

Water Supply and Sanitation Improvement Project - 2022

The audit of financial statements of the Water Supply and Sanitation Improvement Project for the year ended 31 December 2022 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 the Schedule II, Section II (C) (3) of the Financing Agreement No. 5685 – LK dated 06 November 2015 and Article 4.09 (b) of the General Conditions of the Credit and Grants of the International Development Association dated 31 July 2010 entered into between the Democratic Socialist Republic of Sri Lanka and the International Development Association. 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 the Ministry of Water Supply and recently the Ministry of Water Supply and Estate Infrastructure Development is the Executing and Implementing Agency of the Project. The objectives of the Projects are to increase access to piped water services and improved sanitation in selected districts and to strengthen the capacity of associated institutions. The activities of the Project are implemented under 04 components namely, rehabilitation and expansion of urban, rural and estate water supply and sanitation schemes, strengthening of the capacity of the Department of National Community Water Supply, building of sector capacity through training and water quality mapping and Project management and administration. As per the Financing Agreement, the estimated total cost of the Project was US\$ 183.90 million equivalent to Rs.27,590 million and out of that US\$ 165 million equivalent to Rs.24,750 million was agreed to be financed by International Development Association. The balance amount of Rs.2,840 million is expected to be financed by the Government of Sri Lanka and through Community contribution. The project had commenced its activities on 07 December 2015 and scheduled to be completed by 31 December 2021.

However, the date of completion of the activities of the Project had been extended up to 31 December 2023.

1.3 Qualified Opinion

In my opinion, except for the effects of the matters described in the para 2 of my report, the financial statements give a true and fair view of the financial position of the Project as at 31 December 2022, financial performance and its cash flows for the year then ended in accordance with Generally Accepted Accounting Principles.

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 Generally Accepted Accounting principles, and for such internal control as management determines as 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

The following observations are made.

No.	Accounting Deficiency	Amount Rs. million	Response of the Management	Auditor's Recommendations
(a)	The difference of Rs. 112 million relating to the loan balance was observed between the balance shown in the financial statements of the project and the balance shown in the financial statements of the Democratic Social Republic of Sri Lanka and no adequate evidence received to verify the difference.	112.00	We have taken the disbursed amount from the Central Bank Statement and the External Resources Department has taken it to accounts according to the monthly average rate. As per the LKAS 21, December month average rate should be taken when recognizing the WB loan.	Use the similar exchange rate when valuing the loan and differences should be reconciled at the end of the year.
(b)	A sum of Rs.179.64 million out of Rs. 2,796.70 million equivalents to US\$ 10,232,420 incurred as interest on loan disbursement of project had only been recorded in the financial statements at the end of the year under review as per records maintained by External Resources Department. Further, a sum of Rs.539.56 million equivalents to US\$ 2,915,309.40 had been charged by the lending agency as service fee for the loan at the end of the year under review had not been recorded in the financial statements of the project. Therefore, working progress had been understated by Rs. 3,156.62 million as at 31 December 2022.	3,156.62	This policy has been suspended by treasury during the year 2018 and also it does not show in our treasury vote reports as it is identified as government expenditure by Treasury.	Adjustment in the financial statements should be done for the interest and commitment fees incurred during the Project period.
(c)	The correction made for the interest charged in the year 2016 amounting to Rs.110 million had been adjusted to the loan balance in the year under review, instead of being adjusted it as prior year	110.00	We will make sure to correct this error during the year 2023.	When make error corrections for prior periods, it should be adjusted retrospectively.

adjustments. Therefore, comparative loan balance in the financial statement had been understated by similar amount.

(d) An Aggregate value of Rs.29 million of completed activities which are under two incomplete urban Projects in Kilinochchi and Rathnapura Districts had been recognised as completed in its financial statements instead of recognising it under work in progress. Therefore, the value of the Work in progress had been understated by that amount.

29.00 Total cost of the Rathnapura Urban Water Supply Scheme is Rs.23, 534, 172.95 and this amount is not fully recognized as completed Pambahinna sub project cost All the cost relevant to the sub activities should be capitalized under main project.

Total cost of the Kilinochchi Urban Water Supply Scheme is Rs. 5,474, 181.68 and the breakdown is assessment cost of Ground water source and Supervision charge of Mulankavil UWSS. Other Institutions payments are taken to the above account as the above is not relevant to the Contractor WIP, therefore this was shown in the year 2018 in Urban Water Supply Scheme – Kilinochchi.

