

## **Supporting Electricity Supply Reliability Improvement Project (Grant -0486 SRI) - 2021**

The audit of financial statements of the Supporting Electricity Supply Reliability Improvement Project for the year ended 31 December 2021 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 Grant Agreement No. 0486-SRI dated 19 December 2016 entered into 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 Grant Agreement, the Ministry of Power and Energy is the Executing Agency and Lanka Electricity Company (Private) Limited is the Implementing Agency of the Project. The objectives of the Project are to support the establishment of hybrid renewable energy systems through the construction of a renewable energy micro-grid system in the Western province. The activities of the Project is implemented under a component namely establishment of renewable energy micro grid system. As per the Grant Agreement, the estimated total cost of the Project was US\$ 1.8 million equivalent to Rs.268.36 million and entire amount agreed to be financed by Asian Development Bank. The Project had commenced its activities on 29 June 2017 and scheduled to be completed by 30 September 2021. However, the date of completion of the activities of the Project had been extended up to 30 September 2022.

### **1.3 Opinion**

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2021, statement of expenditure and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

### **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 my 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 of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

## **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 Non -Compliance with Laws, Rules and Regulations

#### Reference to the Laws Rules and Regulations

#### Non-Compliances

#### Responses of the Management

#### Auditor's Recommendations

Memorandum of Understanding entered into between the Lanka Electricity Company (Private) Limited and the University of Moratuwa

(i) Section 3.10

The committee shall aggregate research proposals for the forthcoming year at the end of each year and prepare a research plan and budget. Although the project was almost completed as at 31 December 2021 according to the available information to audit, a research plan and budget for the coming year of 2022 had not been prepared.

Once the project is fully completed and handed over to the university while finalizing the mechanism to source the R&D fund, committee has to prepare a research plan and budget in a transparent manner.

Actions should be taken to make arrangements as agreed with two parties in order to gain success in micro grid pilot project.

(ii) Section 07

A joint working legal contract reflecting the MOU shall be signed between the parties not later than 3 months after signing the MOU. Even though the MOU had been signed in October 2018, a joint working legal contract had not been signed by parties even as at the end of the year under review.

In order to finalized the agreement, the R&D fund mechanism has to be agreeable by all the parties including the metering arrangement of the Solar PV generation, backup generator operational cost etc.

Action should be taken as agreed in the MOU.

### 3. Physical Performance

#### 3.1 Physical and Financial Progress of the Activities of the Project

The Project Agreement had been entered on 19 December 2016 with the Asian Development Bank and the Lanka Electricity Company (Private) Limited for US\$ 1.8 million equivalent to Rs.268.36 million for support the establishment of hybrid renewable energy systems through the construction of a renewable energy micro-grid system in the Western province. Accordingly, a memorandum of understanding had been signed between the Lanka Electricity Company (Private) Limited and the University of Moratuwa on 16 October 2018 to establish a renewable energy micro-grid system at the University as a pilot project. Although the project was scheduled to be completed by 30 September 2021, the completion date was extended up to 30 September 2022. The establishment of the renewable energy micro-grid system at the University had been completed by 30 September 2022. However, the pilot project was only in the stage of preparing the plans for future research and development activities. The following observations are made.

No	Component	Audit Issue	Management Responses	Auditor's Recommendations
(a)	Total Grant proceeds	The project had utilized only US\$ 1.16 million or 65 per cent of the total grant proceeds as at 31 December 2021.	Payments for contractors still ongoing based on the payment milestones as per the contract agreement.	Action should be taken to complete the project within the scheduled time period.
(b)	Works and consultancy services	Out of the total grant proceeds, US\$ 1.5 million and US\$ 0.3 million had been allocated for works component and consultancy services respectively. Although the project had utilized US\$ 1.05 million or 70 per cent for works component as at the end of the year under review, it was observed that only US\$ 0.109 million or 37 per cent had been utilized for consultancy services as at 31 December 2021.	The local consultant was not much involved in the process and therefore his budget was not significantly utilized.	Action should be taken to complete the project within the scheduled time period.

(c) Installation of micro grid and the Research & Development Lab	As per the revised project schedule, the activities of installation of micro grid and the Research & Development Lab were scheduled to be completed by 01 September 2021 and 07 July 2021 respectively and handing over the entire project by 30 November 2021. According to the information made available to audit, installation of all equipment except the wireless communication system had been completed by 31 December 2021 and commissioning and operational testing of the micro grid was ongoing by the date of audit on 20 May 2022. However, handing over the entire project had not been taken place even as at the date of audit.	The Project will not be taken over by LECO till the contractor fulfill the contractual obligations stipulated the tender documents. Currently, the mandatory operational period is on progress and LECO will take over the project after this operational period.	Prompt actions should be taken to expedite the activities of the Project and close supervision is required to make on the activities of contractor in order to complete the project within the project period.
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### 3.2 Contract Administration

#### Audit Issue

The selected bidder for designing, construction, installation and commissioning of Renewable Energy Micro Grid Pilot Project had not quoted for mandatory spare parts for two years of operation of Micro grid system. However, Technical Evaluation Committee recommended the bid subject to agreeable solution pertaining to above bid item prior to award of contract. Subsequently, the contract had been awarded on 11 February 2020 as contractor had provided two year or more warranties for the other mandatory spare parts quoted.

#### Response of the Management

This matter was discussed during one of the meetings had with the contractor before awarding the contract. Since they have provided two year or more warranties for the equipment mentioned, it is considered that cost for the spare parts for two years also included with the offer.

#### Auditor's Recommendation

This matter should be considered along with warranty period agreed by the supplier, as the bidder is obliged to supply of mandatory spare parts for two years operation of micro grid system.