

Jaffna and Kilinochchi Water Supply and Sanitation Project (Additional Financing) – 2019

The audit of financial statements of the Jaffna and Kilinochchi Water Supply and Sanitation Project (Additional Financing) for first accounting 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 4.03(a) of Article IV of the Loan Agreement No. 3603-SRI and No. 3604-SRI dated 15 December 2017 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank. My comments and observation which I consider should be report to parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreements, then Ministry of City Planning, Water Supply and Higher Education, presently the Ministry of Water Supply is the Executing Agency and the National Water Supply and Drainage Board is the Implementing Agency of the Project. The objectives of the Project are to support the restructuring of the original Jaffna and Kilinochchi Water Supply and Sanitation Project for the improvement of access to safe drinking water in targeted urban and suburban areas and security of water resources in the Jaffna Peninsula. As per the Loan Agreements, the total estimated cost of the Project was US\$ 153 million equivalent to Rs. 23,256 million. Out of that US\$ 120 million equivalent to Rs.18,240 million was agreed to be financed by the Asian Development Bank. The balance amount of US\$ 33 million equivalent to Rs. 5,016 million expected to be financed by the Government of Sri Lanka. The Project commenced its activities on 15 December 2017 and scheduled to be completed by 31 December 2025.

1.3 Qualified Opinion

In my opinion, except for the effects of the matters described in the table 02 of this report, the accompanying financial statements give a true and fair view of the financial position of Project as at 31 December 2019, 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 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 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.

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 Deficiency

Accounting Deficiency -----	Impact -----	Response of the Management -----	Auditor's Recommendation -----
Interest charges amounting to Rs.1.33 million and commitment charges amounting to Rs.44.68 million recovered by the Lending Agency up to 31 December 2019 had not been brought to the financial statements.	Understatement of disbursement shown in the financial statement.	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.	Total disbursements should be shown in the financial statements of the year under review.

2.2 Non-compliance with Laws, Rules, and Regulations

Audit Issue -----	Impact -----	Responses of the Management -----	Auditor's Recommendation -----
<p>Eventhough contractor for construction of the Sea Water Reverses Osmosis Desalination Plant and a contractor for supply and laying of distribution networks in Jaffna City area had been selected after 3 years and 1 year respectively, approval of the Cabinet of Ministers had not been granted even up to 19 October 2020. Further, in terms of the section 4.2.3 of the supplement No.31 of the Procurement Manual of 2006, the procurement process of the competitive bidding procedure should be completed within 17 weeks with pre-qualification.</p>	<p>Delaying the completion of Project activities.</p>	<p>Tender for the SWRO Plant was called on 07th December 2016 and closed on 17th July 2017. The Technical Bid opened on 17th July 2017 and Financial Bid was opened on 30th July 2018. However, during procurement process up to 31st August 2020, 89 days taken for seeking clarifications from Bidders and Central Bank of Sri Lanka, 41 days taken for Consultant assistance and review, 151 days taken for TEC evaluation, 379 days taken for SCAPC decisions and 181 Days taken for ADB comments and concurrences, 201 days taken for Cabinet Memorandum Submission and 99 days taken for appeal procedure. In JMC Distribution System, a Draft cabinet memorandum for Supply and Laying of Jaffna City area distribution submitted on 15th June 2020. the project is waiting for the approval from Cabinet.</p>	<p>Need to comply with the circular instructions.</p>

3. Physical Performance

3.1 Physical Progress of the activities of the Project

Activity	Physical Progress as at 31 December 2019		Impact	Responses of the Management	Auditor's Recommendation
	Expected Performance	Actual Performance			
Construction of Sea Water Reverses Osmosis desalination plant.	Contract is scheduled to be completed in October 2021.	Contract has not been awarded even up to 30 November 2020.	Delaying to supply to safe drinking water in Jaffna Peninsula.	The Project and the relevant authorities are taking prompt action to award the SWRO plant by end 2020 as per revised procurement plan.	Action should be taken to award the contract as scheduled.

3.2 Contract Administration

Audit Issue	Impact	Responses of the Management	Auditor's Recommendation
Eventhough a sum of US\$ 120 million equivalent to Rs.18,240 million had been allocated under the proceeds of the Loans for the activities of the Project, an amount of US\$ 0.97 million equivalent to Rs.175.16 million	Incurring additional cost to the Government of Sri Lanka.	As per the Project Administration Manual (PAM), the following Contract Packages are included in Additional Finance. 1. SWRO Desalination component 2. JMC Distribution System 3. Water Tower and Distribution System 2 4. Distribution System (2 additional)	NWSDB is required to negotiate with ADB regarding the reduction of commitment charges.

had only been utilized at the end of the year under review, due to slow physical progress of the Project. As a result of the slow utilization of funds, commitment charges of Rs. 44.68 million had been recovered by the Lending Agency up to 31 December 2019.

The Distribution Network 02 package (DN02) is awarded on 29th October 2018 and the construction work is in progress. This shown a significant financial progress in the additional finance.

In Jaffna Municipal Council Distribution System, a draft cabinet memorandum for Supply and Laying of Jaffna City Area Distribution submitted on 15th June 2020. the project is waiting for the approval from Cabinet.

The SWRO Desalination Plant consume major component in the additional finance. The SWRO Contract has not awarded due to the procurement process.

As a result, the project was not able to achieve the expected financial progress until 31-Dec-2019. Kindly note that after awarding cited Contracts, the project may show significant physical and financial progress in 2020.