

Eastern Province Water Supply Development Project - 2015.

The audit of financial statements of the Eastern Province Water Supply Development Project for the year ended 31 December 2015 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 4.08(a) of Article III of Loan Agreement No. SL-P 98 dated on 26 March 2010 entered into between Democratic Socialist Republic of Sri Lanka and the Japan International Cooperation Agency. My comment and observation which consider should be reported to parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Memorandum of the Project, then Ministry of Finance and Planning, presently the Ministry of Finance and Mass Media 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 provide safe drinking water by expanding water supply facilities in the Eastern Province and thereby contribute to improve living standards of the people of the area. As per the Loan Agreement, the total estimated cost of the Project amounted to Japan Yen 6,054 million equivalent to Rs. 7,703 million and out of that Japan Yen 4,904 million equivalent to Rs. 6,239 million was agreed to be provided by Japan International Cooperation Agency. The Project commenced its activities on July 2010 and scheduled to be completed by December 2013. Subsequently, the period of the Project had been extended up to 23 January 2018.

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 Generally Accepted Accounting Principles 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 identification of the purchases made out of the Loan etc.
- (d) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.
- (e) Whether the funds, materials and equipment supplied under the Loan 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 Generally Accepted Accounting Principles.
- (h) Whether 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 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, 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 2015 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2015 in accordance with Generally Accepted Accounting Principles,
- (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 Loan 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 Loan Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following observations are made.

- (a) Value Added Tax aggregating Rs. 583.47 million paid up to 31 December 2015 had been set off against the proceeds of the contribution received from the Government of Sri Lanka.
- (b) Interest and commitment charges amounting to Rs. 55.78 million and Rs. 24.50 million respectively recovered by the Lending Agency up to 31 December 2015 had not been brought to account.

2.2.3 Un-reconciled Balances

The following observations are made.

- (a) A sum of Rs. 4,177.97 million claimed during the year under review from the Lending Agency through the withdrawal applications and shown in the financial statements of the Project was not agreed with the value of claims aggregating Rs. 5,181.71 million made as at 31 December 2015, as per records maintained by the Department of External Resources.
- (b) As per the financial statements of the National Water Supply and Drainage Board, the work-in-progress of the activities carried out by the Project as at 31 December 2015 amounted to Rs. 4,835.22 million. However, according to the financial statements of the Project, the corresponding amount was shown as Rs. 4,740.22 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 upto 31 December 2015 are shown below.

Source of Fund	Amount agreed for financing in the Loan Agreement		Allocation made in the Budget Estimate for the year under review	<u>Fund Utilized</u>	
				during the year under review	as at 31 December 2015
	JPY million	Rs. million	Rs. million	Rs. million	Rs. million
JICA	4,904	6,239	850.00	876.76	4,177.97
GOSL	1,150	1,464	198.59	46.34	563.67
Total	<u>6,054</u>	<u>7,703</u>	<u>1,048.59</u>	<u>923.10</u>	<u>4,741.64</u>

3.2 Physical Progress

According to the progress reports, the activities carried out by the Project had been substantially completed at the end of the year under review. However, pipe laying works under the Panama Water Supply Scheme in Ampara district had not been completed even as at 31 December 2016.

3.3 Issues on Financial Control

The following observations are made.

- (a) The transactions of the Project during the year under review were not subjected to audit of the Internal Audit Section of the National Water Supply and Drainage Board as required by the Financial Regulation 133 and Management Audit Circular No. 05 of 26 July 2010 of the Department of Management Service.
- (b) As per the financial statements of the Project, the proceeds of the loans received from Lending Agency amounting Rs. 4,177.97 million had been segregated and shown in the financial statements as a Loan of Rs. 1,099.77 million and a Grant of Rs. 3,078.2 million. However, no subsidiary Loan Agreement had been entered into thereon even 31 December 2017.
- (c) According to the Financial Regulation 626, the financial statements of the Projects are required to be prepared based on separate accounting records maintained in accordance with generally accepted accounting principles. However, a single cash book to record the receipt and payments of all donor funded project implemented by the National Water Supply and Drainage Board had been maintained.
- (d) The Register of Fixed Assets had not been maintained by the Project in updated manner, as required by the Circular No. 842 of 19 December 1978 of the Ministry of Finance and Planning.