

Dry Zone Urban Water and Sanitation Project - 2019

The audit of financial statements of the Dry Zone Urban Water and Sanitation Project for the year ended 31 December 2019 was carried out under my direction in pursuance of the 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 Project Agreement No. 2477 SRI (SF) of 29 June 2009 and Grant Agreements Nos. 0129/0130 SRI (SF) of 29 June 2009 entered into between the National Water Supply and Drainage Board and the Asian Development Bank and Section 4.03 of Article IV of the Loan Agreement No. 2977-SRI(SF) of 13 February 2013 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank. My comments and observation which consider should be report to parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan and Grant Agreements of the Project, then Ministry of Water Supply and Drainage, presently the Ministry of Water Supply is the Executing Agency and National Water Supply and Drainage Board is the Implementing Agency of the Project. The objectives of the Project are to improve physical well-being of the urban population in Mannar, Vavuniya, Puttalam districts. As per the Project and Grant Agreements, the total cost of the Project amounted to US\$ 163.33 million equivalent to Rs. 19,165 million and out of that US\$ 99.78 million equivalent to Rs. 11,809 million was agreed to be provided as a Loan and US\$ 23.22 million equivalent to Rs. 2,649 million was agreed to be provided as a Grant by the Asian Development Bank. The Netherland Trust Fund (NTF) had also agreed through Asian Development Bank to make a Grant of US\$ 2 million equivalent to Rs.228 million under the Water Financing Partnership Facility and balance of US\$ 38.33 million equivalent to Rs. 4,479 million was required to be contributed by the Government of Sri Lanka. The Project commenced its activities on 13 November 2009 and scheduled to be completed by 31 December 2016. However, the completion date of the activities of the Project had been extended up to 31 December 2018.

1.3 Qualified Opinion

In my opinion, except for the effects of the matters described in the table 02 of my report the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2019 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 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 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	Amount Rs. million	Impacts	Responses of the Management	Auditor's Recommendation
(a) Value Added Tax paid up to 31 December 2019 had been set off against the contribution received from the Government of Sri Lanka.	135.47	Understatement of contribution received from the Government.	VAT paid can set off against Government fund.	Total Government contribution should be shown in the financial statements.
(b) Interest charges recovered by Lending Agency up to 31 December 2018 had not been brought to the financial statements of the year under review.	404.10	Understatement of foreign disbursements.	It is treated as a cost of Ministry of Finance, Therefore, not brought to the account.	Total disbursements should be shown in the financial statements of the year under review.
(c) As per the financial statements of the Project the refund made to ADB as at 31 December 2019 was Rs. 82,869 and as per the statements prepared by the Department of External Resources and the ADB it was US\$ 449 and US\$ 20 respectively. However, no action had been taken to reconcile the difference of US\$ 429.		Difference in refund made to ADB.	Project reconciled disbursement out of Impress Account with Central Bank statements. The refunded amount was US\$ 469.23 which is equivalent to the LKR value is 82,869.54 and Project informed it to ADB.	Action should be taken to reconcile the balances of Impress Account with the statement of ADB.

3. Physical Performance

3.1 Physical Progress of the activities of the Project

The Project had implemented several water supply and sanitation activities in the Northern and North Western Provinces in order to improve physical well-being of the urban population under the components of the development of water and sanitation infrastructure and strengthen of water sector institutions North and North Western regions.

Activities	Physical performance as at 31 December 2019		Impacts	Auditor's Recommendations
	Expected Units	Achieved Units		
Supply and laying of pipes, fittings and valves for transmission main and distribution system				
(a) Laying of transmission lines in Vavuniya	24 km	22 km	Related costs would be increased, due to delays in completion.	Actions should be taken to complete the work within the Project period.
(b) Laying of transmission lines from Eluthoor to Pesalai in Mannar	16 km	11km	Loan period closed in September 2019. Hence, there may be additional burden to the Government.	Immediate actions should be taken to complete the works.
(c) Laying of distribution lines from Chillaw to Puttlam	48.90 km	36km	Possibility of delaying the completion of works within the Project period.	Immediate actions should be taken to complete the works.

3.2 Contract Administration

The following observations are made.

Audit Issues	Impacts	Responses of the Management	Auditor's Recommendations
(a) The Project had awarded 04 additional pipe laying contracts to 03 contractors in September and	The works will be remained uncompleted even at the end of the period of the Project.	With the recommendation of the Ministry of City Planning and Water Supply and the approval of the External Resources Department the	Project should asses the physical & financial viability of project before entering into new contract.

