Supporting Electricity Supply Reliability Improvement Project - 2020

The audit of financial statements of the Supporting Electricity Supply Reliability Improvement Project for the year ended 31 December 2020 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 2.09 of Article II of the Project Agreement No. 9186 SRI dated 19 December 2016 entered in to between the National Water Supply and Drainage Board and Asian Development Bank. My comments and observations which I consider should be reported to parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Project and Grant Agreement of the Project, then Ministry of City Planning and Water Supply, presently the Ministry of Water Supply is the Executing Agency and the National Water Supply and Drainage Board is the Implementing Agency of the Project. The objective of the Project is to support productive energy use for small isolated island and rural communities in 3 islands in the Jaffna area of the Northern Province (Nainathivu, Analativu and Delfts). As per the Grant Agreement entered into between Democratic Socialist Republic of Sri Lanka and Asian Development Bank to finance externally, the estimated cost of the Project amounted to US$ 2 million equivalent to Rs.288 million agreed to be financed by the Japan Fund for Poverty Reduction administered by the Asian Development Bank. Out of the estimated cost of the Project, allocation of US$ 1.25 million equivalent to Rs. 180.72 million had been made for the activities of the Project expected to be carried out by the National Water Supply and Drainage Board whilst US$ 0.75 million equivalent to Rs. 106.56 million had been allocated for the activities of the Project expected to be carried out by the Sri Lanka Sustainable Energy Authority. This report consisted with the observations made on the activities of the Project implemented by the National Water Supply and Drainage Board. The Project had commenced its activities on 19 March 2017 and scheduled to be completed by 30 September 2021.

1.3 Qualified Opinion

In my opinion, except for the effects of the matters described in the table 2.1 of my report, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2020 and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.4 Basis for Opinion

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

1.5 Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Those charged with governance are responsible for overseeing the Project's financial reporting process.

1.6 Auditor's Responsibilities for the Audit of the Financial Statements

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 internal control of the Project.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with those charged with governance regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

2. Comments on Financial Statements

2.1 Accounting Deficiencies

No	Accounting Deficiencies	Amount Rs. million	Responses of the Management	Auditor's Recommendations
(a)	Exchange gain amounting to Rs.2.46 million had been erroneously shown under the current liabilities instead of being shown as separate item under the financing category of the statement of financial position.	2.46	Since the dollar account was opened for date to date operations of the financial transactions of the project, year-end closing balance of 31-Dec-2020 was shown under current assets in statement of financial position according to Accounting Standards. The year-end closing balance of 31-Dec-2020 was consisting of monthly dollar revaluation gains and losses as well. As a result, the dollar account's year end net revaluation gains and losses were shown under current liabilities in statement of financial position	Action Should be taken to account under the financing category.
(b)	A sum of Rs. 13.52 million paid as Value Added Tax during the year under review had been erroneously deducted from the financing category of the statement of financial position instead of being shown as separately under the Project administration expenses.	13.52	As per Accounting Instruction No.01.2021 dated on 12.02.2021 for Accounting Instructions for Foreign Funded Projects, if VAT payments of the projects are funded by the GOSL Grant, the VAT payments to the Contractors/Suppliers/Service Providers should be accounted separately in the books of the project accounts without debiting the WIP account. Accordingly, project's VAT expenditures of Rs 13.52 Mn was shown in the project's financial statements for the year ended 31st December 2020.	Action Should be taken to account under the Project Administration expenses.

2.2 Non- compliance with Laws, Rules and Regulations

No	Reference to the Laws, Rules and Regulations	Non-Compliances	Responses of the Management	Auditor's Recommendations
(a)	The written permission should have been obtained from the Coastal Conservation Department before commencing development activities within costal area in terms of Section (14) (1) of the part III of costal conservation Act No 57 of 1981.	Even though construction of two intake wells had been completed by the Project, permit for Intake wells had not been obtained even up to 31 January 2021.	Project Management, Coordination and Implementation Unit have applied for the approval from the Coastal Conservation Department to build the SWRO plant as well as the Intake wells on 04th October 2018 and the CCD granted the approval for SWRO buildings on 14th December 2018. The approvals for Intake wells have been followed up by sending reminders to the CCD. The process of approval is ongoing by CCD and NWSDB will get CCD's approval at the earliest.	Follow up actions should be taken to obtain the permit for Intake wells.
(b)	In terms of Section 26 of the Marine Pollution Prevention Act No 35 of 2008, permit should be obtained by the Project before discharging the concentrated water to sea.	Project had not been obtained the permit from the Marine Environment Protection Authority before the discharging of concentrated brine water to sea from the sea plant water desalination plant.	Project Management, Coordination and Implementation Unit have contacted the Marine Environmental Protection Authority (MEPA) for the approval of discharging concentrated brine water to Sea from SWRO plant. But MEPA have instructed PMCIU to apply after the commissioning the SWRO plant. Because they need the real water quality parameters of the brine/concentrated water for this approval purpose.	Follow up actions should be taken to obtain the permit.

