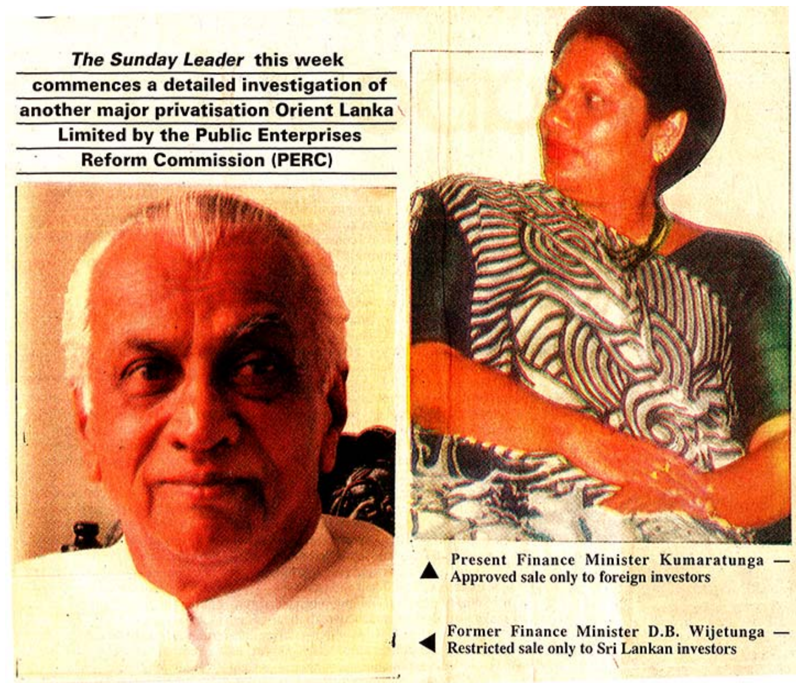
DROWNING SORROWS OVER A BAD SALE

The Sunday Leader this week commences a detail investigative exposure into another major privatisation carried out by the Public Enterprises Reform Commission [PERC]. This investigative exposure is in conformity with the policy of investigative journalism, that is being pursued by *The Sunday Leader*. It has been said that - *"Public scrutiny of what people do is probably the most powerful pressure towards probity of conduct"* and that- *"Rules alone do not prevent malpractice, public scrutiny does"*.



▲ Present Finance Minister Kumaratunga — Approved sale only to foreign investors

◄ Former Finance Minister D.B. Wijetunga — Restricted sale only to Sri Lankan investors

This major privatisation that is being subject to scrutiny in the public interest by *The Sunday Leader* is that of Orient Lanka Ltd., which operates duty free shopping facilities at the Bandaranaike International Airport, to sell exclusively, liquor, tobacco, perfumes, cosmetics and confectionery.

The exclusive sales of liquor included all the well known international premium brand names in Whisky, Cognac, Brandy, Gin, Vodka, Rum, Liqueurs, Wines, Sherry etc., and the exclusive sales of tobacco included the well known international brand names in Cigarettes, Cigars, Pipe Tobacco, etc. The range of perfumes and cosmetics included the well known international premium names, whilst the range of confectioneries also included the well known international brand names.

Orient Lanka Ltd. was established in 1919 as the Orient Company of Ceylon Ltd., a wholly owned subsidiary of British Ceylon Corporation Ltd. Subsequently, the company was acquired by the Government of Sri Lanka on February 25, 1972 under the Business Undertakings [Acquisitions] Act No. 35 of 1971 and carried on business as Government Owned Business Undertaking of Orient Company Ceylon Ltd. It was subsequently incorporated as a public limited liability company on October 21, 1988, under the Conversion of Public Corporations and Government Owned Business Undertakings into Public Limited Liability Companies Act No. 23 of 1987.

A NEW WINDOW FOR YOUR DUTY-FREE DISPLAY

Orient Lanka Ltd.