2.2 Unsettled Balances

No.	Description	Amount Rs.million	Period unsettled	Response of the Management	Auditor's Recommendations
(a)	Contractor Retention	233.625	Over 3 years	<p>The contractor has not requested the retention money yet. We will inform the Contractor and make necessary arrangements to release retention.</p> <p>Retention for some contract had been released and others will be released during the year.</p>	<p>Actions should be taken to settle the contractor's retention as per the conditions mentioned in the contract agreement.</p>

(b)	Short term deposits kept in external institutions	69.245	Over 3 years	We have cleared the 2016/2017 deposits amount of Rs. 21, 767, 852.94 during the year 2023.	Make sure to clear the short term deposit after completion of the job.
				Short term deposits kept in Road Development Authority for over 3 years' time will be released once the sub project defect liability period is covered.	

2.3 Non Compliance with Laws, Rules and Regulations

No.	Reference to the Laws Rules and Regulations	Non Compliance	Response of the Management	Auditor's Recommendations
(a)	Financial Regulations of Democratic Socialist Republic of Sri Lanka			
	(i) Section 7.7.2	Seventy three items of fixed assets valued at Rs.2 million were damaged at the end of the year under review as per the Board of survey reports. However, action had not been taken regarding the above assets as per the Financial Regulation 7.7.2 up to 31 May 2023.	We will make sure to complete and submit the asset disposable reports before 30 th September 2023.	Required action Should be taken on this matter as per the Finance Regulations.
	(ii) Section 170(3)	Liquidated damages amounting to Rs.7.493 million deducted from 3 contractors during the year under review and the preceding year had not been credited to the consolidated fund even as at 31 May 2022 in terms of Section 170 (3) of Financial Regulations of Democratic Socialist Republic of Sri Lanka.	We have sent Liquidated damages (LD) amounting of Rs.4.7 Million during the month of June 2023 to Ministry of Water Supply and this amount (LD amount) contains 2 projects out of 3 as only 2 projects were completed up to date.	Should adhere to the provisions in the financial regulations.

(iii) Section 245 and 257	As per random test check, it was observed that an amount equivalent to Rs.58 million had been paid for 6 payment vouchers without being certified and An amount of Rs.14 million had been paid by 10 payment vouchers without being approved.	We will send it in due course.	Vouchers should be sign at the time of payment made.
(b) Condition 24.1 (02) General Conditions of Request for Proposal	Insurance coverage had been obtained after the commencement of the consultancy service from the Greentech Joint Venture instead of take it before commencement of the service as per the condition of contract.	The date of Contract Agreement was 28.10.2016. Accordingly the consultant has provided PII with a minor delay of 2 months. Public Liability Insurance too was available from 04.01.2017.	Should be adhere with the provisions in the contract agreements.

3. Physical Performance

3.1 Physical progress of the activities of the Project

With respect to thirty five Urban and Rural Water Supply Schemes, Rehabilitation Projects, Public Sanitation, Indigenous Sanitation and School Sanitation projects, a considerable delay ranging from 60 days to 1,800 days was observed due to improper planning of project duration, poor performance of the several contractors, import restrictions, community objections, environmental and resettlement issues etc. even after granting extensions ranging from 01 to 08 occasions. Therefore, it was observed that there was a risk of incompleteness of the project within the extended period if the management did not take remedial actions to overcome above identified issues and keep close supervision on this project.

3.2 Contract Administration

No.	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	Extensions of time period had been given to the contractors who engage in seven water supply projects ranging from three to eight instances for the same project even exceeding the original contract period and allowing contractors to keep the mobilization advances amounting to Rs.113.39 million with them for more than two years.	Diyathalawa contract was terminated and advance and performance guarantee fully encashed. Therefore, no pending advance recovery. Other contracts advance deducted as per the condition contracts. For the pending advance recovery contracts, advance	District Managers should monitor the progress of the project in order to complete the projects within scheduled time period and delay charges should be deducted from poorly performed

guarantees are in PMU Account section.

contractors instead of granting time extensions.

