

1.1 Qualified Opinion

The audit of the financial statements of the of Sri Lanka Institute of Local Governance for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 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 a summary of significant accounting policies, 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 tabled 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 financial statements give a true and fair view of the financial position of the Sri Lanka Institute of Local Governance as at 31 December 2019, 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 based on the matters described in paragraph 1.5 of this report. I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAS). 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 Institute'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 intends to liquidate the Institute or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Institute's financial reporting process.

As per Sub-section 16 (1) of the National Audit Act No. 19 of 2018, the Institute 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 Institute.

1.4 Scope of the Audit

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 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 Institute'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 Institute'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 Institute 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 Institute, and whether such systems, procedures, books, records and other documents are in effective operation;

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

1.5 Financial Statements

1.5.1 Non-compliances with Sri Lanka Public Sector Accounting Standards

Non-compliance with Reference to the Relevant Standard	Comment of the Management	Recommendation
<p>a) Sri Lanka Public Sector Accounting Standard 02.</p> <p>The interest income of Rs. 522,436 should have been eliminated in computing the net cash flow generated through the operating activities. However, the said amount had not been deducted from the cash flow generated through the operating activities. The sum of Rs. 16,000,000 invested during the year in a fixed deposit had not been shown under investment activities in the cash flow statement.</p>	<p>It is agreed with the matters pointed out. Action will be taken to follow the Standards when preparing the financial statements.</p>	<p>Attention of the management is brought on the accurate preparation of financial statements.</p>
<p>b) Sri Lanka Public Sector Accounting Standard 09</p> <p>Inventories shall be measured at the lower of cost and net realizable value in terms of Section 15 of the Standard. However, the stock of publications valued at Rs. 1,517,202 had been measured at the cost without computing the net realizable value.</p>	<p>It is agreed with the matters pointed out. Following the instructions given at the meeting of the Audit and Management Committee of the Institute in regard to the said stock of publications, the said stocks are being physically surveyed at present.</p>	<p>Attention of the management should be brought on measuring the inventories in accordance with the Accounting Standard.</p>

1.5.2 Accounting Deficiencies

Audit Observation	Comment of the Management	Recommendation
a) An accounting policy had not been identified with respect to the Government grants amounting to Rs. 506,057,702 shown under equity in the statement of financial position. Action had not been taken to identify and amortize the assets relating to the grants amounting to Rs. 2,601,484.	It is agreed with the matter pointed out. It is expected to introduce an accounting and amortization policy for the grants in due course.	A policy should be introduced to account the capital grants.
b) Depreciation on buildings and library books in the Property, Plant and Equipment had been over computed by Rs. 218,774 and shown in the financial statements.	Assets of the Institution had been revalued excluding the buildings and library books. As such, depreciation had been computed for those assets on cost basis during the period from 01 September 2019 to 31 December 2019. Corrective measures will be taken in due course.	Expenditure on depreciation should be computed correctly and shown in the financial statements.

1.6 Monies Receivable

Audit Observation	Comment of the Management	Recommendation
a) No further action had been taken on the Balances receivable from 14 officers either interdicted or resigned, and a deceased officer, totalling Rs. 1,272,582 and Rs. 805,860 respectively	The declaration is correct. Action has been taken under relevant approvals to settle some of the balances from the gratuity scheduled to be paid, recover from the guarantors, and through legal action on securities.	Recovery of loan balances should be expedited.
b) The sum of Rs. 492,000 receivable from the Ministry of Provincial Councils and Local Government with respect to the diaries printed by the Institute in the year 2015,	The said sum has not yet been received although the Ministry was informed on several occasions.	Attention of the management is brought on the recovery of the sum receivable.

had not been recovered even in the year 2018.

- c) Action was not taken to properly recover the balance of Rs. 160,596 out of the sum of Rs. 175,596 that remained outstanding due to paying the gratuity without recovering the sum receivable from a Driver who had been interdicted after being found guilty in a disciplinary inquiry. It is expected to take legal action for the recovery of the said amount. Action should be taken to recover the unrecovered sum that should have been recovered when paying gratuity.

1.7 Non-compliances with Laws, Rules, Regulations, and Management Decisions

	Reference to Laws, Rules, and Regulations, etc.	Non-compliances	Comment of the Management	Recommendation
a)	Section 15.1 (IX) of Chapter II of the Establishments Code of the Democratic Socialist Republic of Sri Lanka.	Due to failure in conducting efficiency bar examinations on time, granting promotions and making permeant the positions of 35 officers had not been done properly.	Action has been taken for obtaining approval.	The efficiency bar examinations should be conducted on time as stated in the Establishments Code. Promotions should be granted and service of the officers should be made permanent properly.
b)	Guideline 8.9.3 (a) of the Procurement Guidelines.	Contrary to the objectives of the Procurement Guidelines, an agreement had not been entered into with the two parties with respect to the CCTV system purchased at the value of Rs. 742,288.	The observation that an agreement should be entered into with the two parties relating to the said transaction in terms of the Guideline 8.9.3 (a) of the Procurement Guidelines, is accepted. When such transactions are performed in the future, action will be taken to prepare formal agreements. At present, the supplier has	the Procurement Guidelines should be followed.

furnished a certificate of warranty.

