

Ratmalana / Moratuwa and Ja- Ela / Ekala Wastewater Disposal Project - 2015

The audit of financial statements of the Ratmalana/ Moratuwa and Ja-Ela/ Ekala Wastewater Disposal Project 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 with Article 11 of the Specific Agreement No. 71001436 dated 02 March 2006 entered into between the Government of Sri Lanka and the Swedish International Development Cooperation Agency (SIDCA).

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Specific 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 is the Implementing Agency of the Project. The main objective of the Project is to assure the management of pollution in the two areas of Ratmalana / Moratuwa and Ja-Ela /Ekala with appropriate collection of industrial and domestic wastewater treatment in central treatment plants with disposal of treated wastewater and sludge in such a way that it is not harmful to the environment or the people. The long term overall objectives of the Project are to contribute to improve health and living conditions for people in the area, improved environmental conditions in sensitive eco-systems and establish a sustainable development of the industrial areas around Colombo through provision of sewerage networks and treatment facilities in Ratmalana /Moratuwa and Ja-Ela / Ekala areas. As per the Specific Agreement, the estimated total cost of the Project is US\$ 120.02 million equivalent to Rs. 12,135 million and out of that US \$ 91.92 million equivalent to Rs. 9,058 million was agreed to be financed by the Swedish International Development Cooperation Agency as a Loan and US\$ 4.14 million equivalent to Rs. 474 million as a Grant. Subsequently, the total cost of the Project was revised up to US\$ 148.91 million equivalent to Rs. 17,471 million and out of that US \$ 95.06 million equivalent to Rs. 11,315 million was agreed to be financed by the Swedish International Development Cooperation Agency as a Loan and US \$ 8.99 million equivalent to Rs. 1,034 million, as a Grant. The Project commenced its activities on 01 February 2008 and scheduled to be completed by 30 June 2013. Subsequently, the period of the Project had been extended up to 30 June 2016.

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 and 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 Loan and Grant, etc.
- (d) Whether the funds, materials and equipment supplied under the Loan and Grant 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 Sri Lanka Accounting Standards.
- (g) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (h) Whether the financial covenants laid down in the Loan and 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 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 Sri Lanka Accounting Standards,⁵
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the Statements of Expenditure submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Specific 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 covenants laid down in the Specific Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following observations are made.

- (a) Value Added Tax aggregating Rs. 1,440.30 million paid up to 31 December 2015 had been set off against the proceeds of government contribution instead shown under the work-in-progress. As a result, government contribution and the work-in-progress shown in the financial statements had been understated by similar amount.
- (b) Liquidated damages amounting to Rs. 1.17 million recovered by the Project from the contractor during the year under review had been deducted from the capital work-in-progress. As a result, the value of work done shown in the financial statements had been understated by similar amount.
- (d) Commitment charges, management and administration fees etc, aggregating Rs.71.8 million paid directly to the Lending Agency by the Government of Sri Lanka had not been brought to the accounts.
- (e) It was observed that the necessary accounting adjustments had not been made in the Ledger Accounts on fixed assets handed over to the National Water Supply and Drainage Board. Therefore, values of free hold lands aggregating Rs. 114.21 million and other assets aggregating at Rs. 214.14 million shown in the financial statements was not agreed with the corresponding amounts of Rs. 44.35 million and Rs. 15.68 million respectively shown in the Register of Fixed Assets and the physical verification reports.

2.2.2 Non - Compliance with Laws, Rules and Regulations

According to Section 08 of the Public Contract Act No. 03 of 1987, contractors who accepted contracts exceeding the value of Rs. 5 million should be registered under Register of Public Contract. Further, within 60 days after the awarding of the contract, the agreement should be

registered with Register of Public Contract. However, 03 contractors who dealt with the Project had not been complied with the above mentioned requirements.

