

Head 223 - Sri Lanka Navy – 2019

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Sri Lanka Navy for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 and the statement of financial performance and cash flow statement for the year then ended 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. In terms of Section 11(1) of the National Audit Act, No. 19 of 2018, the summary report including my comments and observations on the financial statements of the Sri Lanka Navy was issued to the Accounting Officer on 17 June 2020. In terms of Section 11(2) of the National Audit Act, the Annual Detailed Management Audit Report relating to the Department was issued on 14 September 2020 to the Accounting Officer. This report is submitted to Parliament in pursuance of provisions in Article 154 (1) of the Constitution of the Democratic Socialist Republic of Sri Lanka, which should be read in conjunction with provisions of the National Audit Act, No. 19 of 2018.

In my opinion, except for the effects of the matters described in paragraph 1.6 of this report, the financial statements prepared in terms of provisions of State Accounts Circular bearing No. 271/2019 of 03 December 2019 give a true and fair view of the financial position of the Sri Lanka Navy as at 31 December 2019, and of its financial performance and cash flows for the year then ended in accordance with Generally Accepted Accounting Principles.

1.2 Basis for Qualified Opinion

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibility, under those standards is further described in the Auditor's Responsibility 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 Responsibility of the Chief Accounting Officer and the Accounting Officer on the Financial Statements

The Chief Accounting Officer and the Accounting Officer are responsible for the preparation of financial statements that give a true and fair view in accordance with Generally Accepted Accounting Principles and in terms of Section 38 of the National Audit Act, No.19 of 2018 and for such internal control as the Chief Accounting Officer determines is necessary to enable the

preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

In terms of Sub-section 38 (1) (c) of the National Audit Act, the Accounting Officer shall ensure that an effective internal control system for the financial control exists in the Department and carry out periodic reviews to monitor the effectiveness of such system and accordingly make any alterations as required for such systems to be effectively carried out.

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 judgement 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 Department's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.

- 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.

I communicate with the Accounting Officer regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

1.5. Report on Other Legal Requirements

As required by Section 6 (1) (d) and Section 38 of the National Audit Act, No.19 of 2018, I state the followings:

- (a) The financial statements of the year under review are consistent with the preceding year.
- (b) Recommendations made by me in relation to observation included in paragraph 1.6.1 of this Report had not been implemented.

1.6 Comments on Financial Statements

1.6.1 Financial Statements are not in compliance with the Circulars

Audit Observation	Recommendation	Comments of the Accounting Officer
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<p>According to the Public Accounts Circular No. 267/2018 of 21 November 2018, the principal ledger value of those assets had to be compiled when reporting non-financial assets. If there were any balances that were not so, that value should be kept as a balance to be revised in the main ledger until they are identified. However, action had not been taken accordingly.</p>	<p>Action should be taken in compliance with the Circular.</p>	<p>Action will be taken to rectify this by 31 December 2019.</p>

1.6.2 Statement of Financial Performance

Audit Observation	Recommendation	Comments of the Accounting Officer
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Expenditure for the year under review had been overstated by Rs. 6,483,191 due to accounting expenditure related to the previous year pertaining to the commercial advance account as expenditure of the year under review.	Accounts must be prepared accurately.	Comments had not been made.

1.6.3 Statement of Financial Position

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) The value of property, plant and equipment totalling to Rs.54,563,044,895 in the Statement of Non-Financial Assets (ACA-6) had been stated as Rs. 51,777,781,170 in the statement of financial position. As a result, the value had been understated by Rs.2,785,263,725.	Accounts must be submitted correctly.	I kindly inform you that the value of property, plant and equipment should be Rs.54,563,044,894.51 and the amount of Rs.2,785,263,725, the value of lands stated in one page had not been added to the total mistakenly when the values had been included in the financial statements.

<p>(b) Although the acquisition of capital assets amounted to Rs.2,264,057,163, the acquisition of assets in the statement of non-financial assets was stated as Rs. 1,862,631,721 and as a result, there was a difference of Rs.401,425,442.</p>	<p>Accounts must be submitted accurately.</p>	<p>A sum of Rs.398,413,816.77 was accounted by accounts summary in the month of February 2020. Action has been taken to account the error in the year 2020 since the remaining difference had taken place due to an error in the Northern Naval Command.</p>
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1.6.4 Balances of Advance Accounts

Audit Observation -----	Recommendation -----	Comments of the Accounting Officer -----
<p>According to the reconciliation statement related to the advance 'B' account, the balance of the control account of the Sri Lanka Navy as at 31 December 2019 was Rs.390,599,202 and the total of the individual balance classification summary by that day was Rs.368,606,975. Accordingly, a difference of Rs.21,992,227 was observed.</p>	<p>Accounts must be submitted accurately.</p>	<p>Comments had not been made.</p>

1.6.5 Non-compliance with the Laws, Rules and Regulations

The following are the instances of non-compliance with the provisions of laws, rules, and regulations observed during the audit test check.