Request for Expressions of Interest

The Government of Sri Lanka, through the Public Enterprise Reform Commission, invites expressions of interest from potential investors for the acquisition of a controlling ownership in Orient Lanka Ltd.

Orient Lanka Ltd. Orient Lanka is one of the duty-free operators at the International Airport of Colombo. Orient Lanka has concession rights to market liquor, tobacco, fragrances and confectionery. The company has enjoyed a significant track record of profits during the last five years, and, provided the air traffic in and out of Colombo continues at present levels, Orient Lanka has a bright and profitable future. Total revenues in 1994 were distributed among the different commercial lines according to the following breakdown: (i) liquor (60%), (ii) tobacco (22%), confectioneries (11%), and (iv) fragrances (7%). The company has a labour force of 126 employees with payroll representing 7% of the total revenues. Average expenditure per passenger was US $ 30.00 during 1994.

Investor's Profile. Duty-free operators with international experience, and a solid track record of operational skills and profitability. Previous experience in operating duty-free concessions in developing markets will be an added advantage. Investors interested in participating in the acquisition of a controlling ownership in Orient Lanka should send their Statement of Qualification (SOQ) to the Public Enterprise Reform Commission, Bank of Ceylon Building (30th floor) No. 4, Bank of Ceylon Mawatha, Colombo 1, Sri Lanka no later than 11th August 1995.

Pre-qualification. Based on the SOQ's, the Public Enterprise Reform Commission will pre-qualify the potential investors interested in the acquisition of 60% of Orient Lanka Ltd. shares. Results of the pre-qualification of potential investors will be announced no later than 26th August 1995.

Bidding Documents. Bidding conditions and any further information about Orient Lanka Ltd. will be available to the pre-qualified investors no later than 11th September 1995. Such information will also include the Government's divestiture strategy with respect to the rest of the shares (40%)

Potential investors should send the SOQ's and all related correspondence to the Public Enterprise Reform Commission, Bank of Ceylon Mawatha, Colombo 1.

R.N. Asirwatham,
Chairman,
PUBLIC ENTERPRISE REFORM COMMISSION,
Bank of Ceylon - 30th Floor,
No.4, Bank of Ceylon Mawatha, Colombo 1, Sri Lanka.
Telephone: 94-1-338756/8, Fax: 94-1-326116

Former PERC Chairman Asirwathan's letter

As the exclusive duty free operator at the Bandaranaike International Airport selling liquor, tobacco, perfumes, cosmetics and confectioneries, Orient Lanka Ltd. enjoyed renewable lease agreements with the Airport & Aviation Services Sri Lanka Ltd. The company originally had entered into an agreement with the Director Civil Aviation in 1967 to operate the duty free shopping complexes at the Airport for a period of five years. Airport & Aviation Services Sri Lanka Ltd. was incorporated on March 18, 1983. The Government Owned Business Undertaking of Orient Company Ceylon Ltd. entered into an agreement with the Airport & Aviation Services Sri Lanka Ltd., on July 2, 1984. Such lease agreements in respect of duty free shop premises, both in the departure lounge and arrival lounge, were renewed every 3 years.

Under the previous Government, the importance placed on Orient Lanka Ltd. was evident by the fact that M.G.D. Jayawardena, who was also Chairman, Air Lanka Ltd., was the Chairman of Orient Lanka Ltd., with the then powerful Secretary, Ministry of Finance & Policy Planning, R. Paskaralingam also on its Board of Directors, together with S. Dhanabala, a then Director of Air Lanka and G. Sathasivam, of Geekay Organisation Ltd., a then local Duty Free Shop Operator.

