

## **Greater Kandy Water Supply Project -Phase I , Stage II - 2013**

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The audit of financial statements of the Greater Kandy Water Supply Project - Phase I, Stage II 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 Loan Agreement No SL-P 90 dated 28 March 2007 entered into between the Government of Sri Lanka and the Japan Bank for International Cooperation (JBIC) presently known as Japan International Corporation Agency (JICA) along with Section 4.03 of Article IV of the Subsidiary Loan Agreement No.SL-P 90 dated 3 September 2008 entered into between the National Water Supply and Drainage Board and the Government of Sri Lanka.

### **1.2 Implementation, Objectives, Funding and Duration of the Project**

According to the Loan Agreement of the Project, then Ministry of Water Supply and Drainage, presently the Ministry of City Planning and Water Supply is the Executing Agency and the National Water Supply and Drainage Board (NWSDB) is the Implementing Agency of the Project. The objective of the Project is to improve the water supply service level of the Greater Kandy and suburb areas. As per the Project cost estimate, the estimated total cost of the Project was JapanYen 4,664 million equivalent to Rs. 4,164 million and out of that, JapanYen 3,447 million equivalent to Rs. 3,078 million was agreed to be provided by the Japan Bank for International Corporation. Subsequently, the cost estimate had been revised up to Japan Yen 5,497 million equivalent to Rs.7,146 million due to additional works and price fluctuations. Out of that, JapanYen 4,634 million equivalent to Rs.6,024 million was

agreed to be provided by the Japan International Corporation Agency. The Project commenced its activities on 30 March 2007 and scheduled to be completed by 30 September 2012. Further, the period of the Project had been extended up to 20 June 2015.

### **1.3 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 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.

### **1.4 Auditor's Responsibility**

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Project's preparation and fair presentation of the financial statements 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 the Project's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management as

well as evaluating the overall presentation of the financial statements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion. The examination also included such tests as deemed necessary to assess the following.

- (a) Whether the systems and controls were adequate from the point of view of internal control so as to ensure a satisfactory control over Project management and the reliability of books, records, etc. relating to the operations of the Project.
- (b) Whether the expenditure shown in the financial statements of the Project had been satisfactorily reconciled with the enhanced financial reports and progress reports maintained by the Project.
- (c) 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 identifications of the purchases made out of the Loan.
- (d) Whether 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 Loan Agreement.
- (e) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.
- (f) Whether the funds, materials and equipments supplied under the Loan had been utilized for the purposes of the Project.
- (g) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (h) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles.
- (i) Whether the opening and closing balances, withdrawals from and replenishments to the Imprest Fund 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.
- (j) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (k) Whether the financial covenants laid down in the Loan Agreement had been complied with.

## **1.5 Basis for Qualified Audit Opinion**

My opinion is qualified based on the matters described in paragraph 2.2 of this report.

## **2. Financial Statements**

### **2.1 Opinion**

So far as appears from my examination and to the best of information and according to the explanations given to me, except for the effects of the adjustments arising from the matters referred to in paragraph 2.2 of this report. I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2013 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2013 in accordance with Generally Accepted Accounting Principles,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) 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 Loan Agreement,
- (d) the opening and closing balances, withdrawals from and replenishments to the Imprest Fund 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 as at that date
- (e) the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (f) the financial covenants laid down in the Loan Agreement had been complied with.

## **2.2 Comments on Financial Statements**

### **2.2.1 Accounting Deficiencies**

The following observations are made.

- (a) Remuneration amounting to Rs. 1.3 million paid by the National Water Supply and Drainage Board for the staff of the Project had not been brought to accounts of the Project.
- (b) A sum of Rs. 1,030.9 million paid by the Project to the contractor of other Project called the Greater Kandy Water Supply Project Phase -I Stage- I, had been accounted under the work-in-progress of this Project.

### **2.2.2 Un-reconciled Balances**

The following observations are made.

- (a) The proceeds of the Loan amounting to Rs.787.83 million received during the year under review, as shown in the financial statements as at 31 December 2013 was not agreed with the proceeds of Rs.717.90 million shown in the records maintained by the Ministry of Water Supply and Drainage.

