in the general ledger to include cash received for such loans. The balance of the said account as at 31 December was Rs.3,439,409. In the financial statements, this balance has been recorded under other liability instead of deducting against loans receivable balance</p>	<p>Noted The current termination overpayment A/C balance is Rs.1,811,237.13. Executive Credit Committee (ECC) held on 12.08.2020 has approved to enter the repayment in to system for rectify the issue subject to the system outstanding balance to the manual balance except Small & Medium Industry owners Co-op Society due to branch has been taken the legal action against the PO.</p>	<p>System should be adjusted for the purpose of rectify the said balance.</p>
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1.6 Accounts Receivable and Payable

1.6.1 Receivables

Audit Issue	Management Comment	Recommendation
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<p>(i) Four receivable balances aggregating to Rs.1,275,142 had remained unchanged for more than four years period in the accounts of Post-dated cheque discount, Advance Hire Purchase, Leasing suspense and Sundry debtors.</p>	<p>Agreed and will be rectified in year 2020. An extensive exercise being carried out for the reconciliation work with the support from Scierter System. Almost completed the unreconciled items (As per the Management Committee decision, Special Committee has been appointed to identify.</p>	<p>Bank should take actions to reconcile and clear the said balances.</p>
<p>(ii) An amount aggregating to Rs.1,228,836 remained in the seven control accounts without clearing at the end of the year under review with related to loans and advances.</p>	<p>Agreed and will be Rectified in year 2020. An extensive exercise being carried out for the reconciliation work with the support from Scierter System. Almost completed the unreconciled items (As per the Management Committee decision, Special Committee</p>	<p>Bank should take actions to reconcile and clear the said balances.</p>

has been appointed to identify unreconciled account balances and report to be submitted.)

- (iii) Discount paid at the maturity of money markets bills of PSDB customers has been included in an account called discount paid in advance. Bank's provision for above balance was higher than the stated balance.
- Agreed & to be rectified in year 2020.
- Bank should take actions to reconcile and clear the said balances.

	Rs.

Amount in discount paid in advance	13,534,878
Provision	18,006,622
Over provision	4,471,744

1.6.2 Payables

Audit Issue

Management Comment

Recommendation

Credit balances of Rs.1,975,871 and Rs.1,428,707 were shown in an error correction savings account and error correction control account respectively as at 31 December 2019. Actions had not been taken to reconcile the above balances.

Agreed and will be Rectified in year 2020. An extensive exercise being carried out for the reconciliation work with the support from Scierter System. Almost completed the unreconciled items (As per the Management Committee decision, Special Committee has been appointed to identify unreconciled account balances and report to be submitted.)

Actions should be taken to reconcile the above balances.

1.6.3 Loan and Advances

Audit Issue

Management Comment

Recommendation

- i. The loan outstanding balance of Rs.99,992,620 which is recoverable from six community-based

Loans have been granted to Trincomalee Distric Gandhi Sevai Association, Ai-Quraish Social Development, Sri Rohana Death Relief

Take necessary actions to recover the outstanding loan balances from relevant

organizations had not been recovered since 2015. These borrowers had not provided any security against loan balances. Therefore, the recoverability is doubtful.

& Society and Kilakin Olichuder Social Service Organization by NDTF Company before merge with SLS Bank and according to the company policies no security has been taken while granting loans. However currently legal actions have been taken for these loans by recovery department of SLS Bank.

Further loans have been granted to HOPE Micro Finance Services (Guarantee)Ltd and People Economic Development (PEEDO) by NDTF Company before the merge with SLS Bank according to the NDTF company policies no security has been taken at that time. After the merge HOPE Micro Finance Services (Guarantee) Ltd and People Economic Development (PEEDO) entered into E-Financial system on 09.02.2013 and 04.10.2013 respectively. After merge, Rs.892,541.03 and Rs.8,353,139.03 have been obtained from HOPE and PEEDO respectively according to SLS Bank loan policies. However, legal action has been taken for these two loans also by the recovery department of SLS Bank.

organizations.

ii. Out of total loan outstanding amount of Rs. 53,049,906 granted under the loan scheme of “Rehabilitation of Person, Property, Industries Authority (Reppia)”, a sum of Rs. 48,893,664 or 92 per cent was reported as non performing as at 31 December 2019.

Noted

Take all necessary actions to recover the non-performing loans granted under “Reppia” category.

1.7 Non-compliance with Tax Regulations

Audit Issue

Management Comment

Recommendation

a. Income Tax

As per section 11 of the Inland Revenue Act, No. 24 of 2017 rent paid for the right of use assets has not been adjusted and Rs.1,886,442 had been over claimed.

Agreed and will be corrected in annual return for Y/A 2019/2020.

Bank should comply with the Inland Revenue Act.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs. 447,816,707 and the corresponding profit in the preceding year amounted to Rs. 351,266,136. Therefore, an improvement amounting to Rs. 96,550,571 of the financial result was observed. The reasons for the improvement were the increase of the other operating income and reduction of the other expenses incurred.

