

**MAHAWELI WATER SECURITY INVESTMENT PROGRAM**

**FINANCIAL MANAGEMENT ASSESSMENT**

**OF**

**MINISTRY OF MAHAWELI DEVELOPMENT AND ENVIRONMENT  
MAHAWELI AUTHORITY OF SRI LANKA  
DEPARTMENT OF IRRIGATION**

**JUNE 2015**

## ABBREVIATIONS

ADB	–	Asian Development Bank
ADBS	–	Asian Development Bank Specific
AG	–	Auditor General
CAGR	–	Compounded Annual Growth Rate, %
CEO	–	Chief Executive Officer
CFO	–	Chief Financial Officer
CIA	–	Chief Internal Auditor
CIGAS	–	Computerized Integrated Government Accounting System
DG	–	Director General
DGI	–	Director General of Irrigation
DOI	–	Department of Irrigation
EA	–	Executing Agency
GIS	–	Geographic Information Systems
GOSL	–	Government of Sri Lanka
HA	–	Hectare (1ha = 10,000sqm)
IA	–	Implementing Agency
KPIs	–	Key Performance Indicators
MASL	–	Mahaweli Authority of Sri Lanka
MCM	–	Million Cubic Meters (1 MCM = 811 Acre feet)
MDP	–	Mahaweli Development Program
MFF	–	Multi-tranche Financing Facility
MMDE	–	Ministry of Mahaweli Development and Environment
MOI	–	Ministry of Irrigation
O&M	–	Operating and Maintenance
PPTA	–	Project Preparatory Technical Assistance
SLRs	–	Sri Lankan Rupees
TA	–	Technical Assistance

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## I. EXECUTIVE SUMMARY

1. The Mahaweli Water Security Investment Program (“investment program”) will assist the government to complete outstanding water conveyance investments under the Mahaweli Ganga Development Program (MDP). Completion of the MDP will maximize the productivity of the Mahaweli River Basin’s water resources by transferring available water to the country’s northern dry zone areas for irrigation, drinking and commercial purposes. The investment program will be financed under a \$675 million multi-tranche financing facility (MFF). The investment program is designed to be implemented over 10 years from 2015 to 2024. The executing agency for the program will be the Ministry of Mahaweli Development and Environment (MMDE). The Mahaweli Authority of Sri Lanka (MASL), a sub-agency of MMDE, and the Department of Irrigation (DOI), under the Ministry of Irrigation (MOI), will second staff to the investment program’s Program Management Unit (PMU) and Project Implementing Units (PIUs) under MMDE.

2. A financial management assessment (FMA) of MMDE, MASL and DOI were conducted from August 2014 to October 2014 in accordance with ADB’s Guidelines for the *Financial Management and Analysis of Projects* and Financial Due Diligence: a Methodology Note.<sup>1</sup> The FMA considered the capacity of MMDE, MASL and DOI in terms of their fund-flow arrangements, staffing, accounting and financial reporting systems, financial information systems, internal controls and internal and external auditing arrangements. The FMA has carried out by desk review of existing assessments; in particular the Governance Risk Assessment under the latest Country Partnership Strategy for Sri Lanka,<sup>2</sup> the World Bank Implementation Completion Report for the Mahaweli Restructuring and Rehabilitation Project,<sup>3</sup> the ADB-financed Water Resources Management Project Completion Report,<sup>4</sup> for as well as interviews conducted with key MMDE, MASL and DOI staff.

3. MMDE is structured to guide MASL (and previously DOI) by exercising supervision and progress control of programs and projects. These include projects that are geared to enhance the productivity in existing systems and new projects to serve all regions of the country including new frontiers contemplated under the MDP such as the investment program. MMDE has extensive past experience in executing large foreign-financed projects and currently has an on-going portfolio of development projects under its purview.

4. MASL operates under MMDE but as a separate institution. MASL is the cornerstone of the MDP which relates to regulating and harnessing the waters of Mahaweli River for power generation, land settlement and food production and thereby the provision of employment. MASL has already completed an array of large hydropower and water resource development initiatives and its past experience will serve well for successful implementation of the investment program. It is also responsible to operating and maintaining the existing MDP infrastructure. MMDE together with the MASL has a budget allocation of over \$300 million for 2014, which reflects the combined magnitude of strength of the two organizations and their scale of technical and administrative expertise.

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<sup>1</sup> During the FMA, MMDE was called “Ministry of Irrigation and Water Resources Management” and DOI was under this ministry. Following the change in government in January 2015, the ministry was renamed to MMDE and MOI was moved under the new Ministry of Irrigation. This report has been updated to reflect these changes.

