

**Greater Colombo Water and Wastewater Management Improvement Investment Programme – Project 02 - ( The National Water Supply and Drainage Board - The Asian Development Bank. – Agreement No.3029 SRI and 3030 SRI ) - 2024**

---

The audit of financial statements of the Greater Colombo Water and Wastewater Management Improvement Investment Programme - Project 2 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 2.10 (a) of Article II of the Project Agreement No. 3029 SRI and 3030 SRI (SF) dated 03 June 2014 entered in to between the National Water Supply and Drainage Board 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 Project and Loan Agreements of the Programme - Project 2, then Ministry of Water Supply and Drainage, presently the Ministry of Urban Development, Construction and Housing is the Executing Agency and the National Water Supply and Drainage Board is the Implementing Agency of the Programme - Project 2. The objective of the Programme Project 2 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 Programme - Project 2 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 percent of the total estimated cost of the Programme - Project 2 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 percent of the total estimated cost of the Programme - Project 2 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 percent was expected to be contributed by the Government of Sri Lanka. Further, out of the estimated total cost of the Programme - Project 2, allocation of US\$ 107.05 million equivalents to Rs. 13,917 million had been made for the activities of the Programme - Project 2, 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 Programme - Project 2 expected to be carried out by the Colombo Municipal Council. This report consisted with the observations made on the activities of the Programme - Project 2 implemented by the National Water Supply and Drainage Board. The Programme - Project 2 had commenced its activities on 03 September 2014 and scheduled to be completed by 30 June 2019. Subsequently, the period of the Programme - Project 2 had been extended up to 29 February 2024.

**1.3 Qualified Opinion**

In my opinion, except for the effects of the matters described in the section 2.1 of this Report the accompanying financial statements give a true and fair view of the financial position of the Programme - Project 2 as at 31 December 2024 and its cash flows for the year then ended in accordance with Sri Lanka 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 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 Accounting Deficiencies

	<b>Accounting Deficiencies / Audit Issue</b>	<b>Amount Rs.  Million</b>	<b>Responses of the Management</b>	<b>Auditor's Recommendations</b>
(a)	As per the paragraph 39(a) of Sri Lanka Accounting Standard 21, the parity adjustments amounting to Rs. 2,671 million relating to the foreign loan of the project had not been accounted in the financial statements for the year under review.	2,671	NWSDB has no loan repayment obligation. Therefore, no Parity adjustments have been made.	Adhere to the Sri Lanka Accounting Standards.
(b)	An amount of Rs. 12.3 million had been paid to the project 01 (Loan Agreement No.2948 – SRI) in the year 2023. However, it had not been recorded as a receivable in the project financial statements for the year under review. As a result, current assets in the financial statements had been understated by the similar amount.	12.3	Due to forex crisis prevailed at that time. The project was compelled to settle this amount.	Accounting error should be corrected.

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

Reference to the Laws Rules and Regulations	Non-Compliance/ Audit Issue	Responses of the management	Auditor's Recommendation
Financial Regulation 502(2) the Treasury Circular No. 842 dated 19 December 1978	Fixed asset registers had not been properly maintained separately for each project by the PMU.	Action has been initiated to update the values of these assets.	Circular instructions should be followed.

## 3. Physical performance

### 3.1 Physical progress of the activities of the project

The Project commenced its activities on 03 September 2014 and as per the basic agreement and the implementation plan the project scheduled to be completed on 30 June 2019. However, the management failed to achieve the expected target and the period of the Project had been extended up to 29 February 2024. According to the information given, the overall physical and financial progress of the Project at the end of the year under review was 99 percent and 84 percent respectively.

### 3.2 Contract Administration

Audit Issue	Responses of the management	Auditor's Recommendations
(a) 42 DMA meters had been installed by the project for the western and southern part of Colombo at a cost of USD 476,373, and out of these, 34 meters were non-operational despite a 5-year warranty for all meters valid until November 2023, the Project failed to claim the warranty or finalize a maintenance agreement. As a result, it severely impacted to the effectiveness of NRW management. However, 17 meters under ICB-03 were repaired using project funds at a cost of Rs. 24.28 million through an unauthorized variation order.	All meters were subsequently handed over to the O&M section for maintenance, and as of 30 May 2025, due to some reason fault identification and rectification can be done through the contractor once payments are received.	Immediate action should be taken to rectify the existing issues.

