

## **State Development and Construction Corporation - 2021**

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### **1. Financial Statement**

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#### **1.1 Qualified Opinion**

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The audit of the financial statements of the State Development and Construction Corporation (“Corporation”) for the year ended 31 December 2021 comprising the statement of financial position as at 31 December 2021 and 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 and Finance Act No. 38 of 1971. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the accompanying financial statements give a true and fair view of the financial position of the Corporation as at 31 December 2021, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

#### **1.2 Basis for Qualified Opinion**

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My opinion is qualified 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 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 Corporation’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 Corporation or to cease operations, or has no realistic alternative but to do so.

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

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Corporation 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 Corporation.

#### **1.4 Audit Scope**

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

## 1.5 Audit Observation on preparation of Financial Statements

### 1.5.1 Non-Compliance with Sri Lanka Accounting Standard

| Non Compliance with the reference to particular Standard  | Management Comment   | Recommendation  |
|---|--|---|
| <p>(a) <b>LKAS 08 – Accounting Policies, Changes in Accounting estimates and errors</b></p> <p>The comparative information had not been restated and the relevant disclosures had not been done in respect of the prior year adjustment of Rs.5,785,978 made in the changes in equity statement during the year under review as per the section 45 and section 49 of LKAS 08.</p> | <p>Actions will be taken.</p>  | <p>The Corporation should ensure that the entity is adherent with Sri Lanka Accounting Standards.</p> |
| <p>(b) <b>LKAS 16 – Property, Plant and Equipment.</b></p> <p>Fully depreciated Computer Accessories and Software, Office Furniture, Machinery and</p>  | <p>Asset revaluation has been done in the year 2021 and actions are being taken to get</p> | <p>The Corporation should ensure that the entity is adherent with Sri Lanka</p>                       |

Equipment, Motor Vehicle and Other Assets costing to Rs.8,521,619 , Rs.7,355,774 , Rs.101,121,258 , Rs.194,103,638 and Rs.65,999,216 respectively are being continuously used by the Corporation without reassessing the useful economic lifetime of those assets and accounted them accordingly as per the provisions in Section 51 of LKAS 16 – Property, Plant and Equipment.

the revalued amounts in to the financial statements in the year 2022.

Accounting Standards.

**(c) SLFRS 10 - Consolidated Financial Statements**

Devcoshowa (Pvt) Ltd, the fully own subsidiary of the Corporation had been inactive for a long time and the board had taken a decision to wind up the company in the year 2006. The winding up process was not get completed and the consolidated financial statements were not prepared by the corporation.

Devcoshowa (Pvt) Ltd, had been inactive for a long period of time and consolidated accounts had not been prepared since its incorporation. By now it is in the liquidation process.

The Corporation should ensure that the entity is adherent with Sri Lanka Accounting Standards.

**1.5.2 Accounting Deficiencies**  
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| <b>Audit Issue</b><br>-----   | <b>Management Comment</b><br>-----  | <b>Recommendation</b><br>-----   |
|---|---|--|
| (a) According to section 02 of the Economic Service Charges Amendment Act No.13 of 2015, Economic Service Charges (ESC) and surcharges there on amounting to Rs.64,158,596 and Rs.13,654,032 respectively had not been paid or brought to the financial statements for the year 2021. | Due to the financial difficulties faced by the corporation, it has not been able to pay the Economic Service Charges (ESC). A request has been made to the Inland Revenue Department through the ministry of finance to waive off ESC surcharges. | Necessary measures to be initiated to ensure the accuracy and reliability of accounting treatments made in the financial statements. |
| (b) Debit balance of Rs.80,335,283 shown as the Salaries and wages control Account under Sundry Debtors had not been settled by the end of year under review.   | Actions will be taken to rectify the salary payable account and salary control account in the year 2022.  | Necessary measures to be initiated to ensure the accuracy and reliability of accounting treatments made in the financial statements. |
| (c) The surcharge of Rs.25,871,900 imposed on the contributions payable to the EPF for the year 2020 and 2021, had not been accounted in the financial statements.  | Actions will be taken to account the EPF surcharge in the financial statement year 2022.  | Necessary measures to be initiated to ensure the accuracy and reliability of accounting treatments                                   |

made in the financial statements.

- (d) Evidence was not provided regarding capital grant of Rs.53,000,000 received from treasury to verify whether the amount was a Government grant or Loan. The Rs.53,000,000 has been provided as a recurrent grant during the COVID period and in the accounts this will be rectified as a recurrent grant. All documentary evidence should be submitted for audit to satisfactorily vouch and accept the transactions and amount shown in the financial statements.