- (b) It was observed that poorly performed contractors to whom projects had been already awarded had not been evaluated based on their existing performance when awarding new contracts. Hence it was observed that seven contracts had been awarded to two contractors when they performed poorly in existing contracts and keep an advance of Rs.52.57 million without utilizing in project activities effectively.
- At this stage, Main pipe laying works and Electro mechanical works are completed in Orubendiwewa phase ii and phase iii contracts. Water is pumping from Ulhitiya intake to water treatment plant. Flushing and disinfection works are in progress. Pending works are house connections.
- Performance of the existing contractors should be evaluated prior to award new contracts.
- (c) It was observed that out of 24,000 lavatories scheduled to be constructed in the 07 districts during the period of project, only 21,862 lavatories or 91 per cent had only been completed at the end of the year under review even though the Second project extension is to be lapsed on 31 December 2023.
- Up to now 85% is completed. Some beneficiaries resign the sanitation program implementation reasons to revise the planned sanitation target.
- Achievable target should be established at the initial stage to avoid unnecessary cost.
- (d) As per the initial action plan of the project, 84 special need beneficiary sanitation units of Rs.250,000 each to be constructed in Kegalle, Monaragala and Kilinochchi districts. However, only 48 units or 57 percent had only been constructed in Kegalle and Monaragala district and the construction activities in Kilinochchi district had been suspended.
- Reason for the target not achieved is in the implement stage Ministry of Health, Ministry of Welfare and other relevant authorities were provide 36 identified disable persons toilets.
- Achievable target should be established at the initial stage to avoid unnecessary cost and action should be taken to expedite the scheduled works.
- (e) As per the financial statements submitted to audit an amount equivalent to Rs.961.14 million of payment for consultancy services had been made at the end of the year under review. However, as per the random physical audits conducted, it was observed that project terminations, project extensions, approving variation orders, approving extra works, re-designing of construction of official quarters etc. occurred continuously throughout the period of the project due to poor monitoring and supervision of the contracts.
- Quality and Cost based selection method were applied for selection of ISC consultant.
- Management had to be made a strong agreement with the consultant to avoid weaknesses and action should be taken against the poor performance of the consultants.

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| (f) | The objectives of the development of Website for the Project could not be achieved due to non-working of the site as at 05 June 2023 due to poor maintenance. | CBO Monitoring Web site was developed under WASSIP funds and handover to Department of community water Supply. | Monitor the Project developed assets until the end of the project period. |
| (g) | Even though the Cabinet of Ministers had approved the host for the International Water conference without incurring any additional burden to the General Treasury under decision no22/1636/611/015 dated 26 November 2022, the amount of Rs. 9.5 million spent to provide meals for the conference had been charged to the WASSIP Project under institutional capacity Development component. However, Project had spent Rs. 9.5 million for Lunch 1,350 even the consent from the World Bank had only been obtained to provide 100 Lunch valued at Rs.4.4 million (USD 12,000). Finally this amount had become burden to the General Treasury even there was economic crisis in the country. Finally, it had been included to the loan value. | Necessary approval was obtained for this payment. | Funds of the Project should be used only for the project activities. |
| (h) | Even though the Web based cloud server system for Monitoring and Evaluation (M&E) of data had been developed and handed over to the Department of National Community and water supply on 16 January 2020, the Project had hired upgraded cloud server system Management services to maintain the developed system under the institutional capacity strengthening component and spent Rs.8 million. | Consultancy contract was awarded to develop the above M&E system. Several discussions were conducted with stake holders (DNCWS/NWSDB/PHDT etc) and their comments were considered at the development stage of web site. After handed over, DNCWS request additional facilities for this web site. They were requested additional facility to keep as a data base while operating the M&E system. Therefore, projects get the service from individual consultant to develop additional facilities to web based M&E system. | Requirements of the system should be decided at the initial stage and activities should be closely monitored during the development period. If there are any losses occurred due to the inefficiency, it need to take action against the responsible officers. |

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| (i) | Contract for the Udubaddhana Rural Water Supply Scheme had been mutually terminated on 27 November 2017 due to temporary hold the construction works on Court injunction order. However it had been re award to the new contractor at a cost of Rs.104.41 million including price escalation of 38.25 million. After terminating the contract when the physical progress was remained at 52 percent, new contract awarded on 15 November 2021 and scheduled to be complete on 18 July 2022. However, due to continuous protesting from community for stoppage of construction of surface water intake, the progress of the new contract had remained at 80 per cent even by the end of April 2023 after the extension given up to 24 July 2023. Accordingly, Project had not been done a feasibility study at the initial stage to identify the protest from community. | Udubadana contract was mutually terminated due to water source. Water source issues were raised at the Court. As per Court injunction order temporary hold the construction works. | Management is responsible to failure of this project since the works commenced without having feasibility study. |
| (j) | Even though the Scheduled Completion date of the WASSIP Project is 31 December 2020, it had been extended to 31 December 2023. However, Loan repayment of Rs.3,462 million equivalent to US\$ 13 million had been done by General Treasury from 2020 onwards. Due to the delay and poor performance of the project activities loan repayment had to be done without achieving the expected objective. | Time extensions were given on changes effected in country and world such as COVID -19 pandemic and the economic crisis in the country. Loan repayment based on loan agreement and there was no correlation project period extension and loan repayment. But project extension for original project and additional financing. | Need to make a Discussion with donor to get extension for loan repayments according to the extension given to extend the loan period. Make sure to complete the project as planned |

