State Engineering Corporation of Sri Lanka - 2018

The audit of activities and transactions of the Sri Lanka State Engineering Corporation (SEC) ("the Corporation") for the year ended 31 December 2018 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 13(1) of the Finance Act, No. 38 of 1971. My observations on operations of the Corporation during the year under review, which I consider should be tabled to Parliament in terms of the Article 154(6) of the Constitution of the Democratic Socialist Republic of Sri Lanka, appear in this report.

2. Financial Statements

2.1 Presentation of Financial Statements

Although Management is responsible for the preparation and fair presentation of the financial statements in accordance with Sri Lanka Accounting Standards, the annual financial statements of the year 2017 and year under review had not been furnished to audit even up to the September 2019 in terms of Section 6.5.1 of the Public Enterprises Circular No. PED/12 dated 02 June 2003.

2.2 Comments on Activities of the Corporation

2.2.1 Cash flow of the corporation

The cash flow position of the each division of the corporation during the year under review as follows.

(a) According to the information furnished to audit the service division and construction component division shown negative cash flow161,516,310 and Rs.5,956,669 while construction division ,Mechanical and electrical- division, consultancy division and Special Operation division shown positive cash flow Rs.94,096,400, Rs.10,172,204 ,Rs.5,956,669, Rs.20,426,983,and Rs7,397,000. As a results of that negative balance of net cash flow Rs.35,380,391 shown in corporation at end of the year 2018.

(b) The financing cash out flow of the Corporation had increased 5 per cent to 9.2 of total cash out flow from beginning to end the year under review.

(c) The bank overdraft interest cost increased 1.9 per cent to 9 per cent of the total cash out flow of the Corporation, from January to December year under review.

(d) Even though Corporation had obtained bank loans several times and outstanding balance Rs.1720 million at the end of the year under review. However, negative balance of net cash flow Rs.15,006,067 shown at the end of the year 2018.

2.3 Non-compliance with Laws, Rules, Regulations and Management Decisions

The following instances of non-compliance were observed in audit.

	Reference to Laws, Rules, and Regulations, etc.	Non-compliance
(a)	Employees' Provident Fund Act, No. 15 of 1958 and Employees' Trust Fund Act, No. 46 of 1980.	Surcharges of Rs.153.91 million and Rs.20.98 million had to be paid by the Corporation to the Employees' Provident Fund and the Employees' Trust Fund respectively due to un-remittance of contributions of Rs.307.82 million and Rs.41.97 million to the respective Funds on the cost of living allowances paid to the employees since January 2006 to July 2015.
(b)	Section 2(c) of the Circular, No. 121/1979 of 20 December 1979 issued by the Chairman of the Corporation.	Once the advances are given by cheques together with orders, such advances should be settled within a period of 30 days. However, such advances totaling Rs.85,220,662 relevant to period of 1999 to 2018 given had remained unsettled at State Engineering Corporation (SEC). Further cheque with order advances totaling Rs,6,445,194 had remained unsettled from 2016 to year under review at National Equipment and Machinery Organotin(NEMO).
(c)	Section 4 of the Circular, No. 122/1979 of 20 December 1979 issued by the Chairman of the Corporation.	Once the cash advances are given supply of service or goods, such advances should be settled within a period of 14 days. However, Rs.1,012,000 and Rs.1,257,890 cash advances of relating year 2017 and 2018 had remained unsettled even up to end of August 2019. Further cash advances Rs.2,216,480, Rs.606,790 and Rs.6,332,538 relating to years 2016, 2017 and 2018 had remained unsettled end of August 2019 in respect of National Equipment and Machinery Organotin.
(d)	Guideline 5.4.8(a) of the Procurement Guidelines 2006	The performance bond had not been obtained before commencing construction works in respect of seven construction contracts value at Rs.55,338,226.
(e)	Guideline 5.4.8(b) of the Procurement Guidelines 2006	Although validity period of the performance bond had been expired, but corporation had not been taken action to extend the period in respect of four ongoing construction contract valued at Rs.39,165,796.

3. Operating Review

3.1 Performance

The main objectives of the Corporation are: (i) Investigation, planning, designing and construction of building, civil engineering and other engineering projects (ii) Provision of consultancy and project management services (iii) Undertake property development works (iv) Manufacture and sale of ready mix concrete, reinforced concrete and pre-stressed concrete products (v) Manufacture, sale, import and export of construction materials, machinery and equipment required for engineering projects/undertakings (vi) Training of engineering and technical personnel (vii) Carrying out of research into construction materials, methods and techniques utilized for the above purposes..