### 1.5.3 Documentary Evidences not made available for Audit

Since supporting documents were not provided for the following balances, it was unable to ensure the accuracy and validity of such balances.

| Item of Account                     | Value<br>(Rs.) | Evidence not made available          | Management Comment  | Recommendation   |
|-------------------------------------|----------------|--------------------------------------|---|--|
| (a) Creditors balance               | 43,829,526     | Individual schedule and age analysis | Rs.43,829,526 is the creditor balance long outstanding unidentified and a report will be presented to take actions in the future. | All documentary evidence should be submitted for audit to satisfactorily vouch and accept the transactions and amount shown in the financial statements. |
| (b) Letter of credit Margin Account | 114,127,998    | Detail schedule                      | Actions will be taken to provide schedules.   |  |
| (c) Sub contract advances           | 15,299,042     | Detail schedule                      | Actions will be taken to provide schedules.   |  |
| (d) Due to customer                 | 131,756,060    | Detail schedule and Age Analysis     | Actions will be taken to provide schedules.   |  |
| (e) Trade Creditor –                | 19,393,442     | Detail schedule and                  |   |  |

|     |                                   |             |                                  |   |  |
|-----|-----------------------------------|-------------|----------------------------------|---|--|
|     | Debit Balances                    |             | Age Analysis                     | Actions will be taken to provide schedules.   | All documentary evidence should be submitted for audit to satisfactorily vouch and accept the transactions and amount shown in the financial statements. |
| (f) | Sundry Creditors – Debit Balances | 2,620,086   | Detail schedule and Age Analysis | Actions will be taken to provide schedules.   |  |
| (g) | Sundry Debtors                    | 29,563,152  | Detail schedule and Age Analysis | Actions will be taken to provide schedules.   |  |
| (h) | Sundry Creditors                  | 278,652,082 | Detail schedule and Age Analysis | Long outstanding unidentified and a report will be presented to take actions in the future. |  |

**1.6 Accounts Receivable and Payable**

**1.6.1 Receivables**

| <b>Audit Issue</b>  | <b>Management Comment</b>   | <b>Recommendation</b>                                       |
|---|---|---|
| Debtor balances of Rs.587,623,905 had remained over 03 years without being recovered. Effective actions had not been taken to recover those debtors other than the provisioning for the doubtful debts. | The corporation is in the process of collecting the remaining receivable amounts. | Action should be taken to recover the outstanding balances. |

**1.7 Non-compliance with Laws, Rules, Regulations and Management Decisions etc.**

| <b>Reference to Laws, Rules Regulations etc.</b>       | <b>Non-compliance</b>   | <b>Management Comment</b>   | <b>Recommendation</b>  |
|--|---|---|--|
| (a)Public Enterprises Circular No PED 01/2018 Dated 18 | According to the circular approval of the Director General of the public enterprise should be | The purchase of the bus was happened during the COVID period as an urgent | Due attention to be paid to comply with Laws, Rules, Regulations and |

|                |   |   |                           |
|----------------|---|---|---------------------------|
| September 2018 | obtained for purchasing motor vehicles, but such an approval had not been obtained for the purchase of a bus valued at Rs.4,350,000 during the year under review. | requirement to provide transport to the employees and as per the circular of Public Enterprise a letter has been sent on 02 May 2022 to obtain the approval of the Director General of the Public Enterprise. | Management Decisions etc. |
|----------------|---|---|---------------------------|

|   |  |  |  |
|---|--|--|--|
| (b) Management audit<br>Circular No:<br>DMA(2)2009/ Dated 01<br>July 2009 | Required Details of the Assets register had not been included. | Actions are being taken to include all required details in the asset register in the year 2022 with the revaluation of assets. | Due attention to be paid to comply with Laws, Rules, Regulations and Management Decisions etc. |
|---|--|--|--|

**1.8 Cash Management**  
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| <b>Audit Issue</b><br>-----   | <b>Management Comment</b><br>-----   | <b>Recommendation</b><br>-----  |
|---|--|---|
| The bank loan outstanding balance as at 31 December 2021 was of Rs.1,844 million and the interest expense for those loans Rs.200 million. As the loan and borrowing had increased by Rs.415.67 million or 29 per cent as against the preceding year, the financial position will be further weaken in case of the corporation failing to earn sufficient profit through the projects in the future. | Audit finding is correct. The corporation had to obtain huge amount of loans in the last years due to the working capital requirements and as a result, corporation had to pay huge interest cost for the loans. | Actions should be taken to minimize interest expenses by using suitable strategies. |

**1.9 Non- compliance with Tax Regulations**  
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| <b>Audit Issue</b><br>-----  | <b>Management Comment</b><br>-----   | <b>Recommendation</b><br>-----                 |
|--|--|--|
| (a) The value added tax had totaling to Rs.1,111,086,511. not been paid since 2002   | Due to the financial difficulties faced by the corporation VAT and NBT had remained unsettled. | Corporation should be comply with the tax law. |
| (b) Nation Development Tax totaling to Rs.6,342,105 had remained over ten years without been settled as at 31 December 2021. | Due to the financial difficulties faced by the corporation VAT and NBT had remained unsettled. | Corporation should be comply with the tax law. |

## 2. Financial Review

### 2.1 Financial Result

Operations of the Corporation during the year under review had resulted in a pre-tax net profit of Rs.43,124,611 as compared with the corresponding pre-tax net loss of Rs.257,420,711 for the preceding year, thus indicating a severe increase of Rs.300,545,322 in the financial results for the year under review. Increasing of revenue and decreasing other expenses were the main reason for attributed for this financial result.

