

Iranamadu Irrigation Development Project (IIDP) – 2015

The audit of financial statements of the Iranamadu Irrigation Development Project (IIDP) for the year ended 31 December 2015 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 Article IX, Section 9.03 of Financing Agreement No. I-857-LK dated 30 January 2012 entered into between the Democratic Socialist Republic of Sri Lanka (GOSL) and the International Fund for Agricultural Development (IFAD).

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Financing Agreement of the Project, then Ministry of Provincial Councils and Regional Development, presently the Ministry of Provincial Councils and Local Government is the Executing Agency and the Provincial Department of Irrigation and the Department of Agriculture of the Northern Province are the Implementing Agencies of the Project. The objectives of the Project are to promote the effective and sustainable management of the irrigation infrastructure and to achieve sustainable improvement of water and land productivity. As per the Financing Agreement, the estimated total cost of the Project amounted to US\$ 29.32 million equivalent to Rs.3,782.20 million and out of the US\$ 22.23 million equivalent to Rs. 2,819.77 million was agreed to be financed by the International Fund for Agriculture Development. In addition, US\$ 1.23 million equivalent to Rs. 160 million and US\$ 2.70 million equivalent to Rs. 351 million expected to be contributed by the private sector and beneficiaries of the Project respectively. The Project commenced its activities on 30 January 2012 and scheduled to be completed by 31 March 2017.

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 the Guidelines of International Fund for Agriculture Development 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 and International Fund for Agriculture Development Guidelines for Project Audits. 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 controls 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 identification of the purchases made out of Loan etc.
- (d) Whether the opening and closing balances and withdrawals from and replenishments 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 2015 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date.
- (e) Whether withdrawals under the Loan had been made in accordance with the specifications laid down in the Financing Agreement.
- (f) Whether the funds, materials and equipment 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 and International Fund for Agriculture Development Guidelines.
- (i) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (j) Whether financial covenants laid down in the Financing 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 2015 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2015 in accordance with Generally Accepted Accounting Principles and the Guidelines of International Fund for Agriculture Development,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the opening and closing balances and withdrawals from and replenishments 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 2015 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 Financing Agreement,
- (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 Financing Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following accounting deficiencies are observed in audit.

- (a) Retention money amounting to Rs. 21.52 million deducted from the payments for civil works had not been brought to account. As a result, the value of civil works and the retention money payable had been understated by Rs. 21.52 million.
- (b) Computers and accessories valued at Rs. 254,300 had been erroneously shown under the cost of civil works. Further, furniture, motor cycles and information technology equipment procured at a cost of Rs. 1.86 million had also been classified under the cost of advisory services.
- (c) It was observed that civil works valued at Rs. 490 million which remained uncompleted as at 31 December 2015 had been shown as civil works completed in the Statement of Financial Position as at that date.

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 2015 are shown below.

Source	Amount agreed for financing in the Grant Agreement		Allocation made in the Budget Estimate for the year under review	Fund utilized during the year 2015 up to 31 December 2015			
	US\$ million	Rs. million		Rs. million	US\$ million	Rs. million	US\$ million
IFAD	22.23	2,819.77	846.60	3.35	459.04	9.02	1,197.97
Private Sector Contribution	1.23	160.00	-	-	-	0.01	0.58
Beneficiaries Contribution	2.70	351.00	-	0.12	16.02	0.13	17.06
GOSL	3.16	451.43	153.40	0.31	40.69	1.01	131.24
Total	<u>29.32</u>	<u>3,782.20</u>	<u>1,000.00</u>	<u>3.78</u>	<u>515.75</u>	<u>10.17</u>	<u>1,346.85</u>

According to the above information, US\$ 9.02 million equivalent to Rs. 1,197.97 million, representing 40 per cent of the allocation of US\$ 22.23 million equivalent to Rs.2,819.77 million had only been utilized from the proceeds of Loan after lapse of 04 years from the commencement of the activities of the Project. Further, it was observed that 45 per cent of allocation for the infrastructure development purposes under the Component - 01 of the Project and 11 per cent of allocation for the production extension and marketing purposes under the Component -02 of the Project had been utilized as at 31 December 2015.