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 according to the Loan Agreement -----				Allocation made in the Budget Estimate for the year under review -----	Funds Utilized -----			
	Initial Allocation -----		Revised Allocation -----			during the year under review -----		as at 31 December 2015 -----	
	US \$ million	Rs. million	US \$ million	Rs. million		US \$ million	Rs. million	US \$ million	Rs. million
SIDCA									
- Loan	91.92	9,058	95.06	11,315	694.00	4.59	633.95	90.28	10,468.83
- Grant	4.14	474	8.99	1,034	57.00	0.07	8.31	8.07	969.12
GOSL	23.96	2,603	44.86	5,122	315.25	1.29	175.77	28.73	3,749.62
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	120.02	12,135	148.91	17,471	1,066.25	5.95	818.03	127.08	15,187.57
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3.2 Physical Progress

According to the progress reports furnished by the Project, the construction works of Ja-Ela / Ekala wastewater treatment plant and pipe laying activities had been completed as at 31 December 2012. The construction works of Moratuwa / Ratmalana wastewater treatment plant and pipe laying activities had shown a progress of 94.18 per cent as at 31 December 2015. Further, the Project had targeted to provide connections to the sewerage systems for 253 industrial locations and 25,000 residents in Moratuwa and Ratmalana areas. However, the connections only to 121 industrial locations and 15,228 residents had been provided as at 31 December 2015

3.3 Contract Administration

The following observations are made.

- The contract of wastewater disposal system of Ratmalana / Moratuwa area awarded in 2008 had been terminated in 2013 by the Project as the contractor was bankrupt during the period of implementing of the Project. However, the Project had failed to encash the performance bond of US\$ 9.06 million and guarantees of US\$ 7.96 million from a foreign Commercial Bank eventhough the legal charges amounting to Rs. 3.55 million had been incurred during the year under review. Further, the Project had not taken action to recover over payments of US \$ 6.74 million made to the contractor. It was further observed that,

a sum of Rs. 18.39 million had been claimed by the third parties from the Project on damages made to the properties by the contractor.

- (b) A fresh contract on wastewater disposal system of Ratmalana / Moratuwa had been awarded to other contractor excluding several pipe laying works after cancellation of the first contract agreement. Further, the drawing works and re-installation of the damaged ventilation pipes which were not completed by the first contractor had also not been completed by the new contractor even as at 31 December 2015.
- (c) The contract for the supply and laying of internal sewer network at the Central Workshop and Training Centre of National Water Supply and Drainage Board and provide connections to the interceptor manhole of the public sewer network at Ratmalana awarded at an estimated cost of Rs 7.37 million in 2014 had not been commenced as at 31 December 2015 even though the mobilization advances amounting to Rs. 1.3 million had been released.
- (d) As per the Article I of the Specific Agreement, the treated water and sludge required to be disposed in such a way that is not harmful to the environment or the people in the areas of Ja-Ela and Ekala. However, no such a mechanism had been implemented even as at 31 December 2016, under the Ja-Ela / Ekala Wastewater Control Treatment Plant.

3.4 Extraneous Transactions

A sum of Rs. 69.1 million spent by the Project for construction of the wastewater treatment and disposal system for Madiwala Link Housing Scheme, design and building contract for the construction and completion of quarters of Soysapura for the employees of National Water Supply and Drainage Board were not directly related to the objectives of the Project.

3.5 Issues on Financial Control

The following observations are made.

- (a) Eventhough it was highlighted in my report for the previous year, 05 refundable deposits aggregating Rs.12.98 million placed at the Road Development Authority in 2012 and 2013 for road reinstatement works which were completed as at 31 December 2014 had not been recovered even as at 31 December 2016.
- (b) The transaction of the Project had not been audited by the Internal Audit Section of the National Water Supply and Drainage Board, as per the Financial Regulation 134 (3) and the Circular No. 05 of 26 July 2010 of the Department of Management Audit of the Ministry of Finance.

3.6 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 overhead is being charged from the Project 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 as at 31 December 2015 amounted to Rs. 253.27 million.