

Mahaweli Water Security Investment Programme - Tranche 2 - 2022

The audit of financial statements of the Mahaweli Water Security Investment Programme - Tranche 2 for the year ended 31 December 2022 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-SRI and Section 4.02(a) of the Loan Agreement No. 3626 –SRI (COL) 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 Agency 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 two components namely North Central Province Canal Construction and North Western Province Canal Constructions.

As per the Loan Agreement, the estimated total cost of the Programme was US\$ 242 million equivalent to Rs. 38,177.67 million and out of that US\$ 210 million equivalent 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 30 June 2024.

1.3 Opinion

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Programme as at 31 December 2022, statement of expenditure and its cash flows for the year then ended in accordance with Sri Lanka Public Sector 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 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 Programme.
- 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 Physical Performance
2.1 Contract Administration

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	<p>A contract agreement was signed on 15 December 2020 with a foreign company for the construction of tunnel water line spanning of 27.7 km from Konduruwawa to Namalpura under the North Central Province Grand Canal Project with a total value of Rs. 40,073 million. The project is expected to be completed between 2020 – 2027. Following observations are made in this regard.</p>		
(i)	<p>Although, according to the loan agreement signed for Tranche 2, programme to be completed on 31 December 2021. Due to the delay of 2 ½ years in offering the contract, the date of completion of the contract was extended until 10 March 2027.</p>	<p>Although, in 2017 Procurement process had been finalized, due to the water ingress and issues in the “Umaoya” project, stake holders and government decided to review this project including design which resulted in 2 ½ year delay.</p>	<p>Arrangements should be made to obtain additional fund by discussing with ADB.</p>
(ii)	<p>In accordance with the Cabinet approval on 7th October 2021 to expedite the contract timeline to 7 June 2025, a 2nd tunnel boring machine had been purchased at a cost of Rs. 6,691 million in October 2022. However due to the economic crisis prevailed in the country and the challenges in securing additional funds promptly, it was decided by the Cabinet decision dated 03 April 2023 on No.23/0533/623/014, the newly imported tunnel boring machine to be temporarily kept idle until March 2024. Consequently, the expenditure incurred on the second boring machine was become idle during this period.</p>	<p>However discussion is underway to commence the TBM-2 in October, 2023 while getting approval for the funding from ADB.</p>	<p>Should be prepare a proper plan to use the second tunnel boring machine affectively and machine should be operated according to the plan.</p>

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| <p>(iii) Even after two years by the end of the year under review, only 50 meters of the tunnel had been completed and the construction progress was at a low level of 10 percent.</p> | <p>For manufacturing of TBM-1 machine and delivery the same to site, it took nearly one year as per construction Programme. Due to non-availability of explosive with the imports restrictions access shaft and required length along the tunnel to install the TBM machine was delayed. From the beginning of the year 2023, TBM-1 machine has achieved 1110-meter length of tunnel up to now.</p> | <p>The remedial actions should be taken to stipulated a new time frame and to complete the task within the time frame.</p> |
| <p>(b) Under the North Western Province Grand Canal project, the construction of Mahakitula Inlet Tunnel, Mahakitula and Mahakirula Reservoirs and Feeder Canal Mahakirula Reservoirs valued at Rs. 9,978 million, had been awarded to a foreign company for completion by 2024. However, during the period of 2 years the construction progress reminded low level of 2.97 percent due to lack of proper staff, insufficient construction equipment, and poor work site management. In response to the unsatisfactory situation measured are being under taken to terminate the contract. However, it's noteworthy that the contractor has already been paid a mobilization advance of Rs. 1,197 million and payment for completed work amounting to Rs. 355 million.</p> | <p>The Contract was terminated in 11th May, 2023. The advance payment had been fully recovered</p> | <p>(i) Selecting a new contractor according to the ADB guideline</p> <p>(ii) The contractor should be black listed</p> <p>(iii) Performance Guarantees amounted Rs.459.18 million and US\$ 3.021million should be charged.</p> |
| <p>(c) Regarding Tranche 03, a contractor for 6 contract packages out of 09 planned contract packages, had selected at a cost of Rs.1.7 million from the allocation received under Tranche 2. However, since the necessary credit provisions for the implementation of Tranche 3 had not been received, the contracts could not be executed and leading to the idling of the expenditure incurred under Tranche 2 for procurement activities.</p> | <p>The situation was beyond our control due to the pathetic situations prevailed in the country in 2021-2022, Required funds under Tranche-3 and additional funds was not received as we expected while ADB and ERD and the government instructed not to proceed awarding the contract. Therefore, idling of cost incurred for the procurement process was unavoidable.</p> | <p>Necessary actions should be taken against the officers who commenced the procurement procedures of Tranche 3 without having financial provisions.</p> |

