

REGULATORS REFRAIN FROM ACTION

THE Sunday Leader has received the following commendation from Shirley Peiris, of 31/11, Sulaiman terrace, Colombo 5 in a letter dated March 11,1997.

“Your article on MBSL was excellent. I think you have prevented mass scale manipulations by merchant’s banks by drawing the attention of Central Bank. Let’s hope the Central Bank will take your advice.

“Merchant Bank of Sri Lanka is not just another quoted company owned by private investors. As pointed out by you, it’s a company financed by the government, Bank of Ceylon owns 54% of its shares.”

STOCK EXCHANGE CONCEDES



**New Chairman, Stock
Exchange, Rienzie Wijetilleke
— What action will he take?**

As far back as 1995, Shirley Peiris had made representations to the Colombo Stock Exchange (CSE) and the Securities and Exchange Commission (SEC) on the need for proper reporting and disclosure by merchant banks in their published accounts.

In response to Shirley Peiris’ letter dated October 5, 1995, the Colombo Stock Exchange by its letter dated October 13,1995, also copied to the SEC, replied to Shirley Peiris as follows:

“In general terms, we agree with you that financial reporting standards for merchant banks need to be further strengthened to avoid any possibility of misleading / inadequate information being published.

ACCOUNTANTS’ INSTITUTE NOTIFIED

On August 2, 1996, Shirley Peiris wrote to the Institute of Chartered Accountants seeking clarifications on the following issues that he had raised with the SEC:

“At times the accounts of quoted companies are circulated to shareholders with material misstatements / omissions or the accounts circulated do not comply with Sri Lanka accounting standards.”

“These financial statements are relied upon for various purposes. What is the responsibility of an auditor once it is brought to their attention that accounts reported upon by them contain certain material omissions? Are they required to circulate a statement explaining the correct position to the parties, to whom accounts have been already circulated?”

“In the absence of such a statement can the users of accounts hold the auditors responsible for any loss arising due to any decision taken on the basis of incomplete statements of accounts circulated? Do the directors of the company have any obligations to bring to the notice of the shareholders and the investing public such omissions in the accounts circulated?”

SEC NOTIFIED

On August 5, 1996, Shirley Peiris wrote to the director general, Securities and Exchange Commission underscoring the need for uniformity in preparation of accounts of merchant banks. Shirley Peiris had taken the trouble to do a comparative analysis of the basis of accounting and the adherence to accounting standards by a number of merchant banks in their published accounts. In his submissions to the SEC, Shirley Peiris, inter-alia, stated:

“Can quoted investments purchased by a company over a period of years as trade investments, be converted to long term investments by a mere change of an accounting policy, in the preparation of accounts? The changes in the accounting policies of a company, materially affecting the results or the value of assets require board approval. Obviously, companies which have changed the policy will have such approval on record, but these decision are taken within the course of the year and not after the preparation of accounts for the last quarter at the year end. Nevertheless, are the directors acting in a responsible manner, when changes not relevant to the industry as a whole are made purely to show better results?”

“Why cannot these banks be compelled to adopt a basis of disclosure with more transparency? I am analyzing these accounts from a layman’s point of view, who has no knowledge of operations of these financial institutions. The accounts of DFCC appears to be the most transparent and are in conformity with accepted norms of accounting

..... It may therefore be appropriate for the commission to obtain the services of the DFCC to study and report on a uniform basis to be adopted by merchant banks, in the key areas in the preparation of accounts, so that the investing public can rely on the accounts presented with greater confidence.”

SEC AGREES TO ACT

Director general, Securities and Exchange Commission, Ariththa Wikramanayake, by letter dated August 23, 1996 responded to Shirley Peiris’s letter of August 5, 1996, thus:

“The Securities and Exchange Commission has given serious thought to the matters raised by you in your letter, and sincerely appreciates the suggestions made by you. The commission wholeheartedly agrees that these are issues which need to be addressed as early as possible, to harmonies the presentation of accounts of merchant banks. The commission has been in touch with the Colombo Stock Exchange on this matter, and has been informed that they too received a copy of the said letter, and that they are examining the course of action open to them in implementing your suggestions. The Securities and Exchange Commission, on its part will also conduct a study, in addition to seeking the advice of the Institute of Chartered Accountants to bring in measures for the adoption of these changes.”

Consequently, technical director / consultant of the Institute of Chartered Accountants, S. Sockaliangam by a letter also dated August 23, 1996, had circulated Shirley Peiris’ letter of August 5,1996, which apparently had been referred to the institute by the SEC, to a committee of members of the institute, chaired by its president, M.R. Mihular, for observations and comments.

MBSL ACCOUNTS

At the very same time, Shirley Peiris addressed another letter dated August 19, 1996 to the director general, SEC given a review of the accounts circulated by the Merchant Bank of Sri Lanka Ltd., for the year ended December 31, 1995,. Shirley Peiris in his opinion, raised issues of compliance with Accounting Standards, SLAS 10 – on changes in accounting policies, SKAS 12 – on contingencies and events occurring after the balance sheet date and SKAS 30 – related party disclosure, drawing reference to specific matters in such connection. Shirley Peiris in his letter of August 19, 1996, inter alia, has also raised the following issues:

“For instance note 9.1 of the company’s accounts indicate there is an unreconciled bills discounted figure of Rs. 63 million. In the absence of the indication of the component attributable for year 1995, it would not be unreasonable to assume the bulk of this unreconciled bills remained even as at December 31, 1994. Accounts were audited by the same firm in the previous years but they failed to report on same, although the amounts involved are material in

When interested members of the public raise relevant issues with SEC, CSE or Institute of Chartered Accountants, why is action not taken ?

value..... taking the above into account can anyone conclude that the auditors have reported to the shareholders with the sense of responsibility?.... Do the directors of the company expect the shareholders to take the audit report seriously?

