

Conflict Affected Region Emergency Project (CARE) (Component C) - 2013

The audit of Financial Statements of the Conflict Affected Region Emergency Project (CARE) – Component – C for the year ended 31 December 2013 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 Schedule 2, Section II B of the Loan Agreement No.2626-SRI dated 07 June 2010 entered into between the Democratic Socialist Republic of Sri Lanka (GOSL) and the Asian Development Bank (ADB).

1.2 Implementation, objectives, Funding and duration of the Project

According to the Loan Agreement, then Ministry of Economic Development presently, the Ministry of Policy Planning Affairs, Child, Youth and Cultural Affairs is the Executing Agency and the Ministry of Public Administration and Home Affairs, Ministry of Youth Affairs for Vocational Training Authority, Provincial Irrigation Department of the Northern Provincial Council are the implementing Agencies of the Project. The objective of the Project is to restore and improve, livelihood, economic infrastructure and administrative and legal services in the conflict affected areas. As per the Loan Agreement, the estimated total cost of Component -C- of the Project was US\$ 39.06 million and out of that, US\$ 35.27 million or 89 per cent of the total cost was agreed to be financed by the Asian Development Bank. The Project Commenced its activities on 07 June 2010 and was completed by 30 June 2013. However, the Project had submitted the financial statements for the year ended 31 December 2013 for audit

1.3 Activities of the Project

According to the Agreement, the activities relating to Component C of the Project is summarized below.

- Part 6: Restoration of about 10 medium and small irrigation schemes.
- Part 7: Rebuilding 10 administrative offices and provision of related facilities.
- Part 8: Rehabilitation and reconstruction of district vocational training centres in Kilinochchi, Mannar and Mullaitivu.

1.4 Responsibility of the Management for the Financial Statements.

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Generally Accepted Accounting Principles. This responsibility includes; designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error, selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

2. Scope of Audit and Basis of Opinion

My responsibility is to express an opinion on these financial statements based on my audit. Audit opinion, comments and findings in this report are based on review of the financial statements presented to audit and substantive tests of samples of transactions. The scope and

extent of such review and tests were such as to enable as wide and audit coverage as possible within the limitations of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes the examination on a test basis of evidence supporting the amounts and disclosures in financial statements and assessment of accounting policies used and significant estimates made by the management in the preparation of financial statements as well as evaluating their overall presentation. I have obtained sufficient information and explanations which to the best of my knowledge and belief were necessary for the purpose of my audit. I therefore believe that my audit provides a reasonable basis for my opinion. The examination also included such test of systems and controls, transactions, assets, liabilities and accounting records as deemed necessary to assess the following.

- (a) Whether the systems and controls were adequate from the point of view of internal controls so as to ensure a satisfactory control over Project Management and the reliability of books, records etc. relating to the operation of the Project.
- (b) Whether adequate accounting records were maintained on a continuing basis to show the expenditure of the Project from the funds of the Government of Sri Lanka and the lending agency, the progress of the Project in financial and physical terms, the assets and liabilities arising from the operations of the Project, the identification of the purchases made out of Loan etc.
- (c) Whether withdrawals under the loan had been made in keeping with the specifications laid down in the Loan Agreement.
- (d) Whether the funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (e) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (f) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles and presented fairly.
- (g) Whether the withdrawals from and the replenishments made to the Special Dollar Account had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2013 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date.
- (h) Whether financial covenants laid down in the Loan Agreement had been complied with.

3. Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, and except for the effects of the adjustments arising from the matters referred to in paragraph 5 of this report, I am of opinion that,

- (a) the Project had maintained proper Accounting record for the 31 December 2013 and the financial statements give satisfactorily prepared to present fairly in all material respects, the financial at 31 December 2013 and the financial performance year then ended,
- (b) the funds provided had been utilized for the purpose for which they were provided,
- (c) the withdrawals from and replenishments made to the Special (Dollar) Account during the year ended 31 December 2013 had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2013 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date.
- (d) the statements of expenditure (SOEs) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Agreement, and
- (e) financial covenants laid down in the Credit agreement had been complied with.

4. Financial Statements

4.1. Financial Performance

- (a) According to the Financial Statements and information made available, the expenditure of the Project for the year ended 31 December 2013 amounted to Rs. 2,246,480,822 and the cumulative expenditure as at 31 December 2013 amount Rs. 4,491,658,831. The following statement shows a summary of the expenditure for the year under review. proceeding year and cumulative year expenditure as at 31 December.