3.2 Physical Progress

According to the information collected from the Project, civil construction works carried out under 18 contract packages had been completed as at 31 December 2015 whilst other civil construction works under 39 packages were remained in progress ranging from 17 per cent to 67 per cent as at 31 December 2015. Further, it was explained by the Project that the physical progress of other activities under production, extension and marketing etc had remained at 61 per cent as at 31 December 2015. The following further observations are made.

- (a) According to the progress reports, it was expected to rehabilitate 123 kilometres of the distribution canals and out of that only 85.62 kilometres had been completed as at 31 December 2015. Further, it was identified that 1,650 structures of the irrigation systems need to be repaired and out of that only 1,038 structures had been repaired as at 31 December 2015. In addition, no water height rulers had been installed in the canals, eventhough 135 water height rulers were expected to be installed. The Project had expected to rehabilitate 150 kilometres of the farm roads, however no such rehabilitation works had been initiated as at 31 December 2015. Further, 40,000 forest trees expected to be planted to strengthen canal bunds and only 10,500 trees

had been planted as at 31 December 2015. In addition, the action had not been taken to develop other infrastructure facilities eventhough 250 agro wells, 21 drying floors and 03 paddy stores were planned to be constructed by the Project.

- (b) The production and marketing development activities of the Project had shown slow progress due to late selection of a Non- Government Organization in May 2015. Therefore, a sum of Rs. 86.34 million had been estimated to implement the social awareness and training programme and out of that Rs.14.34 million had been spent during the under review It was observed that only a sum of Rs. 2.58 million had been spent for training purposes and the balance sum of Rs. 11.76 million had been spent for the administration purposes of the Non-Governmental Organization hired for social mobilization and training purposes.
- (c) Further, no extension offices had been established under the sub component of production extension and marketing, out of 03 extension offices expected to be established and no training for extension officers had been provided thereon during the year under review. As a result, the farmers in the area were not encouraged enough to apply best practices on commercial farming and use of credit facilities provided by commercial banks to ensure the sustainability of agri- businesses.

3.3 Contract Administration

The following observations are made.

- (a) It was observed that the procurement process adopted by the Project was not used as an effective tool of financial control. The time schedule for procurements to be made under 136 packages of contract works had not been prepared in chronological order as enable to ensure the steps of each individual procurement action taken from the point of commencement of the procurement process until its completion. Further, the Register of Attendance of the members for the meetings of the Procurement Committee had not been maintained over last 04 years in terms of the Section 2.11.2 of the Government Procurement Guideline.
- (b) According to the contract agreement of 13 May 2015 for the civil works, the rehabilitation woks of Paranthan Main Cannel were expected to be completed by 16 December 2015. However, the respective works were remained abandoned since November 2015 after completing of 55 per cent of works, due to failures of the contractor.
- (c) It was observed that contracts of civil works at an estimated cost of Rs. 10.8 million under 12 contract packages had been awarded to the Farmers' Organizations without being assessed their financial capacity and experiences. As a result, the civil works thereon had been carried out through the sub-contractors.

3.4 Issues on Financial Control

The following observations are made.

- (a) It was observed that internal audit plan and audit programme thereon had not been prepared by the Internal Audit Sections of the Executing and Implementing Agencies to cover the activities performed by the Project. As a result, the internal audit reports had not contained material observations on the internal audit activities executed during the year under review.

- (b) Value Added Tax aggregating Rs. 1.98 million had been paid to 02 contractors who were nor registered for Value Added Tax purposes. Further, the validity of registration of Value Added Tax and invoices thereon had not been examined by the Project at the time of payment of Value Added Taxes.