

Monaragala, Buttala Integrated Water Supply Project - 2014

The audit of financial statements of the Monaragala, Buttala Integrated Water Supply Project for the first accounting year ended 31 December 2014 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 the Credit Agreement dated 16 June 2014 entered into between the Democratic Socialist Republic of Sri Lanka and KBC Bank NV of Belgium.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Credit Agreement of the Project, then Ministry of Water Supply and Drainage, presently the Ministry of City Planning and Water Supply is the Executing Agency and the National Water Supply and Drainage Board is the Implementing Agency of the Project. The objective of the Project is to provide improved water supply to 50,000 household consumers and other consumers in commercial and industrial sectors in Monaragala and Buttala towns and suburban areas. The estimated total cost of the Project amounted to Euro 31.41 million equivalent to Rs.5,545.48 million. Out of that the KBC Bank NV had agreed to provide Euro 13 million equivalent to Rs. 2,291.76 million as a Loan and Euro 02 million equivalent to Rs. 353.27 million as a Grant under the Belgium Export Portion. The Hatton National Bank had agreed to provide Euro 8.98 million equivalent to Rs.1,590.45 million The Project commenced its activities on 30 December 2014 and scheduled to be completed by 30 June 2017.

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 Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

1.4 Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Project's preparation and fair presentation of the financial statements 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 Project's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management as well as evaluating the overall presentation of the financial statements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion. The examination also included such tests 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 the expenditure shown in the financial statements of the Project had been satisfactorily reconciled with the enhanced financial reports and progress reports maintained by the Project.
- (c) 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 Agencies, the progress of the Project in financial and physical terms, the assets and liabilities arising from the operations of the Project, the identifications of the purchases made out of the Loan, etc
- (d) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Credit Agreement.
- (e) Whether the funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (f) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (g) Whether the financial statements had been prepared on the basis of Sri Lanka Accounting Standards, and
- (h) Whether the financial covenants laid down in the Credit Agreement had been complied with.

2. Financial Statements

2.1 Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2014 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2014 in accordance with Sri Lanka Accounting Standards,
- (b) the funds provided had been utilized for the purposes for which they were provided, and
- (c) the financial covenants laid down in the Credit Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Presentation of the Financial Statements

The financial statements of the year ended 31 December 2014 required submit to the Auditor General on or before 31 March 2015, as required by the Circular No. MOFP/ERD/2007/02 of 07 August 2007 of the Ministry of Finance and Planning had been submitted for audit only on 30 August 2017.

2.2.2 Non - Compliance with Laws, Rules and Regulations

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

- (a) According to the paragraph 8.9.3 of the Government Procurement Guidelines 2006, the formal contract agreement of the Project is required to be signed by the Secretary to the Line Ministry. However, formal contract agreement of the Project was signed by the Chairman of the National Water Supply and Drainage Board.
- (b) According to the Section 6 (1) a of the Public Contract Act, No. 03 of 1987 and 13 supplementary to the Procurement Guideline in 2006, the contractors those who accepted contracts Rs. 5 million or more required to be registered under Registrar of Public Contract. Further, within 60 days after awarding the contract, the contract agreement should be registered with the Registrar of Public Contract. However, the contractor who dealt with the activities of the Project had not complied with the above requirements.

2.2.3 Un-reconciled Balances

The value of work-in-progress amounting to Rs. 4.24 million shown in the financial statements of the Project for the year ended 31 December 2014 was not agreed with corresponding value of work-in-progress amounting to Rs. 4.74 million shown in the financial statements of the National Water Supply and Drainage Board.

3. Financial and Physical Performance

3.1 Utilization of Funds

Certain significant statistics relating to the financing, budgetary provision for the year under review and the utilization of funds up to 31 December 2014 are shown below.

Source	Amount agreed for financing in the Credit Facility Agreement		Allocation made in the Budget Estimate for the year under review	Funds utilized as at 31 December 2014	
	Euro million	Rs. million		Rs. million	Euro million
KBC – Loan	13.00	2,291.76	} 550	2.99	478.04
Grant	2.00	353.27			
HNB	8.98	1,590.45	-	1.81	286.18
GOSL	7.43	1,310.00	-	0.03	4.23
Total	<u>31.41</u>	<u>5,545.48</u>	<u>550</u>	<u>4.83</u>	<u>768.45</u>

The following observations are made in this regard.

- (a) It was observed that a Subsidiary Loan Agreement had not been signed between the National Water Supply and Drainage Board and the Government of Sri Lanka on repayment of Loans obtained from foreign and local agencies. Therefore, the proceeds aggregating Rs.764.24 million received during the year under review had been erroneously segregated and shown in the financial statements, as the proceeds of Loans amounting Rs.114.64 million and Grant amounting to and Rs 649.61 million. According to the records maintained by the Department of External Resources, the proceeds of Loans and Grant amounting to Rs.482.25 million and Rs.291.22 million respectively had been received during the year under review.
- (b) To ensure the achievement of Project objectives using allocated resources within scheduled time period, there should be a comprehensive detailed action plan highlighted financial and physical targets with fixing responsibilities in monthly, quarterly, biannually etc. covering entire period of the Project. However, such a plan had not been prepared and implemented by the Project.
- (c) It was observed that the Engineering Estimates on civil works made at a cost of Euro 20.67 million equivalent to Rs.3,100.50 million by the National Water Supply and Drainage Board in 2011 had been revised subsequently as Euro 19.67 million equivalent to Rs.2,950.50 million. However, the contract had been awarded at a cost of Euro 23.98 million equivalent of Rs.3,597 million.

3.2 Physical Progress

The following observations are made.

- (a) According to the paragraph 3.3 of the Supplement - 23 of the Government Procurement Guidelines, the financing terms under the unsolicited contracts should be at least with 15 years repayment period including 03 years grace period. However, the unsolicited contract agreement entered by the Project to carry out the activities of the Project consisted with the period of 03 ½ years including 06 months grace period.
- (b) According to the documents of the Project, the construction works of Intake and Ground Reservoir at Buttala, office and administrative buildings, officers' quarters and pipe laying for distribution purposes etc required to be commenced during the year under review had not been commenced even as at 31 December 2014, eventhough a contractor had been selected for the respective works.

3.3 Issues on Financial Control

The following observations are made.

- (a) The financial statements of each project should be prepared based on separate accounting records maintained by the Project as required by the Financial Regulations 626. It was observed that the general cash book of the National Water Supply and Drainage Board had been used to record receipts and payments of the Project, contrary to the above mentioned requirement.

- (b) According to the Treasury Circular No. 842 dated 31 December 1988, a Fixed Asset Register of the Project had not been maintained in proper manner.
- (c) According to the Financial Regulation 133 and Management Audit Circular No. 05 of 26 July 2010, the activities of the Project had not been audited by the Internal Audit Section of the National Water Supply and Drainage Board.