

Jaffna and Kilinochchi Water Supply and Sanitation Project - 2019

The audit of the financial statements of Jaffna and Kilinochchi Water Supply and Sanitation Project for the year ended 31 December 2019 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(a) of Article IV of the Loan Agreement No.2710-SRI (Ordinary Operations) and Section 4.03(a) of Article IV of the Loan Agreement No.2711-SRI (SF) (Special Operations) dated 08 February 2011 entered between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank. My comments and observations which I consider should be reported to Parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreements, then Ministry of Water Supply and Drainage, presently the Ministry of Water Supply is the Executing Agency and the National Water Supply and Drainage Board, Provincial Irrigation Department of Northern Province and Local Authorities in the Northern Province are the Implementing Agencies of the Project. The objectives of the Project are to improve water supply and sanitation infrastructure for residents living in the areas of the Project and to protect and manage the water resources of the Jaffna Peninsula. As per the Loan Agreements, the total estimated cost of the Project under the components implemented by the National Water Supply and Drainage Board was US\$ 147.45 million equivalent to Rs. 16,474.59 million. Out of that US\$ 76.45 million equivalent to Rs.8,541.76 million was agreed to be financed by the Asian Development Bank and US\$ 48 million equivalent to Rs.5,363.04 million was agreed to be financed by the Agence Francaise De Development. The balance amount of US\$ 23 million equivalent to Rs. 2,569.79 million expected to be financed by the Government of Sri Lanka. The Project commenced its activities on 15 February 2011 and scheduled to be completed by 14 August 2017. Subsequently, period of the Project had been extended up to 31 December 2020.

1.3 Qualified Opinion

In my opinion, except for the effects of the matters described in the Table 2.1 of this report the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2019, financial performance and its cash flows for the year then ended in accordance with Generally Accepted Accounting Principles.

1.4 Basis for Opinion

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of this report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

1.5 Responsibilities of management and those charged with governance 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.

In preparing the financial statements, management is responsible for assessing the Project ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Project or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Project's financial reporting process.

The Project is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared by the Project.

1.6 Auditor's Responsibilities for the audit of the Financial Statements

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 internal control of the Project.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with those charged with governance regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

2. Comments on Financial Statements
2.1 Accounting Deficiencies

Accounting Deficiencies	Impacts	Responses of the Management	Auditor's Recommendation
<p>(a) Interest charges amounting to Rs.315.45 million and commitment charges amounting to Rs. 31.32 million recovered by the Lending Agency up to 31 December 2019 had not been brought to the financial statements of the Project.</p>	<p>Understatement of disbursement shown in the financial statement.</p>	<p>In accordance with NWSDB's policy decision, commitment and interest charges for ADB's financing were not accounted as expenditures in the project financial statements for the year ended 31-Dec-2019 because these commitment and interest charges were accounted as expenditures by Department of Treasury Operations in its books and reports for year 2019.</p>	<p>The respective cost should be brought to account as enable to reflect the total disbursements under the Project at the end of the year under review.</p>
<p>(b) The motor vehicles and heavy vehicles procured at a cost of Rs.16.44 million and Rs.25.30 million respectively during the year under review had been accounted under civil works.</p>	<p>Understatement of costs of the non-current assets and overstatement of civil works in the financial statement.</p>	<p>Since cited vehicles were purchased through Civil Works Contract packages of TWTM01 and TWTM02, these purchasing was shown under Civil Work Category in the financial statements for year 2019. However, the project assures that these purchasing will be transferred from Civil Work category to Vehicles categories and it will be shown next financial statements for year 2020 promptly.</p>	<p>Need to be recognized in the non-current assets based on different lifetimes of the assets.</p>