Therefore, we have applied for the approval from MEPA after commencement of the SWRO plant operation on 19th August 2020. MEPA has visited the site on 04th March 2021. The process of approval is ongoing by MEPA and NWSDB will get MEPA's approval at the earliest.

3. Physical Performance

3.1 Physical Progress

Project components	Audit issues	Responses of the Management	Auditor's Recommendations
(a) Supply and installation of the two no's of 75 m^3/day sea water reverse osmosis plant with related civil works (b) Supply and installation of 0.5 ton ice making factory and refrigeration system.	The Project includes two Project components namely, Installation of sea water reverse osmosis (SWRO) desalination plant and Supply and installation of 0.5 ton ice making factory and refrigeration system. Out of that Supply and installation of the two no's of 75 m^3/day sea water reverse osmosis plant with related civil works had only been completed and commissioning as at 31 December 2020. However, other component namely, construction of Ice making factory of the Project had not shown significant performance and preparation of tender document is in progress as at	The original scope of Supporting Electricity Supply Reliability Improvement Project, installation of Sea Water Reverse Osmosis Plant with small storage tanks (Herein after called "SWRO Plant") and an Ice cubes making Factory with refrigeration facilities were supposed to be construct by the NWSDB. The total cost of the Project was USD 1.255 Million and the Project works commenced on 19th March 2017 and scheduled to be completed on 30th September 2021. Main part of the NWSDB's scope was construction of the SWRO plant and it was already completed by Project Monitoring and	Discuss with Electricity Board regarding this matter whether there is a temporally solution to supply of electricity at low cost until the implement of CEB's Hybrid power system.

	31 December 2020. Hence, as per the progress report of the Project the overall physical and financial progress of the sea water desalination plant including related civil works was 99 per cent and 72 per cent respectively as at 31 December 2020.	Implementation Unit of the NWSDB. But, operation of the Ice cubes making plant with refrigeration facilities is depending on availability of Electricity Supply from CEB's hybrid power system project implemented at Nainathivu. Hence "Tender calling" for Ice cubes making Plant will be feasible when CEB project is completed and this is beyond the control of NWSDB. Therefore, the NWSDB considered only construction of the SWRO plant for the progress of the Project.

3.2 Contract Administration

	Audit Issues	Responses of the Management	Auditor's Recommendations
(a)	Project had initially planned to award the contract for Supply and installation of 0.5 ton ice making factory and refrigeration system by end of 4th quarter of year 2019. As per the revised procurement plan of the Project, it had been delayed up to 23 July 2021 and scheduled to be completed by 23 February 2022. However, it was observed that the operation of the Ice making plant is depends on the Electricity Supply available from CEB'S hybrid power system Project at Nainathivu Island. Nevertheless, according to the information given	The Fisheries Society of Nainathivu who is going to operate the Ice cubes making plant in future, requested an on-grid solar panel system to reduce the operational cost of the Ice cubes making plant since this poor society could not manage high operational cost of the plant with limited income by selling of Ice cubes. Therefore, the NWSDB adopted the Fisheries Society's request in the document of ICE plant for sustainable usage of ICE plant by the Community. But, the CEB's existing system at Nainathivu did not support any kind of renewal energy power generation system. Hence, the operation of Ice cube making plant with refrigeration	Prompt action should be taken to complete the contract before the expiry date of Grant.

	by CEB, construction of Hybrid Power System at Nainathivu had not been awarded even up to 15 March 2021.	facilities is depending on the Electricity Supply from the CEB's hybrid power system project at Nainathivu. Hence "Tender calling" for Ice cubes making Plant will be feasible when the CEB's Hybrid Power System project is completed and it is beyond control of the NWSDB. But the Tender Document is being prepared in conformity to Procurement Category of Goods, for the review of the PPC. Due to the Covid-19 pandemic situation, price of all equipment going up and correct estimate value of the Ice plant is necessary to finalize the bid document. Therefore, it is better to finalize the Engineer's estimate and then finalize the document immediately soon after start of the hybrid project by CEB. But a draft tender document has already been prepared. Project Monitoring, Implementation Unit of NWSDB expects to start construction by 23rd July 2021 and foresee to complete by 23rd Feb 2022, before expiry date of Grants. However, both the Project Management, Coordination and Implementation Unit and WSP division of the NWSDB are closely monitoring the progress of the Contract to complete within the scheduled time frame.	
(b)	Even though the installation of 150 m^3/day capacity of RO plant at Nainathivu Island for cater the drinking water for community, proper water distribution system had not been included in the scope of the Project. Therefore, Project had planned to complete the distribution system through another water supply Project of the Jaffna Kilinochchi which is funding by ADB.	Main cause for the delay of completing the Elevated Water Towers is the 2nd wave of the Covid 19 Pandemic situation in the Country. The officials from Medical Officer of Health did not allow the laborers coming from outside of Northern Province to enter into the island work sites and their strict regulations especially in island sites affected the progress. Further, flood followed by Puravi cyclone in early December 2020	The progress of the contracts required to be monitor closely to complete within scheduled time frame by PMU and water supply Project Division of the NWSDB

