

## **Mahaweli Water Security Investment Programme – Tranche 02 - 2024**

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The audit of financial statements of the Mahaweli Water Security Investment Programme - Tranche 2 Project for the year ended 31 December 2024 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 4.02 (a) of the Loan Agreement No.3625 and Article 4.02 (a) of the Loan Agreement No. 3626 dated 18 May 2018 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 Programme**

According to the Loan Agreement of the programme, the Ministry of Irrigation is the Executing Agency and Sri Lanka Mahaweli Authority and Department of Irrigation are the Implementing Agencies of the Programme.

The objective of the Programme is secure access to water resources for agricultural, drinking and commercial purpose in programme area. The activities of the Programme are implemented under three components namely North Central Province Canal Project, North Western Province Canal Project, Minipe Left Bank Canal Rehabilitation Project.

As per the Loan Agreement, the estimated total cost of the Project was US\$ 242 million equivalents to Rs. 38,177.67 million and out of that US\$ 210 million equivalents to Rs. 33,129.39 million was agreed to be financed by Asian Development Bank. The balance amount of Rs 5,048.28 million is expected to be financed by the Government of Sri Lanka.

The Programme had commenced its activities on 13 December 2017 and scheduled to be completed by 31 December 2021. However, the date of completion of the activities of the programme had been extended up to 24 June 2025.

### **1.3 Qualified Opinion**

In my opinion, except for the effects of the matters described in the paragraph 2.1 of my report, the accompanying financial statements give a true and fair view of the financial position of the programme as at 31 December 2024, expenditure account and its cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

### **1.4 Basis for Qualified 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 in 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 Public Sector 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 Programme'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 scepticism 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

	<b>Accounting Deficiency / Audit Issue</b>	<b>Amount Rs. Million</b>	<b>Response of the Management</b>	<b>Auditor's Recommendations</b>
(a)	The equity balance as per the statement of financial position was Rs.65,148.04 million. However, as per the statement of changes in equity it was Rs.65,119.7 million. Hence, a difference of Rs.28.34 million observed between two balances.	28.34	Agreed. It will be rectified in 2025.	PMU should record the reconciled balances in the financial statement accurately.
(b)	The revaluation gain amounting to Rs.5,300.95 million had been erroneously recognized as Rs. 7,053.73 million in the financial statement of the year under review. As a result the revaluation gain had been overstated by Rs. 1,752.78 million.	1,752.78	Agreed. It will be rectified in 2025.	PMU should calculate the revaluation gain or loss accurately.

## 3. Physical Performance

### 3.1 Physical progress of the activities of the Project

<b>Audit Issue</b>	<b>Responses of Management</b>	<b>Auditor's Recommendation</b>
At the end of the reviewed year the project expected target for MLBCRP was 86%, for MWPCP was 100% and MCPCP was 62%. However the physical progress of the activities is 85% for MLBCRP, 61% for NWPCP and NCPCP is 55%.	Agreed.	Performance should be align with target framework.

### 3.2 Contract Administration

	<b>Audit Issue</b>	<b>Response of the Management</b>	<b>Auditor's Recommendation</b>
(a)	The following consideration were observed regarding the Construction of 27.7 km Tunnel Canal (UEC – ICB-2A)		
(i)	It was observed that no proper cost-benefit analysis was conducted regarding the procurement of the second TBM. From the proposal to purchase the machine up to the importation process, the Cabinet of Ministers was not presented with complete and accurate information. Total amount paid to the contractor was Rs. 6,691 million cost at clearance stage at Trincomalee port was Rs. 2,148 million. There was no evidence to clarify balance of Rs. 4,543 million expenses.	Several options were studied / evaluated by the Engineer to the contract and submitted a justification report. Accordingly, it was finalized to adopt 2nd TBM for excavation as the most economical, feasible and time reduction method.	Action should be taken to ensure a comprehensive cost-benefit analysis is conducted and properly documented for all major procurements.
(ii)	The State Finance Department–appointed committee (13 August 2021) and the Ministry's eight-member committee (13 August 2021) had both concluded, through meetings held in August and September 2021, that the project faced significant uncertainties in cost and time, and that it was not reasonable to invest additional funds for the purchase of the second Tunnel Boring Machine (TBM 2). Further, as per the Program Director's	The Ministry reconstituted the Technical Committee to review and re-examine the previous technical reports to facilitate a clear decision at the SCAPC level. The reconstituted committee subsequently recommended ensuring economic and financial viability while achieving the project objectives by providing additional irrigation and drinking water to the Anuradhapura District through the simultaneous implementation of the tunnel (UECP-ICB-2A) and the	Implement proper governance and accountability mechanisms to prevent unnecessary or unjustified procurement actions in future projects and Chief Accounting Officer should conduct an investigation on this matter.

letter dated 30 July 2021, remaining NCPCP packages similar concerns had already been raised. However, the third TEC, which met on 04 and 05 October 2021, merely recommended the expeditious completion of tunnel works after obtaining a certificate of economic and financial feasibility, without clearly recommending the purchase of TBM 2. Accordingly, the audit observed that the decision-making process concerning the purchase of the second TBM was undertaken without proper justification, ignoring previous technical and financial assessments, and that the repeated appointment of TECs appeared to be an attempt to justify the procurement decision without a valid basis.