- (d) A contract for excavate a tunnel 8.83 Km long, to bring the water from Kaluganga Reservoir to Moragahakanda Reservoir, to be completed during the year 2018 – 2021 at a cost of Rs. 7,146.91 million had been awarded to a foreign company. Following observations are made.
- (i)The contract period had been extended up to 16 July 2022.
- (ii)By the end of the year under review, the total performance of the contract was 82 percent and the construction progress in the year 2022 was only 12 percent.
- (iii)It had been allocated Rs.274.5 million for price variations of the contract. However, Rs.781.48 million had been paid as price variance by the end of the year under review, by exceeding Rs.506.98 million.
- (iv)Further, it had been forecasted that the cost of the contract will be increased up to US\$ 35 Million (Rs.12,600 million) in future.
- Actual date of commencement was delayed due to fuel crisis situation of the country. Fuel, construction material and labour mobility issues for the major reasons for the delay in program. The extended date of contract is 16 July 2022 and forecast cost of the contract at completion will be Rs.8.25 billion as per the amended agreement to be signed.
- Acknowledge in writing the contractors and the consulting company to complete the contract as soon as possible.

2.2 Extraneous Activity made out of the Project Objective.

Audit Issue	Response of the Management	Auditor's Recommendation
<p>A sum of US\$ 39 million out of the allocated US\$ 140 million for 02 main construction contracts and US\$ 50 million additionally had been approved by the Asian Development Bank for the purchase of agricultural inputs, for paddy cultivation in the 2022/2023 season. Out of which Rs. 14,202 million was spent and 41,876 metric tons of fertilizer had been imported. This entire stock of fertilizer, packaged in 50Kg bags was delivered to 02 government owned fertilizer companies and handed over to the Secretary of the Ministry of Agriculture on 5 December 2022. However, there has been no confirmation from the Secretary of the Ministry of Agriculture regarding the receipt. Further, there was a shortage of 161.5 metric tons (3,230 bags) of fertilizer valued at Rs. 55.233 million. The attention had not been made for resolution and of this matter.</p>	<p>On September 23, 2022, the Ministry of Irrigation, Mahaweli Water Security Investment Program Project Management Unit entered into an agreement with a company to supply 40,000 metric tons of Chemical Fertilizer(MOP) to 1 metric ton at a price of 950 US dollars. Fertilizer was ordered accordingly and stock arrived at Colombo port on 02.12.2022. As informed by the shipping agent PRUDENTIAL SHIPPING LINE (PVT) LTD. According to the bill of lading submitted by the supplier through the Bank of Ceylon, it was shown that 41,876 metric tons of fertilizer (MOP) had been supplied. As per our letter no.</p>	<p>A formal inquiry should be conducted regarding the shortage of fertilizer.</p>

MI/MWSIP/PMU/PRO/MOP/Fertilizer dated on 5th December, 2022 fertilizer stock was arranged to be handed over to the Secretary, Ministry of Agriculture.

Distribution process were done by the Ministry of Agriculture as per cabinet instructions. Daily discharge statement issued by the Sri Lanka Ports Authority, stated the received and delivered quantity of fertilizer was 41,876 metric tons. The Daily discharge quantity and discharge no of bags of 50 kg.

The quantity of bags issued was less than to the actual bags had to be issued. Therefore, the shortage was arisen during the packing process which was done by the Ministry of Agriculture.

2.3 System and Controls

Audit Issue	Response of the Management	Auditor's Recommendation
<p>On 18 May 2018 loan agreement No.3625 was signed stipulating the execution of 2 contract packages totaling US\$ 140.47 million. However, the contracts were only offered, 2 ½ years after the loan agreement signed, in December 2020. As a result, commitment charges totalling to Rs. 113.19 million had to be paid to the Asian Development Bank from 15 November 2018 to 15 November 2020.</p>	<p>The Delay of awarding the contract of UECP-ICB-1 due to re-bidding process which had to be done as the recommended. CML-MTD was in poor financial position which was affected in already awarded contract of UECP-ICB-1 to the same contractor.</p> <p>The delay in the awarding of contracts was also due to the Covid-19 epidemic that, our country faced in 2019 followed by economic recession in the country in 2022. It has resulted low disbursement once underutilized funds.</p>	<p>Loan should be used for relevant tasks within the stipulated time.</p>