Reference to Laws, Rules and Regulations	Audit Observation	Recommendation	Comments of the Accounting Officer
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Public Administration Circular No. 21/2015	Action had been taken to recover the arrears balances amounting to Rs. 1,043,270 prior to the termination of services of retiring officers,	Reducing the number of installments for recovering the amount in order to enable the recovery of the total amount prior to the termination of service of the officers or recovering the amount from an amount to be paid to the officers at the retirement.	Comments had not been made.

2. Financial Review

2.1 Imprest Management

The following observations were made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) Even though the limit of the monthly sub imprest in the North Central Naval Area was Rs. 2,167,500, a monthly average of Rs. 6,997,390 had been retained as cash in hand within the period of 10 months from January to October in the year 2019.	Should be responsible for functioning within the limit of approved imprest.	Comments had not been made.

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| (b) | <p>The amount submitted for the audit at the internal audit examination conducted in relation to petty cash, which was in the custody of the Assistant Director (Finance) at 16.00 hours on 21 October 2019 in North Central Naval Area was Rs. 7,246,340. Later, according to the information obtained from the bank records and the audit examination conducted by the Internal Audit (Civil), the balance that should be in the petty cash register by that day was Rs.10,644,391. Accordingly, a cash deficit of Rs. 3,398,051 prevailed by 21 October 2019.</p> | <p>The internal control process related to money must be strengthened.</p> | <p>Comments had not been made.</p> |
| (c) | <p>According to the time analysis of the loans of employees, the unrecovered loan balance of the officers excluding the officers currently serving in the Sri Lanka Navy, outstanding for more than one year was Rs. 23,813,970. It was 85 percent out of the total loan that should be recovered. Likely, the loan balance outstanding for more than 5 years without recovering was Rs. 22,056,336 and it was 79% out of the total loan amount to be recovered.</p> | <p>Action should be taken in accordance with paragraphs 01, 03 and 08 of the National Budget Circular No. 118 of 11 October 2004 and Sections 8.1 and 8.2 of Chapter XLVII of the Establishments Code.</p> | <p>Comments had not been made.</p> |
| (d) | <p>There was a loan balance of Rs.2,630,371 outstanding for a period of 5 to 20 years at the Trincomalee Naval Base.</p> | <p>Appropriate action should be taken expeditiously to recover the loan balance.</p> | <p>Comments had not been made.</p> |

2.2 Income Management

The following observations were made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) It was observed that the revenue of Rs. 8,861,429 earned from the harvest of the crops in the 2019 and expenditure of Rs.3,570,163 will be excluded from the audit of the Auditor General and the income earned from the harvest had not been credited to the Consolidated Fund of the Government and it had been credited to the Agricultural Fund of the Sri Lanka Navy.	The income should be credited to the Consolidated Fund and a Commercial Advance Account should be prepared for that purpose and it should be submitted to the audit.	All the income earned from these projects will be used for the upliftment and improvement of agricultural projects and for the welfare projects of the Navy. The accounting activities of this project will be audited transparently by external audit officers as well as by the Internal Audit Unit with the full supervision. It had been informed that it is possible to submit accounting information for further auditing.
(b) According to the revised estimate, the income was Rs.102,000,000. However, the revised estimate in the ACA-1 Revenue Statement had been mentioned as Rs.110,000,000.	Information must be submitted accurately and the approval of the General Treasury should be obtained for the revised estimate.	Although the basic revenue estimate for the year 2019 had been submitted to the General Treasury in the year 2018 as Rs.102 million, the General Treasury had presented it as Rs.210 million. The actual income of Rs. 110 million credited to the Government revenue for the year 2019 had been mistakenly recorded in the column of revised estimate in the ACA 01 Form.

2.3 Expenditure Management

Audit Observation	Recommendation	Comments of the Accounting Officer
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It was observed that savings of Rs.1,578,620,383 were made in relation to 33 recurrent objects and savings of Rs. 1,363,361,656 in	The time period of commencing the role should be determined and provision	According to the National Budget Circular No. 5/2019 of 24 September 2019, a sum of Rs. 865 million had to be

relation to 11 recurrent objects (other than compulsory savings). The savings were in the range of 10 per cent to 100 per cent out of the total net provision.

commensurate with the amount of work that can be accomplished during the year should be made.

saved from the allocated capital provision. It has been informed that the remaining savings were due to non-receiving of sufficient amount of imprest.

