

Construction Guarantee Fund (CGF) – 2017

The audit of financial statements of the Construction Guarantee Fund for the year ended 31 December 2017 comprising the statement of financial position as at 31 December 2017 and the statement of financial performance, statement of changes in net assets and statement of cash flows 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(3) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Section 11(d) of Deed of Trust No.3/136 of 08 February 2010. 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

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

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 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 judgment, 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

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

2. Financial Statements

2.1 Opinion

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 2017 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

2.2.1 Accounting Policies

The following observations are made.

- (a) The accounting policies applied for recognition of revenue had not been disclosed in the financial statements.
- (b) The Fund had applied a flat rates of 5 per cent and 100 per cent for the outstanding period from 1 to 5 years and over 5 years respectively for computing the provision for doubtful debts as mentioned in paragraph 2.8 under Significant Accounting Policies to the financial statements without ascertaining the real credit risk of debtor (Demand made by CGF).

2.2.2 Accounting Deficiencies

The following deficiencies are observed.

- (a) Interest income on fixed deposits and treasury bills had been overstated by Rs. 30,851,335 in the financial statements due to erroneous computations.
- (b) Withholding tax payable balance of Rs. 2,591,496 as at the end of the preceding year had not been brought to accounts. However, a sum of Rs. 8,967,368 had been erroneously credited to the accumulated surplus for the year under review as an adjustment for refunded withholding tax.

2.2.3 Lack of Evidence for the Audit

The following evidence as indicated against each item of account shown below had not been submitted to audit for verify the accuracy of such items.

Items of Account	Value	Evidence not made available
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	Rs.	
Interest Receivable on Fixed Deposits	47,129,645	Details of computation
Fixed Deposit Income Overstated	2,798,932	Supporting documents

2.3 Non-Compliance with Laws, Rules, Regulations and Management Decisions

The following instances of non-compliance were observed in audit.

Reference to Laws, Rules, Regulations and Management Decisions etc.	Non- compliance
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(a) Section 10 of the Employees' Provident Fund Act, No. 24 of 1971.	(i) The Fund had recruited 6 officers on contract basis during the year 2016. However, the contribution to the Employee Provident Fund (EPF) had been made for only one officer contrary to the provisions in the Act. (ii) A permanent officer working for over 18 years had not been contributed to the EPF since his date of appointment to the post of advisor.
(b) Section 7 of the Deed of Trust No.3/136 of 08 February 2010.	Even though there is no entitlement to claim any allowance from the Fund for the service provided other than reimbursement of the expenditure incurred on behalf of acting as the Trustees of the Board of Trust of the Fund, in contrary to that a sum of Rs.9,802,100 had been paid as Chairman allowance and allowances for meetings of the Board of Trustees during the year under review and the preceding years.
(c) Public Enterprises Circulars -----	
(i) No. PED 38 of 14 July 2006	The Fund had not registered for the purpose of Value Added Tax with the Department of Inland Revenue
(ii) No. PED 03/2016 of 29 April 2016	Actions had not been taken to recover the Pay As You Earn Tax from three officers who are liable to pay such tax and remitted it to the Department of Inland Revenue

3. Financial Review

3.1 Financial Results

According to the financial statements presented, the operations of the Fund for the year ended 31 December 2017 had resulted in a surplus of Rs.108,980,219 as compared with the corresponding surplus of Rs.82,968,314 for the preceding year, thus indicating an improvement of Rs.26,011,905 in the financial results. Increase of interest income from fixed deposits by a sum of Rs.37,363,019 was the main reason attributed for the above improvement.

4. Operating Review

4.1 Performance

Providing guarantees to the registered contractors when undertaking construction contracts is the main objective of the Fund. The following observation is made in this connection.

