

## **Construction Guarantee Fund - 2015**

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The audit of Financial statements of the Construction Guarantee Fund for the year ended 31 December 2015 comprising the statement of financial position as at 31 December 2015 and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information, 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 Section 23 of the Trust Deed No.3/136 dated 24 August 2005. My comments and observations which I consider should be published with the Annual Report of the Fund appear in this report.

### **1.2 Management's Responsibility for the Financial Statements**

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Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Public Sector Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

### **1.3 Auditor's Responsibility**

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My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000 - 1810). Those Standards require that, I comply with the ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Fund's preparation and fair presentation of the financial statements 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 Fund's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

### **1.4 Basis for Qualified Opinion**

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My opinion is qualified based on the matters described in paragraph 2.2 of this report.

## **2. Financial Statements**

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### **2.1 Qualified Opinion**

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In my opinion, except for the effects of the matters described in paragraph 2.2 of this report, the financial statements give a true and fair view of the financial position of the Construction Guarantee Fund as at 31 December 2015 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

### **2.2 Comments on Financial Statements**

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#### **2.2.1. Accounting Deficiencies**

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The following observations are made.

- (a) The draft presented by the client to encash the bonds as the related contract not been completed according to the Contract Agreement relating to the Advance Guarantee amounting to Rs.7,400,000 and the Performance Bond amounting to Rs.2,400,000 issued to a contractor on 22 June 2015 and 30 June 2015 respectively had not been brought to account.
- (b) Despite the client had cancelled the Contract Agreement relating to the advance Guarantee and the performance Bond issued by the Fund, due to non-completion of related construction, the Fund had used an another contractor and that construction had been completed at a cost of Rs.5,700,000 without a proper approval and a contract Agreement. Accordingly, instead of being brought to accounts the amount payable to the Contractor had been written off against the surplus brought forward with the intention of setting off for Rs.5,199,307 recoverable from the Contractor.

### **2.3 Non-compliance with Laws, Rules, Regulations and Management Decisions.**

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The following non-compliances were observed.

<b>Reference to Laws, Rules, and Regulations.</b>	<b>Non-compliance</b>
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(a) Section 7 of Trust Deed No. 3/136 dated 24 August 2005	Even though the Chairman or trustees of the fund are not entitled to obtain any allowance out of the Fund for the services provided except the reimbursement of expenses incurred for working as the Chairman or trustees of the Board of Trustees of Fund, contrary to that, a total sum of Rs.7,377,100 had been obtained for the year under review and the preceding years as Chairman's allowance and board of trustees meeting allowance.

- (b) Treasury Circular No. A fixed assets register had not been properly maintained IAI/2002/02 dated 28 for computers and software. November 2002

## 2.4 Lack of Evidence for Audit

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The evidence stated against the following transactions had not presented to audit.

Item	Value Rs.	Evidence not made available
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(a) Reimbursement of expenses	450,000	Bills settled
(b) Debtors	70,576,790	Confirmations of Balance
(c) Furniture fittings and office equipment	6,633,368	Registers of Fixed Assets
(d) Pre-payments	613,367	} Detailed Schedules
(e) Cash in Transit	5,239,219	

## 3. Financial Review

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### 3.1 Financial Results

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According to the financial statements presented, the financial result for the year ended 31 December 2015 had been a surplus of Rs.36,930,287 as compared with the corresponding surplus of Rs.133,519,853 for the preceding year, thus indicating a deterioration of Rs.96,589,566 in the financial result for the year under review as compared with the preceding year. The decrease of security bond revenue by Rs.54,827,041, revenue of Special project security bonds by Rs.25,643,750 and decrease of fixed deposit interest income by Rs.20,644,467 and increase of contractual service expenses by Rs.3,585,960 had mainly attributed to the above deterioration.

In analyzing the financial result of the year under review and the four preceding years, financial surplus had regularly increased from the year 2011 to 2013 whereas the financial result had deteriorated by 72 per cent in the year 2015 as compared with the year 2014. Eventhough, in considering the employees' remunerations, taxes paid to the Government and depreciations for Non-current Assets, the contribution of the Fund amounting to Rs.24,726,684 in the year 2011 had gradually increased up to Rs.166,685,641 in the year 2013, it had decreased by 57 percent in the year 2015 as compared with the year 2014.

## 4. Operating Review

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### 4.1 Performance

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The objectives of the Construction Guarantee Fund in terms of the Trust Deed, No.3/136 dated 24 August 2005 were issuance of Bonds such as bid bonds and performance bonds required to present for local construction contractors and their industries and provision of

funds required for that purpose. Number of Bonds issued in the preceding year and the year under review had been 3,039 and 1,559 respectively and a decrease of issue of bonds by 1,480 or 48.7 per cent in the year under review as compared with the preceding year was observed.

#### **4.2 Management Activities**

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The following observations are made.