2.4 Utilization of provisions granted by other Ministries and Departments

Audit Observation	Recommendation	Comments of the Accounting Officer
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A total of Rs. 259.37 million had been allocated by other four Ministries, one Department and 02 Offices for various purposes and provision amounting to Rs. 35.95 million had only been utilized by the end of the year under review. Accordingly, 86 per cent of the provision allocated had not been utilized.	In carrying out other roles, planning should be done and only the necessary provision should be obtained. proper following up activities etc. should be carried out and action should be taken to utilize the maximum provision out of the annual provision made.	Comments had not been made.

2.5 Deposit Balances

The following shortcomings were observed.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) The amount provided by the Jaffna District Secretary for 05 projects from 2016 to 2018 was Rs.135,220,167 and the expenditure was Rs. 74,728,091 according to the expenditure details provided by the Northern Naval Command for those projects. Accordingly, balance of the deposit account was Rs. 30,228,488 although the saving of imprest should be Rs.60,492,076. As a result, the balance of the deposit account had been understated by Rs. 30,263,588.	Should be careful about the accuracy of the accounts.	Comments had not been made.
(b) According to the details of receiving cheques for projects implemented by the Northern Naval Command up to the years 2017 and 2018, the cash receipts were Rs.102,560,101. However, it was Rs.135,220,167 according to the details of cheques provided by the Jaffna District Secretary for projects. Accordingly, there had been a difference of Rs. 32,660,066.	Internal control over money should be strengthened.	Comments had not been made.

2.6 Operation of Bank Accounts

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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Even though the prior approval of the General Treasury should be obtained for opening an official bank account in terms of FR 381, the bank account bearing number 74976591 had been opened to collect agricultural income in contrary to the provisions.	Prior approval of the General Treasury should be obtained for official bank accounts.	The officers who worked in that regard at that time have now retired. Therefore, it is not possible to submit information regarding non-receipt of the approval of the General Treasury.

3. Operational review

3.1 Procurement

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
(a) According to Section 4.3.1 (a) of the Government Procurement Guidelines, the procurement entity shall prepare a total cost estimate including all associated expenses. However, procurement of goods, services and work had been done in 17 procurements of goods, services and works worth Rs. 48,295,411 without preparing a total cost estimate.	According to Section 4.3.1 (a) of the Government Procurement Guidelines, the procurement entity shall prepare a total cost estimate including all related expenses.	Hereinafter, relevant purchases will be performed only after submitting a total cost estimate. It has been informed that the need for repairs could be identified. However, the extent of the repairs could only be conclusively ascertained after the ship had been docked at the dry dock and the relevant measurements and tests had been carried out. Therefore, there was a practical problem in preparing pre-cost estimates.
(b) During the second bidding done for repairing the Nandimithra ship, the shopping system was used in accordance with Section 3.4 of the Procurement Guidelines. However, in relation to warships, goods, services or works were of high value and were not easily procured and shopping system should not be used for bidding.	An accurate procurement method should be used for bidding.	It has been informed that bids were invited under the Shopping System under Section 3.4 of the Procurement Guidelines.
(c) According to Section 8.9.1 (a) of the Government Procurement Guidelines, a formal agreement had to be signed for work contracts exceeding Rs. 250,000. Nevertheless, action had not	A formal agreement should be signed in relation to work contracts exceeding Rs. 250,000 in terms of Section 8.9.1 (a) of	It had been informed that action had been taken to sign one agreement for one ship covering all the repairs of the shipyard dry dock in coordination with the Legal Division as discussed at the Internal Audit

been taken in compliance with that provision in relation to 10 work procurements totaling to Rs. 27,542,958.

the Government Procurement Guidelines.

and Management Committee meeting for the first quarter of 2019 held on 17 June 2019.

3.2 Asset Management

The following deficiencies were observed.

Audit Observation	Recommendation	Comments of the Accounting Officer
(a) A difference of Rs. 15,895 million had been existed between the opening balance of the statement of Non-Financial Assets (as at 01 January 2019) and the final balance (as at 31 December 2018) of the report on movements of non-current assets of the financial statements for the previous year.	Accounts must be presented accurately.	I kindly inform you that a difference of Rs. 15,895 million had occurred by entering opening balances, that should be entered in the year 2018, to the opening balances of the year 2019.
(b) The balance amounting to Rs.54,563 million, the value of assets included in the statement of non-financial assets for the year under review had not been reconciled with the balance of Rs.64,220 million stated in the fixed assets register. Therefore, it was not possible to obtain a reasonable confirmation on the accuracy of the balances mentioned in the fixed assets register.	Accounts must be submitted accurately.	Equivalent to the final Treasury Accounting Statements as at 31.12.2019.
(c) The Navy was utilizing an extent of 448.08 hectares of lands, owned by other institutions and value of which had not been presented to the audit and 17 vehicles, of which value had not been presented to audit without formal transfer of assets.	The assets should be properly transferred as problems may be arisen on the legitimacy of those transactions since the Sri Lanka Navy will also have to bear the cost of maintaining and developing the assets owned by the other entities when such assets are used.	It was informed that the transferring activities were being carried out.