2.2 Non-compliance with Laws, Rules and Regulations

Audit Issues	Impacts	Responses of the Management	Auditor's Recommendation
(a) As per the section 14.8 of the General Condition of the FIDIC Guideline the certified bill required to be settled within 56 days. However, contractor had made claim of Rs.6.83 million as delay charges, due to delay of payment of the GOSL portion of the bills as at 31 December 2019	Possibility of incurring additional costs due to violation of the FIDIC Guidelines.	In accordance with initial funding arrangement for the project's Original Loan, ADB had to pay out 78% of total payable amount of the Contracts IPC and balance 22% had to be paid out from GOSL funds. As all are aware of, the project was unable to settle these GOSL unpaid amounts to the Contractors because of non-availability of GOSL funds in year 2019. After receiving GOSL funds in July 2020, all outstanding bills in hands were settled on 28th July 2020. However, in line with Terms and Conditions of the Contracts Agreements, 14.8, Delayed Payments, the Contractors claimed interest charges for its delayed only GOSL payments since the Contractors received ADB's payments in time in the future.	Action should be taken to settle the payment in time to avoid delay payment charges.
(b) As per the paragraph 8.13.4 of the Government Procurement Guidelines and Public Finance Circular No.02/2012 dated 07 August 2012, when it is apparent the cost variance exceeded 10 percent of the total cost estimate of the contract or when the approved scope of work is changed, reports of Technical Evaluation committees with regard to proposals for cost estimate revisions and duly perfected relevant form should be sent	Possibility of increasing Project cost unexpectedly	The project always takes every effort to manage the scope changes and quantity variations within Contingency Provision of each Contract. Contract variations exceeding the Contingency Provision, the project obtains necessary approval of relevant authorities timely. However, during the Contract implementation, many major Contracts are generally having Variations, Savings and Omissions itself because of scope change and the site conditions. Kindly note that in the PEIC/JKWSSP/TWTM/2014/02 contract, a major omission was made for the omission of Transmission	Action should be taken to include approved variation only in the interim payment certificate.

to the Director General of public finance with observation of the Secretary of the Ministry of Water Supply, in order to submit them to the Cost Estimate Examination Committee. However, the Project had failed to follow the above regulation in respect of Contract No. PEIC/JKWSSP/TWTM/2014/02

- (c) .As per the Letter No.BD/ID166/08/Ven-Tem of the Department of National Budget dated 05 August 2018, Project had obtain approval to Procured 02 double Cabs, Backhoe Loader and Boom Crane Truck within minimum price limit Rs.42.00 million. However, Project had spent a sum of Rs.45.03 million to procure the above vehicle without approval for the additional payment of Rs.3.03 million.

Project performance may adversely affect due to violating the National Budget Circular.

Main from Chavakachcheri Junction to Poonery Sump for a sum of Sri Lankan Rupees 242,507,258.00 due to the scope change as drinking water source from Iranaimadu Tank to Sea Water Desalination Plant, Thalaiyadi. Approval for the scope change obtained from the Project Appraisal Committee and Asian Development Bank as well. To accommodate this scope change, Paranthan to Poonery transmission line was implemented and it was considered as variation.

The Project Director for JKWSSP requested approval to purchase vehicle in May 2018. Approval of Department of National Budget obtained via Ministry of Water Supply on 13th August 2018. Due to procurement process, the vehicles were purchased in later 2018 and earlier 2019 respectively. During the period from approval to purchasing date, due to the significant foreign exchange rate fluctuation, the market prices of the vehicles were increased to. These vehicles were purchased at the cost of the market prices on that date through widely competitive bidding process.

Project should get approval for additional payment from Department of National Budget.

3. Physical Performance

3.1 Physical progress of the activities of the Project

	Activities	Physical Progress as at 31 December 2019		Impacts	Responses of the Management	Auditor's Recommendation
		<u>Expected</u>	<u>Actual</u>			
(a)	Construction of water tower at Poomaveli, karaveddy, Nainathivu, Analathivu and Eluvaithivu	05 water tower	10 %	Delaying the supply of safe drinking Water to Jaffna Penisiula.	The Contract was awarded on 28 th May 2019, commencement of Contract was 02 nd July 2019 and original date of completion is 22 nd December 2020 (540 days). The physical progress at 31 st December 2019 was 10% and financial progress was 19% including mobilization advance, the current physical progress is 33% as at 30 th September 2020 and financial progress as at 30 th September 2020 is 40%. However, the Project Management, Coordination and Implementation Unit and WSP, NWSDB are closely monitoring the progress of the Contract to complete within scheduled time frame.	Action should be taken to expedite the contract activities.
(b)	Laying of distribution Network in Palai, Kodikamam, Meesalai, Poonkary, Puttur Nawathkuli, Karaingar	250km	110km	Related costs would be increased, due to delays in the completion	The Project Management, Coordination and Implementation Unit and WSP, NWSDB are closely monitoring the progress of the Contract to complete in time. 170 km of pipe laying work was completed as at 30 th September 2020 by the Contractor even in the Global Covid-19 Pandemic situation. Anyhow,	Action should be taken to expedite the contract activities.

