

Kandy City Wastewater Management Project - 2015

The audit of financial statements of the Kandy City Wastewater Management Project for the year ended 31 December 2015 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 Loan Agreement No. SLP 99 dated on 26 March 2010 entered in to between Democratic Socialist Republic of Sri Lanka and the Japan Bank of International Cooperation, presently known as Japan International Cooperation Agency.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan 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 improve the living environment and water quality of Mahaweli River through better sanitation facilities by constructing a proper system for collection, treatment and disposal of wastewater in Kandy City including rehabilitation of sanitation facilities in densely populated areas and thereby enhance the standard of living, health and well-being of the people in the area. The estimated total cost of the Project amounted to Japan Yen 17,278 million equivalent to Rs. 21,982 million and out of that Japan Yen 14,087 million equivalent to Rs.17,922 million was agreed to be provided by the Japan International Cooperation Agency. The Project commenced its activities on 20 September 2011 and scheduled to be completed by September 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 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 Lending 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 Loan etc.
- (d) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan 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 Statements of Expenditure submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement.
- (h) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles.
- (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.

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 2015 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2015 in accordance with Generally Accepted Accounting Principles,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the Statements of Expenditure submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan 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 Loan Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Presentation of Financial Statements

According to the Circular No MOFP/ERD/2007/2 of 07 August 2007 of the Ministry of Finance and Planning, the financial statements of the Project for the year ended 31 December 2015 required to be submitted to the Auditor General on or before 31 March 2016 had only been submitted on 11 November 2016.

2.2.2 Non - Compliance with Laws, Rules and Regulations

According to the Section 8 of the Public Contract Act, No. 03 of 1987, contractors who accepted contracts valued at Rs. 5 million or more should be registered under Registrar of Public Contract. Further, the contract agreements should be registered with Registrar of Public Contract within 60 days after the awarding of the contractor. It was observed that 02 contractors who entered in to contract agreements with the Project had not complied with the above mentioned requirements. Eventhough this matter was highlighted in my previous audit reports, no action had been taken to comply with the regulations.

2.2.3 Lack of Documentary Evidence for Audit

The contractor had spent a sum of Rs. 3.05 million during the year under review to procure furniture and fittings. However, supporting documents and other evidence thereon had not been made available for audit.

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 2015 are shown below.

Source	Amount agreed for financing according to the Loan Agreement		Allocation made in the Budget Estimate for the year under review	<u>Funds utilized</u>			
	JPY million	Rs. million		Rs. million	JPY million	Rs. million	JPY million
JICA	14,087	17,922	3,226	410.60	470.00	1,367.90	1,707.90
GOSL	3,191	4,060	312	14.22	16.22	193.52	247.60
Total	<u>17,278</u>	<u>21,982</u>	<u>3,538</u>	<u>424.82</u>	<u>486.22</u>	<u>1,561.42</u>	<u>1,955.50</u>

The following observations are made in this regard.

- (a) A sum of Japan Yen 1,367.9 million equivalent to Rs 1,707.9 million representing 9 per cent, out of the allocation of Japan Yen 14,087 million equivalent to Rs. 17,922 million had only been utilized as at 31 December 2015, after lapse of 04 years from the date of commencement of the activities of the Project. In addition, out of the allocation amounting to Rs. 3,538 million made in the Budget Estimate for the year 2015, only Rs. 486.22 million equivalent to 13 per cent had been utilized during the year under review.
- (b) As mentioned in my previous audit reports, the Project had not prepared comprehensive plan to achieve objectives of the Project using allocated resources and as a result, a slow progress of 16.65 per cent on physical activities and 11.36 per cent on utilization of funds of the Project had been shown as at 31 December 2015. Therefore, commitment charges amounting to Rs. 104.5 million on funds underutilized had to be paid by the Project as at 31 December 2015.

3.2 Physical Progress

According to the progress reports of the Project, the civil construction works expected to be carried out at an estimated cost of Japan Yen 12,636 million equivalent to Rs. 16,077 million had been implemented under 04 major packages. However, the civil construction works under the Package - 01 expected to be commenced in July 2015 was not commenced even up to 31 December 2015. Further, the civil construction works under Package - 02 which expected to be commenced in July 2012 was commenced only in April 2015 and physical progress thereon was remained at 17 per cent at the end of the year under review. The contracts for the civil construction works under other 02 packages had not been awarded even up to 31 December 2015. Therefore, the risks of completion of the activities of the Project during the target period and price fluctuations thereon cannot be ruled out in audit.

3.3 Contract Administration

The following observations are made

- (a) The National Water Supply and Drainage Board had obtained a land on lease basis for main pump station at Bowala at a cost of Rs. 1.09 million in November 2005 under the Phase-01 of the Project. However, action had not been taken to enter into a lease agreement with the Urban Development Authority thereon until 30 November 2016.
- (b) According to the Environment and Safety Management Plan, precautionary actions are required to be taken in carrying out of the construction works of the Project to avoid harmful effects on environment. However, 119 complaints received by the Project thereon within 04 months period of the year under review and it proved that contractor had not adhered with necessary safety requirements.

3.4 Issues on Financial Control

The following observations are made

- (a) The Board of Surveys on property, plant and equipment valued at Rs. 15.78 million procured by the Project had not been carried out during the year under review, as required by the Financial Regulation No.756. Further, the Fixed Assets Register required to be maintained as per the Treasury Circular No. 842 of 19 December 1978 had not been maintained.
- (b) The transactions of the Project during the year under review was not subjected to audit of the Internal Audit Section of the National Water Supply and Drainage Board, as per the Financial Regulation 134 (3) and Circular No. 05 of 26 July 2010 of the Department of Management Services.