<u>Item of Expenditure</u>	<u>Expenditure</u> <u>2013</u>	<u>for the year</u> <u>2012</u>	<u>Cumulative</u> <u>Expenditures as at 31</u> <u>December 2013</u>
	Rs	Rs.	Rs
Civil Works	2,158,139,415	1,414,076,206	4,243,059,904
Office Equipment	106,654	-	650,454
Consultancy	38,842,907	41,584,104	150,049,269
Incremental Operating Cost	30,185,821	15,226,286	61,285,627
Commitment Charge	19,206,025	12,687,390	36,613,577
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	2,246,480,822	1,483,573,986	4,491,658,831
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4.2. Imprest Fund Account

According to the financial statements and information made available, the operations of the Imprest fund Account during the year under review and the balance as at 31 December 2013 are given below.

	<u>US\$</u>	<u>Rs.</u>
Opening balance as at 01 January 2013	470,469	59,825,196
Add: Replenishments	5,024,358	644,595,682
Revaluation Gain	-	2,077,717
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	5,494,827	706,498,595
Less: Withdrawals	5,487,540	705,545,724
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Balance as at 31 December 2013	<u>7,287</u>	<u>952,871</u>

5. Audit Observations.

5.1. Accounting Deficiencies.

The following observations are made.

- (a) Mobilization advances aggregating Rs. 98,180,975 made to 06 contractors had been accounted as payments made to the contractors.
- (b) Electricity and telephone expenses amounting to Rs. 114,248 incurred on behalf of the Department of Irrigation had been erroneously charged as the operating expenditure of the Project.
- (c) Survey equipments valued at Rs. 2,460,000 purchased by a contractor, out of the proceeds of the Loan had been treated as cost of the contract instead of being treated as the fixed assets of the project.

5.2. Non - Compliance with the laws Rules and Regulation etc.

According to Public Finance Circular No. 364(3) of 30 September 2003, the information on payment of Value Added Tax should be furnished to the Commissioner General of Inland Revenue monthly in respect of each contractor separately with a copy to the Auditor General. An audit test check had revealed that the details of payments of Value Added Tax aggregating Rs.70,291,633 paid to the contractors had not been informed to the Commissioner General of Inland Revenue within the stipulated time.

5.3 Lack of Evidence for Audit

Reports of the Consultant on physical observations made on interim payments amounting to Rs. 38,842,907 made to the contractors relating to the rehabilitation of 44 tanks had not been made available for audit.

6. Financial and Performance Review

6.1 Utilization of Funds

According to the information received, certain significant statistics relating to the financing and budgetary provision for the year under review, utilization of funds during the year under review and the cumulative utilization as at 31 December 2013 are shown below.

Source	Amount agreed to be provided		Budgetary provision for the year 2013	Fund utilized during the year		Funds utilized up to 31 December 2013	
	US\$ million	Rs. million	Rs. million	US\$ million	Rs. million	US\$ million	Rs. million
ADB	35.27	3,985.51	548.30	14.67	1,907	26.29	3,417.95
GOSL	3.79	428.27	207.00	1.73	225	3.82	496.26
Total	39.06	4,413.78	755.30	16.40	2,132*	30.11	3,914.21

* These figures do not agree with the amounts shown under paragraph 4.1 of this report, as payables at the year end are not included therein.

The following observations are made.

- (a) An Action Plan which need to be identify the responsibilities of core- staff with target to be achieved during the period had not been prepared. Therefore, the progress of the Project as a whole could not be properly evaluated in order to take corrective measures and to make necessary changes for achieving objectives set for.
- (b) The activities as per Project Agreement to be conducted on rehabilitation and reconstruction of District Vocational Training Centers in Kilinochchi, Mannar and Mullaitivu had not been commenced even after lapse of 03 years of the date of commencement of the activities of the Project.

6.2 Contact Administration

The following observations are made.

- (a) It was observed that the Value added Tax aggregating to Rs. 2,457,468 under 05 rehabilitation works carried out by the Project had been made without verifying the validity of registration numbers for Value Added Tax purposes. It was revealed in audit that the registration number for Value Added Tax of respective contractive were remained invalied at the time of payment made.
- (b) Audit inspections had been carried out at the sites of the rehabilitation works conducted by the Project and following observations are made thereon.
 - (i) Eventhough a sum of Rs. 4,046,951 had been spent by the Project for supply and transport of rubble for the construction of a bund under rehabilitation of a tank at Kalvilankulam in Mullaithivu District, the assigned works had not been completed. Further, it was observed that the bund of the tank was damaged at several locations, as a result of compaction works not properly done.
 - (ii) It was observed that the defects pointed out by the Consultant on rehabilitation of tanks at Thannimurippu in Mullathivu and puthumurippu in Kilinochchi had not been carried out successfully during the specified period.

- (c) It was observed that the ground surveys had not been carried out at the initial stages of the rehabilitation works and as a result, the payments for extra works thereon had been done as a regular feature. Therefore, the extra works ranging from 14 per cent to 44 per cent had been approved under 06 rehabilitation works carried out by the Project. Further; approval for the variation orders issued under six rehabilitation works at a cost of Rs. 90,965,990 had been granted by the Deputy Project Director instead of Project Director.