- c) Section 04 of the Public Finance Circular, No. 01/2014, dated 17 February 2014. The Action Plan had not been prepared in accordance with the priorities based on the annual budget. This issue had been raised in the previous audit queries as well, and the Action Plan of the Institute for the year 2020 was prepared in accordance with the Public Finance Circular, No. 2014/01. Circular instructions should be followed.

2. Financial Review

2.1 Financial Results

The operating result of the year under review had been a deficit of Rs. 935,590 as against the surplus of Rs. 2,836,486 for the preceding year thus observing a deterioration of Rs. 3,772,076 in the financial result. This deterioration had mainly been attributed by the decrease in special project income and the certificate income by sums of Rs. 7,808,191 and Rs. 3,075,375 respectively whilst the expenses had not been decreased.

2.2 Trend Analysis on the Main Items of Income and Expenditure

a) The special project income had decreased by Rs. 7,808,191 or 61.75 per cent as compared with the preceding year. The decrease in the income from the project to empower community organizations for promoting participatory control, and the project for introducing a new accounting system to the local authorities under the United Nation's Development Programme, along with the income from the preparation of modules in the year under review had attributed to the said decrease. The income from the certificate courses had decreased by Rs. 3,075,375 equivalent to 76.31 per cent.

b) There had been an increase in the expenditure on the development of human resources by Rs. 5,229,908 representing 25.07 per cent whilst the administrative expenses had increased by Rs. 2,007,738 equivalent to 5.55 per cent.

2.3 Ratio Analysis

The current ratio and the quick ratio for the year under review and the preceding year, were as follows.

Ratio	Year	
	2019	2018
Current Ratio	11:1	8:1
Quick Ratio	11:1	7:1

Due to failure in evaluating the optimum requirements for current and quick assets of the Institute, the ratios of current assets and quick assets had increased.

3. Operating Review

3.1 Management Inefficiencies

Audit Observation	Comment of the Management	Recommendation
All the staff members of the Institute had not been provided with letters assigning duties properly. The Scheme of Recruitment for the absorption of staff for the new positions created in the wake of restructuring the staff, and making new recruitments, had not been revised even up to the date of this report.	It is agreed with the matter pointed out. The preliminary activities relating to the preparation of job descriptions for the entire staff had been commenced through the internal letter, dated 25 February 2019. At present, this activity has been completed with respect to a majority of employees. The Department of Management Services has been informed on the amendments and rectifications relating to some of the positions approved. Furthermore, action has been taken for completion of the said task through a Committee comprising persons with subject specific expertise.	The said amendments should be done immediately.

3.2 Underutilization of Funds

Audit Observation	Comment of the Management	Recommendation
A sum of Rs. 62,335,000 representing 50 per cent of the capital provision totalling Rs. 75,000,000 including the recurrent provision granted by the Treasury in the year under review and the training expenses, had not been utilized.	Delays in receiving funds cause the capital expenses to decrease whilst the existence of vacancies cause the recurrent expenditure to decrease.	Provision should be allocated only to the extent of utilization.

3.3 **Projects Abandoned without being Completed**

----- Audit Observation -----	----- Comment of the Management -----	----- Recommendation -----
<p>Bids had been called in the year 2013 for the construction of a 4 storied building to be used by the Institute, and having selected a contractor, a contract agreement valued at Rs. 53,196,907 had been entered into. The main contractor had assigned a subcontractor for laying the deep foundation. Having been decided by the Board of Directors of the Institute on 04 November 2013 that the number of stories of the building be increased from 04 to 05, the main contractor had been informed in writing. However, due to the failure of the main contractor to apprise the subcontractor in that connection, the deep foundation had been laid to be suitable only for 04 floors. As the Institute accepted that construction of the building on the existing foundation is not suitable, the expenditure of Rs. 44,757,072 incurred thereon became fruitless.</p>	<p>The sum was paid upon recommendation of the of the Ministry. As the construction of the building ended up in failure, a Cabinet Memorandum was presented to the Cabinet on 19 December 2017 by the then Minister of Provincial Councils and Local Government, and the Cabinet decision was received to annul the constructions contract and the consultancy contract. Nonetheless, the said agreements have not so far been annulled, and it is informed that action will be taken in due course to annul those agreements as soon as the Board of Governance is appointed to the Institute.</p>	<p>Action should be taken properly for the recovery of loss sustained by the Government.</p>

4. **Accountability and Good Governance**

4.1 **Environmental Issues**

----- Audit Observation -----	----- Comment of the Management -----	----- Recommendation -----
<p>Waste management is a key activity of the local authorities, but no training programme or workshop whatsoever had been conducted by the Sri Lanka Institute of Local Governance in that connection.</p>	<p>Discussions are underway to conduct such programmes in this year.</p>	<p>The necessary training programmes should be conducted.</p>

4.2 Sustainable Development Goals

Audit Observation	Comment of the Management	Recommendation
As the Sri Lanka Institute of Local Governance had not become aware of the “2030 Agenda”, action had not been taken to identify the sustainable development goals, and targets relating to their activities along with the milestones in reaching those goals and the indicators to measure the achievement thereof.	Not commented.	The Institute should adhere to the provisions of the Act.