3.3 Observations made on site visits

No.	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	The contract for construction of Monaragala Septage treatment plant had been planned to complete on 19 October 2021 at cost of Rs.67 million. However, due to poor performance of the contractor, contract agreement had been terminated at the 45 per cent stage of the progress after spending Rs.9.4 million. Further; bid called for balance work is still in evaluation	Due to Continuous garbage dumping by Pradeshiha Saba, contractor took long time to clear the garbage to prepare the land for construction of septage plant. Garbage dumping issue was occurred before awarding	Action should be taken to avoid unnecessary delays in completion of the contract

- stage. The garbage had been dumped by the local authorities to land by disturbing the constructions due to absence of the fence which should be built at the beginning of the activities of the contract.
- the first contact.
- (b) The construction activities of sanitation facilities planned for persons with special needs in Monaragala District had been awarded on 30 April 2021 at a cost of Rs.18.37 million with scheduled completion date of 30 October 2021. However, only 14 facilities valued at Rs.10.8 million out of planned 35 facilities had been completed even time extension had been given up to 31 August 2022.
- Programme Implemented after reallocation program requires sanitation facilities to disable persons. Initial target is 84. Up to now 48 special needs sanitation facilities were provided. Disable sanitation program were completed.
- Requirement should be assessed at initial stage of the Project.
- (c) The construction of 92 latrines planned for Indigenous People in Rathugala had been awarded on 12 February 2021 at a cost of Rs.14.8 million with scheduled completion date of 12 August 2021. However, No any facilities had been completed at the physical verification date of 25 November 2022 even one year time extension had been given up to 31 August 2022.
- Not replied.
- Requirement should be assessed at initial stage of the Project.
- (d) The construction of the Project in relation to the Mahagama Rehabilitation Rural Water Supply Scheme had been awarded on 18 December 2020 at a cost of Rs.53.2 million with scheduled completion date of 17 December 2021. However, only 65 per cent progress had been achieved the physical verification date of 25 November 2022 even two time extensions had been given up to 09 July 2023 due to poor performance of the contractor.
- Now at completion stage.
- Should take actions to complete the contract works within the expected period.
- (e) The construction of the Project in relation to the Peelakandura Rural Water Supply Scheme had been awarded on 27 November 2017 at a cost of Rs.127.03 million with scheduled completion date of 27 November 2018. However, contract had been completed as at 31 December 2022 after lapse of four years and under the 08 extensions. Contractor's poor performance and public objections had been affected to the delay in completion of the
- Partially WSS is functioning. Out of 600 house connections, 360 houses hold getting water.
- Should take actions to complete the contract works within the expected period.

Project. Further, the Project had been layoff the DI pipes and GI pipes and fittings even though those items had not been supplied as per the Bill of Quantity. Evidence was not available to verify supply of those pipes and fittings with required quality as per the Bill of Quantity.

3.4 Issues Related to Human Resources Management

No.	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	Project had deployed 108 employees under contract agreement contrary to the Department of Management Service Circulars No.01/2019 of 15 March 2019. Out of that 05 employees had been deployed for 07 positions such as Quantity Survey and Draftsmen which had not been approved by Department of Management Service.	Some position such as quantity surveyor, draftsmen were not in MSD approval list. But requirement of the project activities, project got the service from short term service contracts.	Strictly adhere with the provisions of Department of Management Service Circulars.
(b)	The Project Director had been promoted as Deputy General Manager (Western North) of National Water Supply Drainage Board with effect from 05 November 2020 even though he should be always recruited on full time basis in order to ensure effective project management in terms of the Section 2.3.2 of the Circular No.01/2019 of 05 March 2019 of the Department of Management Services.	Not replied.	Actions should be taken to appoint a Project Director on full time basis.