<sup>2</sup> ADB. 2011. *Country Partnership Strategy: Sri Lanka, 2012-2016*. Manila. Governance and Public Management in Sri Lanka [http://www.adb.org/sites/default/files/linked-documents/cps-sri-2012-2016-oth-04\\_0.pdf](http://www.adb.org/sites/default/files/linked-documents/cps-sri-2012-2016-oth-04_0.pdf) and Summary Risk Assessment and Risk Management Plan

<sup>3</sup> World Bank. 2004. *Implementation Completion Report (TF-26603 IDA-30580 PPFI-Q0070) for Mahaweli Restructuring and Rehabilitation Project*. Washington D.C.

<sup>4</sup> ADB, 2007. *Completion Report: Sri Lanka: Water Resources Management Project*. Manila

5. **Strengths.** Until January 2015, DOI was also under MMDE (now under MOI) but it functioned as an independent department with separate budget accounts. It has been playing a key role in the irrigation sector of the country for over 100 years and has responsibility for some of the nation's main irrigation systems. It is well staffed and has suitable reporting and organizational structures in place to implement, operate and maintain investments such as the investment program. DOI's 2014 budget was about \$100 million. DOI also has considerable past experience in implementing major irrigation systems and schemes funded both locally as well as by development partners. Although accounts are not maintained on a full accrual basis, regular and reliable financial accounting is performed on the modified cash basis, the accounting system prevailing in Sri Lanka. Annual appropriation accounts are audited by the Auditor General's Office, and prior years audited accounts do not indicate any significant irregularities. A functional Internal Audit unit is also in place. MMDE, MASL and DOI, therefore appear to have sufficient financial management capacity and expertise to implement, operate and maintain the planned investment program.

6. Despite the above, due to factors summarized below, the projects overall pre-mitigation financial management risk is rated as 'Substantial'. With the proposed risk mitigating measures the financial management arrangements are considered adequate and the risk acceptable.

7. Despite capacities and capabilities of MMDE, MASL and DOI, there are a few limiting areas which require improvements:

- (i) ADB has not engaged with the MMDE, nor funded any MMDE projects for more than 10 years. The investment program will therefore be the first ADB-support program MMDE, MASL and DOI will be executing and implementing which therefore require a comprehensive procedure manual along with training of central and regional financial management staff, on ADB's policies, procedures and guidelines. Capacity building and training through workshops are therefore required prior to implementation of the investment program – **Responsibility with investment program implementation consultants.**
- (ii) There have been instances where the Treasury re-prioritized projects during the fiscal year resulting in some non-disbursements and delays. A firm commitment from the Treasury is therefore required to prioritize the investment program to ensure timely fund disbursements – **Responsibility with ADB to obtain assurance from Treasury on behalf of MMDE.**
- (iii) In line with country systems, most government departments that report to the Treasury, including MMDE, do not yet prepare a full set of financial statements including a balance sheet, profit and loss account and a cash flow statement. An appropriation account is prepared on a modified cash basis. The government is already addressing this on a countrywide basis under an accounting reform roadmap. MMDE shall also be requested to incorporate details of the investment program in separate notes to their appropriation account. – **Responsibility with MMDE to comply with ADB requirements and implement new accounting system once introduced by the government.**
- (iv) Even though MMDE prepare Corporate Plans, these are not detailed and therefore limit the usefulness of the document. In addition, these plans are not updated regularly. MASL's 5 year Corporate Plan is satisfactory albeit there is room for

improvement. It is therefore recommended that comprehensive 5-year Corporate Plans be developed by MMDE and these are updated periodically on an annual basis which will also improve accuracy of estimates. An initial 5-year Corporate Plan for MMDE should be formulated through extensive participation of staff in the form of workshops – **Responsibility with MMDE under ADB guidance recommended.**

- (v) Review and update key performance indicators (KPIs) of MMDE to enable effective monitoring of physical progress of project linked with financial targets. It is recommended to introduce a new KPI system using ADB's best practices and guidance. KPIs are also recommended for regular monthly monitoring in Appropriation Accounts. KPIs should be developed with participation of staff through workshops - **Responsibility with MMDE under ADB guidance.**
- (vi) Explore the possibility of making MASL a separate cost center under the Treasury. This is enable effective budgetary monitoring as well as assist MASL seek direct Treasury assistance for urgent matters – Responsibility with ADB.