However, laying of transmission line in 3 islands had already been completed under Jaffna Kilinochchi Project. Even though the construction of Elevated towers under this Project was scheduled to be completed by month of December 2020, overall physical progress was only 44 percent. As a result, construction contract was extended up to April 2021. Further, supply and laying contract for distribution system in three islands under this Project had been awarded only on 25 January 2021.

also affected the progress. But currently the work force and machinery are increased in the sites and the Contractor has been instructed to complete the works within the extended time frame. Contract for Distribution Networks in Islands was awarded on 25th January 2021 and the agreement was signed on 04th March 2021.

However, both the Project Management, Coordination and Implementation Unit and WSP division of the NWSDB are closely monitoring the progress of the Contract to complete within scheduled time frame.

3.3 Observations made on site visits

No	Audit Issues	Responses of the Management	Auditor's Recommendations
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(a)	The Project had completed the supply and installation of 150 m^3/day (2 Nos of 75m^3/day tains) sea water osmosis plant with related civil works at Nainathivu and commissioning is in progress. The main objective of the establishment of desalination plant in Nainathivu island is to provide acceptable quality drinking water to three islands of Nainathivu, Analathivu and Eluvathivu. Out of that people of the Nainathivu have no sufficient and acceptable quality drinking water and current average drinking water requirement of about 100,000 liters per day. Eventhough NWSDB had completed the laying of transmission line in	Water demand at Nainathivu is 100 cu.m per day based on the urban area calculations. Currently, the 2x75 cu.m per day SWRO plant is sufficient to supply water to all 3 Islands. Also, the available grant was sufficient for construction of 2x75 cu.m per day capacity SWRO plant only. In future, the NWSDB will monitor the demand pattern and take necessary actions to meet total demand of all three Islands. The Elevated Water Towers at Nainathivu, Analaithivu and Eluvaithivu are under construction and contract for Laying of Distribution Networks at Islands have been awarded in January, 2021. Until completion of this Distribution Networks contract, the NWSDB provides water to public through common temporary PE Storage Tanks. Current demand is nearly 50 cu.m per day. Then, the plant average	Instructions should be given to contractors to expedite the works relating to distribution network to provide house hold connections to three Islands on their request

	these three islands under the Jaffna kilinochchi Project, elevated towers and distribution system are to be constructed to cater the drinking water of the peoples in 3 islands. Therefore, presently Project provides the water to people from the desalination plant using six temporary storage tanks, which were installed in several common locations in Analathivu and Eluvathivu islands and temporally pumping to the existing tower located at Nainathivu until the completion of elevated towers and water distribution lines. As a result, average daily production was only $50m^3$ equivalent to 33 percent of the plant capacity of $150m^3$ /day and Operational and Maintenance section of the Regional support service of Jaffna was able to provide only 73 no's of water connections out of the 197 connections were requested by community of Nainathivu island from 10 February 2016 to 8 February 2021.	daily production also satisfying the current demand. After completing of the Distribution Network, the demand will increase. Accordingly, the production of SWRO plant will be increased up to its maximum capacity of 150 cu.m per day. The O&M division of NWSDB has provided maximum number of connections through available distribution networks at Nainathivu. After completing the Distribution Network, the NWSDB will provide house connections to all households on three Islands, on their request.	
(b)	As per the Administration Manual of the Project, NWSDB required to install the temporary storage tanks in several common locations in Analathivu and Eluvathivu islands to provide water to people from the RO plant until the completion of Elevated towers and distribution lines. However, significant water consumption had not shown	NWSDB will take all the possible steps to make aware the public to use the SWRO plant Treated Water carefully. Currently, the Officer in Change and the Regional Chemist from O&M section of NWSDB visit Islands weekly to check the Quality of Water and showing the results to Community Leaders, to make them aware to use SWRO water. In addition, the staff of Project Management, Coordination and Implementation Unit are also taking	Action should be taken to supply the sufficient water to existing PE tanks which was installed to the islands and immediate action should be taken to complete the Distribution network to increase the water demand by provide the household connections .

