

**1. Financial Statements**

**1.1 Qualified Opinion**

The audit of the financial statements of the National Engineering Research and Development Centre of Sri Lanka (“Center”) for the year ended 31 December 2024 comprising the statement of financial position as at 31 December 2024 and the 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 material accounting policy information, 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 presented in Parliament appear in this report.

In my opinion, except for the effects of the matters described in paragraph 1.5 of this report, the accompanying financial statements give a true and fair view of the financial position of the Center as at 31 December 2024, 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**

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**

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 Center’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 Center or to cease operations, or has no realistic alternative but to do so.

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

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

## 1.4 Audit Scope

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 risk 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 procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Centre's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Center'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 Centre to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the

presentation of information to enable a continuous evaluation of the activities of the Centre and whether such systems, procedures, books, records and other documents are in effective operation;

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

## **1.5 Audit Observations on the Preparation of Financial Statements**

### **1.5.1 Non-compliance with Sri Lanka Public Sector Accounting Standards**

<b>Non-compliance with Reference to the Relevant Standard</b>	<b>Comment of the Management</b>	<b>Recommendation</b>
a) Revenue and expenses shall not be offset in terms of Paragraph 48 of the Sri Lanka Public Sector Accounting Standard 01. However, the revenue on the auditorium amounting to Rs. 933,715 and expenses on the auditorium incurred in several instances during the year totalling Rs. 539,031 had been offset, thus showing a sum of Rs. 394,684 in the financial statements as revenue of the auditorium.	Action will be taken in due course to separately show in the accounts the revenue and expenses relating to the auditorium.	Revenue and expenses should not be offset, and shown separately in the financial statements as per the Standard.
b) The gross carrying amount of 3,178 items of Property, Plant and Equipment costing Rs. 462,659,616 which were still in use despite being fully depreciated in terms of Paragraph 92 of the Sri Lanka Public Sector Accounting Standard 07, had not been disclosed in the financial statements.	Action will be taken in due course to show the value of Property, Plant and Equipment still in use after being fully depreciated, through a Note.	The value of assets still in use despite being fully depreciated, should be disclosed.
c) The policy for recognizing the income and expenditure of the projects relating to the sums of Rs. 95,659,068 and Rs. 22,039,616 brought to accounts as covering income under the project technology assignments and commercial technology exchange projects of the Center, and the related expenditure	Action will be taken in due course to disclose the policy followed in recognizing the income and expenditure of the project in the financial statements.	When accounting for income and expenditure of the projects, the accounting policy followed in that connection, should be disclosed.

amounting to Rs. 62,120,252, had not been disclosed in terms of Paragraph 39 (a) of the Sri Lanka Public Sector Accounting Standard 10.

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| d) | Treasury grants amounting to Rs. 30,598,147 received in the year under review, had not been recognized as an income received from non-exchange transactions in terms of Sri Lanka Public Sector Accounting Standard 11. Instead, the amount had been shown as net assets/equity.  | A sum of Rs. 41,936,946 had been recognized as being utilized in the year 2024 out of the capital grants, and that amount had been shown under income of the year under review.   | The amount of Rs. 41,936,946 shown in the statement of financial performance, is the value of amortization for the year, and the total of the capital provision received during the year, should be recognized as the revenue. |
| e) | The income and expenses arising under construction contracts, should be accounted for in terms of paragraph 41 of the Sri Lanka Public Sector Accounting Standard 16. However, the expenses of Rs. 34,882,366 relating to 12 commercial construction projects implemented in the year under review, had been disclosed as work in progress under the stock. As such, the assets had been overstated by the same amount. | Action will be taken in due course to show the value of work in progress relating to the commercial construction projects implemented with the objective of generating income, as work in progress in the financial statements. | The cost of such projects should not be shown as work in progress, but accounted for in terms of Standard 16.  |
| f) | Action had not been taken to show in the accounts the present value of past employment benefit obligation and related conversion service cost with respect to gratuity allocations of Rs. 114,695,335 in terms of Paragraph 76 of Sri Lanka Public Sector Accounting Standard 19.   | Gratuity will be computed in due course in accordance with Sri Lanka Public Sector Accounting Standards.  | The present value of post employment benefit obligation and related conversion service cost with respect to gratuity allocations, should be shown in the financial statements.   |

### 1.5.2 Accounting Deficiencies

<b>Audit Observation</b>	<b>Comment of the Management</b>	<b>Recommendation</b>
a) As a balance of Rs. 2,337,359 receivable with respect to a project jointly implemented by the Center and the Line Ministry, had been shown under trade and other payable balances, liabilities had been overstated, whilst assets had been understated by the same amount.	Corrective measures will be taken in due course on the amount of Rs. 2,337,359.	The receivable and payable balances should be correctly shown in the accounts.
b) As the expenditure of Rs. 3,543,215 (including VAT) incurred by the Center for restoring a collapsed wall belonging to Industrial Development Board, had been recognized as an asset of the Center, the assets had been overstated whilst the expenses had been understated by the same amount in the financial statements.	The buildings and other infrastructure facilities owned by the Center existing at this premises, are mentioned as capitalized assets in the accounts. Accordingly, restoration of the collapsed building needed to be prioritized, and the necessary provision had been allocated through the capital budget of the year 2024, thus recognizing as an asset in the financial statements by the end of the year.	Such immovable formed assets can be accounted for as assets only if the Center holds ownership of the land where it is located. Assets belonging to external parties that do not meet this condition should not be capitalized, and the expenses incurred should be either appropriately recovered or accounted for as expenditure.