8. The World Bank Implementation Completion Report (ICR)<sup>5</sup> for the Mahaweli Restructuring and Rehabilitation indicates that the overall sustainability of their project is unlikely. However, this was focused more on the completion of the reform process, which had ambitious organizational restructuring objectives. With respect to the physical infrastructure, the ICR highlighted significant savings in O&M costs, which would contribute to the future sustainability of the project assets. The project was implemented during a difficult time for Sri Lanka, with the ethnic conflict in the early years of the project prior to February 2002, and the political uncertainties associated with Presidential and Parliamentary Elections. Accordingly, we consider that the above factors will not unduly affect the sustainability of the proposed ADB funded program.

9.

## II. INSTITUTIONAL OVERVIEW

### A. Ministry of Mahaweli Development and Environment

9. MMDE is committed to manage the irrigation sector and the water resources of the country, maintaining the equilibrium between the trends in rapid economic development and sustainable use of water resource base. It gains from the support of the implementation agencies under the Ministry, which are manned by competent technical personnel experienced and trained in their respective disciplines.

10. MMDE's vision statement is *"prosperous Sri Lanka through water and irrigation heritage"* and its mission statement is *"providing well-being of community while fulfilling all water needs through water resources management."*

11. The main functions of MMDE include:

- Formulation of policies and implementation of projects and programs
- Promotion, construction, operation, maintenance and management of irrigation systems, rain water harvesting and ground water development
- Salt water exclusion programs
- Drainage and flood protection

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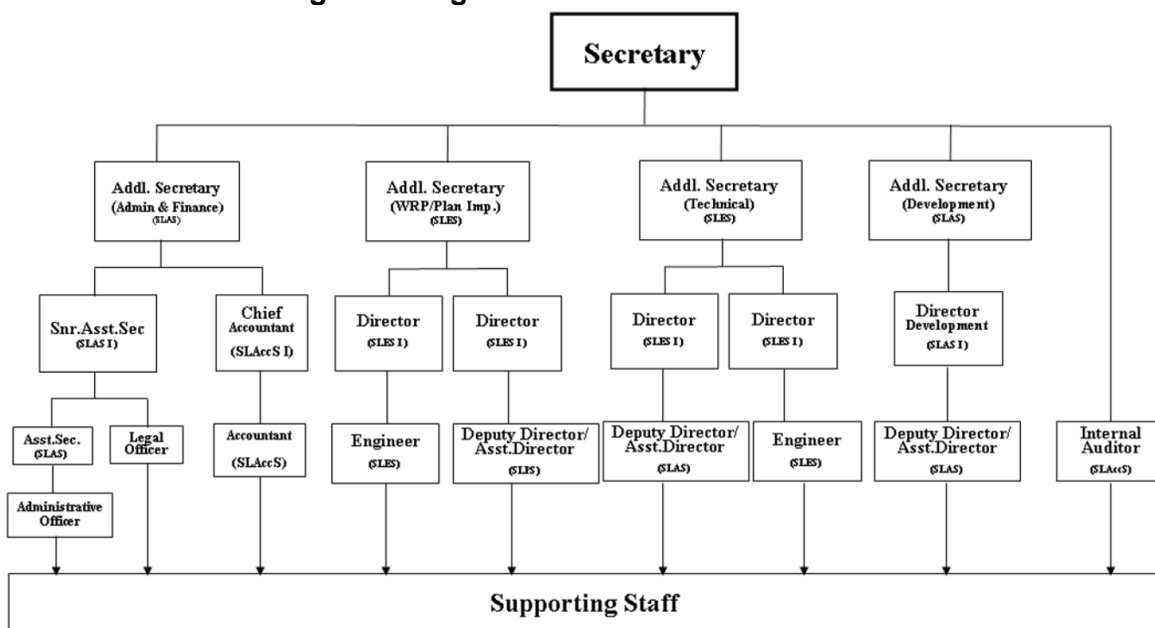
<sup>5</sup> See footnote 3.

- Prevention of the pollution of rivers, streams, reservoirs and other water bodies
- Engineering consultancy services and construction
- Implementation of legislative enactments relevant to the subjects and Institutions under the Ministry
- Matters relating to Mahaweli development

12. MMDE has seventeen institutions under its purview including MASL. The Treasury has allocated expenditure appropriation head number “152” to MMDE and number “282” to DOI.

13. MMDE’s head office is located at 500, T.B. Jayah Mawatha, Colombo 10. The Secretary to the Minister heads the operations of the Ministry. As shown below, four Additional Secretaries in the fields of administration and finance, water resource planning and implementation, technical, and development report to the Secretary.