2.2 Trend Analysis of major Income and Expenditure items

In an analysis of income and expenditure items for the year under review compared with the preceding year, following major changes were observed.

Description	Variance Increase/(Decrease) (Rs.Mn)	Variance %	Reason for the Variance
Other Operating Income	117,031,750	619%	Reversal of Tax payable penalty provision due to waive off the tax penalty during the year under review.
Personal Expenses	(11,870,635)	7%	Reversing the over provision for salary and bonuses as per the proposed collective agreement.
Other Expenses	(64,942,043)	46%	Decreased of Other expenses by Rs.65 million or 46 per cent due to no provision for tax penalty and not incurred losses on selling fixed assets during the year under review compared with previous year.

Income Tax	49,307,264	36%	During the year under review, Operating profit after tax on financial services had been decreased by 29 percent.
Debt Repayment Levy	45,704,385	342%	DRL has been charged for the full year of 2019 and it was charged only for the final quarter in 2018 due to imposition of DRL has been started since in 4 th Quarter Of 2018.

2.3 Ratio Analysis

According to the information made available, some of the important ratios of the bank for the year under review and the preceding year with sector ratios are given bellow.

Description -----	Bank		Sector Ratio
	2019	2018	2019
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<u>Profitability Ratio</u>			
Return on Average Equity (ROE) (Percentage)	8.68	6.52	6.8
Return on Average Assets (ROA) (Percentage)	7.09	5.22	0.8
Net Interest Margin (Percentage)	11.48	11	3.4
<u>Capital Adequacy</u>	83	90*	12.3
Capital Adequacy- Tier I (Minimum 5%)			
<u>Asset Quality</u>			
Gross Non- Performing Advance (Including PSDB)	41.44	36	5.5
Gross Non- Performing Advance (Excluding PSDB)	14.48	11	3.9
<u>Liquidity Ratios</u>	514	110*	53.1
Liquidity Coverage Ratio (Percentage)			

*Capital Adequacy (Tier II) and Liquidity Ratios were taken from the information submitted by Bank to the Central Bank of Sri Lanka. PSDB refers to Premuka Savings & development Bank.

- i) Return on Equity (ROE) and Return on Assets (ROA) had been increased up to 8.68 per cent and 7.09 per cent respectively as at 31 December 2019 when compared with the preceding year mainly due to increasing of profit in 2019.
- ii) High net interest margin of 11.48 per cent was observed for the year 2019. It was at highest level as compared with the Licensed Specialized Bank ratio of 3.4 per cent.

- iii) Total Capital Adequacy Ratio of the Bank reported as 83 per cent as at the 31 December 2019 which is much higher than the minimum statutory requirement of 12.5 per cent.
- iv) The gross non performing advance ratio excluding PSDB at the end of year 2019 was 14.48 percent which was higher than sector ratio of 3.9 percent. Increase of non-performing loans of RAPPIA loan (rehabilitation of persons, properties and industries authority – 90%) and individual & corporate loan (25%) had affected to above increase. Further the gross non - performing advance ratio including PSDB as at end of year 2019 was 41.44%.
- v) Bank’s Liquidity ratio was at the higher level of (514%) as compared with sector ratio of 53%.

3. Operational Review

3.1 Management Inefficiencies

Audit Issue	Management Comment	Recommendation
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i. Performance of the Bank		
<p>-----</p> <p>The bank’s main objective as per the article of association is to identify, develop, promote, catalyze and support sustainable income generating opportunities and a higher quality of life for the poor through a range of activities including productive self-employment micro enterprises and rural work by the provision of financial assistance and services. However, without considering above main objectives, bank had invested nearly 72 percent of its total investment in fixed deposits, financial instruments, equity instruments etc at the end of year under review.</p>	<p>Bank operations have been done only 04 branches and approval has not been granted to open new branches, staff recruitment and capital expenditure etc. Hence, continue banking operations through 04 branches and surplus invest in short term and long-term instruments.</p>	<p>Ensure that more focus is given on the main objective of the Bank.</p>
ii. Initial objectives of the bank at the time of incorporation		
<p>-----</p> <p>According to section 1.3 of the memorandum of cabinet paper No. PED/NDTF dated 24 May 2010, the bank was established in 2006 to provide relief to the depositors of the failed Pramuka Savings and Development Bank (PSDB). Accordingly, the</p>	<p>Bank had followed 10 year deposit repayment plan which was approved by Monetary Board of Central Bank Of Sri Lanka. Bank has no any</p>	<p>Bank should take actions to settlement of the PSDB deposits.</p>

PSDB liability outstanding as at 31 December 2019 and 2018 were 651,396,194 and 656,486,357 respectively. These balances should be paid by the Bank as per the scheme introduced and published by the Central bank of Sri Lanka in December 2009. Settlement of PSDB Liability During the year 2019 and 2018 was Rs.9,155,700 or 1.4 per cent and Rs.541,174,926 or 47 per cent respectively.

outstanding customer requests and paid their demand in full.

iii. Recovery of non-performing PSDB loans

The PSDB non- performing loan outstanding amount as at 31 December 2018 was Rs.1,020,102,438. Bank has recovered only Rs 6,665,501 or 0.65 Percent during the year under review. Accordingly, the loan balance to be recovered by the bank as at 31 December 2019 was Rs. 1,013,436,937.