- |     |  |   |  |
|-----|--|---|--|
| (b) | Out of the 78 installed Electro Magnetic Flow Meters, 53 were been inactive at the audited date of 30 May 2025. A total of Rs. 26.55 million was spent on materials for repairs of those meters. However, Rs. 15.78 million worth meters remained unused in stock, including 53 batteries worth Rs. 1.92 million expiring by April 2028,. These procurements were done as variations to the main contract without having proper approval and suppliers and service providers have been selected without following the procurement guideline. | All required repair materials were purchased from the local agent due to a lack of local availability.  | Procurement Guideline should be strictly followed and disciplinary actions should be taken against responsible officers who violated Procurement Guidelines. |
| (c) | Under the ICB-03 contract, the Project Director approved the procurement of 26,623 customer meters, significantly exceeding the 9,306 required quantities as per the original BOQ. Evidence had not been given to the audit to verify the neediness of excess meters, However the actual requirement was been only 10,482 units. Further it was observed that the project had prepared a fraud BOQ latterly which included the meter requirement aligning to above excess meters which was purchased.  | Estimated quantity of 26,623 nos. was purchased by the project through the relevant BOQ item. However, after a critical study, NWSDB decided to replace only the defective water meters. Accordingly, balance meters were handed over to O & M section with proper handing over procedures. | Investigation should be conducted to identify the responsible officers for those failures.   |
| (d) | The stock warehousing facility for the ICB-04 contract, located on Urban Development Authority land in Thelawala, reported a significant stock shortage valued at approximately Rs. 351 million as of 24 December 2023. Additionally, 3,432 decommissioned water meters, valued at around Rs. 3.07 million and belonging to the  | Once the material reconciliation is completed, the losses will be reduced from contractor's IPC.  | Investigation should be conducted to identify the responsible person for those misuses and recover the losses from them.                                     |

NWSDB, were not returned after replacement by the contractor.

- (e) The ICB-04 System Rehabilitation Contract, originally awarded for Rs. 6,990.73 million, was increased twice and final revised value was Rs. 10,056.12 million by January 2025. Further, it was noticed that variation orders were carried out using new rates amounting to USD 9.2 million plus LKR 3,906 million, representing over 51 percent of the original contract sum. That was compromised the credibility of the competitive bidding process, indicating failures in the bidding documents prepared by the PMU without necessary approval as prescribed in Section 8.13.4 of the National Procurement Guidelines.
- Due to inadequate pressure, after forming the DMAs only, the contractor can identify the leaks. Accordingly, revised laying length as well as revised contract sum cannot be predicted until the final DMA is formed. Due to above fact, project was unable to predict the revised contract amount well in advance.
- National Procurement Guideline should be followed and disciplinary actions should be taken against responsible officers who violated Procurement Guidelines.
- (f) A total of Rs. 1,714.73 million, representing 27 percent of the ICB-03 Contract, and Rs. 1,798.71 million, equivalent to 26 percent of the ICB-04 Contract, were allocated for pipe laying using trenchless technology. This methodology was a critical consideration in selecting specialized international contractors, who typically come at a higher cost. However, during implementation, the PMU unilaterally changed the methodology, replacing trenchless techniques with conventional open trenching. This change effectively descope critical BOQ items and indicated a significant failure to identify feasible technology during planning, which resulted in the
- Due to heavy traffic and to avoid public inconvenience, the project decided to use trenchless method at the project formulation stage. Later we were compelled to use open trench method due to most of the pipe sizes are need to be increased due to un predictable demand increase. The Tender documents prepared by the project were evaluated by a separate TEC appointed for the purpose. In lieu of trenchless method, the project adopted open trench method using BOQ
- Investigation should be conducted in this matter to identify the real situation of those changes.

loss of an opportunity to obtain a competitive price for the contract. It was further observed that the removal of BOQ items exceeding 10 percent of the contract sum constitutes a material variation. In accordance with National Procurement Guidelines, such changes require prior Cabinet of Ministers' approval, which was not obtained. The variation was authorized solely by the Project Variation Committee, representing a serious violation of established procedures with potential implications for project governance and transparency.

rates. As a result, contract sum was not changed beyond 500 mn.