**Figure 1: Organizational Structure of MMDE**

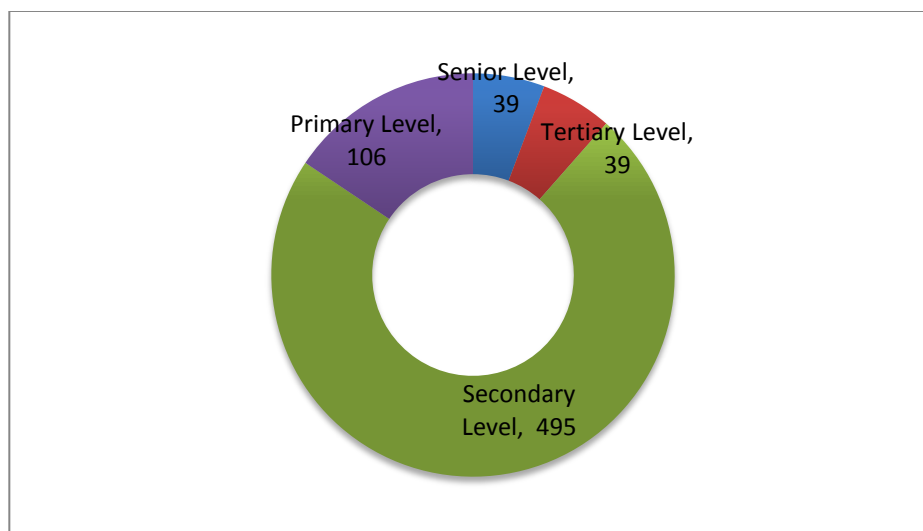


Source: MMDE

14. In 2014 MMDE has a direct work force of 675. However, in 2013, MMDE’s staff base was only 295. Accordingly, estimated work force in 2014 represents over 133% year-on-year increase. The main area of this increase is at secondary grade level employees. As shown below, secondary level employees now represent around 30% of the cadre base. 14% are employed at senior level and 17% are at tertiary level. Remaining 39% of MMDE’s direct staff base is made up of primary, casual and contract employees.

**Figure 2: Employee Grade Levels of MMDE (2014)**





Source: MMDE

## B. Mahaweli Authority of Sri Lanka

15. MASL was established in 1979 by way of a Parliament Act with a mandate to implement the MDP. After successfully completing several large-scale reservoir projects with hydroelectricity plants accompanying large extents of irrigable land such as the Victoria dam project, Randenigala, Rantambe, Kothmale, Polgolla and Bowatanne, MASL is presently planning to develop the balance area proposed by the MDP Master Plan. In addition, MASL carries out the maintenance and rehabilitation of irrigation network, land administration, increasing agricultural production and post-settlement activities. Further, MASL is responsible for managing irrigation water for over 175,000 ha of irrigable land in the dry zone at present.

16. The Master Plan of the MDP envisages storing 7,400 MCM (6 million acre-feet) of water in 15 reservoirs on the Mahaweli and its tributaries and Maduru Oya Basin. About 60% of water resources available in the Mahaweli Basin is used within the basin and the balance to be diverted to the water shortage areas in the dry zone. The regional boundaries of the project fall within the basins of the Mahaweli, Kalaoya, Malwathu and Yan Oya and the Maduruoya. The MDP project area spreads over 13 administrative districts and covers about 39% of the land area in the country and of 55% of the dry zone area.

