

1. Financial statements

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1.1 Qualified Opinion

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The audit of the financial statements of the National Engineering Research and Development Centre of Sri Lanka for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the statement of financial performance, statement of changes in equity and cash flow statement and notes to financial statements for the year then ended 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 and Finance Act, No. 38 of 1971. My comments and observations which I consider should be tabled in Parliament appear in this report.

In my opinion, except for the effects of 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 Centre as at 31 December 2020, and 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 (SLAuS). 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 determines 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 Centre'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 Centre or to cease operations, or has no realistic alternative but to do so.

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

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

#### 1.4 Scope of the Audit

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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:

- Appropriate audit procedures were designed and performed to identify and assess the risk of material misstatement in financial statements whether due to fraud or errors in providing a basis for the expressed audit 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.
- An understanding of internal control relevant to the audit was obtained in order to design procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Centre'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 Centre's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my audit 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 audit report. However, future events or conditions may cause the Board 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 Centre and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Centre has complied with applicable written law, or other general or special directions issued by the governing body of the Centre;
- Whether the Centre has performed according to its powers, functions and duties; and
- Whether the resources of the Centre had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

## 1.5 Audit Observations relating to the Preparation of Financial Statements

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### 1.5.1 Internal Control over the Preparation of Financial Statements

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The Centre is 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.

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

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	Audit Observation -----	Comment of the Management -----	Recommendation -----
(a)	The sum of Rs. 7,011,595 including the value of bonds recovered with respect to the period 2007-2011 and the interest received thereon after being banked, was considered to have belonged to the Consolidated Fund, and the Treasury retrieved that sum. Out of the sum so obtained, the value of Rs. 6,676,014 credited to the Accumulated Fund in the preceding years, was written off against the revenue as an expenditure of	The said bond income was brought to accounts in the relevant years of accounts before being temporarily invested in the call deposits and the State Institute Surplus Fund. What is shown in the accounts of the current year was the write off of the loss sustained by the NERDC due to the value of deposits that was credited to the Consolidated Fund. Due to being identified as per the accounting principles that the	Balances relating to the preceding years should be adjusted on historical basis.

the year under review instead of being adjusted on historical basis in terms of Public Sector Accounting Standard 03. Accordingly, the deficit of the year under review was overstated by that value in the financial statements.

loss was sustained owing to the deprivation of assets, it was not considered as a previous year adjustment. Matters to be further disclosed in accordance with Section 54 of the Standard, 03, will be presented.

- (b) A sum of Rs. 33,867,115 remained unutilized from the capital grants of the Treasury received by the National Engineering Research and Development Centre for the year under review, and a sum of Rs. 43,612,678 that had remained unutilized over a period of 02 years, had been shown under capital contribution of the Treasury in the statement of financial position. However, no disclosures in that connection had been made by the Center contrary to Sri Lanka Public Sector Accounting Standard 11.
- The said unutilized sum relating to the year under review had been received by us on 30 December 2020 in respect of the then committed activities. The value totaling Rs. 43,612,678 and remaining unutilized over a period of 02 years had arisen due to inefficiency in the accounting procedure. Corrective measures will be taken thereon through adjustments.
- The necessary disclosures should be made in accordance with the Accounting Standards.
- (c) Corrections should be made in the accounting estimates by identifying the useful life of assets in terms of Sri Lanka Public Sector Accounting Standard 03. However, due to failure in doing so, the useful life of infrastructure facilities costing Rs. 116,014,265 and still in use despite being fully depreciated, had not been brought to financial statements after being revalued.
- Action will be taken in due course to show the fair value of those fully depreciated assets through a revaluation.
- The useful life of assets still in use despite being fully depreciated, should be revalued and shown in the financial statements.

### 1.5.3 Accounting Deficiencies

Audit Observation	Comment of the Management	Recommendation
<p>(a) Although a sum of Rs. 148,653,535 had been shown in the financial statements as being the capital contribution received from other Government entities, a schedule in that connection had not been included in the financial statements. Furthermore, the Center had not identified a policy to be followed in deducting the carrying cost on the Property, Plant and Equipment purchased from that contribution thus recognizing that value as a <b>revenue</b>.</p>	<p>This was a result of an omission. Corrective measures will be followed in the ensuing year to ensure accuracy in accounting.</p>	<p>The necessary schedules should be maintained properly, and the required accounting policies should be identified.</p>
<p>(b) The sum of Rs. 5,452,216 being the value of capital works in progress during the year under review had not been separately shown in the statement of financial position; instead, that sum had been added to the value of Property, Plant and Equipment, and shown in the financial statements. As such, the value of Property, Plant and Equipment had been overstated by that value in the year under review.</p>	<p>Due to the possibility in adding the value of capital works in progress to that of the Property, Plant and Equipment, the said value had not been shown in the statement of financial position separately. However, for the sake of clarity, action will be taken in the ensuing year to separately show that value in the statement of financial position.</p>	<p>The financial statements should be prepared in a manner so that works in progress and capital works would be separately identified.</p>

## 2. Financial Review

### 2.1 Financial Results

The operating result of the year under review was a deficit of Rs. 42,242,355 as compared to the corresponding deficit of Rs. 5,269,474 in the preceding year thus observing a deterioration of Rs. 36,972,881 in the financial result. Decrease in other revenue and increase in administrative expenses as against the preceding year, had mainly attributed to the said deterioration in the financial result.

3. Operating Review

3.1 Operating Inefficiencies

Audit Observation	Comment of the Management	Recommendation
(a) The decisive factors such as, technical issues and obtaining raw materials had not been taken into consideration when deciding on project duration. Accordingly, the periods of 04 projects scheduled to be completed in the year 2020 had been extended by 01 to 05 years.	Given the nature of research projects in progress, research activities are also carried out. As such, it is difficult to accurately decide on the project duration. The period so decided, changes oftentimes. Nevertheless, we have been instructed by the Board of Directors that action be taken to complete the researches within the period specified. As such, all the measures will be taken in due course to complete the projects on time.	Project duration should be decided by taking into account the practical issues.
(b) Action had not been taken to obtain patents, issue licenses, or provide for use with respect to 04 technical innovations made in the year 2020 at a cost of Rs. 1,731,860. Those innovations are essential as well as crucial for the present day society, thus observing that the said technologies should be put into practical use without delay.	It is not possible to obtain patents for all the technologies, instead, action will be taken to obtain patents for the possible ones. Transfer of technologies relating to the innovations will be done in due course.	Patents should be obtained whenever possible, and the new innovations should be put into social use without delay.
(c) Licenses are issued to the entrepreneurs in view of new technologies invented by the Center so that such innovations would be used practically. However, lack of interest in renewing such licenses was observed with the entrepreneurs due to reasons such as, failure of the Center	Response of the licensees received for renewal of licenses during the particular period remained poor. Furthermore, some of the entrepreneurs had obtained the technologies on the spur of the moment without dedication to further improve the technologies.	Once licenses are issued to the entrepreneurs, follow up action should be taken with necessary instructions given, thus encouraging them to renew the licenses.

in taking follow up action after issuing licenses for the technologies and giving instructions for further improvements. Although there were 102 licensees at the beginning of the year under review, only 63 of them renewed the licenses.

The delay or failure in the renewal of licenses had been caused by the economy of the entrepreneurs being adversely affected by the spread of the pandemic. Action has been taken to ensure follow up action on the licensees, and instructions are given to them whenever necessary.