November 2018 at a total cost of Rs.244.88 million on a request made by the member of the parliament without considering the date of completion of the activity of the Project as at 31 December 2018. Out of total laying distance of 28.5km the distance of 16km in Mannar District had been divided into two contracts and awarded to one contractor.

pipe line was extended. The 16 km in Mannar was divided to two contracts in order to expedite the work. However as only one contractor was selected as per the tender procedure, it was awarded to the same contractor.

(b) Contracts namely PIPES/MAN/29-A and PIPES/MAN/29-B required to be completed before 31 December 2018. However, the work of these contracts are being continued even after 31 December 2019 without being obtained approval for extension of period of completion from the Project Director.

Delay in project completion due to poor Project activities monitoring mechanism.

Contracts were delayed due to high ground water level due to heavy rain along pipe laying, Delay to issue Railway Crossing Approval by Railway Department, Bomb Blasts on 21st April etc. Contractor was instructed to complete the works.

Immediate actions should be taken to complete the project activities since loan closed on October 2019.

(c) Eventhough the various construction work had been completed in Chilaw, Puttalam and Vavuniya Districts, the ownership of the respective lands had not been transferred to the National Water Supply and Drainage

Possibility of delaying in transferring the ownership of the lands which may affect delaying the utilization of the project.

Acquisition of Land and transfer of title to NWSDB are handled by the Land Section of NWSDB. Land division submitted Assets Forms for the Cost of LKR 6,847,530.54.

The NWSDB should be taken immediate actions to get transferred the ownership of the lands in advance.

Board, even the activities of the Project had closed as at 31 October 2019.

3.3 Matters in Contentious Nature

Audit Issue	Impact	Response of the Management	Auditor's Recommendation
Eventhough the validity period of deposit had been lapsed, the Deposit of Rs. 49,445,124.44 made to the Bank account of the Road Development Authority in 2016 for the road reinstatement works had not been recovered even as 31 December 2019.	Poor financial management.	Staff is in processing to recover that Deposits made to the Road development authority.	Immediate actions should be taken to recover the outstanding balances.

3.4 Matters pointed out in Previous Audit Reports which remained unresolved

Audit Issues	Impacts	Responses of the Management	Auditor's Recommendations
(a) The National Water Supply and Drainage Board had signed a Memorandum of Understanding in 2014 to renovate 03 tanks and re-vamping of lands in Pathiyakulam and Katkulam for paddy cultivation with the Assistant Commissioner of the Department of Agrarian Development in Vauniya without obtaining the concurrence of the Department of Agrarian Development. However, then Assistant Commissioner had not worked accordingly and therefore the work had been delayed. As a result, out of the contribution received from the Government of Sri Lanka the Project had been paid a sum Rs. 21.8 million as an additional compensation and other infrastructure facility in previous years.	The Project had incurred a sum Rs. 21.8 million as an additional compensation and other infrastructure facility.	We already informed these losses to the government Agents, Vavuniya and Director General, Agrarian Development. This issue was already brought to legal officer, NWSDB and Attorney General's Department.	Action should be taken to resolve the issue before winding up Project.

(b) As per the Cabinet of Ministers decision dated 05 April 2013, action should be taken jointly by the Ministry of City Planning and Water Supply and National Water Supply and Drainage Board to implement a suitable mechanism to monitor the activities of the Project closely. However, suitable mechanism had not been implemented by the both parties even as at 31 December 2019.

Possibility of not achieving the Project objectives.

There are several mechanisms to monitor the activities of the Project which have been implemented by the Ministry of City Planning, Water Supply & Higher Education, Project & NWSDB.

Action should be taken to resolve the issue before winding up the Project.

3.5 System and Controls

Audit Issue	Impact	Response of the Management	Auditor's Recommendation
Action had not been taken by the Project to recruit an Internal Auditor to carry out audit of the transaction of the Project activities or engaged with the Internal Audit Section of the National Water Supply and Drainage Board, in terms of Management Audit Circular No. 02/2016 of 10 June 2016 and Financial Regulation 133.	Poor internal control system.	There was no post as Internal Auditor in the carder of Project. Internal Audit section of National Water Supply and Drainage Board carried out internal Audit yearly.	Actions should be taken to recruit an internal auditor.