

## National Defence Fund - 2022

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### **1. Financial Statements**

#### **1.1 Qualified Opinion**

The audit of the financial statements of the National Defence Fund for the year ended 31 December 2022 comprising the statement of financial position as at 31 December 2022 and the statement of comprehensive income, 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 financial statements give a true and fair view of the financial position of the fund as at 31 December 2022, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

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

I expressed qualified opinion 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**

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 Fund's stability 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 Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the fund's financial reporting process. As per Sub Section 16 (1) of the National Audit Act No. 19 of 2018, the Fund 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 Fund.

#### **1.4 Auditor's Responsibility for the Audit of the Financial Statements**

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

## 1.5 Audit Observations on the preparation of Financial Statements

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

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.

### 1.5.2 Accounting Deficiencies

Audit Observation	Management Comment	Recommendation
(a) During the year under review, a fixed deposit amounting to Rs. 53,314,521 had been matured and reinvested as Rs. 54,389,574, but it had been shown in the financial statements as at 31 December 2022 as Rs. 53,314,521, so the investment and investment interest income of the year under review, had been understated by Rs. 1,075,054 each.	Noted to correct the new value as Rs.54,389,574 after maturity of fixed deposits.	Correct values relevant to the year should be accounted.
(b) A fixed deposit of Rs. 200 million had withdrawn before maturity on 2 <sup>nd</sup> August 2022 and for that the interest income of Rs. 1,464,152 received for 213 days of the year under review had been adjusted to the previous year's profit. Accordingly, the investment income of Rs. 1,464,152 had not reflected in the accounts in the year under review.	An amount of Rs. 1,989,041 as interest income receivable on 31.12.2021 related to this deposit has been shown in the previous year's financial statements. The interest income of Rs.1,910,959 received from the said fixed deposit on 02.08.2022 had been adjusted to the interest income receivable of the previous year and the difference of Rs.78,082 to the accumulated fund.	The income received in respect of the year under review should match the income of that period.
(c) Rs. 109,706 had been returned from the administrative expenses given to the Police Department and the Sri Lanka Air Force in the year 2022, but it was adjusted to the profit of the previous year. As a result, the expenditure for the year under review had been overstated by that amount.	Since the administrative expenses money given to the Police Department and the Air Force in the year 2022 was a refund of the administrative money given in relation to the Meth Sevana Project in the year 2021, the money had been adjusted to the previous year.	Since it was accounted as an expense incurred during the year, the amount returned should match that period.
(d) It had been stated that the value of a printer and two computer Monitors worth Rs. 330,000,	The governing board of the Fund had approved the provision of	Control procedures should

which were purchased without approval by using the money given to the Sri Lanka Air Force for the administrative expenses of the half-housing project, should be recovered from the Sri Lanka Air Force, but it had not been identified as a receivable of the Fund and accounted as an administrative expense.

administrative expenses for fuel expenses, vehicle rental and stationery expenses incurred by the armed forces and the Sri Lanka Police in relation to the half-housing project, but the approval of the governing board had not been obtained for the purchase of the printer and computer screens. The amount will be recovered from the Sri Lanka Air Force.

### 1.5.3 Documentary Evidences not made available for Audit

Item	Amount Rs.	Evidence not available	Management Comment	Recommendation
Payment of housing Assistance premiums.	48,936,509	Even though, a sum of Rs. 101,426,861 had released to the accounts of the Three Armed Forces and the Police, for the payment of Housing Assistance premiums to 150 selected beneficiaries under the Meth Shevana Half-Housing Project, documents confirming that Rs. 48,936,509 payable to 82 beneficiaries were received by those beneficiaries during the year under review were not submitted.	As indicated by the audit in the year 2021, the supporting documents are currently being brought from tri forces and the relevant beneficiaries, and the supporting reports have already been submitted to the audit. There are further supporting reports to be received, and arrangements will be made to submit the reports to the audit as soon as they are received.	A system should be implemented to ensure that the housing assistance money paid has been received.

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

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
Financial Regulations 877 (2) (d) and the Guidelines 04 as amended by Public Finance Circular No. 01/2020 and dated 28 August 2020.	At the end of each quarter, so that the progress of the fund can be reviewed, a quarterly report on the main functions of the Fund should be prepared and submitted to the Auditor	Kindly inform that quarterly reports will be submitted to the Auditor in terms of Financial Regulations 877(2) (d).	Should be followed the amended Financial Regulation 877(2) (d) and guidelines 04 by the Public Finance Circular No. 01/2020

General 15 days before the end of the quarter, but those reports were not submitted for the audit for the year 2022.

dated 28 August 2020.

