

## **Fiscal Management Efficiency Project -2016**

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The audit of financial statements of the Fiscal Management Efficiency 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 Section 4.05 (a) of Article IV of the Loan Agreement No.2624 SRI dated 07 June 2010 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank (ADB).

### **1.2 Implementation, Objectives, Funding and Duration of the Project**

According to the Loan Agreement of the Fiscal Management Efficiency Project, then Ministry of Finance and Planning, presently Ministry of Finance and Mass Media is responsible for the execution and implementation of the activities of the Project. The objective of the Project is to enhance the fiscal space and efficiency in the public financial management system of Sri Lanka. According to the Loan Agreement, the estimated total cost amounted to US\$ 40.80 million equivalent to Rs.5,344.80 million and out of that US\$ 30.80 million equivalent to Rs.4,034.80 million was agreed to be provided by the Asian Development Bank. The activities of the Project commenced on 01 May 2010 and scheduled to be completed by 31 October 2013. Subsequently, the period of the Project had been extended up to 31 October 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 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, 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 2016 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date.
- (e) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan 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 Sri Lanka Accounting Standards.
- (i) Whether the 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 Loan Agreement had been complied with.

## **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, 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 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 2016 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 Loan 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 Loan Agreement had been complied with.

### **3. Financial and Physical Performance**

#### **3.1 Utilization of Funds**

Certain significant statistics relating to the financing, budgetary provisions for the year under review, utilization of funds during the year under review and up to 31 December 2016 are shown below.

| Source | Amount agreed to be financed as per the Loan Agreement |                        | Allocation made in the Budget Estimate for year 2016 | Funds utilized during the year under review as at 31 December 2016 |                     |                        |
|--------|--|------------------------|--|--|---------------------|------------------------|
|        | US\$ million   | Rs. million            |  | Rs. million  | US\$ million        | Rs. million            |
| ADB    | 30.80  | 4,034.80               | 667.00   | 664.00   | 11.61               | 1,552.00               |
| GOSL   | 10.00  | 1,310.00               | 96.00  | 95.00  | 2.06                | 275.00                 |
|        | <b><u>40.80</u></b>                                    | <b><u>5,344.80</u></b> | <b><u>763.00</u></b>                                 | <b><u>759.00</u></b>   | <b><u>13.67</u></b> | <b><u>1,827.00</u></b> |

According to the above information, out of the total allocation of US\$ 30.80 million equivalent to Rs.4,034.80 million, only US\$ 11.61 million equivalent to Rs.1,552.00 million or 37.69 per cent had been utilized by the Project even after lapse of 06 ½ years from the date of the commencement of the activities of the Project. Therefore, the possibility of use of the balance of allocation of US\$ 19.19 million during the rest of the period of 10 months, upto the closure of the Loan facility is remained very remote.

#### **3.2 Physical Progress**

The activities of the Project were comprised with 02 main components namely, establishment of the Integrated Treasury Management Information System and Capacity Development. The following observations are made on physical progress of the activities under such components as at 31 December 2016.

- (a) The contract for the supply of information system infrastructure, customization and implementation of Integrated Treasury Management Information System had been awarded at US\$ 17.76 million equivalent to Rs. 2,356.75 million to a foreign company on 14 October 2013 and expected to be completed by 23 April 2015. However, the physical progress thereon was remained slow as at 31 December 2016 due to delays in installing of Local Area Network, upgrading of existing accounting system and speeding up of the System Requirement Specifications and changes etc. In this connection, the Project Director had informed that the time taken to complete the renovation works of the buildings of the Ministry of Finance and Mass Media and reviewing of the System Requirement Specifications by the experts attached to the Ministry had caused delays to complete the works on establishment of the Integrated Treasury Management Information System.
- (b) It was observed that the annual targets for officers to be trained under the Capacity Development Component had not been determined by the Project at the initial stages. However, the foreign trainings for 82 senior officers and local trainings for 200 other staff members of the Ministry of Finance and Mass Media and other departments under the purview of the Ministry had only been provided during the year under review, under the Component of Capacity Development.

### **3.3 Contract Administration**

The contract for independent assurance for non-functional testing of Integrated Treasury Management Information System had been awarded to the University of Moratuwa at an estimated cost of Rs.14.97 million in September 2016. The following observations are made in this regard.

- (a) Contrary to the requirements mentioned in the paragraph 3.4 of the Government Procurement Guideline for Selection and Engagement of Consultations - 2007, the Project had not prepared a cost estimate and a budget for this purpose.
- (b) A proper procurement committee for the selection of the services providers for consultancy services had not been appointed by the Secretary to the Line Ministry. Instead of that the concurrence of a separate Committee appointed for selection of Consultants for the training purposes had been obtained. According to the explanations made by the Project Director, the respective Committee was appointed by the Secretary of the Ministry of Finance and Mass Media only for the purpose of selection of Consultants for training activities conducted by the Project. Further, the University of Moratuwa as a government owned institution had been selected to award the contract based on the approval of the above mentioned Committee.

### **3.4 Matters in Contentious Nature**

Eventhough the activities of the Project had remained behind the targets, the liquidated damages to be charged thereon had been waived off by Project with mutual understanding with the contractor. According to the explanations made by the Project Director, the delays on achieving millstones of the Project were attributed by both of the Line Ministry and the contractor. Therefore, the responsibilities of individual parties could not be measured due to their interdependency and it was not practical to charge penalties on the contractor.