3.3 Management Deficiencies

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
(a) One vehicle was not running due to the delay in repairing it for over 5 years, 03 vehicles were not running due to the delay in repairing them over 2 years and 20 vehicles were not running due to the delay in repairing them over one year.	Motor vehicles should be repaired and used expeditiously to get the maximum usage from them.	It was informed that repairs were being carried out.
(b) Even though two machines worth Rs. 496,000 over 02 years and five machines worth Rs. 124,550 over one year had been handed over to external institutions for repairs, the vehicles had not been returned to the Navy after the completion of repairs.	Assets should be repaired expeditiously to get the maximum usage of the assets.	It was informed that repairs were being carried out.
(c) Repairs of one machine had been delayed over 4 years and 06 machines had been delayed over 03 years, 11 machines had been delayed over 02 years and 17 machines had been delayed over one year due to non-receipt of spare parts that had been ordered.	Procurement activities on spare parts should be carried out efficiently.	It has been informed that spare parts have been requested and repairs are being carried out.
(d) Seven (07) fixed asset subjects which had been condemned over 10 years as they were irreparable, 08 fixed asset subjects which had been condemned for 5-10 years as they were irreparable and 430 fixed asset subjects which had been condemned for 5-10 years as they were irreparable had been stored in the warehouse idly.	Action should be taken in relation to idle and underutilized assets in accordance with the Public Finance Circulars and FR 771.	It was reported that recommendations were made for disposal by General 47 and certain fixed assets were being made usable.

- (e) Two ships / vessels which had not been submitted for the cost / purchase price auditing had been idling for more than 02 years and six ships / vessels and one vessel which was received as a gift had been idling for more than one year due to delays in repairs.
- The vessels should be repaired expeditiously and used to get the maximum usage out of them.
- It was informed that repairs are being carried out and the required spare parts have been requested and they have not been received so far.
- (f) Action had not been taken to repair or to dispose of 02 ships / vessels which had not been submitted for the cost / value auditing and had been idling for over 09 years and to repair or to dispose of one vessel at the cost of Rs. 19.9 million which had been idling, over 08 years and to repair or to dispose of a ship / vessel at the cost of Rs. 19.8 million, which had been idling, over 06 years.
- Action should be taken in relation to idle and underutilized assets in accordance with the Public Finance Circulars and FR 771.
- It was informed that P 419 had been approved to make the vessel suitable for conducting disaster prevention training. P 470 - It is proposed to install a new engine under a new research and development project. Action was being taken to dispose the P-103. A-530 was being repaired.

4 **Human Resource Management**

The following deficiencies were observed.

Audit Observation	Recommendation	Comments of the Accounting Officer
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<p>(a) <u>Uniformed staff</u></p> <p>There were vacancies for 202 officers in the regular service, 60 volunteer sailors, 7,570 sailors in the regular service and 1207 volunteer sailors. Further, approval of the Department of Management Services had not been obtained for 4640 sailors recruited under the special system.</p>	<p>Action should be taken to fill the essential vacancies and obtain the approval of the Department of Management Services for excess employees.</p>	<p>It had been informed that action would be taken to fill the vacancies.</p>
<p>(b) <u>Civil staff</u></p> <p>There were 52 vacancies for one senior level officer, 11 tertiary level officers, 47 secondary level officers and 277 primary level officers. Further, the approval of the Department of Management Services had not been obtained for 52 employees who had been recruited on casual / temporary / contract basis.</p>	<p>Action should be taken to fill the essential vacancies and obtain the approval of the Department of Management Services for excess employees.</p>	<p>It had been informed that action would be taken to fill the vacancies.</p>
<p>(c) By the end of the year 2019, 941 disciplinary inquiries were being conducted related to officers and sailors. Out of these disciplinary inquiries, 587 disciplinary inquiries were delayed for 1 to 3 years and 84 disciplinary inquiries were delayed for more than 3 years.</p>	<p>Action should be taken in accordance with Public Administration Circular 30/2019.</p>	<p>Comments had not been made.</p>

(d) 387 officers had not submitted declarations of assets and liabilities.

Statements of Assets and Liabilities must be submitted in accordance with the Assets and Liabilities Declaration Law No. 01 of 1975 as amended by Act No. 74 of 1988.

Comments had not been made.