

Local Government Enhancement Sector Project (Pura Neguma) – 2022

The audit of financial statements of the Local Government Enhancement Sector Project (Pura Neguma) 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 Article IV of the Loan Agreement No. 2790-SRI(SF) dated 21 October 2011 and 3431 – SRI(SF) dated 02 November 2016 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

According to the Loan Agreement of the Project, then Ministry of Provincial Councils and Local Government, presently Ministry of Public Administration, Home affairs, Provincial Councils and Local Government is the Executing Agency and Provincial Councils of 07 Provinces are the Implementation Agencies of the Project. The objectives of the Project are to achieve improved Local Government Infrastructure Activates of the Project and effective delivery of services through accountable and financially and technically strengthened local authorities. The objective of the subsequent loans of the project is to improve the infrastructure and services delivered by the Local Authorities and National Water Supply and Drainage Board in less-developed areas of 07 Provinces in Sri Lanka which affected by chronic diseases. Therefore, the issues relating to the improvement of water supply systems, infrastructure basic service delivery local government policy reforms and strengthening capacities are expected to be addressed. As per the Loan Agreement 2790 SRI (SF), the estimated total cost of the Project was US\$ 68.8 million equivalent to Rs.8,940 million and out of that US\$ 59 million equivalent to Rs7,670 million was agreed to be financed by Asian Development Bank. The balance of the estimated cost US\$ 9.8 million equivalent to Rs.1,339.33 million contributed by Government of Sri Lanka. As per the subsequent loan agreement No.3431 SRI (SF) additional loan of US\$ 60 million equivalent to Rs.8,700 million was obtained in the year 2017 to scale up well performance of the original project. The estimated total project cost is US\$ 67.8 million equivalent to Rs.9,771.47 million with US\$ 7.8 million equivalent to 1,071.47 contribution of Government of Sri Lanka. The Project had commenced its activities on 01 July 2012 and scheduled to be completed by 30 June 2015. However, the date of completion of the activities of the Project had been extended up to 30 September 2023.

1.3 Opinion

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2022, statement of expenditure 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.

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 Non-Compliance with Laws, Rules and Regulations

| No | Reference to the Laws Rules and Regulations | Non-Compliance | Response of the Management | Auditor's Recommendation |
|-----|--|---|----------------------------|---|
| (a) | Paragraph 9.3 of Management Service Circular No 1/2019 of 15 March 2019. | The Meetings of the Project Steering Committee required to be held once in 02 months. However, only 03 meetings had been held during the year under review. | No Comments | The meetings of the Project Steering Committee required to be held as per the Circular Instruction. |
| (b) | Department of Management Audit Circular No 01/2019 of 12 January 2019 | The Meeting of the Audit and Management Committees required to be held four in the year. However, two meetings had been held during the year under review. | No Comments | The meetings of the Audit and Management Committees required to be held regularly. |

3. Physical Performance
3.1 Physical progress of the activities of the Project

According to the Project Implementation Plans, the Project had supported to 105 Local Authorities in 07 Provinces to enhance their infrastructural requirements and respective development works of 178 Local Authorities had been completed at the end of year 2017. Further, it was scheduled to carry out 29 water supply projects, 35 construction works in 29 Local Authorities under the supplementary loan facilities. Out of 29 water supply projects 19 projects had been completed during the previous year however there was a delay of 8-24 months in the completion of 10 projects. Out of 35 Civil works 33 infrastructure projects were completed at the end of the year under review, however in which 8 constructions were with a time delay of 3-31 months

3.2 Activities of the project not commenced

Although the following sub projects had to be commenced before April 2017, those sub projects had not been commenced up to 30 June 2022.

| Nos | Activities | Date scheduled to be commenced | Estimated Value Rs. Million | Responses of the Management | Auditor's Recommendations |
|-----|---|--------------------------------|-----------------------------|--|---|
| (a) | Water supply scheme for Thanamalvila and Hambegamuwa distribution system | 2017 April | 1,270 | Considering the additional cost and issues in environmental studies, it was decided not to implement this sub project. | Sub project should be commenced as soon as possible or work schedules in Project Administration Manual should be revised. |
| (b) | Water Treatment plant for Thanamalvila and Hambegamuwa Scheme | 2017 April | 430 | | |
| (c) | Construction of Borehole pump house chlorinators – Central Province (Three numbers) | -Do- | 60 | | |
| (d) | Intake tank for Thanamalvila and Hambegamuwa scheme | -Do- | 100 | Considering the additional cost and issues in environmental studies, it was decided not to implement this sub project. | -Do- |
| (e) | Construction of PS Building at Kotagala | -Do- | 50 | Dropped due to land issue as advised by National Steering Committee. | -Do- |
| (f) | Construction of PS Building at Argarapathana | | | | |

