

Secondary Towns and Rural Community Based Water Supply and Sanitation Project (Loan No 2758 -SRI) - 2013

The audit of financial statements of the Secondary Towns and Rural Community Based Water Supply and Sanitation Project for the year ended 31 December 2013 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 (GOSL) read in conjunction with Section 2.09 of Article (a) of the Project Agreement and the Supplementary Loan Agreement No.2758 SRI dated on 22 July 2011 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank (ADB).

1.2 Implementation, Objectives, Funding and Duration of the Project.

According to the Loan Agreement of the Secondary Towns and Rural Community Based Water Supply and Sanitation Project, the National Water Supply and Drainage Board (NWSDB) under the Ministry of Water Supply and Drainage is the Principal Executing and Implementing Agency of the Project. The ADB has approved the Loan No 1993 SRI – (SF) amounting to US\$ 85.6 million including GOSL portion on 18 August 2003. The objectives of the Project are to provide safe water to 969,000 people and sanitation to 171,500 people in five urban areas and in the rural areas of North Central Province and increases the capacity of the GOSL to provide safe water by strengthening the water sector institutions. As a result of significant cost escalation the ADB had agreed to make a supplementary loan to meet civil work of construction of head work, raw water transmission and treatment plant at Muthur. According to the Supplementary Loan Agreement, the estimated total cost of Project is US\$ 14.9 million and out of that US\$ 13.3 million or 89.26 per cent was agreed to be financed by ADB and US\$ 1.6 million or 10.74 per cent was agreed to finance by the GOSL. Activities of the Project were scheduled to be completed by 30 June 2014.

1.3 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Generally Accepted Accounting Principles. This responsibility includes; designing, implementing and maintaining internal

control relevant to the preparation and fair presentation of the financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

2. Scope of Audit and Basis of Opinion

My responsibility is to express an opinion on these financial statements based on my audit. Audit opinion, comments and findings in this report are based on review of the financial statements presented to audit and substantive tests of samples of transactions. The scope and extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitations of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes the examination on a test basis of evidence supporting the amounts and disclosures in financial statements and assessment of accounting policies used and significant estimate made by the management in the preparation of financial statements as well as evaluating their overall presentation. I have obtained sufficient information and explanations which to the best of my knowledge and belief were necessary for the purpose of my audit. I therefore believe that my audit provides a reasonable basis for my opinion. The examination also included such test of systems and controls, transactions, assets, liabilities and accounting records as deemed necessary to assess the following.

- (a) Whether the systems and controls were adequate from the point of view of internal control so as to ensure a satisfactory control over Project Management and the reliability of books, records, etc. relating to the operations of the Project.
- (b) Whether adequate accounting records were maintained on a continuing basis to show the expenditure of the Project from the funds of the GOSL and the Lending Agency, the progress of the Project in financial and physical terms, the assets and liabilities arising from the operations of the Project, the identification of the purchases made out of the Loan etc.

- (c) Whether withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.
- (d) Whether the funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (e) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (f) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles.
- (g) Whether the opening and closing balances, withdrawals from and replenishments to the Imprest Fund Account had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2013 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date.
- (h) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (i) Whether financial covenants laid down in the Loan Agreement had been complied with.

3. Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, except for the effects of the adjustments arising from the matters referred to in paragraph 5 of this report, I am of opinion that,

- a) The Project had maintained proper accounting records for the year ended 31 December 2013 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2013 in accordance with Generally Accepted Accounting Principles,

- b) The funds provided had been utilized for the purposes for which they were provided,
- c) The withdrawals from and replenishments to the Imprest Fund Account during the year ended 31 December 2013 had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2013 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,
- d) The Statements of Expenditure (SOEs) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement,
- e) Satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (f) The financial covenants laid down in the Loan Agreement had been complied with.

4. **Financial statements**

4.1 **Financial Performance**

According to the financial statements and information made available, the Project expenditure for the year ended 31 December 2013 amounted to Rs. 708,338,287 and the cumulative expenditure as at 31 December 2013 amounted to Rs.1,166,877,660. A summary of the expenditure for the year under review, expenditure for the preceding year and the cumulative expenditure as at 31 December 2013 is shown below.