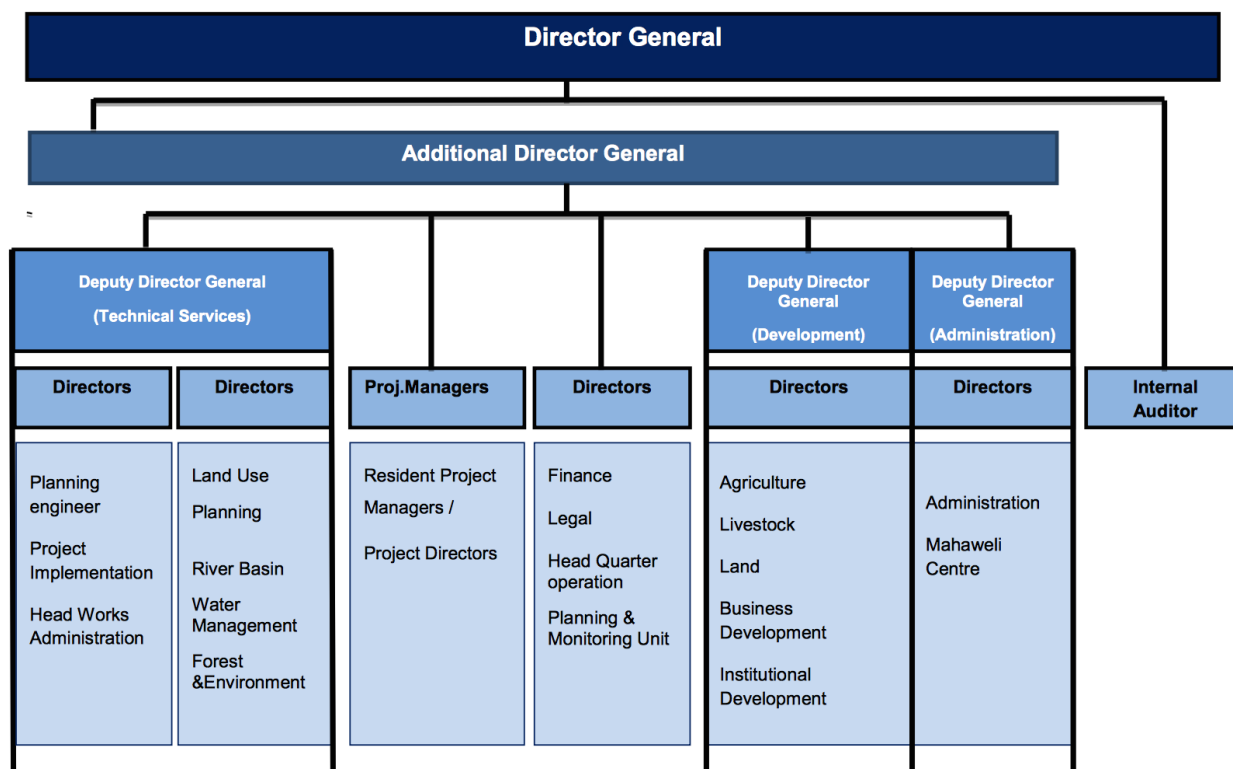
17. The MASL's vision statement is: *"The pioneer body of planning, development and manipulating of river valleys and water resources in Sri Lanka,"* and its mission statement is: *"(a) Increase the national food production together with land and water resource efficiency, (b) transfer the irrigation scheme management to farmer organization by increasing their management ability and (c) increase the water storage capacity of reservoirs and develop new irrigation project to meet the present water need."*

18. MASL's head office is located at 500, T.B. Jayah Mawatha, Colombo 10 with its branch office is at Jawatta Road, Colombo 5. There are 17 site offices located in Northern, North Central, Eastern, Central and Southern Provinces. They are Welioya, Thambuttegama, Dambulla, Huruluwewa, Moragahakanda, Medirigiriya, Welikanda, Dehiattakandiya, Maduru Oya, Mapakada, Randenigala, Victoria, Digana, Kotmale, Embilipitiya and Rambakenoya.

19. The Board of MASL consists of five members. Three members are appointed by the minister, with the approval of the President, and two ex-officio Directors, namely the Secretary to the Ministry in charge of the subject of Finance and the Secretary to the Ministry in charge of the administration of MASL. The Minister with the approval of the President appoints one of the directors to be the Director General (DG) of the authority.

20. The DG is the CEO of the MASL. An Additional DG acts as the Deputy CEO. Three Deputy DGs in the fields of technical, development and administration report to the additional DG. Further, 17 subject specialized directors, 2 project directors and 10 resident project managers support the management. The CIA's division functions as a separate unit directly under the DG.