Noted and however the total PSDB recoveries from 2008 to 2019 is Rs. 1,129.97 Mn

Bank should take actions to recover PSDB loans.

iv. Analysis of assets base of the Bank

Asset Base of the Bank for the year 2015 was Rs.9,175 million and it has decreased to Rs.8,717 million by the end of year 2019 representing a 5 percent decline. However, total asset base of License Specialized Bank (LSBS) has increased by 43 percent during the above-mentioned period. Accordingly, growth rate of the Bank in terms of asset base was below the growth rate of the LSBS during the period under concerned.

This situation comes due to settlement of ADB loan installment of Rs. 821 Mn on November 2019.

Bank should pay attention to growth of asset base of the bank.

v. Market share of the Bank

Market share of the Bank in terms of total deposit base of LSBS was declined by 0.038 percent from 2015 to 2019. Further, the market share of the Bank in terms of total assets base of LSBS was also declined by 0.28 per cent from 2015 to 2019.

Noted

Bank should pay attention to Market share of the bank

3.2 Operational Risk

Audit Issue

Management Comment

Recommendation

a. Major risk areas to the Bank

Out of the total loan portfolio of the bank, a sum of Rs.1,226 million or 32.6 percent represented the micro finance loan as at 31 December 2019 and it was Rs.1319 million or 33.3 per cent as at 31 December 2018.

- i. Out of total outstanding amount of micro finance loans, a sum of Rs.520 million or 42 per cent in 2019 and Rs.568 million or 43 per cent in 2018 had been granted to five community-based organizations and this creates a considerable concentration risk to the Bank. In addition, due to insufficient security coverage of above balances as at 31 December 2019, it may difficult to recover the loan balances.

Noted

Following Risk mitigation factors had been followed by the bank. SLS Bank has granted the Loans to these PO's considering the following factors:

- Financial performance of the Community base Organization.
- Past performance of the PO in Credit activities with the SLS Bank.
- SLSB borrowings as a % of Total loan portfolio of the PO.
- Loan Security Deposit percentage against the Loan portfolio.
- NPL position of the PO
- CRIB status of the PO

Take necessary actions to reduce the dependency on few community-based organizations when granting micro finance loans.

- ii. Another 16 community-based organizations are having loan outstanding balances between Rs.14 million to Rs.50 million in 2019 and the amount represents 37 per cent of the total micro finance loan outstanding balance. In 2018, 10 community-based organizations bare the loan outstanding balances between Rs.20 million to Rs.50 million and this amount represents 28 per cent of the total micro finance loan outstanding balance in that year.

Noted.

Another 16 Po's Total Security deposits Rs. 54.45Mn against the total O/S Balance of Rs. 449.31Mn for the year 2019. Therefore, the percentage of Cash security cover for total loan outstanding Balance is 12.2 percent. 03 PO's are legal actions have been taken for these loans by recovery

Take necessary actions to reduce the dependency on few community-based organizations when granting micro finance loans.

department .Those PO outstanding balance is Rs.102Mn. Other 13 Active Pos outstanding balance is Rs.347Mn and Security deposit is Rs.47.27Mn for the year 2019.

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|--|--------------|--|
| <p>b. There are 18 numbers of legal cases with an aggregate value of Rs. 204,754,990 filed by outsiders against the bank and 109 numbers of legal cases with an aggregate value of Rs.2,054,613,941 had been filed by the bank against outsiders. Out of those cases,</p> <p>i. Fourteen numbers of cases with value of Rs.31,638,240 were unavailable at the court registry.</p> <p>ii. Eleven numbers of cases with value of Rs.158,886,057 were not available in the record room or defendants not available at the address.</p> | <p>Noted</p> | <p>Bank should pay attention to settlement of legal cases.</p> |
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3.3 Human Resources Management

Audit Issue -----	Management Comment -----	Recommendation -----
<p>The approved cadre of the bank for the year under review was 183 and the Bank had deployed only 103 employees at the end 2019. Accordingly, there were 80 vacancies as at 31 December 2019.</p>	<p>Due to restriction imposed by CBSL for the recruitment, Bank was unable to fill the cadre as budgeted. However, it was decided to review the exiting carder and identify the staff requirements of the Bank to ensure smooth operation of the Bank.</p>	<p>Take necessary actions to fill the vacancies after obtaining relevant approval.</p>