

**1.1 Qualified Opinion**

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The audit of the financial statements of the National Institute of Fundamental Studies for the year ended 31 December 2018 comprising the statement of financial position as at 31 December 2018 and the statement of financial performance, 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, except for the matters described in Paragraph 1.5 of this report, the financial statements give a true and fair view of the financial position of the National Institute of Fundamental Studies as at 31 December 2018, and of its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

**1.2 Basis for Qualified Opinion**

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My opinion is qualified based 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**

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Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Public Sector 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 Institute'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 Institute or to cease operations, or has no realistic alternative but to do so.

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

As per Sub-section 16(1) of the National Audit Act No. 19 of 2018, the Institute 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 Institute.

#### **1.4 Scope of Audit (Auditor's Responsibilities for the Audit of the Financial Statements)**

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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 Institute'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 Institute'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 Institute 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 Institute, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Institute has complied with applicable written law, or other general or special directions issued by the governing body of the Institute
- Whether the Institute has performed according to its powers, functions and duties; and
- Whether the resources of the Institute had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

## 1.5 Financial Statements

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### 1.5.1 Internal Control over the preparation of financial statements

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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. Issues with regard to maintenance of key accounting records such as General Ledger, Journal and Journal vouchers, payment vouchers etc. may include under this heading.

### 1.5.2 Non-compliance with Sri Lanka Public Sector Accounting Standards

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Audit Observation	Comments of the Management	Recommendation
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(a) In contravention to the Paragraph 99 of the Sri Lanka Public Sector Accounting Standard, without being stated in the statement of financial performance the income of Rs.32,116,648 and expenditure of Rs.17,659,343 of various 29	Recurrent expenditure of Rs.15,498,385 incurred in cash during the year under review had been stated in the statement of financial performance as income and expenditure while capital expenditure of Rs.2,160,958	Action should be taken in accordance with the Sri Lanka Public Sector Accounting Standard 01.

projects and 12 programmes and workshops of the Institute during the year under review, only the recurrent expenditure of Rs.15,498,385 thereof had been stated as income in the statement of financial performance without carrying out classifications.

had been stated in the statement of changes in equity and the remaining balance of Rs.25,679,920 had been brought to account as special funds and grants under the equity.

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| (b) | Without being complied with the Paragraph 24(a) of the Sri Lanka Public Sector Accounting Standard 03, despite the recognition of a new policy for the amortization of fixed assets received by the Institute as the donations during the year under review, neither this policy had been disclosed nor made adjustments retrospectively. | Since it was found practically difficult to separately identify the assets received as donations to the Institute, retrospective adjustments have not been made during the year under review. Nevertheless, it was noted to make the relevant adjustments and disclose the relevant policy in the future. | Action should be taken in accordance with the Sri Lanka Public Sector Accounting Standard 03. |
| (c) | Without being complied with the Paragraph 75 of the Sri Lanka Public Sector Accounting Standard 07, the useful life of the non-current assets had not been reviewed annually. Hence, the non-current assets worth Rs.123,805,941 were further in use in spite of fully depreciation.  | Revaluation of non-current assets of the Institute is in progress at present. The relevant adjustments will be made in terms of those revaluation reports. Accordingly, the value of assets further in use will be revised.   | Action should be taken in accordance with the Sri Lanka Public Sector Accounting Standard 07. |

### 1.5.3 Accounting Policies

----- Audit Observation -----	Comments of the Management	Recommendation -----
(a) Action had not been taken to identify and account for the amortization value pertaining to the assets worth Rs.75,180,691 purchased from the Government Grants of the year under review and the assets acquired in the preceding years and to reveal the relevant policy in the financial statements.	It was recorded to adjust an amount corresponding to the depreciation of the assets purchased from the Government Grants annually in the future and to disclose the relevant policy in the financial statement.	Revenue relevant to the year should be identified and accounted for.

- (b) The balance of the revaluation reserve as at the end of the year under review amounted to Rs.118,388,385 and the accounting policy adopted by the Institute in connection with the revaluation reserve had not been disclosed in the financial statements.
- It was noted down to disclose the relevant accounting policy in the financial statements.
- Policies related to the revaluation adjustments should be disclosed in the financial statements.

#### 1.5.4 Accounting Deficiencies

Audit Observation	Comments of the Management	Recommendation
(a) The unusable assets worth Rs.29,853,300 and misplaced assets worth Rs.6,037,985 identified at the Board of Survey of the year under review had been included in the non-current assets.	Arrangements are being made to auction the unusable assets and the maintenance of Sub inventory lists has been initiated to find out the misplaced items. Subsequently, the necessary steps are due to be taken in the future in respect of the items that cannot be further find out.	All the fixed assets should be maintained in an updated manner by entering in a formal register of fixed assets

#### 1.5.5 Lack of Documentary Evidence for Audit

Item	Amount	Evidence not Furnished	Comments of the Management	Recommendation
	<b>Rs.</b>			
Fixed Assets	936,095,460	Documents	The fixed assets of the Institute are being revalued as the initial step.	A register of fixed assets should be maintained in terms of Circular No.842 dated 19 December 1978.

