

## **Greater Colombo Water and Wastewater Management Improvement Investment Programme Project - 2 - 2016**

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The audit of financial statements of the Greater Colombo Water and Wastewater Management Improvement Investment Programme Project - 2 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 4.05 of Article IV of the Loan Agreement No. 3029-SRI and Section 4.03 of Article IV of the Loan Agreement No. 3030 – SRI (SF) of 03 June 2014 entered into between the Democratic Socialist Republic of Sri Lanka (GOSL) and the Asian Development Bank (ADB) and Chapter V of the Project Administration Manual.

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

According to the Loan Agreements of the Greater Colombo Water and Wastewater Management Improvement Investment Programme Project 2, 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 efficiency and financial sustainability of water supply and wastewater services in the Greater Colombo area. As per the Loan Agreements, the estimated total cost of the Project amounted to US\$ 118 million equivalent to Rs.15,340 million and out of that US\$ 70 million equivalent to Rs.9,100 million or 59.3 per cent of the total estimated cost of the Project was agreed to be financed by the Ordinary Capital Resources of the Asian Development Bank and US\$ 18 million equivalent to Rs. 2,340 million or 15.3 per cent of the total estimated cost of the Project was agreed to be financed by the Asian Development Fund. The balance amount of US\$ 30 million equivalent to Rs. 3,900 million or 25.4 per cent was expected to be contributed by the Government of Sri Lanka. Further, out of the estimated total cost of the Project, allocation of US\$ 107.05 million equivalent to Rs. 13,917 million had been made for the activities of the Project expected to be carried out by the National Water Supply and Drainage Board and US\$ 10.95 million equivalent to Rs. 1,423 million had been allocated for the activities of the Project expected to be carried out by the Colombo Municipal Council. This report consisted with the observations made on the activities of the Project implemented by the National Water Supply and Drainage Board. The Project commenced its activities on 23 September 2014 and scheduled to be completed by 30 June 2019.

### **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 Loan, etc.
- (d) 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.
- (e) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreements.
- (f) Whether the funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (g) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (h) Whether the financial statements had been prepared on the basis of Sri Lanka Accounting Standards.
- (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 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 (CBSL) 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 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 Deficiency**

Value Added Tax aggregating Rs. 10.61 million had been paid and set off against the proceeds of Government contribution instead of shown under the work-in-progress. As a result, the work-in-progress valued at Rs. 92.87 million and the proceeds of contribution received from the Government of Sri Lanka amounting to Rs.108.02 million shown in the financial statements as at 31 December 2016 were understated by similar amount respectively.

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

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

- (a) According to the Circular No. MOFP/ERD/2007/02 of 07 August 2007 of the Ministry of Finance and Planning, the financial statements of the year ended 31 December 2016 are required to be submitted to the Auditor General on or before 31 March 2017. However, the financial statements of the Project had been submitted only on 25 April 2017.

- (b) According to the Section 17 of the Project Administration Manual of the Asian Development Bank, interest and other charges during the construction should be capitalized. However, interest of Rs.1.58 million and commitment charges amounting to Rs. 15.21 million had not been brought to the accounts as the costs incurred by the Project.
- (c) According to the Section 6(1) (a) of the Public Contract Act. No 03 of 1987, 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 agreements should be registered with the Registrar of Public Contract. However, the contractors who deal with the activities of the Project had not complied with the above requirements.
- (d) The formal contract agreements of the system rehabilitation for the Non- Revenue Water of Southern and Western of Colombo City had been signed by the Chairman of the National Water Supply and Drainage Board instead of the Secretary to the Line Ministry, as required by the paragraph 8.9.3 of the Government Procurement Guidelines.

### 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 in the Loan Agreements		Amount agreed for financing to NWSDB		Allocation made in the Budget Estimate for the year under review	Fund utilized			
	US\$ million	Rs. million	US\$ million	Rs. million		during the year under review		as at 31 December 2016	
	US\$ million	Rs. million	US\$ million	Rs. million	Rs. million	US\$ million	Rs. million	US\$ million	Rs. million
ADB	88	11,440	79.95	10,394	1,034.00	6.70	998.30	7.11	1,058.70
GOSL	30	3,900	27.10	3,523	460.41	0.63	95.00	0.79	118.62
<b>Total</b>	<b><u>118</u></b>	<b><u>15,340</u></b>	<b><u>107.05</u></b>	<b><u>13,917</u></b>	<b><u>1,494.41</u></b>	<b><u>7.33</u></b>	<b><u>1,093.30</u></b>	<b><u>7.90</u></b>	<b><u>1,177.32</u></b>

According to the above information, only US\$ 7.11 million equivalent to Rs.1,058.70 million out of US\$ 79.95 million equivalent to Rs.10,394 million allocated for the National Water Supply and Drainage Board had been utilized after lapse of 31 months of operations as at 31 December 2016, out of 60 months of operations scheduled in the Agreement of the Project.

Further, it was observed that the completion of activities of the Project within specific Project period is in doubt due to lack of comprehensive plan to ensure the achievement of Project objectives using allocated resources within scheduled time period, highlighting financial and physical targets with responsibilities, covering entire period of the Project.

### **3.2 Physical Progress**

According to the progress reports furnished by the Project, the overall physical progress of the Project as at end of the year under review was remained at 3.66 per cent. Further, 07 contracts scheduled to be awarded, out of 13 contracts had not been awarded up to 31 December 2016.

### **3.3 Contract Administration**

The following observations are made.

- (a) Eventhough the activities of the Project is scheduled to be completed by 30 June 2019, the completion date of the contracts for the system rehabilitation for Non Revenue Water for Western Colombo City awarded had been determined as 31 March 2021, beyond the period of the Project.
- (b) The advertisement for calling bids for the contract for System Rehabilitation of Western Part of Colombo City was made on 01 December 2014 and the respective contract had been awarded on 20 October 2016 after lapse of 22 months. However, the activities of the contract had not been commenced even up to 31 December 2016. Further, the bid document for design and build contract for System Rehabilitation in Southern Part of the Colombo City had been approved by the Standard Cabinet Appointment Procurement Committee on 20 March 2014 and the contract was awarded only on 26 January 2017, after lapse of 34 months from the date of approval received.
- (c) According to the Government Procurement Guide Lines 5.3.14 (a) all prospective bidders shall be provided with the same information and shall be assured equal opportunities to obtain additional information. Eventhough the changes had been made in the several items of the Bill of Quantities subsequently, it is doubtful in audit that respective information was communicated to all bidders properly as the bidder who submitted lowest bid had quoted his prices on items of the Bill of Quantities published previously. The Project had revised the prices quoted by the bidder arbitrarily and evaluations made accordingly.

### **3.4 Issues on Financial Control**

According to the Financial Regulation 133 and Management Audit Circular No 05 of July 2010, the activities of the Project required to be audited by the Internal Audit Section of the National Water Supply and Drainage Board. However, Internal Audit Report on the audit of activities carried out by the Project had not been submitted to the Auditor General.