

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Construction Guarantee Fund (“Fund”) for the year ended 31 December 2023 comprising the statement of financial position as at 31 December 2023 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 material accounting policy 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 provisions of the National Audit Act No. 19 of 2018 and provisions in Section 11 (d) of the Trust Deed of the Construction Guarantee Fund dated on 05 August 1999. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, because of the significance 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 Fund as at 31 December 2023, 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 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 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 Non-Compliance with Sri Lanka Public Sector Accounting Standards

Non Compliance with the reference to particular Standard	Management Comment	Recommendation
<p>Although the net income receivable from bonds and guarantees, as stated in the statement of financial position as at 31 December 2023 was Rs. 10.34 million, the age analysis further revealed that this balance includes a credit balance of Rs. 1.96 million, which had been overcharged from contractors. However, these credit balances were offset against the debtors' debit balances and reported in the statement of financial position, contrary to the paragraph 48 of Sri Lanka Public Sector Accounting Standard No. 01.</p>	<p>Thank you for pointing out and we will prepare the financial statements accordingly in the future.</p>	<p>Financial statements should be prepared in accordance with Sri Lanka Public Sector Accounting Standards.</p>

1.5.2 Accounting Deficiencies

Audit Observation	Management Comment	Recommendation
<p>(a) According to the statement of financial position the short-term and long-term fixed deposit balance as at 31 December 2023 was Rs. 1,635.23 million. However, as per the schedule, the balance was Rs. 1,635.28 million. As a result, difference of Rs. 0.05 million was observed.</p>	<p>Thank you for bringing this to our attention. The mentioned difference will be corrected in the following accounting year.</p>	<p>Accounting errors should be corrected</p>
<p>(b) Debtors had deposited Rs. 1.42 million in 05 bank accounts between 05 June 2018 to 28 September 2021. Those balances were not identified and stated as an unrecognized current liability in statement of financial position.</p>	<p>Over the past three years, we have made extensive efforts to identify previously unrecognized deposits and as a result, most of these deposits have now been identified.</p>	<p>Bank direct deposit should be identified and recorded correctly.</p>

1.6 Accounts Receivable and Payable

1.6.1 Receivables

	Audit Observation	Management Comment	Recommendation
(a)	The outstanding bills discounting balance as at 31 December 2023 was Rs.10.30 million. This was due to non-payment of bills by the employers. Out of which Rs. 10.21 million or 98 percent from one Construction company and the remaining 02 percent or Rs. 92,019 from another company was not recovered for more than 04 years.	The arbitration process has already been initiated to recover the funds provided to one of the construction company. Since the other organization has successfully completed the project, no funds to be recovered from that contractor. Therefore, it is approved to be classified as corporate social responsibility.	Actions should be taken to recover outstanding bills discounting balances from contractors.
(b)	The Fund issues Bonds and guarantees to registered contractors without keeping any security and employers demand guarantee money in the cases of poor performance of the contractors. From 2011 to 2019, an amount of Rs. 87.65 million was paid to the employers in 22 cases, out of this balance Rs. 4.67 million could not be recovered and was written off with the approval of the Board of Trustees in 2019. Further, from 2020 to 2022 the amount paid to the employers and to be recovered from contractors to the Fund was Rs. 30.16 million. In addition, in the year 2023 Rs. 26.67 million demanded to the fund. Accordingly, the sum paid by the Fund to the employers amounting to Rs. 139.80 million, had to be recovered back to the Fund by 31 December 2023. In this regard, the judgments of the legal actions including arbitration were in favour of the Fund but unable to recover the related money. The Fund had been spent Rs. 0.85 million for the legal proceedings related to this in the year under review.	After a technical assessment of demand maid by employers at several times due to various reasons, a sum of Rs. 150 million had paid by end of the year 2023. Although contractors were notified to reimburse the payment, in instances where they failed to do so, legal action was taken to recover the loss based on the guarantees they had provided.	The performance of contractors should be properly monitored, and the amounts due to the fund must be promptly recovered.