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

Reference to Laws, Rules and Regulations	Non-compliance	Comments of the Management	Recommendation
(a) Financial Regulation 102	Action had not been taken as per the financial regulations in respect of misplaced items worth Rs.10,219,134 identified at the Board of Survey.	Steps are being taken to find out the misplaced items and necessary actions are due to be taken with regard to the items that cannot be further find out.	Action should be taken as per the Financial Regulation 102.
(b) Financial Regulation 770 (2)	As the General Forms had not been used at the board of survey conducted as at 31 December 2017, the recommendations to be made by the Board of Survey had not been included in the report.	The General Forms of the Government will be used for the board of surveys from the year 2018.	Action should be taken in accordance with the Financial Regulation 770 (2).
(c) Section 6.5.1 of the Public Enterprises Circular No.PED/12 dated 02 June 2003	The financial statements for the year ended 31 December 2018 had been presented on 20 August 2019 by the Institute.	The post of Chairman of the Institute remained vacant up to 23 July 2019.	Action should be taken in terms of the Public Enterprises Circular No.PED/12 dated 02 June 2003.
(d) Section 14(1) of the Finance Act No.38 of 1971.	The final annual report relating to the preceding year and the draft annual report for the year under review had not been prepared even by 29 January 2019.	The officer who had been assigned this task had resigned the service and the other officers involved in the preparation of this report while engaging in other necessary official duties. Therefore, it could not be completed within the expected timeline.	Action should be taken in terms of provisions of the Act in the preparation and submission of the Annual Report.

## 2. Financial Review

### 2.1 Financial Results

According to the financial statements presented, the operations of the Institute for the year ended 31 December 2018 had resulted in a deficit of Rs.104,071,500 as compared with the corresponding deficit of Rs.73,461,847 for the preceding year, thus observing a deterioration of the financial results by Rs.30,609,653 in the year under review as compared with the preceding year. This deterioration was mainly attributed to the failure in adjusting amortization of assets in the statement of financial performance.

In analysing financial results of the year under review and 04 preceding years, a deficit was observed from the year 2014 to 2018. However, when readjusting the employees remunerations and depreciations for the non-current assets to the financial results, the contributions of the Institute amounting to Rs.95,817,273 in the year 2014 had become Rs.117,182,534 in the year 2018.

### 2.2 Tendency Analysis of the Main Income and Expenditure Items

In comparing the expenditure of the year with that of the preceding year, expenditure on foreign grants and local grants had increased by 60 per cent and salaries and wages by 12 per cent while expenditure on supplies and maintenance had decreased by 25 per cent. Further, the income received as donations had increased by 73 per cent during the year under review and the foreign currency exchange profit had increased by 1008 per cent while revenue from surcharge and provision of accommodations had decreased by 96 per cent and 21 per cent respectively.

### 2.3 Ratio Analysis

Even though the optimum level of the current assets ratio of an institute should stand at 1:2, it remained at 1:15 relating to the National Institute of Fundamental Studies.

## 3. Operating Review

### 3.1 Identified Losses

Audit Observation	Comments of the Management	Recommendation
(a) As 04 officers of the Institute had used a Van owned by the Institute for their transportation from Digana official quarters to the Institute daily without obtaining a proper approval, the Institute had suffered a loss of Rs.203,852 during the year under review.	This vehicle facility has been provided for the middle level Managers who are not entitled to the monthly transport allowance and official vehicles in terms of Public Enterprises Circular No.PED 1/2015 and in addition, the Institute has taken steps to recover an amount from the relevant officers.	Provision of facilities to the officers should be done only in accordance with the relevant circulars and under the proper approval.

- (b) Without being taken action to get back an advance of Rs.55,863 paid to the V.W.R. International Ltd. on 18 March 2013 to import chemicals or to obtained the relevant items, it had been written off by journal entry No.476.
- For this items, a permit was issued from the Central Environmental Authority. Although approval of the National Dangerous Drugs Control Board was sought, warehouse charges had to be paid in excess of the value of the items. Further, items could not be found from the Customs. The relevant adjustments were made once the clarification was made by the Board of Directors of the Institute.
- Speedy action should be taken regarding these types of transactions.

### 3.2 Management Inefficiencies

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#### Audit Observation

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#### Comments of the Management

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#### Recommendation

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- (a) Although a period of more than 03 years had elapsed from the payment of an advance of Rs.660,000 for the development of a computer software system for the Institute, the relevant cliental institute had failed to complete and hand over the above system. Computers and accessories worth Rs.6,864,960 had been purchased for this project by the year under review.
- In terms of Paragraph 25 of the Agreement, the delay charges are expected to be recovered in making payments on completion of the works of the combined software system.
- Projects should be initiated after a proper evaluation and implemented in accordance with the agreements.
- (b) Out of 29 observations made by the Internal Audit during the year under review, corrections had been made only for 06 observations.
- It was noted down to make corrections on the relevant observations expeditiously.
- Expeditious steps should be taken in respect of the recommendations set out in the Internal Audit Reports.



