

Greater Colombo Water and Wastewater Management Improvement Investment Programme - Project 2 - 2017

The audit of financial statements of the Greater Colombo Water and Wastewater Management Improvement Investment Programme - Project 2 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 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 between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank 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 equivalents 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 whilst 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 03 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 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 opening and closing balances, 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 2017 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date.
- (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 the 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 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 opening and closing balances, 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 2017 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 observations are made.

- (a) Value Added Tax aggregating Rs.182.41 million paid had been set off against the contribution received from the Government of Sri Lanka instead of being shown under the work-in-progress.
- (b) Interest and commitment charges aggregating US\$ 0.44 million equivalents to Rs.67.29 million recovered from the proceeds of the Loan as at 31 December 2017 had not been disclosed in the financial statements of the Project.
- (c) According to the Fund Disbursement Schedule of the Lending Agency, the disbursements aggregating US\$ 108,553 equivalent of Rs.16.68 million had been made by the Lending Agency in November and December of 2017. However, action had not been taken by the Project to recognize the transactions and brought to account.

2.2.2 Non – Compliance with Laws, Rules and Regulations

The formal contract agreements entered under the Component of the System Rehabilitation for Non- Revenue Water Reduction of Southern and Western regions of the City of Colombo had been signed by the Chairman of the National Water Supply and Drainage Board instead of the Secretary to the Line Ministry, contrary to the paragraph 8.9.3 of the Government Procurement Guidelines.

3. Financial and Physical Performance

3.1 Utilization of Funds

Source	Amount agreed for financing according to the Loan Agreements		Amount agreed for financing to the National Water Supply and Drainage Board		Allocation made in the Budget Estimate for the year under review	Funds utilized			
						during the year under review	as at 31 December 2017		
	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	1,446.20	9.38	1453.89	16.49	2,512.59
GOSL	30	3,900	27.10	3,523	450.40	2.68	416.61	3.47	535.24
Total	<u>118</u>	<u>15,340</u>	<u>107.05</u>	<u>13,917</u>	<u>1,896.60</u>	<u>12.06</u>	<u>1,870.50</u>	<u>19.96</u>	<u>3,047.83</u>

Certain significant statistics relating to the financing, budgetary provision for the year under review and utilization of funds during the year under review and up to 31 December 2017 are shown below.

Out of the total allocation of US\$ 79.95 million equivalent to Rs.10,394 million, only US\$ 16.49 million equivalent to Rs.2,512.59 million had been utilized as at 31 December 2017, after lapse of 03 years and 04 months from the date of commencing of the activities of the Project. Further, it was observed that the completion of activities of the Project within specific period of the Project is remained in doubt, due to lack of a comprehensive plan for implementation purposes.

3.2 Physical Progress

According to the Project document, the Project consisted with 13 Components and progress reports of the Project indicated that the overall physical progress of the Components of the Project at the end of the year under review remained at 5.61 per cent only, due to the reasons such as delays of awarding contracts, poor performance of the contractors and poor project management etc. Further, the contracts for the construction of buildings for the Area Engineer's Office at Pamankada, rehabilitation of plumbing systems in the government owned apartments and procurement of 02 lots of operational equipment for Regional Support Service Centre –Western Central had not been awarded up to 31 December 2017.

3.3 Contract Administration

The following observations are made.

- (a) It was observed that the completion dates of the contracts awarded by the Project under the Components for the System Rehabilitation for Non-Revenue Water for the Western and Southern region of the City of Colombo and consultancy services for Community Mobilization Awareness and Behavior Changes had been determined beyond the date of completion of the activities of the Project scheduled on 30 June 2019.
- (b) It was observed that 504 days had been spent to complete the procurement process of the contract for Non- Revenue Water Reduction region of the City of Colombo eventhough the contract had been approved by the Lending Agency as an advanced procurement. Further, the realistic estimates had not been prepared by the National Water Supply and Drainage Board at the initial stages based on a proper longitudinal surveys and as result, the length of estimated pipe laying works of 99 kilometres under the Component of the System Rehabilitation for Non-Revenue Water Reduction in Western region of the City of Colombo had been significantly increased up to 194.5 kilometres.

- (c) According to the bid document of the contract, the Product Conformity Certificates on the use of materials and details of key persons involving for evaluation purposes required to be submitted by the selected bidder as at the closing date of the submission of bids. However, the contract under the Component of the System Rehabilitation for Non-Revenue Water Reduction in Western region of the City of Colombo had been awarded to a bidder who had not submitted respective Certificates even up to the date of the contract agreement made on 01 December 2016. Further, the activities under the contract had shown slow physical progress of 9.57 per cent as at 31 December 2017, after lapse of 13 months from the date of contract awarded. In addition, the works under said contract for Hydraulic Modeling and detailed design of 18 District Metering Areas and 02 Feeder Mains had not been completed even up to 30 March 2018.
- (d) The works under the Hydraulic Modeling for Feeder Mains System and detailed design of 09 District Metering Areas under the contract for System Rehabilitation for Non-Revenue Water Reduction in Southern region of the City of Colombo awarded on 10 January 2017 had also not been completed even up to 30 March 2018. Further, 15,894 houses subjected had been surveyed as at 31 December 2017, out of the target of 35,000 houses to be surveyed. As a result, the pipe laying works of 02 kilometres had only completed, out of the 155 kilometres of works expected to be completed before 31 December 2019.
- (e) The Project had scheduled to conduct the awareness and behavior programs in 65 District Metering Areas under the Component of Capacity Building of the Communities and the contract agreement thereon had been entered into with a Non-Government Organization on 30 June 2016. However, the awareness programs had been commenced only in July 2017 and not completed as at 31 December 2017.
- (f) It was observed that the progress reports prepared on the public awareness programs for water users consisted only with the number of such programs conducted during the year under review. The details such as programs conducted under each package as at 31 December 2017, recommendations and solutions for identified issues etc. had not been indicated therein and therefore, no proper mechanism stipulated to evaluate the changes on the pattern of water usage after attending for the awareness programs.

3.4 Matter in Contentious Nature

The land owned to the Urban Development Authority acquired by the Project on 02 September 2015 on lease basis for the use of the Area Engineer's Office at Pamankada had been transferred to the Colombo Municipal Council in August 2017 without taking action to recover the advance amounting to Rs.10 million made thereon. In addition, another advance of Rs.2.11 million made during the year under review on architectural designs of the office building had become fruitless, due to transferring of the respective land.

3.5 Issues on Financial Control

Transactions of the Project had not been subjected to audit of the Internal Audit Section of the National Water Supply and Drainage Board, as required by the Circular No. 05 of 26 July 2010 of the Department of Management Audit.

3.6 Human Resources Management

The Executing Agency of the Project had appointed the Project Director for the post of Deputy General Manager (Eastern Province) of the National Water Supply and Drainage Board on acting basis, contrary to the requirement of the Section 2.3.2 of the Circular No.01/2016 of 24 March 2016 of the Department of Management Services.