

## **Local Government Infrastructure Improvement Project - 2013**

---

The audit of financial statements of the Local Government Infrastructure Improvement 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 read in conjunction with Section 4.02 (a) of Article IV of the Loan Agreement No 2201-SRI(SF) dated 19 January 2006 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 Local Government Infrastructure Improvement Project, the Ministry of Local Government and Provincial Councils is the Implementing Agency of the Project. The main objective of the Project is to increase the growth potential of and to reduce poverty in the selected Local Authorities in the Project Area. The purpose of the Project is to improve the urban environment, economy and the living conditions for the population of the Local Authorities in the Project Area through (i) Improving and expanding the infrastructure and services; (ii) enhancing urban livelihoods; and (iii) Improving urban management, planning and financing capacity of the Local Authorities. As per the Loan Agreement, the estimated total cost of the Project is US\$ 66.7 million and out of that US\$ 50 million was agreed to be financed by the Asian Development Bank. The Project commenced its activities on 04 July 2006 and was scheduled to be completed by 31 October 2011. According to the Letter of the Asian Development Bank dated 26 April 2012, the Project period had been extended up to 30 January 2013. However, the activities of the project had been continued up to 31 December 2013 using contribution received from the Government of Sri Lanka.

### **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 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 estimates 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 Government of Sri Lanka 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, material and equipment supplied under the Loan had been utilized for the purpose 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 (CBSL) as at that date,
- (h) Whether 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,
- (i) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (j) Whether the 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) opening and closing balances, 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 expenditure of the Project for the year ended 31 December 2013 amounted to Rs. 16,149,228 and the cumulative expenditure as at 31 December 2013 amounted to Rs. 6,294,027,071. A summary of the component wise expenditure of the Project for the year under review, expenditure for the preceding year and cumulative expenditure as at 31 December 2013 is given below.

Item of Expenditure	Expenditure for the year ended 31 December		Cumulative Expenditure as at 31 December 2013
	2013	2012	
	Rs.	Rs.	Rs.
<b><u>Component-A</u></b>			
Workshops	-	599,815	5,878,418
Manpower Development	-	20,248,824	52,567,075
<b><u>Component-B</u></b>			
Civil Engineering	-	1,447,524,413	4,418,555,009
Equipment	-	34,275,045	453,905,749
<b><u>Component-C</u></b>			

Property, Plant and Equipment	-	168,329	87,111,839
Modernization	-	-	4,675,132
Consultancy	106,644	77,799,913	597,953,295
Administration cost	16,042,584	94,444,454	564,539,452
Interest	-	45,969,250	108,841,103
	-----	-----	-----
	16,149,228	1,721,030,043	6,294,027,072
	=====	=====	=====

## 4.2 Imprest Fund Account

-----

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

	US\$	Rs.
Balance as at 01 January 2013	1,803,147.18	229,289,638
Add: Replenishments	152,165.84	19,948,942
Foreign Exchange Gain	-	260,147
	-----	-----
	1,955,313.02	249,498,727
Less: Withdrawals	1,457,122.21	184,358,784
	-----	-----
Balance as at 31 December 2013	498,190.81	65,139,943
	=====	=====

## 5. Audit Observations

-----

### 5.1 Presentation of the Financial Statements

-----

According to the Section 2.09 (a) of the Project Agreement, the audited annual financial statement should be furnished to the Lending Agency within 06 month at the end of the financial year. However, the draft financial statement of the Project for the year ended 31 December 2013 had been furnished for audit only on 17 October 2014.

### 5.2 Accounting Deficiencies

-----

Assets valued at Rs.87,111,839 had been continuously shown in the Balance Sheet as at 31 December 2013 even though such assets had already been transferred to other Project called Local Government Enhancement Sector Project.

### 5.3 Utilization of Funds

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

Sources	Amount agreed for financing in the Loan Agreement		Budgetary provision for the year 2013	Funds Utilized during the year 2013	Funds utilized as at 31 December 2013	Utilization of funds up to 31 December 2013 as a percentage of the provision
	USD million	Rs. million	Rs. million	Rs. million	Rs. million	
ADB	46.0*	4,933	181	168.28	4,511.28	91.45
GOSL	16.7	1,541	71	70.1	1,421.1	92.21
Total	62.7	6,474	252	238.38**	5,932.38**	91.63

\* As per Letter dated 08 September 2011 of Department of External Resources, US\$ 4 million, out of total amount of US\$ 50 million agreed to be financed had been transferred to other Project called "Local Government Enhancement Sector Project (Puranaguma)".

\*\* These amounts had not been agreed with the figures given in the paragraph 4.1 of the report as the expenses incurred by the Local Authorities was not included.

### 5.4 Closure of the Activities of the Project

The activities of the Project had been scheduled to be completed as at 30 January 2013 and completion report of the Project had been submitted by the Project Director on April 2013. However, action had not been taken by the Executing Agency of the Project to close the activities of the Project.