

## **Improving Community-Based Rural Water Supply and Sanitation Project in Post Conflict Areas of Jaffna and Kilinochchi Districts - 2014**

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The audit of financial statements of the Improving Community Based Rural Water Supply and Sanitation Project in Post-Conflict Areas 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 11 (a) of the Grant Agreement No. JFPR 9154 SRI dated 01 August 2011 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 Grant 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, Delft Pradeshiya Sabha, Valikamam South West Pradeshiya Sabha and Karachchi Pradeshiya Sabha are to serve as the Implementing Agencies of the Project. The objectives of the Project is to reduce poverty and improve the quality of life in post- conflict rural communities and returning internally displaced people in Jaffna and Kilinochchi districts through improved water supply and sanitation services. As per the Grant Agreement, the estimated total cost of the Project was US\$ 2.42 million equivalent to Rs. 268.26 million and out of that US\$ 2 million equivalent to Rs. 221.70 million or 83 per cent of the total cost was agreed to be financed by the Japan Fund for Poverty Reduction (JFPR) through ADB and US\$ 0.26 million equivalent to Rs.28.82 million or 11 per cent of the total cost was agreed to be financed by the Government of Sri Lanka (GOSL). The balance of US\$ 0.16 equivalent to Rs. 17.74 million or 6 per cent of total cost should be financed through Community Contribution. The Project commenced its activities on 01 August 2011 and scheduled to be completed by 30 June 2014. However, the period of the Project had been extended up to 30 September 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 Donor 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 Grant, etc.
- (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 Grant Agreements.
- (e) Whether the withdrawals under the Grant had been made in accordance with the specifications laid down in the Grant Agreement.
- (f) Whether the funds, materials and equipments supplied under the Grant 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 Sri Lanka Accounting Standards.
- (i) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and

- (j) Whether the financial covenants laid down in the Grant 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 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 purpose for which they were provided.
- (c) the Statements of Expenditure (SOEs) submitted could be fairly relied upon to support the application for reimbursement in accordance with requirements specified in the Grant Agreement.
- (d) the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (e) the financial statements laid down in the Grant Agreement had been complied with.

### **2.2 Comments on Financial Statements**

#### **2.2.1 Accounting Deficiency**

Direct payments aggregating Rs.25,968,919 made to the contractors had not been included in the cash flow statement for the year under review.

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

According to the financial statements of the National Water Supply and Drainage Board, the value of civil work-in-progress of the Project as at 31 December 2014 amounted to Rs.4,501,789. However, according to the financial statements of the Project it was shown as Rs.167,575,861. The difference of Rs. 163,074,072 had not been reconciled.

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

The following observations are made.

- (a) Even though the audited financial statements are required to be submitted to Donor Agency within 06 months after the end of the financial year, the financial statements of the Project for the year ended 31 December 2014 had been furnished for audit only on 28 July 2015.
- (b) Transactions of the Project had not been subjected to audit by the Internal Audit Unit of the National Water Supply and Drainage Board according to the Management Audit Circular No. 05 of 26 July 2010.

## 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 Grant Agreement		Allocation made in the Budget Estimate for the year under review	<u>Funds utilized</u>			
	US\$ million	Rs. million		during the year under review		as at 31 December 2014	
	US\$ million	Rs. million	Rs. million	US\$ million	Rs. million	US\$ million	Rs. million
Grant	2.00	221.70	130.00	0.64	83.42	1.18	145.17
GOSL	0.26	28.82	11.00	0.09	11.38	0.18	22.41
Community Contribution	0.16	17.74	-	-	-	-	-
	<b>2.42</b>	<b>268.26</b>	<b>141.00</b>	<b>0.73</b>	<b>94.80</b>	<b>1.36</b>	<b>167.58</b>

Eventhough value of Community Contribution for the Project had been identified as US\$ 0.16 million equivalent to Rs.17.74 million in the Grant Implementation Manual, the value of contribution made by the beneficiaries for the activities of the Project had not been ascertained and brought to accounts.

### **3.2 Physical Progress**

According to the progress reports furnished by the Project, the overall physical and financial progress of the Project at the end of the year under review was 75 per cent and 57 per cent respectively. According to the Grant Implementation Manual, it was expected to provide safe drinking water to 1,900 units of household in Jaffna and Kilinochchi Districts, subsequently it was extended up to 2,535 units of household. However, the Project had provided safe drinking water to 875 units of household as at 31 August 2015, due to delays in completion of Delft water supply scheme and problems in low water quality of Akkarayan water supply scheme. Further, the sanitation facilities in Jaffna and Kilinochchi Districts had been provided only to 301 units of household as at 31 December 2014 eventhough it was expected to be provided for 611 units of household under the component of providing of sanitation and hygiene services.

### **3.3 Contract Administration**

The following observations are made.

- (a) According to the information made available, the Delft water supply scheme had been completed in July 2014. However, the water tower constructed at a cost of Rs. 4.81 million had been collapsed on 08 August 2014 due to stormy weather condition prevailed in the island. A team of officers appointed by the National Water Supply and Drainage Board had identified that the selection of location without a soil investigation, poor workmanship and ignorance of the ground water table fluctuation were the main causes for the collapse. However, the Project had taken action in January 2015 to select other location to construct another water tower through same contractor without incurring additional costs to the Project. The construction works had been substantially completed in September 2015.
- (b) It was observed that the quality of drinkable water had not been tested before initiation of the construction works for Akkarayan water supply scheme which was introduced at the later stage of the Project as an additional work. It was observed at the audit site visit made in September 2015 that the construction works of water tower and intake well had been completed whilst construction works of stand posts was not completed. Further, it was revealed that the water consists with high percentage of Magnesium and Ferrous and not suitable for drinking purposes. An additional treatment process had been introduced to mitigate the problem and works implemented thereon was not completed at the time of audit site visit.