## 1.7 Investment Management

Audit Observation	Management Comment	Recommendation
(a) After incurring Fund's expenses from fixed deposit withdrawals and other income, though the further excess money could be invested in short-term investment opportunity, an excess amount of Rs.1,200,000 for the period of 4 month of January to April 2022, and Rs. 4,000,000 for the period of 07 month from May to 31 December 2022 had been remained in a current account without investing.	Since the income is not sufficient for the payments of the housing project, fixed deposits enchased and kept in a current account to make the payments. Actions are taken to invest such money in a way of effective without underutilization.	A proper plan should be implemented to incurring expenses and investment of surplus funds.
(b) Due to the risen of interest rates in the country in May 2022, Rs. 616.96 million fixed deposits which invested at low interest rates, had been withdrawn before maturity and reinvested on 02 <sup>nd</sup> and 10 <sup>th</sup> August 2022. Due to the delay of more than two months in making decisions regarding these reinvestments, the advantage of the increase in interest rates had not utilized optimally. Accordingly, the estimated interest income lost for 72 days of delay was over Rs. 22 million.	Bank interest rates began to rise from May 2022, at which time the National Defence Fund was under the State Ministry of Defence. No fixed deposit reinvestment had been done during that period. Special Gazette of the Democratic Socialist Republic of Sri Lanka No. 2283/34 and dated 09.06.2022 scheduled the National Defence Fund under the purview of the Ministry of Defence. After that, fixed deposits which were under low interest rates were arranged to reinvest under higher rates. The interest rate in May 2022 was also gradually increasing and at the time of reinvestment in August 2022 by the Fund, the interest rate was at 26%.	As the main source of income of the Fund is interest income, proper investment management should be implemented.

## 2. Financial Review

### 2.1 Financial Result

The operating result of the year under review amounted to a deficit of Rs. 17,189,698 and the corresponding deficit in the preceding year amounted to Rs. 34,987,345. Therefore an improvement amounting to Rs.17,797,647 of the financial result was observed. This growth was mainly due to the increase in fixed deposit interest income.

### 3. Operational Review

#### 3.1 Operational Inefficiencies

<b>Audit Observation</b>	<b>Management Comment</b>	<b>Recommendation</b>
(a) Even though it was planned to pay Rs.112.50 million to 150 beneficiaries in the amount of Rs. 750,000 each, in order to complete the half-built houses of war heroes under the Meth Sewana Half House Project of year 2022, had failed to pay any installment during that year. Also, the third installment for 30 housing beneficiaries in the year 2021 had not been paid by 31 December 2022. Delayed payments and delayed construction in the years 2020 and 2021 had affected this.	<p>Due to the epidemic situation since the year 2020, the housing projects related to the respective years could not be completed within those years. As a result, the first installment of the half-house project for the year 2021 was delayed to February 2022. Due to the increase in the price of raw materials due to the economic crisis in the country during that time, the house construction work was delayed.</p> <p>In the year 2023, the Board of Governors has approved the coverage to be implemented as one project including these beneficiaries.</p>	Efforts should be made to achieve expected targets.
(b) According to the action plan of 2022, although, it was planned to award scholarship of Rs. 25,000 each to 140 students who passed the Grade 5 Scholarship Examination in 2021, for the children of dead and disabled war heroes, the scholarships had not been awarded by the end of the year .	In the year 2021, 80 children of war heroes who passed the scholarship examination have been selected and arrangements are currently being made to grant the scholarship as soon as possible.	Efforts should be made to reach the expected targets planned for each year and to provide timely benefits to the students.

#### 3.2 Transactions of Contentious Nature

<b>Audit Observation</b>	<b>Management Comment</b>	<b>Recommendation</b>
Although the Half housing installments of Rs.4,719,806 to be paid to the beneficiaries of the Sri Lanka Air Force should be released to the beneficiaries through an official account of the Sri Lanka Air Force, the payments were made through an external fund maintained by the name of "Central Welfare and Rehabilitation Fund", which had not confirmed as an official account.	In order to provide installments to the beneficiaries without delay, the Sri Lanka Air Force has requested to transfer the money related to the "Meth Sewana" housing project to the Central Welfare and Rehabilitation Fund, and kindly informed that the approval of the Governing Board has been received for the same.	It is recommended that the Fund directly pay the benefits or release the money through an account with full confirmation that it is accountable for public funds.

### 3.3 Under -utilization of Funds

<b>Audit Observation</b>	<b>Management Comment</b>	<b>Recommendation</b>
The investment opportunity had been missed as Rs. 1,490,066 belonging to the Fund remained idle in the custody of the Police Department and the Sri Lanka Navy for almost 03 years due to giving money for administrative expenses annually without considering the actual expenditure of the previous year.	After providing funds for the administrative expenditure to the respective forces as their needs, if there is any remaining amount to settle the accounts at the end of the year or the bills related to the amount spent will be brought. Kindly informed that at the end of each year, the remaining money for administrative expenses will be collected.	Administrative expenses should be given considering the actual expenditure of each year and proper investment management should be implemented.

## 4. Accountability and Good Governance

### 4.1 Tabling of Annual Performance Report in Parliament

<b>Audit Observation</b>	<b>Management Comment</b>	<b>Recommendation</b>
According to Section 13 of the National Defence Fund Act No. 9 of 1985, the fund's financial statements and Auditor General's report had not been tabled in Parliament from 2018 to 2021.	Until the year 2017, the National Defence Fund was under the Ministry of Finance, and as soon as the Auditor General's report for the year 2017 is tabled in the Parliament by that Ministry and notified to this Ministry, it is hereby notified that the Auditor General's reports from the year 2018 to 2022 will be tabled in the Parliament.	Action should be taken as per the provision of section 13 of the National Defence Fund Act No. 9 of 1985.