

Clean Energy and Access Improvement Project - 2014

The audit of financial statements of the Clean Energy and Access Improvement Project for the year ended 31 December 2014 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 2.09 (a) of Article II of the Project Agreements No.2518 and No. 2519 SRI (SF) and Grant Agreement No 0149 - SRI dated 17 June 2009 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement of the Project, the Ministry of Power and Renewable Energy is the Executing Agency and Ceylon Electricity Board, Lanka Electricity Company (Private) Limited are the Implementing Agencies of the Project. The objectives of the Project is to realize affordable and reliable power supply by improving the coverage and service efficiency of the Ceylon Electricity Board and Lanka Electricity Company (Private) Limited through (i) a stronger transmission and distribution network, and demand – side management of municipal street lighting, (ii) removal of network bottlenecks for small hydropower plant, and (iii) stronger transmission network in the Eastern Province and an expanded credit support programme for service connections in selected provinces.

As per the Project Administration Memorandum, the total estimated cost of the Project is US\$ 188.2 million equivalent to Rs 20,274.8 million and out of that US\$ 164.2 million equivalent to Rs.17,689.2 million was agreed to be financed by the Asian Development Bank. The Project commenced its activities on 09 February 2010 and scheduled to be completed by 31 May 2013. However, the period of the completion of the activities of the Project had been extended up to 30 November 2015 for the Loan No. 2518 and up to 30 September 2015 for the Loan No. 2519. Asian Development Bank had extended the closing date for the Grant up to 31 March 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 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.

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 judgment, 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 Loans and Grant etc.
- (d) Whether the withdrawals under the Loans and Grant had been made in accordance with the specifications laid down in the Loan and Grant Agreements.

- (e) 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 2014 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date.
- (f) 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 and Grant Agreements,
- (g) Whether the funds, materials and equipments supplied under the Loans and Grant had been utilized for the purposes of the Project.
- (h) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (i) Whether the financial statements had been prepared on the basis of Sri Lanka Accounting Standards.
- (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 and Grant Agreements 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 2014 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2014 in accordance with Sri Lanka Accounting Standards,
- (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 and Grant Agreements,

- (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 2014 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) 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 and Grant Agreements had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following observations are made.

- (a) As a common feature, the fixed assets procured by the Project had not been properly recognized as the properties of the Project and made accounting treatments accordingly. It was observed that, 02 motor vehicles procured by the Project in 2012 at a cost of Rs. 16.13 million through contractors and used by the Ceylon Electricity Board had been shown under the work- in progress without being shown under the property, plant and equipments of the Project. Further, 17 other motor vehicles procured in 2012 and onwards through contractors at a cost of Rs. 95.56 million had been shown under the work- in progress of the Project eventhough the ownership of such assets had been transferred to the Ceylon Electricity Board by the contractors.
- (b) The electrical equipments and materials procured at a cost of Rs. 97.17 million and remained unused as at 31 December 2014 at the stores of Lanka Electricity Company (Private) Limited had been shown in the financial statements under the work-in progress, as consumed articles instead of being shown under stocks as at 31 December 2014.

2.2.2 Un-reconciled Balances

It was observed that the proceeds of Loan amounting to Rs. 2,342 million and Grant amounting Rs 992,670 disbursed during the year under review and shown in the financial statements as at 31 December 2014 was not agreed with the proceeds of Loan amounting Rs.2,389 million and Grant amounting Rs. 448 million shown in the records maintained by the External Resource Department of the Ministry of Finance. Action had not been taken to reconcile the differences.

2.2.3 Non - Compliance with Laws, Rules and Regulations

The financial statements of the Project required to be submitted to the Auditor General on or before 31 March 2015 had been furnished for audit only on 22 June 2015.

3. Financial and Physical Performance

3.1 Utilization of Funds

Certain significant statistics relating to the financing, budgetary provision for the year under review and the utilization of funds during the year under review and up to 31 December 2014 are shown below.

Source	Amount agreed for financing in the Loan/ Grant Agreements		Allocation made in the Budget Estimate for the year under review	<u>Funds utilized</u>			
	US\$ million	Rs. million		US\$ million	Rs. million	US\$ million	Rs. million
ADB	164.20	17,689.20	3,750.00	17	2,343.00	101	13,071.00
GOSL	24.00	2,585.60	46.00	-	-	-	-
CEB	-	-	426.00	-	218.00	-	1,451.00
Total	188.20	20,274.80	4,222.00	17	2,561.00	101	14,522.00

3.2 Physical Progress

According to the information made available, the contracts for civil works had been awarded as turnkey contracts and the physical progress on activities implemented by the Project as at 31 December 2014 is shown below

<u>Activity</u>	<u>Physical progress as at 31 December 2014</u>
<u>Energy Efficiency Improvement</u>	
(a) System Control Modernization	
Package – A	
Lot 01- Construction of National System Control Centre	Initial designing works had been completed.
Lot 02- Installation of Communication System	Primary activities had been completed.

(b) Transmission System Strengthening

Lot A 01- Construction of Control Building

Lot A 02- Supplementary Contracts

Lot A 03- Construction of foundations for Transformer

Enhancement of scope of work of Puttalam – Maho Transmission Line

Construction works are in progress.

Preliminary and Engineering works commenced.

Construction works are in progress.

Construction works are in progress.

(c) Augmentation of Distribution Substations

Augmentation of Capacity of the substations at Katunayaka, Nawala, Kiribathgoda, Kotikawatta and Hikkaduwa.

Works not yet commenced due to delays in receiving the approval of Asian Development Bank for scope change and tender documents.

(d) Demand - side Management for Municipal Street Lighting

Goods had been procured

(e) Consultancy

The Consultants had not been selected yet.

Access for the Poor

(a) Transmission System Strengthening in the Eastern Province

Action had been taken to import the required equipments

(b) Rural Household Connection

Loans of 1,334 had been awarded for residents in remote areas.

3.3 Management Inefficiency

The activities of the Project were not come under the purview of the Additional General Manager (Projects) of Ceylon Electricity Board who is responsible for all foreign funded projects handled by the Ceylon Electricity Board. As such, overall monitoring of the activities of 08 Parts assigned to the Ceylon Electricity Board had not been properly carried out.