**Figure 3: Organizational Structure of MASL**

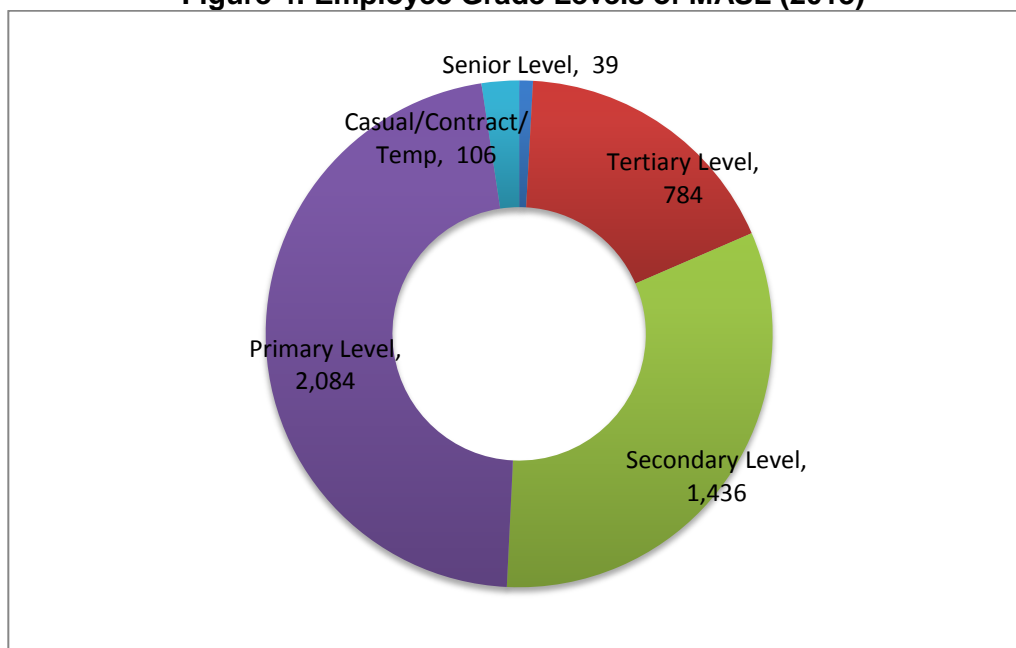


Source: MASL

21. MASL has professional staff required to manage countries most important and complex water regulatory structures involving dams and reservoirs and trans-basin canal network. It carries well trained experienced professionals, trained locally and abroad, worked remote areas in the dry zone with foreign counterparts, specialized in the fields of civil and mechanical engineering, agriculture, physical planning, settlement planning, business development, land management, institutional development, environmental conservation, accounting and administration.

22. MASL has a work force of 4,449 (as at October 2013) of whom 523 are at head office while the balance are in the field. MASL's 2013 staff base represents a 6% increase from 2012 where the total number of staff was 4,205. As shown below, it is noteworthy that less than 1% of the staff is of senior level with nearly 18% are at tertiary level. 79% of the cadre base is made up of primary and secondary level employees with about 2% in casual and contract status.

**Figure 4: Employee Grade Levels of MASL (2013)**



Source: MASL

### **C. Department of Irrigation**

23. DOI was formed over 110 years ago and operates as a separate department under the purview of the MOI. The DG of Irrigation (DGI) heads DOI and reports directly to the Treasury through the Secretary of MOI.

24. DOI implements the policies and programs of the Ministry, as the principal government organization responsible for the regulation and control of inland waters. The main objectives of DOI includes the following:

- Development of land and water resources for irrigated agriculture, hydropower, flood control, domestic usage, industrial usage and aquaculture development
- Provision of irrigation and drainage facilities for cultivable lands in irrigation and drainage projects
- Alleviation of poverty of the rural farming community by increasing their farm income and raising their standard of living
- Management of water for sustainable agriculture
- Productivity enhancement of land and water in major/medium irrigation schemes
- Integrated water resources management and participatory management in major, minor and medium irrigation systems

25. DOI's vision statement is to *"Enhance the development and management of land and water resources towards the socio-economic development of Sri Lanka. Irrigation Department will plan out, design, control and manage land and water resources to derive optimum benefits for irrigated agriculture, hydro power and flood control by harmonizing the modern technologies and human resources"*. Its mission statement is: *"Irrigation department will facilitate sustainable management and improve the land and water resources for food, livelihoods and environment under the framework of government policies."*