- (a) An incentive of Rs.480,000 for 05 officers served on contract basis and employee motivation allowance amounting to Rs.1,857,000 for 29 officers served on duty assignment basis had been paid without an approval of the Department of Management Services and performance evaluation.
- (b) A sum of Rs.2,064,334 for 02 Motor Vehicles obtained on monthly hire basis and a sum of Rs.494,098 for fuel had been spent in the year under review. Daily running charts had not been prepared as to include the information such as distance travelled of this Motor vehicle, duties performed and the information of the officer concerned and payments had been made without calculating the cost per Km run and ensuring the economy and effectiveness of the expenses.
- (c) A sum of Rs.1,200,000 had been paid to the building owner in the year under review at the rate of an estimated amount of Rs.100,000 per mensum instead of the actual cost of the electricity consumption of the Head Office of the Fund. As there was no formal Electricity Bills, this expense could not be accepted in audit as a real expenditure.

#### **4.3 Transactions of Contentious Nature**

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The following observations are made.

- (a) A sum of Rs.20,800,000 recoverable from a debtor for 04 years had been written off from the accounts on the decision of the Council No.046 dated 04 June 2015 without taking necessary action to recover.
- (b) Legal action had not been taken to appoint an arbitrator for the recovery of a sum of Rs.22,840,202 related to the preceding years and a sum of Rs.47,736,588 for the year under review from the related contractors paid by the Construction Guarantee Fund to the employers on behalf of contractors due to encashment of security bonds issued by the Fund to employers for contractors.
- (c) A sum of Rs.1,490,400 had been paid in the year under review for 17 officers of the Institute for Constructions, Training and Development for the preparation of Accounts of the Fund. It was failed to ensure the transparency of such payments in audit as there was no any type of awarding of appointment to them or entering in to service agreements for that purpose.

- (d) A sum of Rs.778,972,629 had been invested in fixed deposits without obtaining the approval of the Ministry of Finance in terms of the Department of Public Enterprises, Circular No. PED/56 dated 27 January 2011.
- (e) The revised Trust Agreement dated 08 February 2012 had stated that the maximum limit of the bond value issuable by the Fund without obtaining the approval of the Secretary to the Treasury, the Arbitrator of the Fund was ten times the liabilities of the Fund in the related period.
- (f) The following payments had been approved by the Board of Management of the Fund without considering the Financial Regulation 71 and Circular No.30 of the Department of Management services.
  - (i) Payment of a cost of living allowance of Rs.300,000 in addition to the monthly remuneration of the officers recruited on contract basis including the Chief Executive Officer of the Fund.
  - (ii) Permission had granted by the decision No.09/2013 of the Board of Management for the reimbursement of medical bills and accidents for obtaining medical treatments subject to a maximum of Rs.500,000 per annum per officer. A sum of Rs.2,089,132 had been paid out of the Fund for the settlement of medical bills of 21 officers of the year under review.
  - (iii) Payment of a sum of Rs.263,786 had been made during the year under review without an approval of the Treasury to the officers of the Fund for the unavailed vacation Leave.
- (g) In issuing securities and bonds for the contractors by the Fund, advances amounting to Rs.24,280,338 paid by the related employers to the contractors instead of obtaining a security had been brought to accounts as cash of the Fund without a proper authority.

#### **4.4 Personnel Administration**

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 The following observations are made.

- (a) Even though, all the Statutory Institutions should restructure their organizational structure in compliance with the Management Services Circular, No. 30 dated 22 September 2006 and the Circular letter No. PED/PU dated 08 July 2009 of the Department of Public Enterprises and schemes of recruitment and promotion, Number of Cadre and the salary scales should be revised and action should be taken to obtain recommendations from the National Salaries and Cadre Commission and approval of the Department of Management Services, the Fund is in operation with 05 officers recruited on contract basis and 29 officers on duty assignment basis without an approved cadre. As such the possibility of taking responsibility on its activities without a permanent staff was not cleared in audit.
- (b) The service of the officers recruited on duty assignment basis had been obtained for 01 year to 11 years continuously without the segmenting the period of service according to

the duty assignments and a monthly salary had been paid them instead of making payment on duty assignments. Twenty officers of them had exceeded 03 years continuous period of service.

**5. Accountability and Good Governance**  
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**5.1 Internal Audit**  
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From the inception of the Fund, either an Internal Audit Division or the Internal Audit Division of the Ministry had not audited its activities and transactions.

**5.2 Audit Committees**  
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The Fund had not held Audit and Management Committee meetings from the inception. Further, the officers of the Fund had not been invited to the Audit and Management Committees of the Ministry.

**5.3 Tabling of Annual Reports**  
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Annual reports from the year 2002 to 2013 had not been tabled in Parliament in terms of the Public Enterprises Circular No. PED/12 dated 02 June 2003.

**6. Systems and Controls**  
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Weaknesses in systems and controls observed during the course of audit were brought to the notice of the Chairman of the Fund from time to time. Special attention is needed in respect of the following areas of control.

<b>Areas of systems and Controls</b> -----	<b>Observations</b> -----
(a) Personal Administration	Non recruitment of separate personnel for the Fund, non-provision of formal job descriptions and not getting done the functions.
(b) Financial Management	Non-Management of expenses as laid down in Section 7 of the Trust Deed.