and last 4 months of both islands. Out of that, Eluvathivu was lowest water consumption had shown and rapidly decreased it last 4 months and it was noted in audit that one of the storage tank located at Eluvathivu had no water consumption last 3 months period, as well as there were no water of the balance two storage tanks were observed in Eluvathivu island at the time of physical inspection carried out on 10 February 2021. Accordingly, it was observed that the adequate water supply had not been available to the storage tanks from the plant and lower demand from the community. Therefore immediate action should be taken to supply the adequate water for storage tanks and Project should plan to held the awareness programmes to the community to aware regarding the quality of the sea water reverse osmosis desalination water of the Project and use to treated water through storage tanks until the completion of distribution line.

necessary actions to aware the community to use SWRO treated water carefully. Without the Distribution Networks, NWSDB could not satisfy the demand for Community. In the Completion stage of the Distribution networks, NWSDB will completely aware the public to use the water from the SWRO plant carefully.

3.4 Issues Related to Human Resources Management

No	Audit Issues	Responses of the Management	Auditor's Recommendations
(a)	According to the Section 3.15 of the contract agreement of Sea water desalination plant, the contractor agreed to organize and provide the all four stages of Reverse osmosis certification training for 2 numbers of mechanical engineers of the NWSDB. The respective training was held at DHP INC. USA and a sum of Rs.8.34 million had been incurred as cost of the training. However, it was observed that the one mechanical engineer and one civil engineer had been participated for training instead of 2 numbers of mechanical engineers as per the contract agreement. Further, it was noted in audit that the NWSDB had not been entered into written bond with training participants up to 31 January 2021. Furthermore, as per the training manual they have to get a minimum of 24 hours of additional training and passing a recertification exam every 3 years with the purpose of giving updated knowledge in the field. Accordingly, action should be taken to enter in to the written bond between NWSDB and those participants, due to the possibility of utilizing as RO specialists for future RO plant Projects of NWSDB.	Reverse Osmosis Specialist Training is not only containing Mechanical Part of the Sea Water Treatment Process but also it contains all the process of Sea Water Treatment. The Civil Engineer, especially chief Engineer in NWSDB should understand the Management of all process of water supply in the area including treatment process, trouble shooting of any issues along all path of water supply from raw water intake to Household supply. Also, the selected Chief Civil Engineer for this training is an efficient permanent key responsible employee in Northern division of NWSDB and he was involved in the installation of Water Treatment Plant at Manick Farm at Chettikulam for emergency water supply for displaced people and Peraru Water Treatment Plant (ADB 05th Project) at Vavuniya. Therefore, the NWSDB decided to include this potential candidate in the participant list of Training. The trained participants by RO Specialists are Permanent Employees of NWSDB and they have already committed to work for NWSDB complying with all instruction given by the NWSDB through the Work Agreement. Further, the Trained RO specialist from NWSDB is involving with rehabilitation works of SWRO plant in Negombo. The NWSDB will take necessary action to arrange	As per the Agreement required to trained two Mechanical Engineers and take necessary action to arrange follow-up training to the participants and instruct to pass the recertification exam during the required period. Further, recommend to obtain a bond because, if he was resign from the board loss to the RO specialist to the board.

		follow-up training to the participants and will instruct the participants to pass the recertification exam during the required period.	
(b)	As per Section 3.14 of the contract document of the sea water desalination plant, the supplier should be given sufficient on field training to the NWSDB staff for minimum two weeks on the operation & maintenance and troubleshooting along with commissioning of the RO plant and other equipment. Even though the 99 percent overall works had been completed and commission of the plant is in progress, supplier had not still given the aforesaid on-going training up to audited date on 10 February 2021. Therefore, immediate actions should be taken to obtain the aforesaid training from the supplier before end of the commissioning period. Then, NWSDB staff can use this practical training knowledge for future maintenance activities without any additional cost and without using any out sourced services.	SIREG-Italy is the supplier of the SWRO plant. SIREG's Technical Experts from Italy will visit Sri Lanka to impart On-Field training. Due to the Covid-19 Pandemic caused Travel Restrictions their visit got delayed. As per the schedule of the Contractor, the Technical Experts shall visit in April 2021 and train the officers.	Immediate actions should be taken to obtain the aforesaid training from the supplier before end of the commissioning period.

3.5 System and Controls

Audit Issue	Response of the Management	Auditor's Recommendation
Transaction of the Project had not been subject to the Internal Audit of the Water Supply and Drainage Board, as required by the Circular No.05 of 26 July 2010 of the Department of Management Audit.	The project requested to Internal Audit Division of NWSDB to audit transactions of the project. The project understands that prevailing Covid-19 pandemic situation in the country, the Internal Audit Division postponed visit to the project. However, they will audit the project as soon as possible. (**Annexure 05)**	Actions should be taken to implement an Internal audit