Item -----	Expenditure for the year ended 31 December		Cumulative Expenditure as at 31 December 2013
	2013 Rs.	2012 Rs.	Rs.
Civil Works	618,923,189	334,789,848	972,038,166
Consultancy Service	18,043,803	58,670,926	115,998,453

Increment Operational Cost	64,402,312	4,263,954	68,666,265
Interest Charges	6,968,983	3,205,793	10,174,776
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Total	<u>708,338,287</u>	<u>400,930,521</u>	<u>1,166,877,660</u>

4.2 **Imprest Fund Account**

According to the financial statements and information made available, the operations of the Imprest Fund Account for the year ended 31 December 2013 and the balance available in that account as at 31 December 2013 are given below.

	<u>US \$</u>	<u>RS</u>
Balance as at 01 January 2013	1,059,018	134,665,570
Add: Replenishments	-	-
Foreign Exchange Gain	-	3,010,696
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	1,059,018	137,676,266
Less: Withdrawals	477,567	61,649,767
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Balance as at 31 December 2013	<u>581,451</u>	<u>76,026,499</u>

5. **Audit Observations**

The following observations are made.

- a) Office equipment and furniture and fittings Procured at a cost of Rs.686,863 had been shown under incremental operational cost instead of being shown under fixed cost.
- b) It was observed that a sum of Rs.2.7 million spent by the Project in connection with the other Projects implemented under Loan Nos. 1993, 2275 and 2276 had also been erroneously included under the incremental operating cost of this Project.
- c) Provisions for gratuity amounting to Rs. 5.5 million had been made in the financial statements of the Project in respect of the officers employed by the Project implemented under Loan No. 1993.

- d) Property, Plant and Equipment and other consumables purchased out of the GOSL contribution of the Project amounting to Rs. 1.1 million had been utilized by the Regional Offices of the NWSDB.
- e) A sum of Rs. 11,435,028 payable to four contractors which was eligible to be claimed from the Loan had inappropriately been accounted as Contribution receivable from General Treasury.

6. **Financial and Physical Performance**

6.1 **Utilization of Funds**

Certain significant statistics relating to the financing and budgetary provision and funds utilization during the year under review and the cumulative utilization as at 31 December 2013 are shown below.

Source	Amount agreed to be provided		Budgetary provision for 2013	Funds utilized during the year under review	Funds utilized as at 31 December 2013	
	US\$ (Mn)	Rs (Mn)	Rs (Mn)	Rs (Mn)	US\$ (Mn)	Rs (Mn)
ADB	13.30	1,206.30	417.00	414.72	6.8	870.03
GOSL	4.57	511.00	277.03	197.88	2.1	276.37
Total	<u>17.87</u>	<u>1,717.30</u>	<u>694.03</u>	<u>612.6*</u>	<u>8.9</u>	<u>1146.4*</u>

* The above mentioned figure differs from the figures shown in paragraph 4.1 of this report, due to effect of accrued expenses

6.2 **Physical Performance**

The following observations are made.

- (a) To ensure the achievement of Project objectives using allocated resources within schedule time period, there should be a comprehensive detailed Action Plan highlighting financial and physical targets with fixing responsibilities in monthly, quarterly, biannually basis covering entire Project period. Such plan had not been prepared and implemented by the Project.
- (b) Contracts awarded for construction of head work, raw water transmission and treatment plant (PA2) at Muttur at an estimated cost of Rs.1,213,378,199 from local funds and US\$. 4,214,369 from foreign funds was expected completion by 20 December 2013. The physical progress of those contracts as at 31 December 2013 had been only 75 per cent, and as such contract periods had been extended up to 30 June 2014.
- (c) The contracts on supplying and laying of treated water pumps for main distribution pipeline (10.5 Km) and construction of two elevated water treatment plants had been completed by the Project at a cost of Rs.1,162,504,731 on 30 September 2011 after delays in 2 years and remained idle even as at 31 December 2013 due to non-completion of the related works under other contracts such as raw water transmission treatment plant and treated water pumping which should have been completed parallel to the respective contract.