FRANCHISE RIGHT - AN ASSET OF GREAT VALUE

The main worth or value of Orient Lanka Ltd. was its exclusive right to sell liquor, tobacco, perfumes, cosmetics and confectioneries at the Bandaranaike International Airport, both to inward bound and outward bound airline passenger traffic and crew. Therefore, in the case of Orient Lanka Ltd. unlike another privatisation, there was no land, building, plant, machinery etc. to have been valued, as such, as main items. In this case it was the valuation to be placed on the exclusive right to carry on duty free selling operations at the Bandaranaike International Airport, to both arriving and departing passenger traffic and crew.

It is well known, that duty free selling operations at international airports are carried out by well established marketing networks, comprising of established duty free operators operating globally at various international airports. It is phenomenally a characteristic of duty free selling, that international brands sell at similar prices at duty free outlets at various international airports.

By such marketing arrangements, gross profit margins of well known prestigious premium brand names of duty free products are assured and maintained by the well organised international duty free trade. The suppliers of the products, themselves, invariably are a part and parcel of such duty free marketing strategy in maintaining the gross profits of high profile premium brand names in the duty free trade. In international duty free operations, particularly at international airports, the gross profit margins, particularly on duty free sales comprising of liquor, tobacco, perfumes, cosmetics, confectioneries are known to be in the rage of 45% to 55%. Orient Lanka Ltd. as a government owned and operated company did not register such gross profit levels of 45% to 55%, but registered gross profit levels around and below 35% during the several years prior to its privatisation in 1996.

Accordingly, any valuation placed on Orient Lanka Ltd. based on the capitalised value of the profit potentials, would have been significantly depressed, influenced by the fact that Orient Lanka Ltd.'s operations had not registered the normal gross profit margins prevalent in the business of international duty free trade, particularly at international airports for such product ranges of liquor, tobacco, perfumes, cosmetics and confectioneries. Any valuation placed on Orient Lanka Ltd., ought to have taken into reckoning such potential gross profit margins prevalent in the international duty free trade, particularly moreso in the hands of an established and experienced international duty free operator.

ORIENT LANKA PAST PERFORMANCE

The annual sales turnovers and gross profits registered by Orient Lanka Ltd. prior to its privatisation for the 5 years 1990 to 1994 had been as follows -

	Sales Turnover Rs.Mn	Gross Profit Rs.Mn.
1990	187.8	60.2
1991	234.5	82.4
1992	354.9	95.1
1993	545.5	181.1
1994	788.6	251.9

Accordingly, the percentages of gross profit margin to sales, registered by Orient Lanka Ltd. prior to its privatisation for the 5 years 1990 to 1994 had been:

	%
1990	32.0
1991	35.1
1992	26.8
1993	33.2
1994	31.9

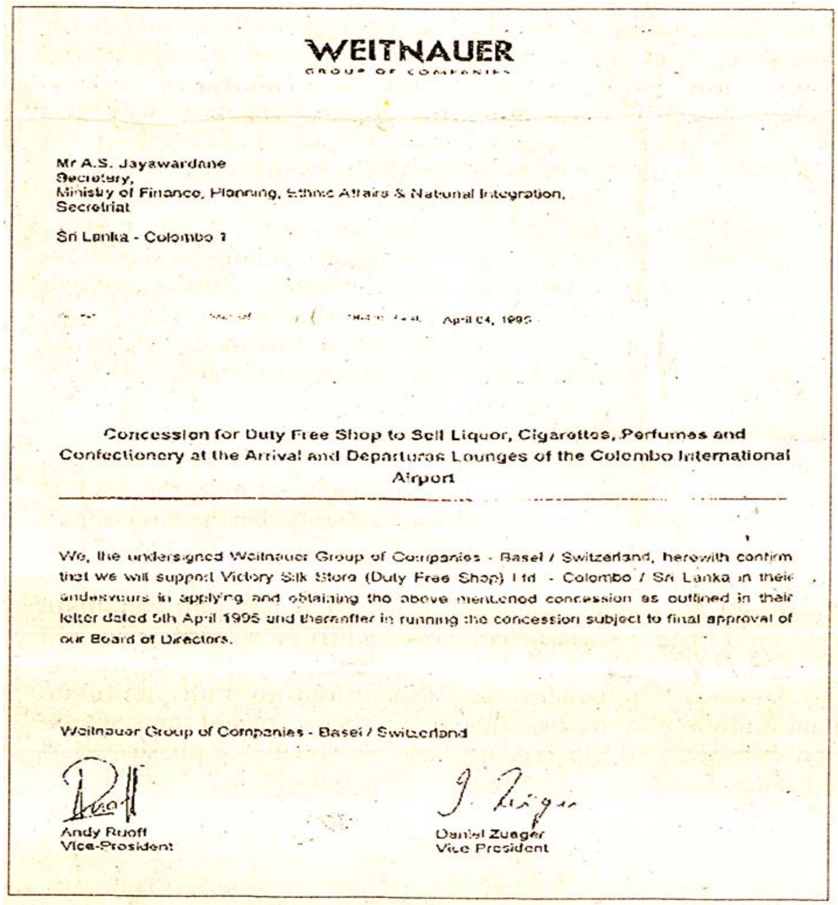
Privatisation is the process by which, private enterprise, capital, management skills and expertise, are mobilised to achieve a greater degree of development, profit, productivity and efficiency, in ventures that had been previously owned and operated by the state, i.e. on behalf of people, where such operations by the state had been far below the expected norms and standards of that particular trade, industry or public utility service.

