

Ratmalana / Moratuwa and Ja- Ela / Ekala Wastewater Disposal Project -2016

The audit of financial statements of the Ratmalana/ Moratuwa and Ja-Ela/ Ekala Wastewater Disposal Project for the year ended 31 December 2016 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 II of the Specific Agreement No. 71001436 dated 02 March 2006 entered into between the Democratic Socialist Republic 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 areas of Ratmalana / Moratuwa and Ja-Ela /Ekala with appropriate collection of industrial and domestic wastewater, treat in the central treatment plants with disposal of treated wastewater and sludge in such a way that 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 amounted to 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. The balance of US\$ 23.96 million equivalent to Rs. 2,603 million was required to be financed by the Government of Sri Lanka. Subsequently, 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 balance of US\$ 44.86 million equivalent to Rs. 5,122 million was required to be financed by the Government of Sri Lanka. 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. However, the financial statements of the Project for the year ended 31 December 2016 had been prepared and submitted for audit.

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 Loan and Grant, etc.
- (d) Whether the opening and closing balances and 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 2016 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date.
- (e) Whether the funds, materials and equipment supplied under the Loan and Grant had been utilized for the purposes of the Project.
- (f) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (g) Whether the financial statements had been prepared on the basis of Sri Lanka Accounting Standards.
- (h) Whether the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (i) Whether the financial covenants laid down in the Specific 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 2016 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2016 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 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) The direct payments aggregating Rs. 299.58 million shown in the financial statements had not agreed with the direct payments aggregating Rs. 306.84 million recorded in the Department of External Resources.
- (b) 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, value of motor vehicles amounting to Rs 3.06 million handed over during the year under review to the National Water Supply and Drainage Board had been deducted from capital work- in progress instead of being deducted from the value of plant, property and equipment.

2.2.2 Non - Compliance with Laws, Rules and Regulations

The following instances of non - compliances were observed in audit.

- (a) According to Section 6.1(a) of the Public Contract Act No. 03 of 1987, contractors who accepted contracts exceeding the value of Rs. 5 million should be registered

under the Register of Public Contract. Further, within 60 days after the awarding of the tender, the tender agreement should be registered with the Register of Public Contract. However, those requirements had not been complied by the three contractors who dealt with the Project.

- (b) A monthly report on payment of Value Added Taxes had not been submitted to the Commissioner General of Inland Revenue with a copy to the Auditor General in accordance with the paragraph 5.4.12 of the Government Procurement Guidelines, Section 21 of the Value Added Taxes Act No. 14 of 2002 and Paragraph 5 of the Public Finance Circular No 364 (3) of 30 September 2002. Total amount of Value Added Taxes paid up to 31 December 2016 amounted to Rs. 1,448.32 million.

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 2016 are shown below.

Source	Amount agreed for financing in the Loan / Grant Agreements				Allocation made in the Budget Estimate for the year under review	Funds utilized during the year under review				as at 31 December 2016			
	<u>Initial Allocation</u>		<u>Revised Allocation</u>			Rs. million	US\$		Rs.		US\$		Rs.
	US\$ million	Rs. million	US\$ million	Rs. million			million	million	million	million	million	million	million
SIDCA													
Loan	91.92	9,058	95.06	11,315	250	2.21	321.29	92.49	10,790.13				
Grant	4.14	474	8.99	1,034	16	0.06	9.67	8.20	978.79				
GOSL	23.96	2,603	44.86	5,122	210	0.85	123.94	29.58	3,873.56				
Total	<u>120.02</u>	<u>12,135</u>	<u>148.91</u>	<u>17,471</u>	<u>476</u>	<u>3.12</u>	<u>454.90</u>	<u>130.27</u>	<u>15,642.48</u>				

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. Eventhough the construction works of Moratuwa / Ratmalana wastewater treatment plant had been completed as at 31 December 2015, the pipe laying activities of 4.5 kilometres was not completed as at 31 December 2016. According to the information received, the balance works of the pipe laying activities was decided to be completed under the Phase II of the Project.

3.3 Contract Administration

The contract for wastewater disposal system of Ratmalana / Moratuwa area awarded in 2008 had been terminated in 2013 as the contractor was bankrupt during the period of the Project. However, the Project was able to recover US\$ 10.50 million, out of the performance bond of US\$ 9.06 million and guarantees of US\$ 7.96 million placed by the contractor. In addition, the Project had not taken action to recover over payments of US\$ 6.74 million made to the contractor.

3.4 Extraneous Transactions

The following observations are made.

- (a) A sum of Rs. 123.84 million spent by the Project for construction of building at Zoysa pura for staff quarters of the employees of the National Water Supply and Drainage Board was not directly related to the objectives of the Project.
- (b) A sum of Rs. 1.40 million spent by the Project for acquisition of land for Phase II of the Project was not related to the objectives of the Project.

3.5 Matters in Contentious Nature

The following observations are made.

- (a) As per the Article I of the Specific Agreement, the treated water and sludge should be disposed in such a way that is not harmful to the environment and organisms in respect of the Moratuwa/ Ratmalana and Ja-Ela / Ekala Wastewater Control Treatment Plants. Eventhough approval was granted for management of dried sludge maintain a testing method on continuous basis, action had not been taken to introduce a proper mechanism thereon.
- (b) The value of 10 bank guarantees aggregating Rs. 20.82 million obtained in 2009, 2010 and 2011 for road reinstatement works had not been released even as at 30 April 2016, eventhough respective works had already completed and handed over to the relevant authorities. Further, action had not been taken to withdraw 05 refundable deposits aggregating Rs.12.98 million placed at the Road Development Authority in 2012 and 2013 for road reinstatement works, eventhough the guarantee period of such contracts had been already elapsed.

3.6 Closure of the activities of the Project

Eventhough the activities of the Project were closed as at 30 June 2016, the action had not been taken by the Executing Agency to transfer all the assets and liabilities of the Project and prepare financial statements for winding up purposes.