1.6.2 Payables

Audit Observation	Management Comment	Recommendation
<p>(a) The Ministry of Roads and Highways had given Rs.33,389 million to the Fund during 2020 to 2023 to pay the certified bills of 314 contractors carrying out the construction contracts under the 100,000 km rural road scheme, of which Rs. 32,782.47 million was released to the contractors. Furthermore, an amount of Rs. 220.62 million was retained by the Fund in the transit money account as of 31 December 2023 without being released to the relevant contractors. Out of this balance Rs.88.10 million was retained from 01 to 03 years and Rs.3.43 million from 03 to 05 years. An amount of Rs. 60.55 million, related to 123 completed projects, was retained by the fund without being released to contractors. Also, out of the money given to the Fund by various other parties to be released to the contractors amounting Rs. 27.77 million had not been settled to the respective contractors on 31 December 2023. Out of this balance the total of Rs. 7.08 million and Rs. 11.89 million was retained by the Fund from 01 to 03 years and 03 to 07 years respectively due to inadequate current performance of the respective projects. Therefore, the responsibility for future settlement of these amounts could not be ascertained in the audit. Thus, it was observed that it is problematic to retain the money given by the employers for settling the contractors' bills as transit money for a long period of time.</p>	<p>Under this project, all payments are processed through the fund to minimize the risk faces when providing guarantees. In cases where the risk has been minimized, funds are released after reviewing each contractor's individual project. As of now, more than 97 percent of the allocated funds have been released. Due to the associated risk, funds of several projects have been temporarily withheld until the liabilities are resolved.</p> <p>Since the contractors had not provided a completion report or returned the original guarantee issued by our institution, it was impossible to fully settle the accounts of the aforementioned projects. Therefore, additional time will be required to release the withheld funds.</p>	<p>In this regard, agreements or a Memorandum of Understanding (MOU) should be established with the Ministry of Highways and Road Development, and the withheld funds should be periodically settled.</p>
<p>(b) With the approval of the Board of Trustees, Rs. 5.79 million creditor balances, received from employers and retained by the fund for more than five years was recorded as miscellaneous income for the year under review, without contacting the creditors or settling the outstanding balances.</p>	<p>An amount of approximately Rs. 5.8 million was added to various income accounts with the approval of the Board of Trustees. In identified cases, it will be decided to reimburse these funds to the respective depositors.</p>	<p>The relevant creditors should be notified, and actions should be taken to release the funds.</p>

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

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
(a) National Audit Act No. 19 of 2018			
(i) Paragraph 40(1)	Although all activities of the Fund should be subject to internal audit, the Fund had not appointed a qualified auditor to carry out internal audit activities in the Fund since its inception.	All the activities of the fund are regularly reviewed by the top management and inter-departmental managers and especially by the internal audit committee.	Activities performed by the Fund should be examined by an independent internal audit.
(ii) Paragraph 41(1)	Although the Fund should conduct audit and management committees to review the operational activities of the Fund and timely report to the Board of Trustees, the Fund never held an audit and management committee meeting. Additionally, the Fund had not participated in the audit and management committee meetings of the Ministry of Finance, Economic Stabilization and National Polices.	The internal audit, periodic audit and inspection of the fund are regularly checked under the initiative of the Director General of the Treasury (Public Finance) acting on behalf of the settlor, advice and attention is given to correct the many errors that occur immediately. As of now, there has not been any necessity for establishing a formal system of record keeping, as the situation has not required such measures.	Audit and Management Committee meetings should be held as per the National Audit Act.
(b) Deed of Trust of the Fund dated 05 August 1999 Section 9 (f)	The Board of Trustees shall not be entitled to receive salaries, allowances or honorarial salaries but may be reimbursed for expenses incurred in the performing of their duties. However, contrary to that the Fund had paid monthly Rs. 50,000 to each trustee, aggregating to Rs. 2.5 million, Rs. 2.3 million and Rs. 2.5 million during the years 2021, 2022 and 2023 respectively.	The trustees of the fund are professionals, appointed by the settlor of the Construction Guarantee Fund, who possess expertise in various specialized fields and contribute directly or indirectly to the construction sector. They actively contribute to the ongoing advancement and development of the	The Fund should complied with the provisions of the trust deed.

Nevertheless, the details of the expenses incurred by the Board of Trustees for the performance of their duties had not disclosed in the financial statements. Furthermore, no disclosure was made in the financial statements regarding these related party transactions.

construction sector, while also playing a key role in the successful achievement of the fund's objectives. For this purpose, an amount previously assessed is reimbursed monthly after evaluating the performance of the trustees. This amount should be considered an expense incurred during the execution of duties.

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| <p>(c) Financial Regulations 876(3) issued by Public Finance Circular No. 01/2020 dated 28 August 2020</p> | <p>If there are any reasonable grounds for continuing non statutory Fund, the Fund should be legalized by an Act of Parliament. However, the Fund had not complied with this requirement even by 31 March 2024.</p> | <p>The Fund had established by the Secretary of the Ministry of Finance. The Fund expected that the Secretary of Treasury as the Settlor of the Fund will take further legislation or appropriate actions as required.</p> | <p>The Fund should comply with financial regulations.</p> |
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1.8 Non-compliance with Tax Laws

Audit Observation

The Fund had paid a lump-sum payment of Rs. 2.54 million as a bonus during the year, but Advance Personal Income Tax (APIT) was not deducted from this amount, in accordance with Section 07(b) of the circular SEC/2023/E/01 issued by the Department of Inland Revenue on 29 March 2023.