FRANCHISE PROPOSAL AS PER INTERNATIONAL PRACTICE

In the case of Orient Lanka Ltd., the real asset of value, was the right to sell exclusively liquor, tobacco, perfumes, cosmetics and confectionery at the Bandaranaike International Airport to both inward bound and outward bound passengers and crew. In other words the intrinsic asset of real value was the franchise right to sell at the Bandaranaike International Airport, which exclusive right Orient Lanka Ltd. had enjoyed for over several years since 1967. Orient Lanka Ltd. being owned by the government and belonging to the people of this country, such right accordingly, belonged to the people of this country, to be exploited perennially for their benefit and in their interest. It is internationally well acknowledged that sales at an international airport is to a captive market that is rightfully domiciled to such destination and country.

In such circumstances, it is the international practice, that the right to sell at duty free complexes at international airports, is franchised on the basis of competitive bids, for a certain number of years only at a time, generally for periods around 3 to 6 years. It is known that at Singapore Airport, such franchises are for periods of 3 years only at a time. Duty free operators in the international duty free trade, competitively bid periodically for such airport duty free selling franchises. This is the established international practice. The right to sell at an international airport is not sold outright, because it is a perennial revenue source to governments from international airports, inasmuch as custom duties levied on imports.

Notwithstanding such established international practice, PERC however unconcerned of and indifferent to such international practice and norms of duty free operations at international airports, went ahead to privatise Orient Lanka Ltd. offering to sell outright 60% ownership of the shareholding of Orient Lanka Ltd. that belonged to the government, i.e. the public. PERC having been supported by technical assistance, both through World Bank and USAID, it is incomprehensible to understand, as to how and why PERC deviated from known and established international practice in the duty free trade prevalent at international airports; thereby causing a continuous loss of tremendous proportions to the government and the public, for which PERC alone ought to stand accountable and responsible.



WEITNAUER
GROUP OF COMPANIES

Mr A.S. Jayawardane
Secretary,
Ministry of Finance, Planning, Ethnic Affairs & National Integration,
Secretriat

Sri Lanka - Colombo 1

April 04, 1995

Concession for Duty Free Shop to Sell Liquor, Cigarettes, Perfumes and Confectionery at the Arrival and Departures Lounges of the Colombo International Airport

We, the undersigned Weitnauer Group of Companies - Basel / Switzerland, herewith confirm that we will support Victory Silk Store (Duty Free Shop) Ltd - Colombo / Sri Lanka in their endeavours in applying and obtaining the above mentioned concession as outlined in their letter dated 5th April 1995 and thereafter in running the concession subject to final approval of our Board of Directors.

