

Rural Infrastructure Development Project in Emerging Regions - 2020

The audit of financial statements of the Rural Infrastructure Development Project in Emerging Regions 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 Para 6(b) of Section 4 in Article III of the Loan Agreement No. SL-P116 SRI (SF) dated 07 July 2017 entered into between the Democratic Socialist Republic of Sri Lanka and the Japan International Cooperation Agency. 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 Loan Agreement of the Project, then Ministry of Provincial Councils and Local Government, presently the State Ministry of Provincial Councils and Local Government Affairs is the Execution Agency and Provincial Councils of 04 Provinces are the Implementation Agencies of the Project. The objectives of the Project are to raise living standards and to develop livelihood of people through improvement of basic infrastructure. As per the Loan Agreement, the estimated total cost of the Project was Japan Yen 15,409 million equivalent to Rs.20,622 million and out of the estimated total cost, Japan Yen 12,957 million equivalent to Rs.17,185 million was agreed to be financed by Japan International Cooperation Agency. The balance amount of Japan Yen 2,452 million equivalent to Rs.3,437 million financed by Government of Sri Lanka. The Project had commenced its activities on 07 July 2017 and scheduled to be completed by 07 July 2024.

1.3 Qualified Opinion

In my opinion, except for the effects of the matters described in the table 2 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, statement of expenditure and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.4 Basis for Qualified 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 scepticism 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)	A sum of Rs.300,427,708 had been shown as advances paid to the contractors under current assets in the statement of financial position. However, according to the ledger accounts it was shown as Rs.268,355,136. As a result, current assets had been overstated by Rs.32,072,572 in the financial position.	32.07	Agreed with observation	Financial statements should be prepared correctly.
(b)	The advances paid to consultancy service had been shown in the statement of financial position as Rs.133,488,236. However, it had been erroneously shown as Rs.115,877,554 in the relevant note 09.	17.61	Agreed with observation	Notes to financial statements should be prepared correctly.
(c)	Cost of civil work had been overstated by Rs.946,464 in the financial position of the Project.	0.95	Agreed with observation	Financial statements should be prepared correctly.
(d)	An amount of Rs.302,588 had been erroneously included to the work-in-progress and current liabilities in the statement of financial position.	0.30	Agreed with observation	Financial statements should be prepared correctly.
(e)	The net cash flow from the operating activities Rs.119 million had been brought from the cash flow statements of four Project Implementing Units. However, as per the calculation net cash flow from operating activities was Rs.128 million In this connection, the difference of Rs.9 million had not been explained.	8.70	Two method had been followed by the PMU and Project Implementing Unit.	Uniform method should be adopted by both Project Management Unit and Project Implementing Units for the preparation of cash flow statements.
(f)	Lease interest payment of Rs.9,890,231 had been shown under the investing activities in the cash flow statement.	9.89	Agreed with observation	Financial statements should be prepared in accordance with Sri Lanka Accounting Standards.

- (g) Capital payment of lease liability Rs.15,493,129 had been shown under investing activities in the cash flow statement which should have been stated under the financing activities as per LKAS 07 and SLFRS 16. 15.49 Agreed with observation Financial statements should be prepared in accordance with Sri Lanka Accounting Standards.
- (h) Payment for civil works Rs.546,906,655 had been shown under the investing activities in the cash flow statements. However, a sum of Rs.562,155,350 was calculated when adjusting the advance amounts and accrued bill amounts on the payment of civil works showing understatement of Rs.15,248,695. 15.25 Agreed with observation Financial statements should be prepared correctly.

2.2 Un-reconciled Balances

Ledger Account	Amount as at 31 December 2020		Description of the corresponding records	Management Responses	Auditor's Recommendations
	As per financial statement Rs. million	As per corresponding records Rs. million			
(a) Advanced to Consultant for Rural Roads and Irrigation.	77.85	-	Confirmation letters.	Informed that calling of balance confirmation letters had been sent to the consultant company.	Books and records should be maintained correctly.
(b) Advanced to Consultant for portable water.	38.03	33.80	Confirmation letters.	The amount shown in the confirmation letter is correct.	Books and records should be maintained correctly.