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| <p>(iii) The procurement of the second TBM (Tunnel Boring Machine) has become an additional financial burden to the government rather than improving the efficiency of the project. Even after deploying the second TBM, the project could not be completed within the targeted timeframe. An amount of Rs. 6,690.97 million already spent on the second machine.</p> | <p>The contractor has offered the same cost (Rs. 6,690.97 million) for the second TBM &amp; payments are done in accordance with the contract agreement. As per end of April 2025, excavation is completed in 18.3km length of tunnel in both ends.</p> | <p>Actions should be taken to investigate on this matter and action should be taken against the responsible officers.</p> |
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| <p>(b)</p> | <p>The audit observed that TBM 2, intended for excavating the southern gate, remained idle for eight months from March 2023. As of the weekly accounting report dated January 5, 2025, the excavation progress for the Tunnel Boring Machines (TBMs) showed a significant shortfall against their planned targets. TBM 01 had a total target excavation of 16,711.86 meters but had only achieved 11,127.55 meters. This represents a deficit of 5,584.31 meters. Similarly, TBM 02 had a total target of 9,833.30 meters but had only excavated 4,366.43 meters. The resulting shortfall for TBM 02 is 5,466.87 meters.</p>  | <p>All possible efforts were taken to minimize damages and rectify the situation.</p>  | <p>Action should be taken to complete the construction works as scheduled time.</p>            |
| <p>(c)</p> | <p>On June 9, 2022, a meeting chaired by the Secretary, Ministry of Irrigation, with Treasury, Agriculture Ministry, ADB, and MWSIP officials, decided to secure funds for MOP fertilizer. Accordingly, MWSIP spent USD 39.78 million (LKR 14,202 million) to purchase 41,876 MT from a private company, Singapore, under contract MI/MWSIP/ADB/GDS/MOP Fertilizer/ICB/2022/037 dated 23 September 2022, at USD 950 per MT (<math>\pm 5\%</math> tolerance). Payment was made on the Bill of Lading weight at Vancouver port instead of Colombo. Although imported for the 2022/23 Maha season, 16,543.7 MT remained unused as at 31 January 2025, and 14,400 MT as at 30 April 2025 in National Fertilizer Secretariat warehouses.</p> | <p>Fertilizer is issued on a raw basis for paddy cultivation and on a mixed basis for tea and coconut cultivation, with small quantities sold to private companies. For 2025, 3,000 MT of MOP is expected to be distributed for the Yala season and about 2,000 MT for tea plantations. The expiry date of the MOP stock was verified as October 2026.</p> | <p>Action should be taken to distribute MOP fertilizer, within the stipulated time period.</p> |

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| (d) | <p>The supplier failed to deliver 200 integrated agricultural systems for chili cultivation within the stipulated timeframe, though the full contract amount of LKR 75.3 million was paid. The purchase order was issued on 12 January 2024, with delivery due by 27 March 2024, but completion occurred on 16 May 2024, a 49-day delay. As a result, the Project Office incurred a financial loss of LKR 6.02 million in liquidated damages.</p> | <p>Delivery was within the contractual timeline and no delay or liquidated damages applied.</p> | <p>Action should be taken to recover of Rs. 6.02 million in liquidated damages.</p> |
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### 3.3 Observations made on site visits

	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	As at 31 January 2024, recorded cracks in 1,298 (44%) of 2,967 installed concrete rings. The report of 05 January 2025 confirmed the issue persisted, with 5,608 (68%) of 8,275 rings cracked. Between 31 January 2024 and 05 January 2025, 4,310 new crack cases were reported, indicating a 52% growth rate.	The Contractor repaired 1,622 segments at its own cost, with core tests confirming strength above design. By April 2025, crack generation had fallen to below 5% per month.	Actions should be taken to rectify this issue to achieve project desired objectives.
(b)	Out of a total of 8,275 concrete segments fabricated by the end of the year, only 1,338 segments had undergone quality testing. This represents just 16% of the total, raising concerns over the quality assurance process of the remaining segments.	The figures in the report are correct for 2024. All quality assurance works are being carried out under the close supervision of the Engineer to the contract.	Actions should be taken to test the quality of concrete segments.

### 3.4 Identified Losses

Audit Issue	Response of the Management	Auditor's Recommendation
<p>The loan for Phase 02, scheduled for utilization by June 30, 2022, remained unused until end-2024. Consequently, commitment charges of Rs. 3.05 million arose during the year, with an accumulated fee of Rs. 232.9 million by December 31, 2024. These unnecessary costs resulted from delays in program execution, contract non-completion, slow progress, land acquisition issues, and additional works due to poor planning.</p>	<p>The KMTC project and UECP-ICB-2A contract were delayed by a 2½-year procurement suspension, COVID-19, the economic crisis, and material shortages factors beyond the PMU's control.</p>	<p>Loan fund should be utilized effectively.</p>