

## **National Defence Fund - 2017**

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The audit of financial statements of the National Defence Fund for the year ended 31 December 2017 comprising the balance sheet as at 31 December 2017 and the income and expenditure account and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory 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 Section 12(2) of the National Defence Fund Act, No. 09 of 1985. My report on the administrative activities of the Fund mentioned in the Section 12(4) of the Act of the Fund included under the following paragraphs. The statement of income and expenditure is shown as annex 01 and the statement of investment of monies is shown as annex 02.

### **1.2 Management's Responsibility for the Financial Statements**

The management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Public Sector Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements whether due to fraud or error.

### **1.3 Auditor's Responsibility**

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards consistent with International Auditing Standards of Supreme Audit Institutions (ISSAI 1000-1810). Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Fund's preparation and fair presentation of the financial statements 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

### **1.4 Basis for Qualified Audit Opinion**

My opinion is qualified based on the matters described in paragraph 2.2 of this report.

## 2. **Financial Statements**

### 2.1 **Qualified Opinion**

In my opinion, except for the effects of the matters referred to in paragraph 2.2 of this report, the financial statements give a true and fair view of the financial position of the National Defence Fund as at 31 December 2017 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

### 2.2 **Comments on Financial Statements**

#### 2.2.1 **Presentation of Financial Statements**

In terms of Section 13 of the National Defence Fund Act, No.09 of 1985 as amended by the National Defence Fund Act, No.10 of 1991, the financial statements of the Fund shall be tabled in Parliament by the Secretary to the Ministry of Finance and accordingly, the Secretary to the Ministry of Finance shall prepare those financial statements and furnish to the Auditor General with the approval of the Minister. Nevertheless, the financial statements for the year ended 31 December 2017 had been furnished to the Auditor General on 26 March 2018 with the signature of the Secretary to the Ministry of Defence and two officers of the Fund without proper approval. The assurance of the Management's Responsibility on the preparation and presentation of the financial statements had not been stated in the financial statements in pursuance of Public Enterprises Circular No.PED/45 dated 02 October 2007.

#### 2.2.2 **Sri Lanka Public Sector Accounting Standards**

The following observations are made.

(a) **Sri Lanka Public Sector Accounting Standard-01**

The statement of changes in equity had not been presented in the financial statements presented by the Fund for the year ended 31 December 2017.

(b) **Sri Lanka Public Sector Accounting Standard-07**

In terms of Paragraph 47 of the Standard, when the fair value of a capital asset differs materially from its carrying amount, further revaluation is necessary. Nevertheless, lands costing Rs.11,030,000 and buildings costing Rs.4,520,000 owned by the Fund had not been revalued subsequent to the year 2008.

#### 2.2.3 **Accounting Deficiencies**

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Entertainment expenditure of Rs.10,145 relating to the year under review had not been included in the financial statements.

#### 2.2.4 **Unexplained Differences**

Even though the interest income on investments for the year under review amounted to Rs.99,872,801 according to the financial statements, it was Rs.101,600,942 according to the computation carried out by the Audit, thus observing an unexplained difference of Rs.1,728,141.

## 2.4 Non-compliance with Laws, Rules, Regulations and Management Decisions

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The following observations are made.

<b>Reference to Laws, Rules, Regulations and Management Decisions</b>	<b>Non-compliance</b>
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(a) Section 3 (1) of the National Defence Fund Act, No. 09 of 1985.	Meetings of the Board of Governors had not been conducted from the date of establishment of the Fund by the end of the year under review.
(a) <u>Treasury Circulars</u>	
(i) Section 4.1(c) of the Public Finance Circular No. PF/423 dated 22 December 2006.	No expenditure whatsoever should be incurred during the relevant financial year without an approved Budget. Nevertheless, the Fund had not prepared a Budget for the year under review and obtained approval therefor.
(ii) Paragraph 04 of the Public Finance Circular No.01/2014 dated 17 February 2014	An annual Action Plan containing the activities aimed at the achievement of the objectives of the Fund had not been prepared for the year under review.
(iii) Treasury Circular No.842 dated 19 December 1978.	A Register of Fixed Assets inclusive of the details on the fixed assets of the Fund worth Rs. 18,572,415 classified under 04 categories had not been maintained.

## 3. Financial Review

### 3.1 Financial Results

According to the financial statements presented, the financial result of the Fund for the year under review was a surplus of Rs. 95,979,933 and the corresponding surplus of the preceding year amounted to Rs. 66,392,540, thus indicating an improvement in the financial results by Rs. 29,587,393 during the year under review as compared with the preceding year. Although the welfare expense had increased by Rs.4,883,280 during the year under review as compared with the preceding year, increase in the interest income on investments by Rs.34,480,696 had mainly attributed for the above improvement in the financial result.

The analysis on financial results for the year under review and 04 preceding years had revealed that the surplus amounting to Rs. 80,688,937 in the year 2013 had deteriorated up to Rs.48,440,571 by the year 2015, whereas it had increased in to a surplus of Rs.95,979,933 by the end of the year under review. However, after readjusting the employees remunerations and depreciations for non- current assets to the financial result, the contribution of the Fund amounting to Rs. 80,884,211 in the year 2013 had deteriorated up to Rs.48,625,395 by the year 2015, whereas it had improved up to Rs. 96,161,368 by the end of the year under review.

## 4. Operating Review

### 4.1 Performance

#### 4.1.1 Operations and Review

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The following observations are made.