Management Comment

Thank you for pointing this out, and we noted to rectify it from the year 2024 onwards.

Recommendation

Actions should be taken in accordance with the provisions of the circular.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a surplus of Rs. 332.69 million and the corresponding surplus in the preceding year amounted to Rs. 285.27 million. Therefore an improvement amounting to Rs.47.42 million of the financial result was observed. Although bond and guarantee income declined by Rs. 88.90 million, the main reason for the improvement was an increase of Rs. 169.94 million in non-operating income.

2.2 Trend Analysis of major Income and Expenditure items

Description	For the year ended 31 December 2023	For the year ended 31 December 2022	Variance {Favorable/ (Adverse)}	Percentage
	(Rs.Mn)	(Rs. Mn)	(Rs. Mn)	(%)
<u>Income</u>				
(a) Income from bonds & guarantees	13.45	102.36	(88.91)	(87)
(b) Interest on Fixed deposit	365.36	194.10	170.26	88
(c) Miscellaneous Income	5.57	0.074	5.49	7,427
<u>Expenditure</u>				
(d) Transport expense	6.51	5.19	(1.32)	(25)
(e) Operational cost	1.21	2.54	1.33	52
(f) Maintenance of Equipment	0.56	0.36	(0.20)	(56)

The following observations are made in this regard.

- (a) The number of bonds issued decreased by 40 in the current year, compared to 74 in the previous year. Consequently, bond income declined from Rs. 89 million or 87 percent.
- (b) Rs. 5.79 million of creditor balances, received from employers and retained by the fund for more than five years had been taken into miscellaneous income as a result miscellaneous income had increased.

2.3 Ratio Analysis

According to the available information, several significant accounting ratios of the fund for the current and previous years are shown below.

Ratio	2023	2022
Liquidity Ratio		
Current Ratio	5.73 : 1	4.29 : 1
Profitability Ratio		
Return on Asset	11.59	10.97
Net Profit ratio	73.43	76.68
Return on Equity	15.97	16.33

During the year under review, the fund's current ratio and return on assets ratio increased, while the net profit ratio and return on equity ratio decreased.

3. Operational Review

3.1 Management Inefficiencies

Audit Observation	Management Comment	Recommendation
<p>(a) The Fund had entered into an agreement with Sri Lanka Telecom during the year 2015 to design and develop a Management Information System (MIS) to the worth of Rs.2.98 million. As per the agreement, the first installment and the second installment to be paid after development, total Rs. 2.08 million or 70 percent of the contract value was paid to the relevant institution in the years 2015 and 2016 and it was shown under non-current assets as software development advances in the statement of financial position. Although about 08 years have been passed since the money was paid, the preparation of this Management Information System (MIS) was not completed even up to 31 March 2024. During the year under review, the fund had also failed to complete the work as per the agreement.</p>	<p>Although agreements were made with Sri Lanka Telecom, changes in government policies discourage its successful completion. Consequently, after various organizations submitted price proposals ranging from Rs. 6.0 million to Rs. 60.0 million, the scope was revised. It is now being pursued in agreement with Sri Lanka Telecom. Initially, the project is proceeding with a value of Rs. 3.0 million, as agreed. Both parties have signed an agreement for this at the beginning of 2024.</p>	<p>The Management Information System should be successfully developed in accordance with the agreement.</p>
<p>(b) The Fund was established in 1999 and received a Capital Grant of Rs. 55 million from the General Treasury in four instances during the period of 2000 to 2005. But there was no mechanism for remittance of annual profits to the treasury. Meanwhile, from the retained earnings of Rs.949.79 million as on 31 December 2020, Rs.500 million was transferred to a reserve account named “Provision for Infrastructure” and remained idle. Retained profits and reserves were Rs.912.95 million, while long-term investments were Rs.1,208.91 million and short-term investments were Rs.1,041.61 million as at 31 December 2023.</p>	<p>Under Condition 12(a) of the approved trust deed, all or part of the asset should be utilized for institution’s purposes, while the Settlor has not provided any guideline other than that, all the reserves have been used to develop service limits.</p>	<p>A system should be established to remit the surplus or portion of the surplus annually to the Treasury as per the circular.</p>
<p>(c) In calculating the fund's bond and guarantee levy income, 2 percent and 2.5 percent were charged from the bond value for advance bonds and performance bonds, respectively, for 100,000 kilometer road development projects. Additionally, bond extension levy charges for advance bonds and performance</p>	<p>To minimize risks to a certain extent and address the need for security if required, the Board of Trustees has delegated all responsibilities to management for variation of fees and arrange security if required. Due to the inability to assess risks</p>	<p>Decisions made by management or committees, with the approval of the Board of Trustees, should be included in the bond and guarantee income files.</p>