### 3.3 Underutilization of Funds

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<b>Audit Observation</b>	<b>Comments of the Management</b>	<b>Recommendation</b>
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(a) Provisions of Rs.94,478,204 made for the capital projects during the year under review and the preceding years had not been utilized for the relevant purpose.	Since the payments for the procurement activities relevant to the year under review and the preceding years would be delayed, a sum of Rs.81,000,000 was deposited in the Account of the Institute bearing No.1-0015-01-03152 maintained in the National Savings Bank according to the Board of Governance decisions dated 01.12.2018. Out of the above amount, a sum of Rs.29,967,390 had been used for making payments for the relevant activities by 30.09.2019.	Attention should be drawn on promptly using the funds available and those received relating to the construction projects.
(b) Out of the grants received for the researches, a balance of Rs.25,679,319 remained as at 31 December of the year under review of which Rs.1,984,035 relating to 06 research projects pertaining to the preceding year had not been utilized.	The balances of the relevant research grants are expected to be used properly.	Attention should be drawn on the use of provisions received for the research projects in terms of the agreements.

### 3.4 Procurement Management

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<b>Audit Observation</b>	<b>Comments of the Management</b>	<b>Recommendation</b>
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(a) Having revised the Procurement Plan of the year under review, it had been approved by the Board of Governance on 29 December 2018 and the overall progress of the procurement activities had been 56 per cent.	It was noted down to look into the matters given rise to revise the Procurement Plan in the year 2018, its weaknesses and to revise the relevant Plan and obtain the due approval in the middle of the year 2019 without waiting until the end of the year.	Annual Plans should be prepared, approved and implemented to use them as effective instruments in management control.

- (b) Although it is a part of the prior procurement process to ensure that the necessary financial provisions for the procurement have been made, as a result of not confirming the financial viability at the time of placing orders by the National Institute of Fundamental Studies, procurements worth Rs.9,261,310, US\$ 2,697 and CHF 76,330 had not been completed during the year. Arrangements will be made to introduce a proper control system required to streamline the internal control of the Institute and the SARASA software is expected to be used to avoid these deficiencies. The procurement process of the Institute should be implemented so as to achieve the objectives of the procurement.

#### 4. Accountability and Good Governance

##### 4.1 Corporate Plan

Audit Observation	Comments of the Management	Recommendation
(a) In terms of Section 5.1.3 of the Public Enterprises Circular No. PED/12 dated 02 June 2003, having prepared a Procurement Plan at least for a period not less than 03 years and updated annually and obtained approval of the Board of Management, it should be presented to the Auditor General, General Treasury, Line Ministry and the Public Enterprises Department 15 days before the commencement of each year. Nevertheless, the National Institute of Fundamental Studies had not taken action accordingly.	Necessary steps are being taken to prepare a Corporate Plan for a period of 05 years in accordance with the relevant Public Enterprises Circular.	Action should be taken in accordance with the relevant circulars and those should be used as effective instruments in management control.

##### 4.2 Annual Action Plan

Audit Observation	Comments of the Management	Recommendation
Even though an Annual Action Plan should be prepared to achieve whole objectives of the Institute, the Action Plan of the Institute had been prepared only for a research project.	Arrangements have been made to prepare the Action Plan from the year 2019 with the inclusion of key performance indicators for the relevant year to achieve the whole objectives of the Institute.	Action should be taken in accordance with the relevant legal provisions and those should be used as effective instruments in management control.

### 4.3 Budgetary Control

Audit Observation	Comments of the Management	Recommendation
(a) The income of Rs.1,122,500 earned for the Annual Research Review of the National Institute of Fundamental Studies had not been recognized in the Budget.	Since it could not be specifically determined the funds received from the external parties for the Annual Research Review 2018 and the balance thereof would be used for the following year, it had not been included in the annual Budget.	Action should be taken to identify sufficient income pertaining to the year and include them in the Budget.
(b) As the Budget of the Institute had been revised on 29 December 2018, the Budget, 2018 had not been made use of as an effective instrument in management control as required by Section 5.2.5 of the Public Enterprises Circular No.PED/12 dated 02 June 2003.	Even though Rs.185 million had been approved for recurrent expenditure of the Institute for the year 2018, the National Budget Department had released another Rs.10 million through F.R.66 for recurrent expenditure in November 2018 in order to spend for the necessary operating activities. Accordingly, the revised Budget was forwarded to the next Board of Governance meeting held on December 2018 and obtained approval thereon.	The Budget of the year should be used as an effective instrument in financial control.