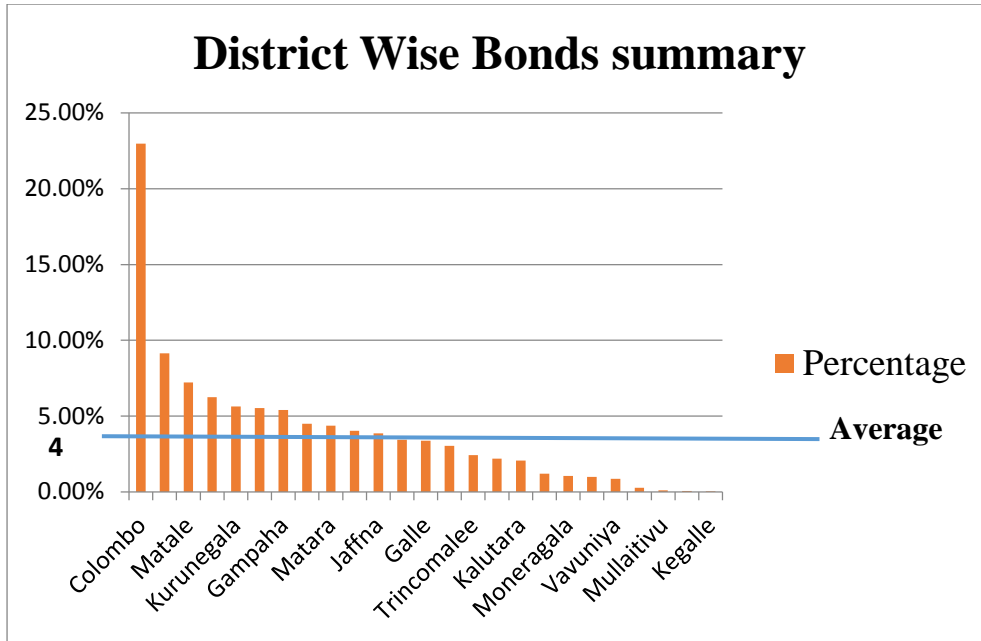
The expected targets and officers responsible to achieve those targets in the year under review had not been set out by the Fund. Hence, the performance of the Fund could not be ascertained in audit. However, the actual achievements of the main activities were provided with audit. Accordingly, the number of security bonds issued in the year under review and the preceding year were 2,105 and 2,927 respectively.

4.2 Operating Inefficiencies

The following observations are made.

- (a) A sum of Rs. 79,711,701 had been paid to client on behalf of 26 security bonds and guarantees provided during the period of 2012 to 2016 due to poor performance of contractors who obtained those bonds and guarantees. However, this amount had not been recovered from the particular contractors.
- (b) According to the information made available, security bonds and guarantees to the total value of Rs. 668,102,130 had been issued to among the districts island wide. Out of that 22.98 per cent had been issued to the constructors of Colombo district. However, only less than one per cent of the total value had been provided to the constructors in 06 districts such as Kilinochchi, Vavuniya, Nuwera Eliya, Mullaitivu, Mannar and Kegalle. The details of such bonds and guarantees issued during the year under review are given in the following table and graph.

	District	Value of Bonds	
		Rs.	Percentage
01	Colombo	153,528,650	22.98
02	Anuradhapura	61,021,672	9.13
03	Matale	48,281,620	7.23
04	Polonnaruwa	41,696,149	6.24
05	Kurunegala	37,695,915	5.64
06	Batticaloa	37,003,487	5.54
07	Gampaha	36,043,580	5.39
08	Kandy	30,012,305	4.49
09	Matara	29,181,362	4.37
10	Hambantota	26,943,099	4.03
11	Jaffna	25,819,105	3.86
12	Ampara	22,900,275	3.43
13	Galle	22,530,705	3.37
14	Ratnapura	20,234,017	3.03
15	Trincomalee	16,220,398	2.43
16	Puttalam	14,621,482	2.19
17	Kalutara	13,806,873	2.07
18	Badulla	8,068,800	1.21
19	Moneragala	6,994,067	1.05
20	Kilinochchi	6,591,655	0.99
21	Vavuniya	5,803,000	0.87
22	Nuwara Eliya	1,770,900	0.27
23	Mullaitivu	697,200	0.10
24	Mannar	362,614	0.05
25	Kegalle	273,200	0.04
Total		668,102,130	



4.3 Management Activities

The following observations are made.

- (a) An approval was granted by the Board of Trustees on 02 August 2013 for a medical scheme to the employees and their 03 other family members under a maximum reimbursement amount of Rs.500,000 per employee without obtaining proper approval from the General Treasury.
- (b) An incentive payment of Rs.1,474,909 had been paid the employees of the Fund in the year under review to. The following matters were observed in this connection.
 - (i) The approval of the Department of Management Services had not been obtained for the Incentive Scheme.
 - (ii) Information on the manner that the incentive was calculated had not been furnished to audit.
 - (iii) An evaluation on the performance had not been carried out before payment of the incentives.