3.3 Idle/ Unutilized/ Underutilized Resources

(a). Front Office System and e-Puraneguma Software

| Audit Issue | Response of the Management | Auditor's Recommendation |
|---|--|---|
| (i) The IT solution has been implemented known as "Front Office System" providing with hardware for 137 Pradeshiya Sabhas by the project. It was observed that the intended objective could not achieve, due to non-availability of back office system in order to support to newly introduced Front Office System. It was further revealed that out of 41 Local Government Institutions in Central Province and North Central Province, 17 Pradeshiya Sabhas have not practiced totally the above system and 16 Pradeshiya Sabhas have purchased new alternative software without implementing above system. | Front office system is a simple solution developed for the low income Pradeshiya Sabhas as an entry level to IT interventions. Regarding not practicing fully all the modules, please note that some Pradeshiya Sabhas are not charging assessment tax and this system is not functional in such Pradeshiya Sabhas. Further please note that project has no authority of preventing Pradeshiya Sabhas from acquiring any other system as the decisions have been taken from the relevant pradeshiya Sabhas or provincial councils. | Actions should be taken to correct weakness of software and use the assets and software for intended purpose. |
| (ii) Even though the e-Puranaguma software had been introduced to all the Local Government Authorities by the Department of Local Government of North-West Province, it is not currently being operated in any Local Government Authority in the North-West Province. The e-Puraneguma software had been inactive for two years in Ridigama local authority, where the e-Puraneguma software had been installed. due to non-intervention by the Puraneguma project to solve the issues arising during its implementation | It was decided in the National Steering Committee discussion held on 17.09.2020 that no intervention of the project staff can be made after 28.02.2021 regarding the work related to the front office and e-puranaguma as the Puranaguma project is scheduled to be completed in the year 2021. | A programme should be launched to prevent the expenditure incurred from becoming idle. |

(b). Asset Management Software

| Audit Issue | Response of the Management | Auditor's Recommendation |
|--|---|---|
| <p>(i) A Sub Project was implemented for seven Pradeshiya Sabhas in seven provinces under a contract agreement signed on 15th December 2018 with an Australian private company. The objective of this sub project is to create Assets Management Software as a Pilot Project. It was observed that foreign private company was selected for this contract without procurement practices required by the National Procurement Agency Circular No.08 and dated on 25 January 2006. It was further revealed that there was no provision in the above agreement for support and maintenance system of the above software. Further, no feasibility study was done by studying existing rules and manuals in the Local Government sector in Sri Lanka. As per the work plan in the above agreement, the activities installation and “Develop Training Material and complete staff training” has not been completed as planned as at 31 December 2019.</p> | <p>Based on ADB's advice, the PMU and the Ministry had followed the CQS method for this procurement and to provide opportunity to other similar firms (if any). Hence, no lapse in the process of the procurement.</p> | <p>The project is required to make influences to contractor to complete the work promptly assuring required quality.</p> |
| <p>(ii) During the audit of 05 out of 07 local government authorities, where the software was installed, only the data of the assets entered at the time of installation of the software was available in the database system of the software and that data had not been updated. Furthermore, it was observed that any information ,from which the decisions can be made for asset management using that data, cannot be prepared and made available to the user through this software, and that Excel Sheets are used by the local government authorities to fulfill their needs without using the software. Therefore, it was observed that useless software had been installed at a cost of US \$133,747.70.</p> | <p>The primary role of the project was to enter the existing complete data of local authorities into this system and provide all the training related to handling the software. Accordingly, it is the responsibility of the council to keep it up-to-date as all necessary training has been provided.</p> | <p>A continuous process such as training of officers should be carried out to make improvements during the project schedule and thereafter to solve the technical problems.</p> |

(c). **Water supply projects**

| Audit Issue | Response of the Management | Auditor's Recommendation |
|--|---|--|
| Non-availability of water supply facilities, non-availability of access road, non-compliance of building design, lack of public demand for a crematorium, feasibility studies not being carried out, ground level not being considered in the construction of water tanks, impact of Covid-19 epidemic, insufficient capacity of water treatment plants, and due to lack of proper planning for utilization of auditorium/community hall Rs. 3,809 million were spent on 33 projects that had been started and stopped midway. | Due to various reasons the project could not be completed | The project should be completed to get the benefits for the general public |

3.4 Matters in Contentious Nature

| Audit Issues | Responses of the Management | Auditor's Recommendations |
|---|---|---|
| An Engineer had been selected as an Individual Consultant for Technical Audit for one year. Then his period had been extended up to November 2019. According to the agreement signed by Secretary of the Ministry and Technical Audit Consultant, the audit had to be carried out accordance with the terms of reference and guidelines provided by the Ministry of Provincial Councils Local Government from time to time and had to include specific section on various objectives tasks as define under the terms of reference. Although the Technical Audit Consultant should record key issues and recommendations in the final report; the report had not contained any key issues and recommendations. | Technical Audit Consultant assisted to the Project Management Unit for undertaking procurement of contract. | The project is required to take actions to recover the payment. |

3.5 Systems and Controls

| Audit Issue | Management Response | Auditor's Recommendations |
|---|----------------------------|--|
| Internal Audit Division of the executing ministry had been expanded to cover the project internal audit. However sufficient internal audit had not been done within the year. | No comments | Internal audit should be functioned properly |