26. DOI's primary functions include:

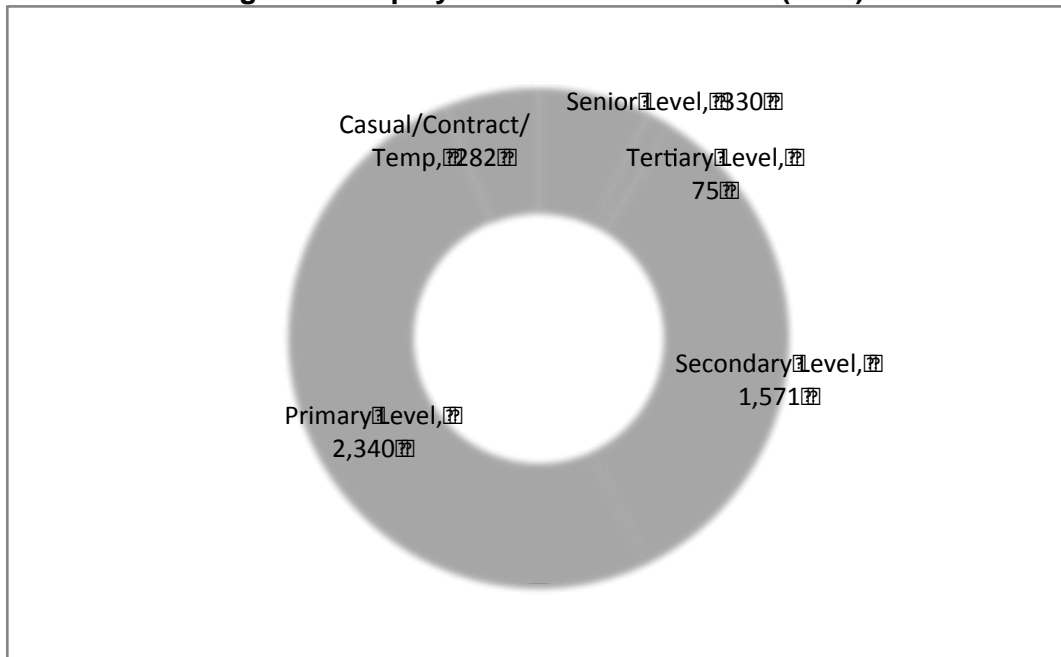
- Preparation of master plans for development of the different river basins for the optimum utilization of land and water resources
- Project formulation and detail designs of irrigation, hydro-power, flood control and reclamation projects
- Construction of irrigation and settlement projects for the conservation, diversion and distribution of water under gravity and lift irrigation to new and existing lands for cultivation by farmers for food crop production
- Construction of drainage, flood protection and salt water exclusion projects for the protection of cultivable land to enable the cultivation of such lands with rainfall for food crop production with minimized risk
- Operation, maintenance, improvements, rehabilitation and water management for medium and major gravity, drainage and lift irrigation projects
- Research in hydraulics, hydrology, soil mechanics, engineering, geology, GIS, engineering materials and land use as applied to water resources development projects
- Human resources development for optimum utilization of human resources
- Operation and maintenance of financial management systems, accounting, reporting, auditing systems of the DOI in accordance with the financial regulation of the government
- Providing consultancy services to government departments, statutory boards/corporations, public and private institutions and individuals; in the fields of water resources development, foundation engineering, quality control of earth work and concrete, hydraulic model testing and land use planning

27. The Treasury has allocated expenditure appropriation head number "282" to DOI. DOI has a separate appropriation number since it is categorized as a department under the Ministry of Finance.

28. DOI's head office is located at 230 Bauddhaloka Mawatha, Colombo 07, and operates in 15 districts around the country. Headed by the DGI, the top management of DOI comprise of five additional DGs overseeing areas such as irrigation and water management, regional development and construction, planning, design and specialized services, and finance and administration.

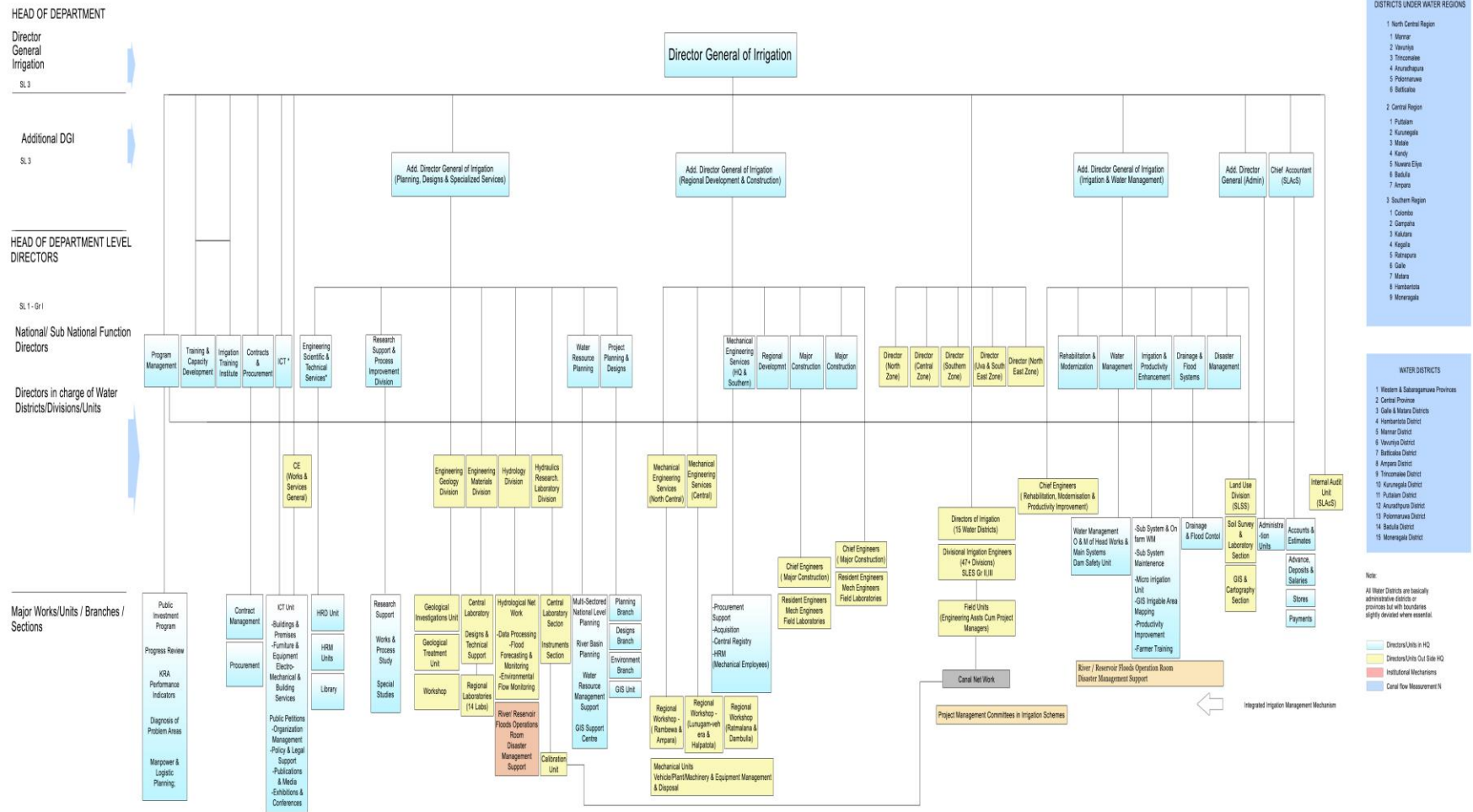
29. At the end of 2013, DOI had a total staff base around 4,600 employees representing a 3% growth from 2012 where the staff base was around 4,470. It is noteworthy that about 7% of the staff is of senior level whilst only 2% are at tertiary level. 81% of the cadre base is made up of primary, secondary, casual and contract employees.