4.4 Transactions of Contentious Nature

The following observations are made.

- (a) A loan of Rs. 97 million had been provided to a private company during the year under review in contravenes to the objective of the Fund. Further, the approval from the General Treasury had not been obtained in this regard and no agreement had been entered into with the above company with regard to repayments of this loan.

Out of the above loan, cheques worth Rs. 60,565,177 and Rs. 10,411,450 had been drawn in favour of 42 suppliers of that private company and 16 personal accounts respectively.

- (b) A loan of Rs. 100 million had been granted to the State Development and Construction Corporation (SD&CC) during the year 2009. Out of that, sums aggregating Rs. 79.2 million had been settled by the SD&CC as capital portion. However, no interest had been received on the loan up to the date of this report even though an interest of Rs.93.51 million receivable from the SD&CC as at 31 December 2017.

According to letter No. MF – 0046 dated 2018 February 07 issued by the Chief Executive Officer of the Fund, it was requested the SD&CC, settle immediately an amount of Rs. 114.31 million (capital portion of Rs. 20.8 million and interest of Rs. 93.5 million) to the Fund. However, the outstanding capital portion of Rs.20.8 million had been written off from the books of accounts in terms of decision taken by the Board of Management of Fund on 04 June 2015 without obtaining proper approval from the General Treasury. In the meantime, the total outstanding of Rs. 114.31 million had been shown as payable to the Fund in the financial statements of the SD&CC as at 31 December 2017.

4.5 Staff Administration

The following observations are made.

- (a) Even though all statutory bodies should restructure their organizational structure in terms of Public Enterprises Circular Letter No. PED/PU of 08 July 2009 and in compliance with the Management Services Circular No.30 of 22 September 2006 and action should be taken to revise the Schemes of Recruitment and Promotions, Cadre and the Salary Scales and obtain the recommendations of the National Salaries and Cadre Commission and the approval of the Department of Management Services, action had not been taken by the Fund in terms of the Circular.
- (b) The Fund had recruited 6 officers on contract basis (Out Sources) without obtaining required approval from the Department of Management Services and out of these officers only one officer had been paid cost of living allowances and incentive payment without prompt reasons.
- (c) The Fund had failed to introduce a proper mechanism for granting annual salary increment to its staff. As a result, the annual salary increment ranging from 0.21 per cent to 12 per cent on their salaries and wages had been given in the year under review.
- (d) An officer who exceeded the age of 60 years had been deployed as a permanent staff with the approval of the Board of Trustees contrary to Public Enterprises Circular No. 60 of 29 April 2011

5. Accountability and Good Governance

5.1 Internal Audit

An Internal Audit Unit had not been established in terms of the Financial Regulation 133 of the Financial Regulations of the Democratic Socialist Republic of Sri Lanka and the Management Audit Circular No. DMA/2009(1) of 09 June 2009 and an audit had not been carried out even by the Internal Audit Unit of the Ministry.

5.2 Audit Committees

No meeting of the Audit and Management Committee had been held in terms of Section 7.4.1 of the Public Enterprises Circular No. PED/12 of 02 June 2003. Further, the officers of the Fund had not been attended for the Audit and Management Committee meetings of the Ministry.

5.3 Tabling of Annual Reports

The Annual Reports from the year 2002 to 2016 had not been tabled in Parliament in terms of Section 6.5.3 of the Public Enterprises Circular No. PED /12 of 02 June 2003.

5.4 Budgetary Control

Significant variations were observed between the budgeted and the actual figures, thus indicating that the budget had not been made use of as an effective instrument of management control.

6. Systems and Controls

Deficiencies 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.

Areas of Systems and Controls

(a) Personnel Administration

(b) Financial Management

Observations

It was failed to obtain recommendations of the National Salaries and Cadre Commission and approval of the Department of Management Services by revising the Schemes of Recruitment and Promotions, Cadre and the Salary Scales.

Investments were made in fixed deposits and Treasury Bills without obtaining the approval of the Secretary to the Treasury.