- (a) It shall be the duty of the Board of Governors to apply, subject to the directions of the President, the moneys belonging to the Fund in such manner, and for such purposes, as it may consider best calculated to promote and ensure national defence, including the payment of any benefit to the families of members of the police force or of the armed forces, who have been injured or who have died in the course of performing their official duties. Nevertheless, no evidence whatsoever had been received to the Audit that the expenditure from the Fund had been incurred under the direction of His Excellency the President and approval of the Board of Governors in terms of the Provisions of the Act.
- (b) Out of the revenue of the Fund totalling Rs.377,254,358 of the year under review and four preceding years, sums totalling Rs.18,745,265 ranging from 0.04 per cent to 11 per cent only had been used for the purposes of the Fund. Deviating from the objectives of the Fund, the excess funds had been invested in the fixed deposits and a Treasury Bill and the value of the investments so existed by the end of the year under review amounted to Rs.997,335,505.
- (c) Although the number of deceased, disappeared and disabled war heroes was 44,215. according to the information received by the Audit, the award of savings deposits totalling Rs.4,875,000 for 195 students of the war hero families who had qualified the Five Year Scholarship Examination in 2015 and 2016 only had been done by the Fund during the year under review.
- (d) The programmes to promote and ensure national defence, the secondary objective of the Act, had not been implemented during the year under review.
- (e) According to the approval granted by the Minister of Defence on 17 August 2017, plans had been drawn to implement a project called Meth Sevana Partly Housing Project in order to construct homes for 145 war heroes by spending at Rs.750,000 per war hero out of the revenue of the Fund. However, selection of 89 war heroes only had been done even by the end of the year under review.

### 4.2 Management Activities

Three houses owned by the Fund had been given to Sri Lanka Army since year 2008, whereas action had not been taken to enter into a lease agreement with the Sri Lanka Army even by the end of the year under review. The rent that remained receivable as at 31 December 2017 amounted to Rs.2,400,000 of which a sum of Rs.1,200,000 represented the rent in arrears relating to the year 2016.

## 5. Accountability and Good Governance

### 5.1 Internal Audit

Under the Internal Audit Plan of the Ministry of Defence for the year under review, plans had been drawn to carry out 02 internal audit programmes for the Funds owned by the Ministry. The copies of the reports thereon had not been furnished to the Auditor General in terms of Financial Regulation 134 (3).

## 6 Systems and Controls

Deficiencies in systems and controls observed during the course of audit were brought to the notice of the Management of the Fund from time to time. Special attention is needed in respect of the following systems and controls.

<u>Systems and controls</u>	<u>Observations</u>
(a) Accounting	<ul style="list-style-type: none"> <li>(i) Instead of maintaining a separate set of accounts for recording transactions, only the memo had been maintained by the Fund.</li> <li>(ii) Notes to the accounts had not been maintained regarding money remitted to the savings accounts relating to the interest income on investments and scholarship holders.</li> <li>(iii) A register had not been maintained for recording fixed assets.</li> <li>(iv) Ledger Accounts had not been maintained for 18 asset, liability, revenue and expenditure accounts.</li> </ul>
(b) Operational Management	Failure to enter into the Rent agreements, failure to revalue assets and not conducting meetings of Governing Board.

**Annex 01****Statement of income and expenditure of the National Defence Fund for the year ended 31 December 2017**


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	<u>2017</u> Rs.	<u>2016</u> Rs.
<b><u>Income</u></b>		
Donations	-	2,520
Interest on Investments	99,872,801	65,392,105
Rent Income	1,200,000	1,200,000
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	<u>101,072,801</u>	<u>66,594,625</u>
<b><u>Expenditure</u></b>		
Allowances of staff	32,400	17,400
Welfare Expenditure	4,911,432	28,152
Depreciation on fixed assets	149,036	156,533
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	<u>5,092,868</u>	<u>202,085</u>
Income over expenditure	<b><u>95,979,933</u></b>	<b><u>66,392,540</u></b>

## Annex 02

**Statement of the investment of monies of the National Defence Fund in the year 2017**

<b>Account Number</b>	<b>Investing Institution</b>	<b>Type of Investments</b>	<b>Date of Investment</b>	<b>Period of Investment</b>	<b>Balance as at 31 December 2017</b>
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2 0065 12 19081	National Saving Bank	Fixed Deposit	30 June 2017	1 year	Rs. 13,461,121
2 0065 12 19090	National Saving Bank	Fixed Deposit	30 June 2017	1	17,320,340
2 0065 12 19073	National Saving Bank	Fixed Deposit	27 June 2017	1	152,823,514
2 0065 11 78202	National Saving Bank	Fixed Deposit	25 September 2017	1	271,257
2 0065 11 86302	National Saving Bank	Fixed Deposit	22 July 2017	1	1,102,682
2 0065 12 17542	National Saving Bank	Fixed Deposit	09 April 2017	1	13,172,334
2 0065 12 17569	National Saving Bank	Fixed Deposit	24 March 2017	1	90,665,893
2 0065 12 19057	National Saving Bank	Fixed Deposit	27 June 2017	1	111,256,821
2 0065 12 19065	National Saving Bank	Fixed Deposit	27 June 2017	1	130,138,204
1098429	Bank of Ceylon	Fixed Deposit	09 May 2017	1	63,087,334
2 0001 2248549	National Saving Bank	Fixed Deposit	07 January 2017	1	1,493,380
1168699	Bank of Ceylon	Fixed Deposit	12 September 2017	1	163,590,119
2 00651025058	National Saving Bank	Fixed Deposit	31 March 2017	1	400,000
2 0149 01 00129	National Saving Bank	Fixed Deposit	14 July 2017	1	103,195,653
1168744	Bank of Ceylon	Fixed Deposit	21 September 2017	1	135,148,752
LKA09118B023	National Saving Bank	Treasury Bills	29 December 2017	One month	208,101
Total					<b><u>997,335,505</u></b>