

## **North and East Water Supply, Sanitation and Hygiene (WASH) Project - 2014**

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The audit of financial statements of the North and East Water Supply, Sanitation and Hygiene (WASH) Pilot Project for the 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 Article 2.06 (c) of Grant Agreement No. TF10773 dated November 2011 entered into between the Democratic Socialist Republic of Sri Lanka and the Australian Agency for International Development.

### **1.2 Implementation, Objectives, Funding and Duration of the Project**

According to the Grant Agreement of the Project, then the Ministry of Water Supply and Drainage, presently the Ministry of Urban Development and Water Supply and Drainage is the Executing Agency and National Water Supply and Drainage Board is the Implementing Agency of the Project. The objectives of the Project are to increase accessibility to safe and sustainable pipe borne water supply and sanitation to complement post conflict housing reconstruction interventions in selected rural communities within two districts of the Northern and Eastern Provinces, including piloting of viable mechanism to strengthen institutional systems to deliver local level water, sanitation and hygiene services, eventually generating lessons and replicable models to contribute to the overall improvement of hygiene practices and to the overall quality of life of communities of returnees. According to the Grant Agreement, the estimated total cost of the Project was US\$ 2.01 million equivalent to Rs 220 million was agreed to be provided by the Australian Agency for International Development. Further, the Cabinet of Ministers had decided at the meeting held on 06 October 2011 to allocate a sum of Rs 40 million for the Project. The Project commenced its activities on November 2011 and scheduled to be completed by 30 June 2014. However, the period of the Project had been extended up to 31 October 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 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 Donor Agency, 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 Grant, etc.
- (d) Whether the withdrawals under the Grant had been made in accordance with the specifications laid down in the Grant Agreement.
- (e) Whether the funds, materials and equipment supplied under the Grant 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 Generally Accepted Accounting Principles.
- (h) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and

- (i) Whether the financial covenants laid down in the Grant Agreement had been complied with.

## **1.5 Basis for Qualified Audit Opinion**

My opinion is qualified based on the matters described in paragraph 2.2 of this report

## **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, except for the effects of the adjustments arising from the matters referred to in paragraph 2.2 of this report 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 Generally Accepted Accounting Principles.
- (b) the funds provided had been utilized for the purposes for which they were provide.
- (c) the Statement of Expenditure (SOEs) submitted could be fairly relied upon to support the applications for reimbursement in accordance with requirements specified in the Grant Agreement.
- (d) the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (e) the financial covenants laid down in the Grant Agreement had been complied with.

### **2.2 Comments on Financial Statements**

#### **2.2.1 Accounting Deficiencies**

The following observations are made.

- (a) Value added Tax (VAT) of Rs.26,348,251 paid during the year 2014 had been set off against the contribution received from the Government of Sri Lanka without being charged to the work-in-progress. As a result, both contribution of Government of Sri Lanka and the value of work-in-progress shown in the financial statements as at 31 December 2014 had been understated by similar amounts.
- (b) The costs aggregating Rs.670,691 incurred in connection with surveying of a land in Mannar and partitioning of the office of the Rural Water Section of the National Water Supply and Drainage Board had been erroneously shown as the costs of furniture and equipment.

**2.2.2 Non - Compliance with Laws, Rules and Regulations**

The following non-compliances were observed.

- (a) A monthly report on payment of Value Added Taxes aggregating Rs.4,405,631 had not been furnished to the Commissioner General of Inland Revenue with a copy to the Auditor General according to Section 21 of the Value Added Taxes Act, No. 14 of 2002 and Paragraph 5 of Public Finance Circular No. 364(3) of 30 September 2002.
- (b) According to Section 8 of the Public Contract Act, No. 03 of 1987, the contractors who accepted contracts valued at Rs. 5 million or more should be registered under Register of Public Contract. Further, the tender agreement should be registered with Register of Public Contract within 60 days. However, such requirements had not been complied with by the contractors who selected by the Project.

**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 during the year under review and up to 31 December 2014 are shown below.

Source	Amount agreed for financing in the Grant Agreement		Allocation made in the Budget Estimate for the year under review	<u>Funds utilization</u>			
	US \$ million	Rs. million	Rs. million	during the year 2014		up to 31 December 2014	
	US \$ million	Rs. million	Rs. million	US \$ million	Rs. million	US \$ million	Rs. million
Donor Agency	2.01	220	80	0.47	61.44	2.01	259.27
GOSL	-	40	27	0.24	26.99	0.45	59.00
	<u>2.01</u>	<u>260</u>	<u>107</u>	<u>0.71</u>	<u>88.43</u>	<u>2.46</u>	<u>318.27</u>

**3.2 Physical Performance**

The following observations are made.

- (a) Although detailed action plan had been prepared covering the entire project period by highlighting financial and physical targets in quarterly manner, a proper mechanism such as preparation of progress reports, keeping records on progress review meetings etc. had not been established to review the performance of the Project comparing with the action plan.

- (b) The following observations are made on the operations of the Project under the Component of providing of sanitation and hygiene services in Mannar and Trincomalee Districts.
- (i) According to the Implementation Plan of the Project, it was expected to improve 900 units of household toilets in 12 villages in Mannar and Trincomalee Districts during the period of the Project. However, the Rural Water Sector Division of the National Water Supply and Drainage Board had estimated to improve 800 units of household toilets only, as the householders in Kaddukarankuiyiruppu village in Mannar District had not made any request thereon.
  - (ii) According to the information furnished for audit, out of 606 units of household toilets estimated, only 517 units of household toilets had been completed by the Project in Trincomalee District as at 31 December 2014. The details of the progress of the activities carried out in this respect in Mannar District was not made available for audit.
  - (iii) Further, the awareness programmes, as scheduled had not been conducted thereon by the Project even at the end of the period of the Project.
- (c) The following observations are made on the operations of the Project under the Component to increase the accessibility to safe and sustainable pipe borne water supply in Mannar and Trincomalee Districts.
- (i) It was observed that the target of the Implementation Plan of the Project to supply safe drinking water to 3,000 families in Mannar and Trincomalee Districts had been revised to 2,480 families subsequently. Further, it was observed that the completion of the water supply schemes had been delayed for the period ranging from 65 to 133 days.
  - (ii) According to the information furnished by the Project, 1,339 families in 10 villages of Mannar District and 1,149 families in 07 villages in Trincomalee District had made requests to purchase of water meters and pipe water connections to their households. According to the progress reports of the Project, 1,188 water meters had been purchased by the villagers in Mannar District whilst 1,039 pipe water connections had been provided by the Project as at 31 December 2014. Further, 1,126 water meters had been purchased by the villagers in Trincomalee District whilst 906 pipe water connections had been provided by the Project as at that date.

### **3.3 Contract Administration**

The following observations are made.

- (a) The Project had released the retention money amounting to Rs. 1,598,554 to a contractor before expiry of the defect liability on a unconditional Bank Guarantees.
- (b) It was observed the rock blasting works on earth excavation for construction of two dug wells had been carried out under a variation order valued at Rs.1,912,876 and the rock material of 208.15 square metre produced thereon had been dumped at the work site without using such material economically.

### **3.4 Funds of the Project Utilized for Other Purposes**

A sum of Rs.162,255 had been spent by the Project, out of the grants proceed of the Government of Sri Lanka to procure 02 air conditioners for the National Water Supply and Drainage Board.

### **3.5 Issues on Financial Control**

According to Financial Regulation 134(3) and Management Audit Circular No. 05 of 20 July 2010, the activities of the Project had not been audited by the Internal Audit Section of the National Water Supply and Drainage Board.