Weitnauer Group of Companies - Basel / Switzerland

Andy Ruoff
Vice-President

Daniel Zueger
Vice President

Weitnauer's proposal to PERC

PERC cannot be heard to say, that they were unaware of such international practice prevalent in the duty free trade at international airports. In fact in April 1995, a local duty free operator, Victory Silk Store (Duty Free Shop) Ltd., in association with its principals, Weitnauer Group of Companies, Switzerland, one of the largest duty free operators in the world had proposed to PERC, offering to operate Orient Lanka Ltd. on the basis of such prevalent international practice of franchise concession. Then Chairman, PERC, R.N. Asirwatham, in response to such proposal by the Weitnauer Group of Companies, by his reply dated May 18, 1995 bearing reference RNA:ND:vf, inter-alia, stated, *"We are conducting studies on Orient Lanka Ltd., and are exploring possible options. Concessions will be arranged only at a much later date and these concessions are likely to be tendered".*

PERC OPTS FOR OUTRIGHT SALE

Contrary to what was stated in the then Chairman, PERC, R.N. Asirwatham's letter dated May 18, 1995, PERC abandoning the tendering for such franchise concessions, advertised on June 30, 1995 calling for pre-qualification from parties interested in the proposed privatisation of Orient Lanka Ltd. specifically for the acquisition of a 60% shareholding of Orient Lanka Ltd. Such pre-qualification applications were restricted only to Duty Free Operators with international experience. Consequent to such advertisement calling for pre-qualification of parties, PERC shortlisted 10 parties, who had applied for such pre-qualification.

The shortlisted parties had been ──

Agate Duty Free - Malaysia
Alpha Retail Trading - U.K
Gebr Heinemann - Germany
Lion City Holdings - Singapore
Downtown Duty Free - Australia
Sriwani Holdings - Malaysia
AerRianta International - Bahrain
Weitnauer Group - Switzerland
Duty Free Shoppers - Hong Kong
Dubai Duty Free - U.A.E.

Subsequently, on August 29, 1995 PERC wrote to all 10 shortlisted parties inviting them to bid for 60% shareholdings of Orient Lanka Ltd. Such letter of invitation dated August 29, 1995 was sent out by the then Chairman, PERC, R.N. Asirwatham and the bid, with all relevant documents, with a bid bond of 10% of the bid price, was required to reach, the then Chairman, PERC, R.N. Asirwatham, himself, on or before 2.00 p.m. on October 11, 1995. To such letter dated August 29, 1995 was also attached the conditions and guidelines for such bidding.

The share capital of Orient Lanka Ltd. was Rs. 30 million, comprising of 3.0 million shares Rs. 10/- each. Therefore the 60% shareholding on offer for sale was accordingly, 1,800,000 shares of Rs. 10/- each. According to the profile of Orient Lanka Ltd., that had been prepared in December 1993 by Ernst & Young, Chartered Accountants the fixed assets of Orient Lanka Ltd. had been summarised as follows:

	Cost Rs.Mn.
Liberty Plaza Premises	**1.43**
Motor Vehicles	**3.53**
Office Equipment	**1.81**
Duty Free Shop Fittings	**28.28**
Office Fixtures	**0.33**
Store Fixtures	**0.58**
	35.96

In addition, Orient Lanka Ltd. had leasehold premises, as given in the Ernst & Young profile - Head Office at York Arcade Buildings- Duty Free Shops, Colombo International Airport- Stores Premises at the Chalmers Stores Complex UDA- Stores at Prince of Wales Avenue.