The following observations are made with regards to main activities perform during the year 2018 in order to achieved the above objectives.

(a) Construction Division

The following observations are made

i. Although it was expected to complete the 05 projects value at Rs.472.37 million Actual progress range of 45 to 85 per cent during the year under review.

ii. The four projects value at Rs.8650.7 million had not been achieved 50 percent of the targeted progress of those projects.

(b) Construction Component Division

The following observations are made

(i) Precast Yard – Rathmalana (Site No 343)

The production decreased by Rs.20.8 million or 21 per cent compared with the budgeted production. Further, actual sales reduced by Rs.19 million or 20 per cent compared with budgeted sales.

(i) Dankotuwa Site (Site No 1099)

The actual production of the above site deteriorated by 71 per cent compared with the budgeted production, while actual sale decreased by 52 per cent compared with the budgeted sale.

(ii) Walikanda Precast Yard (Site No 1738)

The actual production deteriorated by Rs.13.8 million or 8 per cent compared with budgeted production.

(iii) Dematagoda concrete slippers yard (Site No 1510)

Out of targeted production of 21 per cent had not been achieved by the Dematagoda concrete slippers yard .

(iv) The actual progress of the project 46 per cent compared with the budgeted progress in respect of the project bearing no 2292.

(c) Mechanical & Electrical Division

The following observations are made

(i) Dolomite project situated at Mathale had operated under SEC. the quantity of production deteriorated compared with the previous years. It’s, operating loss was Rs.10.5 million during the year under review. Further, observed, corporation has to pay Lease rental Rs.7,227,099 for the period of 1992 to 2017 to Land Reformed commission. However Rs.1.5 million only paid by the Corporation at the end of the year of 2018.In addition the license for excavating had not been renewed from the Geological Survey and Mines Bureau. As a results production of the site had been suspended.

(ii) According to the information furnished to the audit, the actual progress of the workshops range of 25 to 76 per cent compared with budgeted progress due to non-availability of works.

(d) Passenger Bridge of the Maradana

The following observations are made.

(i) State Engineering Corporation had constructed Maradana Passenger Bridge including 100 no’s of sales outlets in the year 1992.The sales outlets had rent out to the private parties with the range of rental Rs.450 to Rs.650 per month. However monthly rental of those outlets had not been increased within 26 years from year1992 to 2018 .

(ii) Some places at the bridge had damaged were observed, but SEC had not taken action to repair those damages it will risk to the passengers who are use the bridge.

3.1.1 Operations of the National Equipment and Machinery Organization (NEMO)

The following observations are made.

(a) The details in respect of Value Added Tax (VAT), Nation Building Tax (NBT), Economic Service Charge (ESC) requested by the audit had not been presented. Hence, the actual payable balances of those taxes could not be satisfactorily ascertained in audit.

(b) VAT and NBT amounting to Rs.123.84 million and Rs. 7.8 million respectively had not been remitted to the Corporation as enable to forward same to the Department of Inland Revenue.

(c) A sum of Rs.235.8 million payable to the National Housing Development Authority had not been paid since the period from 2002 to 2011.

(d) Although the approved cadre for the NEMO was 344, the actual cadre as at 31 December 2018 was 785. Nevertheless, the approval for 441 excess employees had not been obtained by the Institute. Further, the NEMO had created 33 new posts without getting approval of Department of Management Services and 62 employees had been appointed to above 33 unapproved posts.

3.2 Matters of Contentious Nature

According to the details furnished to the audit, due to difference in application of the basis of quantities measured of inputs of Road work at finalization of the bills, the receivable balance of Rs Rs.61,851,213 were observed from 30 contractors of the Provincial Road Development Project at Galle district. Recovery had not been done up to date of audit.

3.3 Resources Released to Other Government Institutions

Thirty one (31) employees of the Corporation had been released to the Ministry of Housing and Construction, Provincial Ministries, Building Department, Government Factory and Urban Settlement Development Authority contrary to the instructions given in Section 8.3.9 of the Public Enterprises Circular No. PED/12 of 02 June 2003. Further, according to the provisions in the above Circular, salaries of these employees should be reimbursed from relevant institutions. However, salaries of 11 employees released to the Ministry of Housing and Construction, 06 employees released to the Building Department, 04 employees released to the Government Factory and 05 employees released to the Urban Settlement Development Authority had not been reimbursed even up to 30 September 2019.