## 3. Operational Review

### 3.1 Operational Inefficiencies

| <b>Audit Issue</b>  | <b>Management Comment</b>  | <b>Recommendation</b>                            |
|---|--|--|
| (a) Although six bridge construction projects valued at Rs.265.69 million had been expected to complete during the year under review, actual projects progress was below 65 per cent.   | The expected level of completion of the construction projects has not been able to achieve as a result of COVID situation in the country, difficulties in finding materials, environmental problems, changes in planned construction work and difficulties in obtaining approvals for the variations in the agreement. | Action should be taken in accordance with plans. |
| (b) A number of 144 rural bridge construction projects valued at Rs.2,184.85 million had been shown without expected physical projects progress and, out of them 72 projects valued at Rs.1,108.82 million indicated actual progress below 50 per cent by the end of the year under review. | The expected level of completion of the construction projects has not been able to achieve as a result of COVID situation in the country, difficulties in finding materials, environmental problems, changes in planned construction work and difficulties in obtaining approvals for the variations in the agreement. | Action should be taken in accordance with plans. |
| (c) Although six road projects valued at to Rs. 839.68 million had been expected to be completed during the year 2021, it was observed that these projects had not been completed even as at 31 December 2021   | The expected level of completion of the construction projects has not been able to achieve as a result of COVID situation in the country, difficulties in finding materials, environmental problems, changes in planned construction work and  | Action should be taken in accordance with plans. |



difficulties in obtaining approvals for the variations in the agreement.

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|--|--|--|
| (d) Six building construction projects valued at Rs. 416.89 million that should have been completed by year 2020, had not been completed up to 31 December 2021, and the physical progress thereof remained less than 60 per cent by 31 December 2021. | The expected level of completion of the construction projects has not been able to achieve as a result of COVID situation in the country, difficulties in finding materials, environmental problems, changes in planned construction work and difficulties in obtaining approvals for the variations in the agreement. | Action should be taken in accordance with plans. |
| (e) A water supply and irrigation project valued at Rs.42.36 million and scheduled to be completed by 30 April 2020, indicated by physical progress at 75 percent only even by 31 December 2021.   | The expected level of completion of the construction projects has not been able to achieve as a result of COVID situation in the country, difficulties in finding materials, environmental problems, changes in planned construction work and difficulties in obtaining approvals for the variations in the agreement. | Action should be taken in accordance with plans. |
| (f) A total loss of Rs.189,977,006 had been identified from 42 projects as at 31 December 2021.  | Difficulties faced due to COVID 19 Pandemic, delay in customer payments, environmental problems (flood), high material cost and financial difficulties faced by the Corporation were the main reasons for the loss making projects.  | Action should be taken in accordance with plans. |

### 3.2 Underutilized Property, Plant and Equipment

| Audit Issue<br>-----  | Management Comment<br>-----   | Recommendation<br>-----   |
|---|---|---|
| It was observed during the physical inspection carried out at the head office in Ratmalana, that there are machinery and equipment valued at Rs.10,392,151 remained idle. | The actions have already been taken to sell these unserviceable assets. | Action should be taken to ensure that assets are properly utilized. |

### 3.3 Human Resources Management

| <b>Audit Issue</b><br>-----  | <b>Management Comment</b><br>-----   | <b>Recommendation</b><br>-----   |
|--|--|--|
| (a) The approved cadre of the Corporation as at 31 December 2021 was 489 while the actual cadre was 634. Accordingly, this shows an excess recruitment of 145 employees to the Corporation to the various positions. | The Corporation had to recruit staff on contract basis based on the labour requirement of the construction work carried out.                 | Action to be taken to ascertain realistic cadre levels, followed by reviews on a periodic basis. |
| (b) Two post of senior management in the corporation had remained vacant as at 31 December 2021.   | A request has been made to the Management Service Department to get the approval to fill these two vacancies.                                | Action to be taken to ascertain realistic cadre levels, followed by reviews on a periodic basis. |
| (c) The approved cadre for civil engineers was 19, however 85 Civil Engineers had been recruited as contract basis.  | The Corporation had to recruit staff on contract basis based on the labour requirement of the construction work carried out.                 | Action to be taken to ascertain realistic cadre levels, followed by reviews on a periodic basis. |
| (d) The 22 Security Guards had been recruited exceeding the approved cadre.  | The Corporation had to recruit security staff to safeguard the assets in project sites in different regions in the country in the year 2021. | Action to be taken to ascertain realistic cadre levels, followed by reviews on a periodic basis. |