Contractor has doubled the working crews to expedite the work. It is expected for completing the Contract by end of March 2021 due to Global Covid-19 Pandemic situation.

(c)	Laying of Jaffna city Area Distribution Net work	283Km	Nil	Delaying the construction may adversely affect the Project objective.	Draft cabinet memorandum for Supply and Laying of Jaffna City area distribution submitted on 15 th June 2020. The project is waiting for the approval from Cabinet to award the Contract. It is expected for awarding by end of this year	Action should be taken to expedite the Project activities since loan closed on 31 December 2020.
(d)	Construction of Chunnakan Water Supply Scheme	50Km	Nil	Delaying the supply of safe drinking Water to Jaffna Penisiula	It is decided with ADB that the bid for Chunnakam water supply scheme will be advertised after awarding SWRO plant in order to make sure the funds availability for the Contract awarding.	Action should be taken to expedite the Project activities

3.2 Contract Administration

The following observations are made.

	Audit Issues	Impacts	Responses of the Management	Auditor's Recommendations
(a)	Under the revised scope of works of the project, it was scheduled to install a sea water reverse osmosis plant and construct allied water towers in order to provide water supply facilities for Jaffna Kilinochchi Region, and expected to complete by 2022. Therefore, the works under the contract	All construction become idle till construction of the SWRO plant in thalyadi and delaying to supply to safe drinking water in Jaffna Peninsula.	In order to accommodate major scope change to SWRO in Thalaiyadi, Maruthankeni by signing Loan Agreements in December 2017, the ADB has financed USD 120 Mn and Government of Sri Lanka has financed USD 33 Mn, totally USD 153 Mn financed to the project to achieve its objectives. According to Detailed Costs Estimates of the Project, referring to PAM, November 2017, of which, USD 70 Mn was estimated for SWRO in Thalaiyadi and it was initially scheduled to award the Contract in	Action should be taken to utilize the completed construction works under the Project for the expected purposes.

awarded to construction 15 water towers at an estimated cost of Rs.1,140 million and laying of treated water transmission pipe at an estimated cost of Rs.5,536 million had completed as at 31 December 2018. However, all these completed construction works under the Project had remained idle over one year due to lack of proper water source

December 2017 accomplishing by end of June 2020.

Due to the procurement process which already taken approximately 1109 days, the SWRO Contract has not been awarded yet under ADB L3603-SRI-Additional Finance.

As this is the first procurement for NWSDB & ADB in design built and operate of a desalination plant. Therefore, series of clarification required from bidders, central bank and as well as SCAPC & ADB in order to select the substantially lowest evaluated bidder.

In addition to this, due to appeal was made by 2nd lower rejected bidder on 19th February 2020 then hearing was held and PAB endorsed the SCAPC decision on 28th May 2020. The cabinet paper submitted in July 2020 and is waiting for Cabinet approval to award the Contract by end of 2020.

(b) The contract for the supply and laying of treated water transmission Main Part 01 had been awarded in 2016 at an estimated cost of Rs.2,646 million and scheduled to be completed in July 2018. Although the total pipe laying works had completed, construction work of two sump in Meesalai and Nallur had not completed even as at 31 December 2019. However, the Project had given time extension to contractor in nine instances from Au-

Possibility of Incurring additional cost to the Government

The Contract Extension for Treated Water Transmission Mains was given based on the Condition of Contract by analyzing the factors below:

Action should be taken to expedite the Project activities

No of Time Extension	Justification for Time Extension
1 st	1. Delay in procession at site of Nallur Sump due to land issue. 2. Encountering of motor shells 3. Re-Alignment of Route at Navakkuly and Kaithadi Bridges.
2 nd	1. Due to Shortage of skilled and unskilled Labourers to complete the

gust 2018 to September 2020.

