

Greater Colombo Wastewater Management Project - 2016

The audit of financial statements of the Greater Colombo Wastewater Management Project for the year ended 31 December 2016 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 2.09 of Article II of the Loan Agreements No. 2557/2558 SRI dated on 18 December 2009 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreements of the Project, the Ministry of Provincial Councils and Local Government is the Executing Agency of the Project. The Colombo Municipal Council is responsible for the implementation of works within Municipal Council area and the National Water Supply and Drainage Board is responsible for the implementation of works within Kolonnawa Urban Council and Dehiwala / Mt. Lavinia Municipal Council areas. My observations on the activities carried out by the National Water Supply and Drainage Board are contained in this report. The objective of the Project is to improve the urban environment and public health for the urban and sub urban residents in the Greater Colombo area through wastewater management services. The expected outcome of the Project is to improve the wastewater management services to 645,000 residents within the area. As per the Loan Agreements, the estimated total cost of the Project amounted to US\$ 116.60 million equivalent to Rs. 13,410 million and out of that US\$ 80 million equivalent Rs. 9,200.80 million or 68.6 per cent was agreed to be financed by the Ordinary Capital Resources of the Asian Development Bank and US\$ 20 million equivalent to Rs.2,300.20 million or 17.1 per cent was agreed to be financed by the Special Funds Resources of the Asian Development Bank. The balance amount of US\$ 16.60 million equivalent to Rs. 1,909 million or 14.3 per cent was scheduled to be contributed by the Government of Sri Lanka. Out of that, a sum of US\$ 12.60 million equivalent to Rs. 1,731.70 million of the total estimated cost of the Project had been allocated to the activities to be carried out by the National Water Supply and Drainage Board. Further, a subsidiary Financing Agreement was signed on 02 July 2010 between the Democratic Socialist Republic of Sri Lanka and the National Water Supply and Drainage Board to provide SDR 3.6 million (US\$ 5.64 million) equivalent to Rs. 647.68 million in a blend of 82.5 per cent as a Grant and 17.5 per cent as a Loan. The balance sum of US\$ 3.17 million equivalent to Rs. 364.35 million was agreed to be financed by the Government of Sri Lanka. The Project commenced its activities on 18 December 2009 and scheduled to be completed by 31 December 2014. Subsequently, period of the Project had been extended up to 30 March 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 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 Loans etc.
- (d) 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 Agreements.
- (e) Whether the opening and closing balances and withdrawals from and replenishments to the Special (Dollar) Account had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2016 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date.
- (f) Whether the withdrawals under the Loans had been made in accordance with the specifications laid down in the Loan Agreements.
- (g) Whether the funds, materials and equipment supplied under the Loans had been utilized for the purposes of the Project.
- (h) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.

- (i) Whether the financial statements had been prepared on the basis of Sri Lanka Accounting Standards.
- (j) Whether the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (k) Whether the financial covenants laid down in the Loan Agreements 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 2016 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2016 in accordance with Sri Lanka Accounting Standards,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the opening and closing balances and withdrawals from and replenishments to the Special (Dollar) Account had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2016 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,
- (d) 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 Agreements,
- (e) the 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 Agreements had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following accounting deficiencies were observed in audit.

- (a) Value Added Tax aggregating to Rs. 62.13 million paid up to 31 December 2016 by the Project had been set off against the contribution received from the Government of Sri Lanka instead of being shown under work-in-progress.

- (b) According to the financial statements of the National Water Supply and Drainage Board, the work-in-progress of the activities carried out by the Project as at 31 December 2016 amounted to Rs. 763.62 million. However, according to the financial statements of the Project it was shown as Rs. 754.56 million.

2.2.2 Non - Compliance with Laws, Rules and Regulations

The Construction Industries Guarantee Fund Levy had not been recovered by the Project on payments aggregating Rs. 666.29 million made to the contractors as at 31 December 2016 and remitted to the Department of Inland Revenue as required by the Part III of the Finance Act, No.05 of 2005.

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 2016 are shown below.

Source	Amount agreed for financing according to the Loan Agreements		Allocation made in the Budgets Estimate for the year under review	<u>Funds utilized</u>			
	US\$ million	Rs. million		US\$ million	Rs. million	US\$ million	Rs. million
ADB	9.43	1,367.35	484	2.31	336.02	4.87	684.55
GOSL	3.17	364.35	150	0.53	77.32	1.05	148.32
Total	<u>12.60</u>	<u>1,731.70</u>	<u>634</u>	<u>2.84</u>	<u>413.34</u>	<u>5.92</u>	<u>832.87</u>

It was observed that the Project had not established a proper mechanism to complete the activities within the period of the Project as there was no comprehensive plan prepared to ensure the achievement of its objectives. It was further proved that the Project had utilized US\$ 5.92 million only representing 47 per cent of the total allocation of US\$ 12.60 million as at 31 December 2016, after lapse of 06 years from the commencement of the activities of the Project. Further, out of the allocation of Rs. 634 million made in the Budget Estimate for the year 2016, only Rs. 413.34 million representing 65 per cent had been utilized during the year under review.

3.2 Physical Progress

According to the progress reports furnished by the Project, the overall physical and financial progress of the Project at the end of the year under review was remained as 89 per cent and 60.5 per cent respectively. The period of the Project had been extended up to 30 March 2017 due to delays in awarding of the contracts for rehabilitation and augmentation of 06 Wastewater Pump Stations at Dehiwala, Mt. Lavinia and Kolonnawa Urban Council areas and further, the period of the contract had been extended up to 30 June 2017 due to disagreement with the contractor relating to the imported submersible pumps.

3.3 Contract Administration

The following observations are made.

- (a) The Project had awarded a contract for civil works at US\$ 7.79 million equivalent to Rs. 1,028 million on 15 July 2014, even though US\$ 5.63 million equivalent to Rs. 739 million only had been allocated for the respective contract. The balance amount of US\$ 3.75 million equivalent to Rs. 289 million had been allocated by the Colombo Municipal Council.
- (b) It was observed that the designs of the works and Bill of Quantities thereon had not been prepared properly by the Project. As a result, the contractor had submitted 33 variation orders at a cost of US\$ 774,918 equivalent to Rs. 111.45 million and out of that the Project had settled the claims of US\$ 458,886 equivalent to Rs. 65.99 million for 10 variation orders submitted up to 31 December 2016.
- (c) The activities of the Project were formulated with broader perspectives of improving the urban environment and public health and systematic disposal of sewerage and wastewater through the existing transmission. However, it was observed in field audit inspection carried out on 13 July 2017 that sludge out from the process exaggerate in pump station without purifying and ruff stone and sand inject to pump house yard. Therefore, risk of environmental pollution and impact of employee's health thereon cannot be ruled out in audit.

3.4 Issues on Financial Control

The following observations are made.

- (a) 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 Management Audit Circular No. 05 of 26 July 2010 of the Department of Management Services.
- (b) The documentary evidence had not been made available to the audit regarding information on 35 trees cut down and revenue collected thereon by the Project.