- (b) As per the information furnished by the National Water Supply and Drainage Board, proceeds of Loan amounting to Rs.4,674.36 million had been received as at 31 December 2013 to implement activities of the Project. However, according to the financial statements of the Project for the year under review proceeds of Loan amounting to Rs.5,819.99 million had only been received as at that date. The Project had not taken action to reconcile the difference and adjust the ledger balances accordingly.

### **2.2.3 Non - Compliance with Laws, Rules and Regulations**

The following observations are made.

- (a) A detailed Register of Fixed Assets had not been maintained by the Project to ensure the existence of the fixed assets procured by the Project.
- (b) Transactions of the Project had not been subjected to audit of the Internal Audit of the National Water Supply and Drainage Board as required by the Circular No. 05 of 26 July 2010 of the Department of Management Audit of the Ministry of Finance and Planning.
- (c) According to the Schedule 2 of the Loan Agreement, general administration expenses and other indirect costs are not eligible for claiming purposes. However, the Project had included general administration expenses amounting to Rs.4.5 million in the contractor's bills and claimed for reimbursements.
- (e) A monthly report on payments of Value Added Tax had not been furnished to the Commissioner General of Inland Revenue with a copy to the Auditor General in accordance with the paragraph 5.4.12 of Procurement Guideline, Section 21 of the Value Added Taxes Act, No. 14 of 2002 and the paragraph 05 of Public Finance Circular No 364 (3) of 30 September 2002. Total amount of Value Added Tax paid in 2013 was Rs. 62.80 million.
- (f) According to Section 08 of the Public Contract Act, No.03 of 1987, the contractors who accepted contracts for Rs. 5 million or more should be registered under Registrar of Public Contract. Further, within 60 days after awarding of the tender, the tender agreement should be registered with the Registrar of Public Contract. This requirement had not been complied with by the contractors who dealt with the Project. Further, the Project had proceeded with the contractors without considering this requirement.

## **3. Financial and Physical Performance**

### **3.1 Utilization of Funds**

Certain significant statistics relating to the financing, budgetary allocation for the year under review and the utilization of funds during the year under review and up to 31 December 2013 are shown below.

Source	Amount agreed for financing according to the Loan Agreement		Allocation made in the Budget Estimate for the year under review	Funds utilized			
	JPY million	Rs. million		Rs. million	during the year under review		as at 31 December 2013
	JPY million	Rs. million	Rs. million	JPY million	Rs. million	JPY million	Rs. million
JICA	4,634.00	6,024.00	718.00	609.50	787.80	3,530.81	4,769.70
GOSL	863.00	1,122.00	200.00	128.43	169.53	743.14	980.95
	<u>5,497.00</u>	<u>7,146.00</u>	<u>918.00</u>	<u>737.93</u>	<u>957.33</u>	<u>4,273.95</u>	<u>5,750.65</u>

According to the above information, the Project had only achieved 76 per cent of financial progress after completing of 6 1/2 years as at 31 December 2013, out of total period of 08 years of the operations of the Project. Therefore, expedite action should be implemented through proper Action Plans to utilize the balance proceeds of Loan of Japan Yen 1,103 million during the rest of period of 1 1/2 years of the operations of the Project.

### 3.2 Physical Progress

According to the progress reports furnished by the Project, the activities of construction of service reservoirs, pump house and supply, laying and installation of transmission and distribution pipelines had been substantially completed as at 31 December 2013. However, the construction of pump house at Gonigoda and service reservoir at Medawala and laying of distribution pipe lines in Medawala and Kopiwatta areas had shown slow progress during the year under review.

### 3.3 Acquisition of Lands

The Project had acquired 06 plots of land from National Housing Development Authority to construct a pump house at Yattawa in Harispattuwa Divisional Secretarite area and a sum of Rs. 6.3 million had been paid thereon in December 2013. However, the ownership of the land had not been transferred to the National Water Supply and Drainage Board due to non-payment of penalty charges and tax amounting to Rs. 607,309.

### 3.4 Matters in Contentious Nature

As a practice, the computation of the remuneration for the staff of the Project is being done by the National Water Supply and Drainage Board and 20 per cent of the salary cost is charged from the Project as overhead expenditure even though the Project had recruited adequate staff for its administration works. The overhead expenditure so paid by the Project to the National Water Supply and Drainage Board for the year under review was Rs.6.9 million.