3.4 Idle Assets

The following observations are made.

(a) The land and building of the C-city project owned to the Corporation had not been utilized for achieving the objectives of the project.

(b) Stock of Aluminum bars and ceiling sheet own to the Corporation remained at the main stores of the NEMO without being utilize by the corporation..

3.5 Identified Losses

A surcharge of Rs.114,399,641 had been imposed by the Department of Inland Revenue due to non-remittance of Value Added Tax, Economic Services Charge and Nation Building Tax on time. Further, Value Added Tax, Economic Services Charge and Nation Building Tax amounting to Rs.628,504,287, Rs.67,996,943 and Rs.15,130,647 respectively had not been remitted to the Department of Inland Revenue at the end of the year 2018.

3.6 Staff Administration

The following observations are made.

(a) In order to make recruitments to most of the posts in the senior management level on permanent basis, the approval of the Department of Management Services had been received by the Corporation in the years 2009 and 2011. However, 35 officers had been appointed on contract basis for 06 posts in the senior management level under higher salary scales. Further, 60 Superintended (Civil) had been also recruited on contract basis.

(b) An appointment should be made only for a post in the approved cadre in terms of Section 1.2 of Chapter II of the Establishments Code. Nevertheless, 550 excessive employees had been appointed for 28 posts in excess of the approved cadre as at 31 December 2018.

(c) In terms of Management Services Circular, No. 28 (ii), dated 01 August 2006 and the letter No. DMS/E3/43/4/265/1 dated 25 November 2009 of the Director General of the Department of Management Services, it had been informed that vacancies should not be filled, nor should new posts be created without approval of the Department of Management Services. However, 07 employees had been appointed to 05 un-approved posts.

4. Accountability and Good Governance

4.1 Corporate Plan

Corporate Plan had been prepared for the period of 2017-2021 by the Corporation in terms of the Public Enterprises Circular, No. PED/12 dated 02 June 2003. That Plan had not been updated in the year under review. Instances of failure in achieving objectives and goals indicated in the Corporate Plan were also observed. The following targets set out in the Corporate Plan had not been achieved as expected.

(a) To improve the average minimum annual income of each Division of the Corporation by 5 per cent and to earn the annual additional income of 5 per cent from projects.

(b) To introduce a system for the recovery of loans and to decrease the current credit level by 20 per cent.

(c) To identify new income earning fields and expansion of business activities under the Diversification of Business Activities.

4.2 Action Plan

Even though an Action Plan had been prepared for the year under review, the time periods had not been determined for achievement some objectives, strategies and activities mention in the Action Plan. It was further observed that, the following key items were also not included therein in terms of public finance circular no PFD/RED/01/04/2014/01 an dated 17 February 2014.

(i) Annual Budget by including income, operating expenses, development expenses, statement of financial position and statement of cash flows.
(ii) Annual Procurement Plan including proposed major investments, capacity building and major procurements
(iii) Human Resources Development Plan
(iv) Loan Repayment Plan
(v) Internal Audit Plan

4.3 Budgetary Control

Although Annual Budget should be submitted to the Line Ministry, Public Enterprise Department and Auditor General before 15 days of the accounting year. It had been submitted on 08 February 2018.Although budget had been prepared for the each month, the method of financing deficit had not been shown.

4.4 Tabling of Annual Reports

The Annual Reports for the years 2015 and 2016 had not been tabled in Parliament even by 20 July 2019 in terms of Section 6.5.3 of the Public Enterprises Circular, No. PED/12 of 02 June 2003.

5. Systems and Controls

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

	Areas of Systems and Controls		Observations
(a)	Financial Control	(i)	Granting advances through cheques with orders.
		(ii)	Non-recovery of funds from the debtors which brought forward over many years.
		(iii)	Significant delays in presenting the invoices for the relevant clients
		(iv)	Existence of purchase advances over a long time without being settled

		(v)	Failure to settle the long term retention money relating to constructions.
(b)	Trade and other Payable	(i)	Existence of mobilization advances over a long period of time without being settled.
		(ii)	Payment of surcharges due to failure in paying taxes on time.
(c)	Staff Administration	(i)	Releasing human resources to other institutions.
		(ii)	Recruiting employees in excess of the approved cadre.
		(iii)	Recruiting officers to the senior management on contract basis.
(d)	Assets Management		Failure to take action to properly utilize the idle assets and take over the ownership of lands.
(e)	Stock Control		Failure to conduct annual verification at all sites