- |     |  |   |   |
|-----|--|---|---|
| (g) | Project – 02 had been started with the objective of reducing non-revenue water below 18 percent, However only 25 out of 42 DMAs fully completed after 123 months. However, loan repayments have commenced, and the government had paid Rs. 5,570.65 million as of 31 December 2024, including commitment and interest charges. | ICB – 04 Contractor is unable to complete the NRW management activity. They agreed to complete all the project activities within six months once the payments are received. | Action should be taken to complete the project soon to avoid additional cost to the Government. |
|-----|--|---|---|

### 3.3 Extraneous Activities/Payments made out of the Project Objectives

<b>Audit Issue</b>	<b>Responses of the Management</b>	<b>Auditor's Recommendation</b>
(a)	As per Project Agreement clauses 2.03(b) and 2.14, loan funds must be used strictly for project activities, Rs. 2,152 million worth of service connection materials were procured for NWSDB needs using project funds during the years 2022/2023. General Manager, Addl.GM (Finance), Addl.GM (WSP) and the Project Director who recommend to the Board of Directors to do this procurement and mentioned that there was a Savings in	Investigation should be conducted against the responsible officers who violated Procurement Procedures.
	Since it is a variation to the ICB -04 contracts, the performance guarantee of the ICB -04 contract will cover the material supply as well. Accordingly, no separate bond is necessary.  Payment was certified by the project with the recommendation of the committee. Payment was	

ICB-04 contract. However the Contract Price has increased by 49.47 % due to this purchase.

A Rs. 628.73 million excess profit (29.24%) was earned by the contractor from this single procurement contract due to inflated unit prices compared to contractor's actual costs and contract terms.

Unit prices used were increased by 6 percent without authority, exceeding cabinet-approved rates. The final contract price was Rs. 341 Million higher than NWSDB published rates, causing a Government loss of over Rs. 300 Million. Additionally, a Rs. 265 Million was paid as overhead and Profit for the Works awarded to the same Contractor as Variation without proper basis or transparency.

The availability of the existing stock had not been assessed before purchasing 250,000 service connections. A stock of Rs. 494.97 Million delivered in April 2023 included Rs. 35.63 Million worth defective items. Without obtaining performance guarantee or contract agreement, NWSDB was not in a position to act against the Contractor. However according to the audit calculations the contractor could be earned Rs. 23.21 Million from this defective stock.

not certified for items which were not recommended by the material Inspection committee. Please note that as per Finance Minister's observation a separate cabinet paper was presented to the ministry to obtain the cabinet approval.

- (b) The contract for ICB 03 System Rehabilitation in West Colombo originally valued at Rs. 6,354 million and increased by 49.47% to Rs. 9,497.80 million, as per the TEC report dated 26 June 2023. The project management also procured chemicals and water meters worth Rs. 1,379 million as a contract variation, including a 15 percent contractor's overhead and profit without prior approval from the Donor and violating the clauses 2.03(b) and 2.14 of the Project Agreement,
- Due to forex issue NWSDB was unable to open the LCs through the local bank. Therefore, it was decided to use the ICB contractor for opening LC with Board of Director's approval. Finally, the above process was approved by the cabinet as well.
- Action should be taken against responsible officers who violated condition of contract.

### 3.4 System and control

Audit Issue	Responses of the management	Auditor's Recommendations
(a) The assets of the project valued at Rs. 13,881 Mn equivalent to 68 Percent had not been Capitalized and handed over to NWSDB up to 31 December 2024. Further it was observed that Assets Forms prepared for assets totaling Rs. 188 Mn relevant to the project had been taken over by the DGM (Western Central), and who was handed over the same assets as project director during the year under Review. Chief accountant or cost accountant had not been Signed and sealed to the assets hand over forms amounting Rs. 194 million.	Assets capitalization is in progress and the delay is mainly due to lack of staff in the project to carry out these activities.	Assets handing over process should be handled by the independent party to avoid conflict of interest.
(b) No action had been taken by the Project management to recover the security deposit amounting to Rs.164.46 million in respect of completed and handed over roads to the Colombo Municipal Council under the ICB-3 /ICB 4 contracts.	This matter is being negotiated with the CMC.	Action should be taken to recover the security deposit.