PREVIOUS GOVERNMENT DECISION - SALE ONLY TO SRI LANKANS

Previously, during the tenure of the former government, the Cabinet Appointed Divestiture Committee on Orient Lanka Ltd., in its report dated March 3, 1994, inter-alia, recommended - "The Committee considered the question, whether foreign investors should be permitted to participate in the sale of these shares. Since all sales in the Duty Free Shop are for foreign exchange, in the event of a foreign investor acquiring a majority shareholding the foreign exchange thus earned would be once again remitted out of the country as profits, dividends, repatriation of capital etc. In the circumstances, since the Duty Free Shop's earnings are entirely in foreign exchange, it is recommended that the bidding for the majority shareholding be limited to Sri Lankan corporate investors in order to ensure that the net foreign exchange earnings of the Company are retained".

Such Cabinet appointed Divestiture Committee, also included M.P.T. Cooray, Director [Investments] of the Board of Investments of Sri Lanka [BOI]. M.P.T. Cooray, himself, being a well experienced knowledgeable expert on foreign investments, was party to such recommendation, that bidding for majority shareholdings of Orient Lanka Ltd. be limited to Sri Lankan corporate investors only.

The Cabinet Memorandum dated March 28, 1994 submitted by then Minister of Policy Planning & Implementation, D.B. Wijetunge, inter-alia, recommended - "The Committee also recommends that the sale of majority shareholding be restricted to Sri Lankan investors only. This is a service item and should remain in the hands of Sri Lankan investors only."

PRESENT GOVERNMENT SELLS TO FOREIGN COMPANY

Such concerns on foreign exchange earnings, apparently was of no consequence to PERC or the present government, which has permitted a foreign investor, Alpha Airports Group PLC, U.K. to acquire and exploit such national right to sell at the country's only international airport; whereas on the contrary, international practice is that, such national right is franchised on bid for short-term periods, the government and the country thereby continuously having a stream of foreign exchange earnings. Who takes responsibility for such debacle causing continuous loss of tremendous proportions detrimental to national interests ?

Not only has 60% shareholdings of Orient Lanka Ltd. been sold to a foreign investor, but the foreign investor has also been afforded an option to purchase a further 37% shareholdings, making a total of 97% shareholdings of Orient Lanka Ltd. Employees of Orient Lanka Ltd. have been given only 90,000 shares i.e. 3% of the 3 million shareholdings of Orient Lanka Ltd. Such a profitable operation of exclusive duty free selling at the Bandaranaike International Airport, makes Orient Lanka Ltd. an excellent candidate to be a listed public company with public shareholdings, - thereby also making transparent its operations to the public; and the public of this country rightfully having a stake in and participating in such profits.

Leasehold rights enjoyed by Orient Lanka Ltd., of the Duty Free Shop premises at the Bandaranaike International Airport in terms of the renewable lease agreements with the Airport & Aviation Services Sri Lanka Ltd., would automatically get renewed, with the reasonable upward revision in the rentals, upon due performance by Orient Lanka Ltd., of its obligations under and in terms of the lease agreements, viz - regular payment of rentals; on the basis of legitimate expectation, which would be legally upheld by court.

TRANSPARENCY & ACCOUNTABILITY

Under the previous regime, in the case of divestiture of each state owned enterprise, the Cabinet appointed a Divestiture Committee, chaired by the Secretary of the relevant line Ministry, under which such state owned enterprise,that was targeted to be divested, functioned. It was such Divestiture Committee, assisted by professional and technical experts,that finalised the relevant documentations and advertised the sale of such state owned enterprise.

The Divestiture Committee deliberations and recommendations were submitted to Cabinet. Prior to Cabinet Decision, the Economic Sub-committee of the Cabinet examined and considered the matter and to which Cabinet Economic Sub-committee Meetings, the relevant officials and concerned parties were invited for clarifications, including any aggrieved party, who had made any representations in regard to such transaction, to be heard thereon, prior to conclusion of such transaction. Though the present government has held high, policies on transparency and public accountability, such much desired transparent systems and safeguards, however, appear to have been questionably abandoned. Why?

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