

SUSTAINABLE POWER SECTOR SUPPORT PROJECT - 2017

The audit of financial statements of the Sustainable Power Sector Support Project for the year ended 31 December 2017 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 Sections 4.05 (a) and 4.03 (a) of Article IV of the Loan Agreements Nos 2733 - SRI (SF) and 2734 - SRI (SF) dated 20 June 2011 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 Power and Renewable Energy is the Executing Agency and the Ceylon Electricity Board is the Implementing Agency for part - 01 to part 06 and part 09 and 10 of the Project whilst the Sri Lanka Sustainable Energy Authority is the Implementing Agency for Part 07 and 08 of the Project. My observations on the activities carried out by Ceylon Electricity Board under the Part 01 to Part 06 and Part 09 and 10 of the Project are contained in this report. The objectives of the Project are to provide reliable, adequate and affordable power supply expanding coverage and improving efficiency and reliability in service delivering through (a) strengthened transmission system in the Eastern, North Central, Southern and Uva Provinces, (b) broadened rural electrification in the Eastern and Uva Provinces and (c) enhanced energy efficiency and further development of renewable energy. As per the Project Administration Manual, the total estimated cost of the Project amounted to US \$ 162.03 million equivalent to Rs.18,135.45 million and out of that, US\$ 120.00 million equivalent to Rs. 13,428.09 million or 74 per cent was agreed to be financed by the Asian Development Bank, and the balance US\$ 42.03 million equivalents to Rs.4,707.36 million or 26 per cent agreed to be provided by the Government of Sri Lanka. The Project commenced its activities on 17 November 2011 and was scheduled to be completed by 30 April 2014. Subsequently, the period of the project had been extended up to 30 October 2016. However, the activities of the Project had been continued up to 31 December 2017 using funds allocated by the Government of Sri Lanka.

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 their overall presentation of the financial statements. I believe that the audit evidence I have obtained sufficient and appropriate to provide a basis for my opinion the examination also included such tests as 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 the operations of the Project, the identifications of the purchases made out of the Loans etc;
- (d) Whether the withdrawals under the Loans had been made in accordance with the specifications laid down in the Loan Agreements;
- (e) 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 Agreements;
- (f) Whether the funds, materials and equipment supplied under the Loans 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 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 2017 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2017 in accordance with Sri Lanka Accounting Standards,
- (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 Agreements,
- (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 Agreements had been complied with.

2.2 Comments on Financial Statements

2.2.1 Presentation of the Financial Statements

The financial statements of the Project for the year under review required to be submitted to the Auditor General within 03 months at the end of the year under review, as required by the Circular No. MOFP/ERD/2007/2 of 07 August 2007 of the Ministry of Finance and Planning had been furnished only on 31 July 2018.

2.2.2 Accounting Deficiencies

The following observations are made.

- (a) The value of works completed at a cost of Rs.2,567.22 million and the motor vehicles procured at a cost of Rs.489.39 million and depreciation amounting to Rs.210.73 million and Rs.113.07 million respectively made thereon had been continuously shown in the financial statements of the Project even though the respective assets had been transferred to the Implementing Agency as at 31 December 2017. Further, the works valued at Rs. 10,256.70 million completed and handed over to the Implementing Agency in 2015 had been shown in the financial statement for the year under review under the work – in – progress.
- (b) It was observed that an advance amounting to Rs.2.45 million had been refunded on 26 November 2015 by a contractor directly to the Lending Agency. However, no adjustment entries had been made in the Ledger Accounts thereon even as at 31 December 2017 and as a result, the proceed of the Loan had been overstated by similar amount.

- (c) As a practice, the Project applies the standard cost method for valuing labour, material and overhead cost for capital jobs instead of being applied the method of actual costs incurred thereon. As a result, the value of Plant, Property and Equipment shown in the financial statements had been overstated by Rs.231.04 million..

2.2.3 Un-reconciled Differences

The proceeds of the Loans amounting to Rs.11,249.02 million shown in the financial statements as at 31 December 2017 was not agreed with the corresponding balance of Rs.11,443.39 million shown in the records maintained by the External Resources Department.

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 2017 are shown below.

Source	Amount agreed for financing in the Loan Agreement		Allocation made in the Budget Estimate for the year under review	during the year under review		Funds utilized As at 31 December 2017	
	US\$ million	Rs. million		US\$ million	Rs. million	US\$ million	Rs. million
ADB	120.00	13,428.09	-	1.24	187.35	87.66	12,343.85
GOSL	42.03	4,707.36	-	-	-	-	-
CEB	-	-	150.00	1.78	269.96	15.39	2,333.02
Total	<u>162.03</u>	<u>18,135.45</u>	<u>150.00</u>	<u>3.02</u>	<u>457.31</u>	<u>103.05</u>	<u>14,676.87</u>

The Secretary of the Ministry of Power and Renewable Energy had highlighted by his Letter No. PE/TEN/SCAPC/SG/2015/41 of 18 July 2016 that the prices of all contracts awarded by the Project had remained below than the Engineer's Estimates made thereon. The audit investigation carried out thereon had revealed that the allocation of US\$ 30.41 million equivalent to Rs.4,652.73 million had remained unspent as at 31 December 2017, due to the above reason.

3.2 Physical Performance

According to the information made available, the works under the developments of New Galle Power Transmission, North East Power Transmission, Rural Electrification and Distribution System in the Uva Province, Reactive Power Management and Preparation of a Detailed Engineering Design of Moragalla Hydropower Station had been completed in the previous years. The works under the augmentation of Kiribathkumbura Grid Substation Project, supply and delivery of materials for expansion of Rural Electrification and Distribution System Improvement Project in the Uva Province and Ampara had remained in

progress as at 31 December 2017 whilst completing of activities on procurement of material for reconstruction of 02 transmission lines as that date.

3.3 Issues on Financial Controls

The following observations are made.

- (a) According to the information received, the commitment charges amounting to Rs.17.96 million had been recovered by the Lending Agency as at 31 December 2017, due to delay in implementation of the activities of the Project.
- (b) The activities of the Project comprised with 08 Parts and the supervision and monitoring of the activities of such parts of the Project were remained under the purview of various Divisional Heads of the Ceylon Electricity Board instead of the Additional General Manager (Projects) who is responsible for the supervision of all donor funded Projects handled by the Ceylon Electricity Board.
- (c) The material procured at a cost of Rs.919.6 million for the Rural Electrification Project had remained unutilized as at 31 December 2017. Further, the inventory items procured at a cost of Rs.211.3 million which remained as goods - in – transit as at 31 December 2017 eventhough the main activities of the Project were completed as at 30 October 2016. Further, it was observed that the material procured at a cost of Rs.533.49 million for the use of Rural Electrification Project of Ampara District and the Uva Province had been distributed for the use of sub offices in other provinces as at 31 December 2017.