

1. Financial Statements

1.1 Opinion

The audit of the financial statements of the Securities and Exchange Commission of Sri Lanka (“Commission”) for the year ended 31 December 2022 comprising the Statement of Financial Position as at 31 December 2022 and the Statement of Financial Performance, Statement of Changes in net assets 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, the accompanying financial statements give a true and fair view of the financial position of the Commission 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 Opinion

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 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 Commission’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 intends to liquidate the Commission or to cease operations, or has no realistic alternative but to do so

Those charged with governance are responsible for overseeing the Commission’s financial reporting process.

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

1.4 Auditor's Responsibilities 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 Commission'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 Commission'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 Commission 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 Commission, and whether such systems, procedures, books, records and other documents are in effective operation;

- Whether the Commission has complied with applicable written law, or other general or special directions issued by the governing body of the Commission;
- Whether the Commission has performed according to its powers, functions and duties; and
- Whether the resources of the Commission had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

2. Financial Review

2.1 Financial Results

According to the financial statements presented, the operations of the Commission had resulted in a deficit of Rs. 331.2 million before taking into account the transfers from the Cess Fund towards net operational expenditure and it was reported the deficit of Rs. 352.5 million for the preceding year. The main reason for decreasing the deficit by Rs. 21.3 million or 6 per cent as compared with preceding year was the increase of grant received during the year under review by Rs. 67.4 million under the Financial Sector Modernization Project.

2.2 Trend Analysis of major Income and Expenditure items

Analysis of major income and expenditure items of the Commission during the year under review, as compared with the preceding year are shown below.

	2021	2022	Difference as a percentage
	Rs.	Rs.	%
<u>Income of the Commission</u>			
Interest Income	1,820,617	717,743	(60.5)
Government Grant (FSMP)	104,804,128	172,252,739	64.3
<u>Expenditure of the Commission</u>			
Staff Salaries	148,721,963	160,983,569	8.2
Staff Welfare and Other Staff Related Payments	30,933,949	37,965,470	22.7
Staff Vehicle Allowance	26,662,653	25,881,000	(2.9)
Staff Medical Expenses & Insurance	15,350,619	16,113,521	4.9
Overseas Training and Travelling	0	7,081,485	100
Rent & Car Park Rental	101,143,670	110,895,458	9.6
Capital Market Development Expenses - Total	55,241,934	50,328,063	(8.9)
• Capital Market and Product Development	14,862,714	19,050,659	28.1
• Public Awareness Programmes	24,840,257	10,278,137	(58.6)
• Educational Programmes	1,802,431	1,678,495	(6.8)
• International Membership Fees – IOSCO	4,210,388	7,334,807	74.2
• Publicity and Advertising	146,664	147,015	0.2
• Market Surveillance Cost	9,349,152	11,820,060	26.4

- a. As part of the Financial Sector Modernization Project (FSMP) funded by the World Bank, the Commission stands to gain approximately USD 10 million; USD 2 million under result based financing component and USD 8 million under the Investment based financing component. As at the end of the year under review, the Commission received Rs.369.30 million in total (Rs. 81,124,254 in 2019, Rs. 11,720,560 in 2020, Rs.104, 804,128 in 2021 and Rs. 171,674,294 in 2022) as part of Result Based financial component of the Project. Further, under Investment based Financing Component of the FSMP, the Commission had withdrawn USD 107,650 in order to pay for the local vendors in LKR and USD 197,303 had been directly paid to the foreign vendors as at 31 December 2022.
- b. Capital Market and Product Development expenditure for the year under review was Rs. 19.05 million and it was 14.86 million in the previous year reflecting an increase of Rs. 4.19 million or 28 per cent during the year under review. However, Public awareness program expenditure for the year under review was Rs. 10.27 million and it was Rs. 24.84 million in the previous year reflecting a decrease of Rs. 14.57 million or 59 per cent during the year under review. Further, total capital market development expenditure for the year under review was Rs. 50.32 million and it was Rs. 55.24 million in the previous year reflecting a decrease of Rs. 4.92 million in the year under review.
- c. As per the Section 156 of the Securities and Exchange Commission Act No. 19 of 2021, it is authorized to utilize the Cess imposed under the Act for the purpose of developing the securities market, meeting all expenditure incurred by the Commission in the management, administration and operation of the Commission in the exercise, performance and discharge of its duties and functions and other purposes.. Accordingly, it was observed that a sum of Rs. 331.26 million had been transferred from Cess Fund to finance the expenses of the Commission. Total expenditure of the Commission was Rs. 542.68 million and a sum of Rs. 50.32 million or 9.2 per cent of the total expenditure had been spent during the year under review for the capital market development activities.