### 1.6 Non-compliances with Laws, Rules, Regulations, and Management Decisions

<b>Reference to Laws, Rules, and Regulations, etc.</b>	<b>Non-compliance</b>	<b>Comment of the Management</b>	<b>Recommendation</b>
a) Financial Regulation 756 of the Financial Regulations code of the Democratic Socialist Republic of Sri Lanka.	Report of the Board of Survey for the year 2024, had not been furnished to the Auditor General even up to the date of this report.	Attention has been brought to expeditiously furnish the report of the Board of Survey.	Action should be taken to expeditiously furnish the report of the Board of Survey.

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| b) | Section 6.6 of the Operational Manual for State Owned Enterprises introduced by the Public Enterprises Circular No. 2021/01 dated 16 November 2021. | The annual report of the year 2023 had not been tabled in Parliament whilst the draft annual report of the year 2024 was not furnished to the Audit. | The annual report of the year 2023 has been forwarded to the Ministry. The annual report of the year 2024 is being drafted. | The annual report should be submitted to Parliament through the Ministry in order to be tabled within the specified timeframe. A copy of the draft annual report should be furnished with the accounts. |
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## 2. Financial Review

### 2.1 Financial Result

The operating result of the year under review was a surplus of Rs. 30,659,721 as compared to the surplus of Rs. 4,878,740 for the preceding year. As such, an increase of Rs. 25,780,981 was observed in the financial result. Increase in the Government grants by Rs. 70,481,740 compared to increase in administrative expenses by Rs. 44,069,138, had mainly attributed to this improvement.

## 3. Operating Review

### 3.1 Management Inefficiencies

	Audit Observation	Comment of the Management	Recommendation
a)	It is the key function of the Center to acquire engineering technologies through engineering research and development, and use and transfer of such technologies. However, the research and development function had not been organized in a manner to make innovations for productively contributing to the development of the country whilst improving the livelihood of the people, improve the traditional technology, and increase the generation of revenue of the Center and the country through identification of the niche market. As such, priority had been given to implement the projects obtained from external parties as technological assignment projects thereby earning revenue. A net revenue of Rs. 33,538,816 had been earned in the year under review through the	The primary objectives under scope of the Center are to carry out research and development activities for engineering functions and thereby contribute to the economic development of the society in Sri Lanka. Accordingly, funds are annually allocated from the annual state budget for the purpose of conducting and disseminating such research and development activities. Through these efforts, the Center has been able to create a significant positive impact on the domestic economy through generating financial savings and creating employment	Great attention should be directed towards achieving the main objectives and functions of the Center.

implementation of technological opportunities within the assignment projects. country.

- b) The capital funds provided annually by the Treasury were continuously invested in fixed deposits instead of being used for the primary objectives of the Centre and the value of these deposits at the end of the year under review amounted to Rs. 170,500,000. Irrespective of this, the Centre had obtained Treasury grants amounting to Rs. 334,811,147 and Rs. 259,228,326 in the year under review and the preceding year respectively.
- As compared to the preceding years, more research and development projects aiming at improving the technology used in local industries had been completed in the year 2024. Plans are already underway to improve the research facilities needed to expand the institution's services by utilizing the deposits in 2025.
- Funds provided as Treasury grants should be utilized for the intended purposes.
- c) A net surplus of Rs. 30,659,721 had been shown in the financial statements of the Center for the year under review. However, excluding the Government grants and amortization for deferred income, the total revenue of Rs. 507,757,266, comprised only the operating income of Rs. 138,736,912, whereas the expenditure amounted to Rs. 434,137,192. Accordingly, the Center had sustained a deficit of Rs. 295,400,279 through operating activities. Only a sum of Rs. 87,647,657 or 18 per cent of the aforesaid expenditure had been incurred on research and development activities and technological assignments, whereas 72 percent equivalent to Rs. 346,489,535 had been expended on administrative expenses.
- The actual revenue earned through technological assignment projects relating to the year 2024 amounted to Rs. 95,659,068 and the actual expenditure incurred thereon amounted to Rs. 62,120,252. As such, the center has earned a surplus of Rs. 33,538,816 from commercial projects,
- Although a surplus of Rs. 33,538,816 had been gained only through technological assignments, a deficit had resulted considering the overall operating revenue and expenditure. Great attention should be captured particularly on the achievement of objectives and improving the performance of operations.

### 3.2 Idle or Underutilized Property, Plant and Equipment

Audit Observation	Comment of the Management	Recommendation
Seven machines of the Incubator technology division valued at Rs. 65,186,117, remained unutilized since 2017. Furthermore, 06 machines in functional status valued at Rs. 21,130,894 used to make specific parts of machinery and tools, remained underutilized without being used for any activity during the year under review.	Three machines were underutilized in 2024 compared to 2023, and the CMM machine became non-functional in the mid-year, thereby reducing its uptime. Moreover, there were no longer enough work for the CNC Hard Ford machine and Surface Grinder and to overcome this, it is expected to launch a new program in collaboration with the Business Development Center. The 07 machines mentioned here were not being utilized as they had been sent for repair.	Tasks should be planned and implemented to ensure optimum utilization of the machines.