bonds were 1.5 percent and 1.75 percent respectively. Although a special management report detailing these fees was submitted for audit, the meeting minutes with board of trustee's approval were not submitted to audit. Additionally, an amount was added to the bond and guarantee levy income based on existing risk levels on bond income. This value was assessed by management according to the prevailing risks and included in the bond and guarantee levy income. However, there was no any document of the risk assessment or any discussion notes in the files. Additionally, the sections regarding service fees in the Fund's annual reports from 2020 to 2023 do not contain any notes.

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| (d) | The fund does not have a computerized accounting system in operation, and all transactions are processed through the Microsoft Excel package. Due to the large volume of transactions reported daily, it is unavoidable that reporting transactions takes a significant time and that may be occurred accounting errors. | The organization has a pre-established accounting system (QB), through which the relevant accounting ledgers are prepared according to a pre-designed format. However, for our requirements, this information must be exported into Excel sheets and then adjusted accordingly to meet specific requirements. | Appropriate steps should be taken to introduce a suitable computerized accounting system. |
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3.2 Procurement Management

	Audit Observation	Management Comment	Recommendation
(a)	According to Section 1.2.1 of the 2006 Government Procurement Guidelines, vehicles should be hired through a bidding process. However, without conducting a new tendering process, the vehicle bearing registration number CAC-6366 has been hired for more than five years at a monthly rate of Rs. 265,000 (inclusive of VAT and Social Security Contribution Levy). As a result, the opportunity to obtain services at the lowest prices through competitive bidding was lost.	The organization properly advertised in newspapers to hire a vehicle without a driver and fuel, and the bids received were reviewed by a Technical Evaluation Committee. The committee's recommendations were subsequently approved by the Board of Trustees.	Suppliers should be selected competitively accordance with the provisions of the Procurement Guide.
(b)	According to Section 4.2, the procurement entity should prepare the main procurement plan. Although the main procurement plan	This proposal is appreciated, and since the organization's activities are conducted under a five-year	The provisions of the procurement guidelines should be followed.

should include the projected procurement activities for at least a three-year period, the fund had not prepared such a procurement plan.

plan, the procurement process also prepared accordingly.

- (c) According to Section 4.2.2, although the annual procurement plan for the year 2023 was submitted for the audit, the fund had not prepared it in accordance with a procurement time schedule that outlines the timeline of procurement activities.
- The procurement program for the year 2024 prepared according to a timeline and being carried out accordingly.
- The provisions of the procurement guidelines should be followed.

4. Accountability and Good Governance

4.1 Tabling of Annual Performance Report in Parliament

Audit Observation	Management Comment	Recommendation
<p>According to Financial Regulation 877(2)(e) issued by the Public Finance Circular No. 01/2020 dated 28 August 2020, the Accounting Officer of the Fund shall prepare the Annual Performance Report in all the three languages under the prescribed provisions, and aforesaid report to be tabled in Parliament within 150 days after the end of each financial year. However, no evidence was presented to the audit regarding tabling annual performance report of years 2020, 2021 and 2022 to Parliament even up to the date of 31 March 2024.</p>	<p>When preparing the relevant report, government guidelines were strictly adhered and the documents do not prepared exactly as per the format. However, all necessary information from Sections 1 to 7 has been systematically included in the reports. This report has been consistently submitted to the Settlor within 60 days after the end of the year.</p>	<p>The provisions of the circular should be followed.</p>

4.2 Budget control

Audit Observation	Management Comment	Recommendation
<p>According to the Financial Regulation 877 (1) (c) issued by Public Financial Circular No. 01/2020 dated 28 August 2020, the budget prepared by the Board of Trustees for the next year should be remitted to the Director General of National Budget before 30 September of the current year for obtaining the approval thereof. However, the budget of the Fund for the year 2023 had not approved as per the provisions in the above circular.</p>	<p>The Settlor has fully delegated all its powers to the Board of Trustees. Accordingly, under section 7 of the trust deed, the trustees have provisions to administer and manage the Fund. The board of trustees submits a copy of the approved budget to the Settlor, Secretary of the Treasury, without any delay.</p>	<p>The Fund should complied with financial regulations.</p>