3. Operating Review

3.1 Conducting of Investigations

Audit Observation	Management Comment	Recommendation
(a) According to the Section 16(r) of the Securities and Exchange Commission of Sri Lanka Act No. 19 of 2021, the Commission shall be to inquire and conduct investigations into any activity of a market institution, market intermediary, a registered person, a listed public company or a listed foreign entity. According to the information made available, the progress of conducting investigations is as follows.	<ul style="list-style-type: none"> • Over the period, investigation process was streamlined and time lines were given to complete the outstanding investigations expeditiously. At the beginning of the year, there were 70 matters pending comprising of full investigations, preliminary investigations, complaints and other special assignments. Further, the Commission had commenced 27 matters (25 fully-fledged 	Need to further expedite the investigation process.

Nature of investigation	As at 01.01.2022	Received during the year 2022	Completed as at 21 st July 2023	To be completed as at 21 st July 2023
Insider dealing in the shares of listed companies	14	7	9	12
Price/Market manipulation in the shares of listed companies	26	12	14	24
Price/Market manipulation and/or Insider Dealing in the shares of listed companies	5	1	0	6
Front Running	3	4	2	5
Contravention of Takeovers and Mergers Code	2	0	1	1
Other Contraventions	1	1	0	2
Preliminary Investigations carried out pursuant to a report submitted by another regulatory body	15	0	15	0
Special assignments /Complaints	4	2	6	0
Total	70	27	47	50

investigations and two special assignments) during the year

- The Commission had concluded 47 matters out of above as at 21 July 2023.
- Accordingly, there are 50 investigations in hand as at 21st July 2023.

(b) According to the Commission approved Investigation Manual, there was a Surveillance and Investigation Committee to decide whether an investigation inquiry is warranted on the receipt of complaint or referral. Further, Findings of the investigation were submitted to the Commission with recommendation by the Committee. However, such mechanism had not been included into the Surveillance/Investigation Enforcement Process Flowchart approved by the commission at its 457 meeting held on 14 December 2021. Accordingly, it was observed that each complaint/ referral should be investigated by the Investigation Division irrespective of the fact that such an inquiry is warranted on the matter. Therefore, in order to decide which matters warrant investigation and further expedite the investigation review process before the review of the Commission, it is proposed to establish an investigation oversight committee comprising the members of the Commission and members of the senior management as appropriate. It may help discuss the investigation reports with the officers who involved in the investigation process and submit its recommendations to the Commission's final approval enabling the Commission to make informed decisions.

Having considered the importance of streamlining the investigation process, number of investigations pending and its timely conclusion, an oversight committee comprising three Members of the Commission was formed pursuant to a decision of the Commission at its 487 Meeting held on 14 July 2023.

Need to further expedite the investigation review process with the oversight of the new committee.

3.2 Human Resources (HR) Management

Audit Observation	Management Comment	Recommendation
<p>(a) It was observed that the post of Director Capital Market Development, Director Surveillance, Director Legal, Director Human Resource and Information technology, three out of nine Assistant Directors, five out of nine senior managers, six out of sixteen managers, nine out of twenty two senior assistant managers and 20 out of 49 assistant managers, which are under the executive category of the approved Cadre of the Commission were remained vacant for a considerable period as at 25 July 2023. Remaining vacant of key managerial positions may have been effected to the effective functioning of the Commission.</p>	<p>The new Commission took steps to fill the vacancies during the reporting period. The Commission was of the view that in order to deliver enhanced performance under the new Act, it needs to attract, remunerate and invest in people with relevant specialized skills and competencies.</p> <p>Further, the Commission took note of the approval given to increase the cadre from 96 to 147 considering the highly specialized nature of the human resources required to carry out the functions of the Commission within the next 5 years beginning from March 2021.</p> <p>However, it became difficult to recruit suitable people even though positions were advertised, re-advertised and interviews were conducted multiple times over the period.</p> <p>Interviews were carried out to fill the positions of Chief Digital Officer, Assistant Director Human Resources, Director Legal and Assistant Managers during the recent past.</p>	<p>Need to fill the remaining vacant positions.</p>
<p>(b) An officer attached to the Commission had been interdicted from service with effect from 19 April 2016. However, an amount equivalent to half of his monthly gross salary excluding transport allowances and other benefits was paid contrary to Sub-Section 31.11 of the Establishment Code of the Democratic Socialist Republic of Sri Lanka. The half month salary cost incurred by the Commission on behalf of him from 20 April 2016 to 31 August 2018 was Rs. 5,212,815. As per the recommendation of the Committee on Public Enterprises (COPE) dated 18 September 2018, the Commission should stop paying salary and make arrangements to recover total paid salary. Accordingly, payment of half month salary was stopped with effect from</p>	<p>Consequent to the COPE recommendations, steps were taken by the Commission to stop half payment of salary paid to the interdicted officer from September 2018. Further, the said officer was informed to refund the half payment of salary paid to him during the period of his interdiction in terms of the COPE recommendation by letter dated 15 November 2018. Since he did not respond to the letter dated 15 November 2018, a further reminder was sent on 26 August 2019 which was acknowledged by him on 27 August 2019. However, he has not deposited the money to date.</p> <p>Further, the domestic inquiry instigated by the Commission with regard to the investigations conducted by officer interdicted is still pending before the</p>	<p>Need to recover the money paid contrary to Sub-Section 31.11 of the Establishment Code.</p>