	works
3rd	<ol style="list-style-type: none">1. Due to the heavy rain balance pipe laying sites are inundate. Delay in placing valve chamber in water area after heavy rain.2. Delay in Beam launching in Kaithady & Navatkuly bridge due to RDA restriction3. Delay in pipe laying due to excessive line stone
4th	<ol style="list-style-type: none">1. Works delayed due to 21st April 2019 Easter attack and subsequent curfews. Contractors Faced difficulties on getting ABC and Quarry dust as these are daily required material (because of rook profile and RDA requirement)2. Changes made in Diesel and Engine room

5th	<p>1. RDA has introduced two new bridges at Kaithady and Navatkuli details are below</p> <p>-Construction commenced Nov.2016 completed on Aug 2018 and defect notification period up to Aug 2019</p> <p>-Subsequently RDA not allowed the open trench laying across the A-09 road and introduced the pre-Cast box culvert type crossing in the discussion with them held on 17th June 2019, in order to reduce the disturbance to the public and future maintenance.</p>
6th	Due to water inundation in the working area, it is difficult to work underground pipe laying.
7th	<p>1. Delay in GOSL payments</p> <p>2. Due to water inundation in the low-lying working area, it is difficult to work underground pipe laying.</p>
8th and 9th	1. works delayed due to the Corona virus Disease (COVID – 19) outbreak, which was declared as a “Pandemic” by the World Health Organization (WHO), in accordance with the Clause 8.4 of Condition of Contract.

(c) Although the activities of the Project had not completed, repayment of the loan had been commenced in 2017. According to the statements of Department

Government facing difficulties to steering the development task as planned.

By regularly updating physical and financial progress with ADB in various levels such as Project, NWSDB and Ministries including ADB Mission visits, ADB is clearly aware of up-to-date physical and financial progress. In order to compliance with signed loan agreements, it is

Action should be taken to expedite the Project activities

of External Resources, a sum of Rs.497.20 million had been made as repayment to the Lending Agency as at 31 December 2019.

(d) Eventhough the various construction work had been completed under the Project in Jaffna Districts, the ownership of the respective lands had not been transferred to the National Water Supply and Drainage Board, even the activities of the Project are scheduled to be closed by 31 December 2020

Possibility of delaying transferring the ownership of the lands may affect delaying the Project activities.

charging commitment and interest from the ADB committed financing for the project. However, the relevant Implementing Agency and Executing Agency may take prompt to negotiate with ADB through the ERD regarding this interest and commitment charges.

Most of the lands' ownerships were transferred to NWSDB where the construction activities already completed except the Karaveddy and Punguduthivu. Construction were completed in Punguduthivu and the compensation not paid to the land owner as the land doesn't have the access and acquiring access is in process. Once the acquisition is completed, the payment will be made to owner and the ownership transferred to NWSDB. Construction of Karaveddy Water Tower is ongoing and before the completion of Construction the vesting order will be transferred to NWSDB by end of this year. (As the acquisition is in completion stage, Section 17).

For the balance land in connection with Construction of Sewerage pumping stations acquisitions are in progress. Before Construction of Sewerage pumping stations commencing, acquisition will be completed and the ownership will be transferred to NWSDB

The NWSDB should be taken immediate actions to get transfer the ownership of the lands without further delay.

3.3 Issue Related to Human Resources Management

Audit Issue	Impact	Response of the Management	Auditor's Recommendations
As per the Paragraph 2.3.2 of the Management Circular No 01/2016 24 March 2016, the Project Director need to be deployed in full time basis in order to ensure effective	The monitoring mechanism of the activities of the Project would be weaken.	The Project Director usually spends more days in PMCIU-JKWSSP per a week, including weekends as much as possible to implement the project successfully. Further,	The Project Director is required to be deployed in full time basis as enable to undertake responsibilities on implementing the activities of the Project in

operations of the activities of the Project. However, contrary to the above mentioned provision, Project Director of this Project cover up the duties of Deputy General Manager of the Northern area since April 2018 and Project Director's duties of the Supporting Electricity Supply Reliability Improvement Project since December 2019.

particularly technical delegation has been arranged among the project staff by the Management for smooth functions and effective management in place. Further, because of effective Information Technology & Communication between RSC, North and JKWSSP-PMCIU, Jaffna, project implementation processes are up-to-date in practice. effective manner.