

## **Health System Enhancement Project -2020**

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The audit of financial statements of the Health System Enhancement 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 Loan Agreement No.3727 SRI (COL) dated 26 October 2018 and the Grant Agreement No.0618 - SRI (SF) dated 26 October 2018 entered into between the Democratic Socialist Republic of Sri Lanka and the 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**

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According to the Loan and Grant Agreement of the Project, the Ministry of Health is the Executing and four provincial councils of Central, North Central, Sabaragamuwa and Uva provinces are the Implementing Agencies of the Project. The Project will improve efficiency, equity and responsiveness of the primary health care system based on the concept of providing universal access and continuum of care to quality essential health services. As per Loan and Grant Agreements, US\$ 37.5 million equivalent to Rs.5,813 million as concessional loan and US\$ 12.5 million grant equivalent to Rs.1,938 million respectively totalling US\$ 50 million equivalent Rs.7,751 million had been agreed to be provided by the Asian Development Bank. The Project commenced its activities on 01 December 2018 and scheduled to be completed by 30 November 2023.

### **1.3 Opinion**

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In my opinion, 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 Opinion**

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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**

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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**

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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. Physical Performance**

**2.1 Physical progress of the activities of the Project**

Component	Activity	As at 31 December 2020		Delay/ Audit Issue	Reasons for delays
		Expected physical performance Percentage	Performance achieved percentage		
W-3, 4,5,8& 9	Building constructions of the five divisional hospitals and six primary medical care units.	100	0	Problems in not completing the constructions in the expected time.	<p>(i) Deficiencies in construction drawing, BOQs and the problems faced in the site condition during project preparation.</p> <p>(ii) Non availability of sufficient construction materials and manpower due to the pandemic situation.</p> <p>(iii) Contractors had to stop work due to treatment of Covid infected patients in these centers.</p> <p>(iv) Most of these constructions are taking place in functional hospitals therefore; contractors have to design their work causing minimum work interference to the hospital function.</p>

**Response of the Management**

That these delays have occurred due to the facts stated.

**Auditor's Recommendations**

Action should be taken to achieve the desired progress.

## 2.2 Contract Administration

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Audit Issue	Response of the Management	Auditor's Recommendation
(a) Although the construction of Dolosbage Divisional Hospital Project had been halted due to inconsistencies in the selected land, the mobilization advance of Rs.5.71 million paid to the contractor had not been recovered.	Construction of Dolosbage Divisional hospital, advance payment has not been recovered due to scope change of the sub project was proposed by the Provincial Health Department. Therefore, possible continuation was under consideration. By the time the difficulties of the terrain identified for the proposed construction contractor has been some preliminary work and there was a cost for that which was under review.	This issue must be resolved expeditiously so that the government does not have to incur a loss.
(b) According to the contract agreement for the improvement of the Ambagaswewa Primary Medical Care Unit, its work should have been completed before July 15, 2020, but it had not been completed by February 1, 2021. Also, Rs.2.36 million had been paid for tiling and fixing the ceiling, but these two subjects had not been carried out to the required standard.	The performance bond has been extended in 3 occasions up to 09 June 2021 and advance has been fully recovered during the extended period.	Necessary steps should be taken to complete the project on time with the expected quality.
(c) According to the contract agreement for the improvement of the Thittagonewa Primary Medical Care Unit building in the Anuradhapura District, the project had scheduled to be completed by August 2020 but had not been completed by May 31, 2021 and employee insurance had not been obtained.	Advance and performance bonds have been extended up to 02 June 2021 and 28 May 2021 respectively.	Necessary steps should be taken to complete the project on time and should be obtained necessary insurance.
(d) The project to renovate the Horowpathana Regional Hospital building had scheduled to be completed by August 15, 2020, but had not been completed by May 31, 2021. Further, the subject of work No.33 had not been performed according to the required standard.	Performance bond has been extended up to 07 August 2021. Insurance policy document has been obtained.	Necessary steps should be taken to complete the project on time with the expected quality.

## 2.3 System and Controls

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Audit Issue	Response of the Management	Auditor's Recommendation
(a) Out of the total loan of US\$ 37.5 million as at 31 December 2020, only US\$ 13.64 million had been disbursed which was only 36.37 per cent of the total loan. As a result, at the end of the year under review Rs.34,435,738 had to be paid as commitment charges on the unused balance.	The ADB had charged the commitment changes as agreed in the loan agreement directly debiting the loan account same have recognized as borrowing cost in the project financial statement.	Action should be taken to achieve the desired progress and mitigate the commitment charges.
(b) As the bids received for the procurement of 07 double cabs and 09 vans had been withdrawn, the two bids bond amounting to Rs.2.95 million had been cashed. But Rs.1.66 million had been returned to the supplier without any reasons or authority.	Supplier has withdrawn the bids submitted for both 7 double cabs and 9 vans during the bid validity period. Based on that we have immediately forfeited relevant bid bonds amounting to LKR 2,950,000. Subsequently bidder has agreed to extend the validity of bid for 9 vans. By that time letters of intention for award were not sent to the bidders and none of bidders were aware about the tender decision. Further, bidder has stated that their inability to supply 7 double cabs due to discontinuation of the production of the particular model. We have refunded the value of the bond pertaining to the bid for 9 vans.	This amount should be recovered from the responsible parties.
(c) Good Issuing Notes had not been issued for goods purchased for a total cost of Rs.226,512,562 and distributed on 84 occasions during the year under review. Also, a Goods Received Note had not been brought from the relevant divisions or institutions to ensure that the goods were recorded in the inventory books.	Necessary actions have been taken to streamline the inventory system as per the government guidelines.	Good Issuing Notes and Goods Received Notes should be issued as per Financial Regulations.
(d) As the lease agreement for the building rented for the project office included the terms of the advance payment, it should be done in consultation with Attorney-General. But the matter had not been consulted with the Attorney General.	This requirement will be complied in the renewal of the lease agreements entered for the office premises	Should be complied with Financial Regulations.

- (e) Rs.808,027 value added tax has been paid on 07 occasions to 04 contractors who did not submit a tax invoice. Furthermore, to an unregistered supplier of the Inland Revenue Department for collection of value added tax on the sale of medical equipment the total amount of Rs.1,590,832 had been paid as value added tax on the sale of medical equipment on two occasions during the year under review.
- When there are supplies liable for Value Added Tax (VAT), the project inspects and verifies the VAT registration details at the procurement stage (before award the contract with taxes) as well as the payment stage accordingly.
- Value added tax should be paid as per the act.
- (f) The maximum financial limit for project directors to be approved at one time is Rs.2,000,000. However, it was observed that the project director had approved payments on 12 occasions exceeding that limit during the year under review.
- These payments had to be approved by the Project director as they had mistakenly considered that the authority limit of the Regional Procurement Committee could be applied in approving the vouchers.
- Should be complied to the circular.