2.3 Non- Compliance with Laws, Rules and Regulations

No	Reference to the Laws, Rule and Regulations	Non-Compliances	Responses of the Management	Auditor's Recommendations
(a)	Para 2.3.3 (C) of the Management Service Circular No 1/2019 dated 05 March 2019	Contrary to the circulars instruction, two permanent government officers who should be appointed as acting bases were appointed as deputy directors of the project and paid Rs.688,975 as salaries.	The officer had been instructed to settle the balance amount on or before 31 October 2021 by the Project Director.	Action should be taken to recover salaries paid contrary to circulars instructions.
(b)	Para 4.3.1 of above Circular	Due to 50 per cent project allowance had been used to calculate the overtime rate, overtime amounting to Rs. 59,940 had been over paid.	Over payment will be recovered in 3 installments.	Action should be taken to recover overtime payments.
(c)	Para 9.3 of above Circular	The Meeting of the Project Steering Committee is required to be held once in 02 months. However, only 02 meetings had been held during the year under review.	Project Steering Committee meetings couldn't be held properly due to Covid-19 pandemic situation.	The meetings of the Project Steering Committee are required to be held regularly.
(d)	Section 3.1 of Public Administration Circular No. 30/2016 of 29 December 2016	Fuel consumption of 10 vehicles had not been re-tested up to 31 August 2021 after tested in October 2019.	Advices had been given to project director to complete before end of this year.	Action should be taken to follow proper control for fuel consumption.

3. Physical Performance

3.1 Physical progress of the activities of the Project

3.1.1 Performance of Designing and Supervision Consultants

No.	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	Designing of 52 portable water consultancy sub projects should be completed as at the end of July 2020. However, only 48 per cent progress of 25 sub consultancy projects had been achieved.	Work plan had been changed due to Covid-19 pandemic situation and other unavoidable circumstance.	Action should be taken to assess monthly works before making payments.
(b)	Even though the Design work of 27 sub projects under Phase 02 - portable water should be completed at the end of the January 2021, only one sub project was completed as at 31 of January 2021.	Work plan had been changed due to Covid-19 pandemic situation and other unavoidable circumstance.	Action should be taken to assess monthly works before making payments.
(c)	As per the agreement signed for the rural roads and irrigation, 112 sub project under phase 01 required to be commenced and 110 sub project required to be complete the detail designing and preparing bid documents before December 2020. However, 41 sub project and 29 sub project respectively had only been completed as at 31 December 2020.	Work plan had been changed due to Covid-19 pandemic situation and other unavoidable circumstance.	Action should be taken to assess monthly works before making payments.

3.1.2 Performance of Sub Projects

Audit Issue	Response of the Management	Auditor's Recommendation
As per the Implementation Schedule attached to the Project Memorandum, construction works of 418 sub projects had to be completed as at February 2021. However, 11 construction works for portable water supply projects, 37 rural road sub projects and 12 irrigation water supply projects had been commenced as at 30 June 2021.	Work plan had been changed due to Covid-19 pandemic situation and other unavoidable circumstance.	Action should be taken to expedite project works.

3.2 Contract Administration

Audit Issue	Response of the Management	Auditor's Recommendation
Agreed team of staff for the consultancy work had not been assigned up to 30 June 2020.	Steps had been taken to rectify.	Agreed staff required to be mobilized promptly.

3.3 Matters in Contentious Nature

Audit Issue	Response of the Management	Auditor's Recommendation
(a) An over payment of Rs. 9.48 million had been made to contractors on insurance expenditure as lump sum expenditure.	When submission of bids provision insurance was considered a lump sum.	Action should be taken to recover over payment.
(b) Contract for the renovation of Ilukthanna Madugolla road in Uva province had been awarded at a cost of Rs.133.30 million higher than the estimated cost without adapting retendering procedure. As a result, a loss of Rs.21.89 million had to be incurred to the project.	When follow retender procedure, benefits to beneficiaries will be late.	Procurement process should be followed to minimize the cost by the relevant authorities.

3.4 Issues Related to Human Resources Management

Audit Issue	Response of the Management	Auditor's Recommendation
An officer appointed as a Management Assistant to project had been attached as a Personal Assistant since date of appointment in 2017 to Additional Secretary (Project) of the Ministry. A sum of Rs.1,554,046 paid to above mentioned Management Assistant by Project Management Unit.	An officer servicing to ministry with experience with JICA projects had been attached to project behalf of Management Assistant.	Actions should be taken to regularized the appointment.

3.5 System and Controls

Audit Issue	Response of the Management	Auditor's Recommendation
A detailed action plan had not been prepared to include the expected financial and physical targets for the sub-projects mentioned in Annex 16 of the Project Memorandum of the Rural Infrastructure Development Project in the Emerging Zones.	Submitted a copy of the relevant page in the action plan of the ministry.	A detailed action plan should be prepared by the Project, including the expected financial and physical targets for the sub projects.