The irony of it all is, the new same auditors are recommended by the directors and are accordingly re-appointed.”

“You will note from the last paragraph of the attached letter from the Colombo Stock Exchange, there is a need to strengthen the existing financial reporting standards of merchant banks. Therefore deterrent measures are necessary at least to discourage non-compliance with the Sri Lanka accounting standards. If an auditor fails to highlight that a company has not complied with a Sri Lanka accounting standard their report cannot be considered correct. The Securities and Exchange Commission should probably introduce regulations to disqualify an auditor being considered for audit of that company for a period of three years, if they have failed to report noncompliance with accounting standards. I am sure even the Institute of Chartered Accounts will be agreeable to same, as such rules will safeguard the interest of the shareholders, who rely on an auditors report...

However, in my view deterrent measures, such as penalising from non-compliance would be more effective.”

AMAZING CONDUCT AND INACTION

From as far back as 1995, Shirley Peiris, an interested member of the public, had been making specific representations to and raising relevant issues with the SEC, Stock Exchange and the Institute of Chartered Accounts, with particular reference, *inter-alia*, to the accounts of the Merchant Bank of Sri Lanka Ltd. During the June 1995 and September 1996 quarters, on other representations that had been made, the SEC had faulted MBSL, who had been required to effect corrections/carry notes to their accounts for contravention of SEC rules.

What is amazing is that given the above background, MBSL published on January 13, 1997 its annual accounts of 1996, giving rise to several controversial issues being spotlighted in the press, some of which were analysed by *The Sunday Leader* in this column. In fact the Institute of Chartered Accountants left it to MBSL to do what they liked. President of the institute, M.R. Mihular, wrote to *The Sunday Leader* in this connection, but however, did not disclose any of the above background of the several issues that had been referred to the institute by the SEC, on representations that had been made by Shirley Peiris, nor

the representations that had been made to the SEC, itself. M.R. Mihular is also an ex-officio member of the SEC in his status as the president of the institute.

This no doubt, is a serious issue, not only for the governor of the Central Bank, A.S. Jayawardena, on the Central Bank's supervisory role over merchant banks, but also is a very serious and pertinent issue for the Chairman, SEC, C.P. de Silva. Let alone the auditors, should not the SEC have an inquiry into this matter of utmost public interest and hold the directors of MBSL accountable and answerable and consider, what action, if any, should be taken against such directors upon such inquiry. More so particularly some of them being professionals and bankers, who ought to have known better ? If not, why?



Chairman SEC, C P de Silva -
"Nobody is above the law" —
will deeds match the words?

After all, Chairman, SEC, C.P. de Silva, was interested in giving effect to Hong Kong standards, on representations made by his friend Ian Hardy of Asia capital, to get rid of the nonsense and shenanigans in the local capital market! What SEC Chairman, C.P. de Silva has to consider is, how would the Securities and Exchange Commission in Hong Kong have acted in the given circumstances, and would they have dealt with the directors concerned, and if so, in what manner?

Incidentally, Ian Hardy, who appeared to be anxious to improve the local standards upto those prevalent in Hong Kong, has so far failed to respond to the invitation extended to him by *The Sunday Leader* on 2, February 1997, to submit a write – up on two recent reported cases in Hong Kong pertaining to securities, to be published in this column for the benefit of the reading public.

SEC CHAIRMAN'S HOLDING OUT

This is what Chairman, Sec, C.P. de Silva, wrote on January 19, 1996 as was published in *The Island*:

Another frequent violation is failure to comply with the listing requirement rules of the SEC "...My advice to the would-be informant is to write a letter to the chairman or the director general of the SEC. He can be sure that if the allegations are well founded they will be investigated and action will be taken against the offender. There are many punishments that the SEC can impose depending on the nature of the offence. Prosecutions will be launched if the evidence is such that the attorney general confirms that there is a case.

"I have written this article because I would like to deter businessmen from committing offences under the act in future. By alerting them to the risks they run through being unaware of the regulations and violating them. I believe I shall save them a lot of pain and the SEC a lot of trouble. The commission consists of a body of very eminent men chosen for their individual expertise and reputations, and their main concern is to ensure the integrity of the share market thereby protecting the interests of investors.

As nobody is above the law, the SEC would not hesitate to take action where it is necessary. Eventually this is the guarantee to both local and foreign investors that our share market is a safe place to invest in.”

Chairman, SEC, C.P. de Silva took very high ground then. Holding out is one thing, but action is another. What action would Chairman, SEC, C.P. de Silva and “the body of very eminent men chosen for their individual expertise and reputations”, as he had been referred to, take now, more so as he had been acknowledged by the SEC letter of August 23, 1996? What action has the Colombo Stock Exchange taken as held out in their letter of October 13, 1995, also copied to the SEC? If not, why? Several issues having been referred by the SEC, what action had the Institute of Chartered Accountants taken? If not, why? What is the inherent duty and responsibility cast on the institute under the statute, wherein its president is an ex-officio member of the SEC?

In view of the privatization of the economy, with resources being transferred to the private sector, this column was started to focus on commercial issues and the business world. The regulatory frame work and institutions should be strengthened to function effectively, ensuring adherence to accepted norms, ethical standards and legal systems in the contemporary capital markets the bottom line being a level playing field with fair competition and transparency with accountability. The public are invited by BISMARCK to participate by forwarding their views and by reporting transactions that need exposure in the public interest.

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