

Supporting Electricity Supply Reliability Improvement Project 2019

The audit of financial statements of the Supporting Electricity Supply Reliability Improvement Project for the year ended 31 December 2019 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 into 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 Grant Agreement of the Project, then Ministry of City Planning and Water Supply, presently the Ministry of Urban Development, Water Supply and Housing Facilities 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\$ 1.26 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 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 2019 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.

In preparing the financial statements, management is responsible for assessing the Project's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Project or to cease operations, or has no realistic alternative but to do so.

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

The Project is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared by the Project.

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	Impacts	Responses of the Management	Auditor's Recommendations
		Rs. million			
(a)	Mobilization advance amounting to Rs. 12.09 million recovered from Interim Payment Certificate No.6 had not been brought to the financial statements during the year under review.	12.09	Understatement of work-in-progress and overstated of mobilization advance.	The Project paid a sum of LKR 14,928,863.23 as mobilization advance for United Tractor & Equipment (Pvt) Ltd for Supply & Installation of two 75m ³ / Day Sea Water Reverse Osmosis Plants & Related Civil Works Including Improvement of Nainathivu Water Supply System in December 2018. Of which, the project recovered amounting to LKR 12,090,149.41 from IPC 06 in Feb 2020 and balance LKR 2,838,713.82 recovered from IPC07 in Apr 2020, these recovery transactions will be presented in the project's financial statements for the year ended 31 Dec2020.	Immediate action should be taken to account the recovery at the time of recovery.
(b)	Exchange gain amounting to Rs.1.9 million had been erroneously shown under the current liabilities instead of being shown	1.9	Understatement of exchange gain and overstated of current liabilities	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-2019 was shown under current assets in statement of financial position according to Accounting Standards. The year-end closing balance of 31-Dec-2019 was consists of	Exchange gain should be shown as separate item under the sources of financed in the financial statements.

	as separate item under the sources of finance.			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	
(c)	Value of civil works, consultancy services and project administration expenses aggregating to Rs.112.28 million had been erroneously shown under the non-current assets instead of being shown as work-in-progress.	112.28	Understatement of work in progress and overstated of non-current assets.	As per the ADB Grant Agreement JFPR-9186-SRI and Project Administration Manual (PAM), the project's non-current assets are categorized into Civil Works, Consulting Service, Equipment and Project Administration. The project's capital expenditures up to 31-Dec-2019 were shown in the financial statements accordingly. In fact, these non-current expenses are working in progress until capitalization. After capitalization by the project/NWSDB, these non-current expenses will be shown as capitalized expenditures in the respective financial statements.	Action should be taken to shown under the work- in -progress in the financial statements.
(d)	The difference of Rs.78.48 million had been observed between the value of work-in-progress shown in the financial statements as at 31 December 2019 and the corresponding value shown in the financial statements of the National Water Supply and Drainage Board.	78.48	Differences in work- in -progress shown in the Project accounts and financial statements of the NWSDB.	The project will take prompt actions to tally the project's work-in-progress value with financial statements of NWSDB.	Prompt action should be taken to reconcile the balances.

3. Physical Performance

3.1 Physical Progress

	Project Components	As at 31December 2019		Impacts	Responses of the Management	Auditor's Recommendations
		Expected (%)	Achieved (%)			
(a)	Supply and installation of the two no's of 75 m3/day sea water reverse osmosis plant with related civil works.	100	63	Possibility of extending the contract period.	Installation of the plant is completed. Commissioning of the plant to be performed by the contractor for the acceptance of the system	Prompt action should be taken to commissioning the plant.
(b)	Supply and installation of 2-ton ice making factory and refrigeration system.	Tendering and awarding of the contract scheduled to be commenced at the end of 4 th quarter of 2019.	–	Delay in commencement of the contract.	Preparation of bid document is in progress. However, Operation of the Ice plant is depending on the Electricity supply available from CEB's hybrid power system project to Nainathivu Island Hence "Tender calling" for Ice making Plant will be feasible when CEB project is completed.	Discussion should be made with the Ceylon Electricity Board (CEB) to expedite the completion of hybrid power system project in order to make power supply for Ice Making Factory of the Project.

3.2 Contract Administration

Audit Issues	Impacts	Responses of the Management	Auditor's Recommendations
(a) According to the progress report of the Project, the overall physical and financial progress of the Project at the end of the year under review remained at 63 per cent and 23.86 per cent respectively. The activities of the Project consisted of two components, out of that tendering and awarding of supply and installation of ice making factory and refrigeration system contract was scheduled to be completed between fourth quarter ending 2019 and the beginning of second quarter 2020. However, invitation to the bidders had not been called even up to 31 May 2020.	Possibility of delay in commencement of the contract.	Operation of the Ice plant is depending on the Electricity supply available and it is expected from CEB's hybrid power system project to Nainathivu Island which is not commenced yet. Therefore "Tender calling" for Ice making Plant will be feasible when CEB project is completed.	Discussion should be made with the Ceylon Electricity Board (CEB) to expedite the completion of hybrid power system project in order to make power supply for Ice Making Factory of the Project.
(b) The written approval should have been obtained from the Coastal Conservation Department (CCD) for land clearance of the construction of intake wells. However, it had not been obtained even up to 31 May 2020. Further, as per the progress report furnished to the audit, out of three intakes wells two intake wells had been completed by 31 May 2020 without being obtained written approval in terms of section (14) (1) of the part III of	Non-compliance with legal requirements.	Application was submitted on 22-09-2017 to CCD for the approval. Subsequently, the CCD had visited the site on the following week. Then a payment was made on 28-12-2018 to process the approvals. Later in the NSC meeting held on 15-10-2019, the Department of Coast Conservation (CCD) granted approval to proceed the civil works and construction and the works were completed accordingly. PMU has been	Action should be taken to comply with legal requirements.

Coastal Conservation Department (CCD) Act, No. 57 of 1981 for land clearance of the construction.

following up with CCD Head office to get the written approval. NSC meeting minutes attached herewith. (Refer annexure 02)

3.3 System and Controls

Audit Issue -----	Impact -----	Responses of the Management -----	Auditor's Recommendations -----
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.	Non-compliance with the Circular requirement.	Internal Audit Division for NWSDB planned before March 2020 to visit for auditing Jaffna-Kilinochchi Water Supply & Sanitation Project (JKWSSP) and Supporting Electricity Reliability Improvement Project (SESRIP). Due to COVID-19, the Internal Auditors were unable visit as per their plan. However, by sharing this audit opinion with them, it is believed that they will audit and submit report as soon as possible.	Action should be taken to comply with the requirements of the circular instruction.