September 2018 and the officer was Tribunal. informed to repay the above mentioned amount by letter dated 15 November 2018. However, it was not recovered by the Commission even up to 25 July 2023.

4 Accountability and Good Governance

4.1 Budgetary Control

Audit Observation	Management Comment	Recommendation																																
<p>Significant variances were observed between budgeted and actual expenditure items during the year under review in the following instances thus, indicating that the budget had not been made use of as an effective instrument of management control in following instances.</p> <table border="1"> <thead> <tr> <th style="text-align: left;">Item</th> <th style="text-align: center;">Budgeted for the year 2022</th> <th style="text-align: center;">Actual for the year 2022</th> <th style="text-align: center;">variance as a percentage</th> </tr> <tr> <td></td> <th style="text-align: center;">(Rs.)</th> <th style="text-align: center;">(Rs.)</th> <th style="text-align: center;">%</th> </tr> </thead> <tbody> <tr> <td>Public Awareness</td> <td style="text-align: right;">64,750,000</td> <td style="text-align: right;">10,278,137</td> <td style="text-align: center;">84</td> </tr> <tr> <td>Capital Market Development</td> <td style="text-align: right;">38,000,000</td> <td style="text-align: right;">19,050,659</td> <td style="text-align: center;">50</td> </tr> <tr> <td>Seminar fees</td> <td style="text-align: right;">3,241,000</td> <td style="text-align: right;">1,678,495</td> <td style="text-align: center;">48</td> </tr> <tr> <td>Foreign Training, Conferences</td> <td style="text-align: right;">25,000,000</td> <td style="text-align: right;">7,081,485</td> <td style="text-align: center;">72</td> </tr> <tr> <td>Subscription, Sponsorship and Local Training</td> <td style="text-align: right;">8,450,000</td> <td style="text-align: right;">3,363,804</td> <td style="text-align: center;">60</td> </tr> <tr> <td>EDP and Equipment Maintenance</td> <td style="text-align: right;">30,382,698</td> <td style="text-align: right;">21,744,149</td> <td style="text-align: center;">28</td> </tr> </tbody> </table>	Item	Budgeted for the year 2022	Actual for the year 2022	variance as a percentage		(Rs.)	(Rs.)	%	Public Awareness	64,750,000	10,278,137	84	Capital Market Development	38,000,000	19,050,659	50	Seminar fees	3,241,000	1,678,495	48	Foreign Training, Conferences	25,000,000	7,081,485	72	Subscription, Sponsorship and Local Training	8,450,000	3,363,804	60	EDP and Equipment Maintenance	30,382,698	21,744,149	28	<p>Public awareness expenditure This is mainly due to the economic and political instability prevailed in the country, which hindered the progress of such programmes. Some of the planned public awareness workshops and seminars were conducted through online means and it brought down the cost drastically.</p> <p>Capital market development expenditure Actual Capital Market Development expenditure significantly reduced due to not incurring cost on proposed broker back office system as requests were not made by the relevant parties during the period under review.</p> <p>Seminar Fees The capital market learning platform provides a learning opportunity to students who are interested in studying capital markets. During the year under review, the programmes could not be conducted due to the economic situation prevailed in the country.</p>	<p>Need to minimize the variance.</p>
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Foreign Training, Conferences, Subscription, Sponsorship and Local Training

The reason for the low expenditure in foreign training is mainly due to the line Ministry restrictions imposed on foreign travels. In addition, most of the regular foreign training programs and conferences were not done due to various reasons. However, Commission's staff attended some of the online sessions to acquire new knowledge in their respective areas of work and during the year some staff members obtained the study sponsorship facilities.

EDP and Equipment Maintenance

The actual amount is lower than the budgeted amount because the Commission managed to enter into maintenance agreements with few suppliers at a lower cost than what was budgeted.