**Figure 5: Employee Grade Levels of DOI (2013)**



Source: DOI

Figure 6: Organizational Structure of DOI



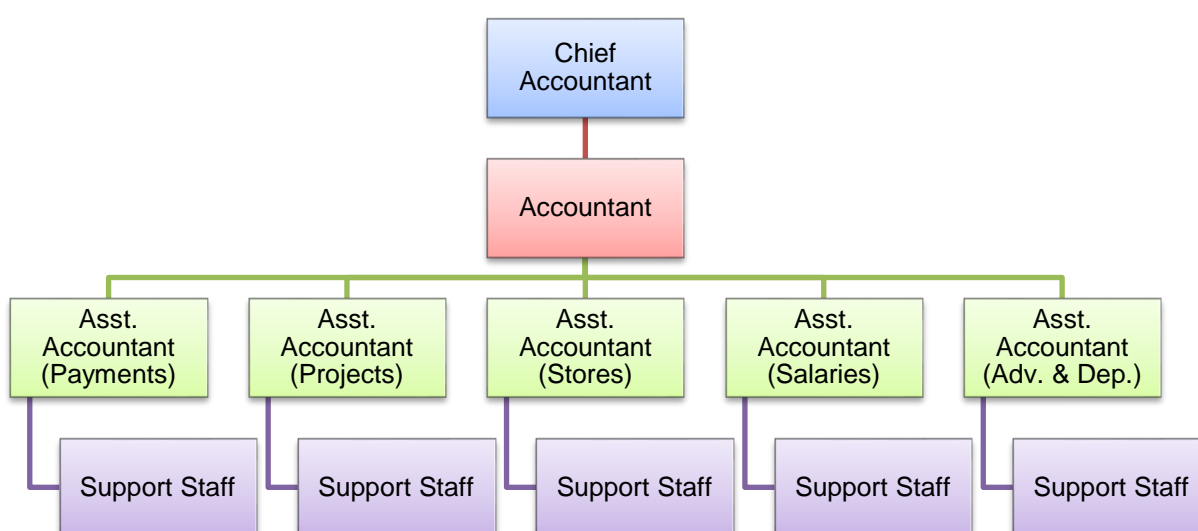
### III. FINANCE DEPARTMENTS

#### A. Ministry of Mahaweli Development and Environment

30. The chief financial executive of MMDE is the Chief Accountant. He is assisted by the Accountant who is engaged in day-to-day finance operations of the Ministry. The Chief Accountant reports directly to additional Secretary (Administration and Finance) as well as to the Secretary of MMDE.

31. There are five Assistant Accountants reporting to the Accountant that are responsible for key functional, administrative and operational areas of MMDE. There is 17 other support staff reporting to assistant accountants.

**Figure 7: MMDE Finance Department Structure**



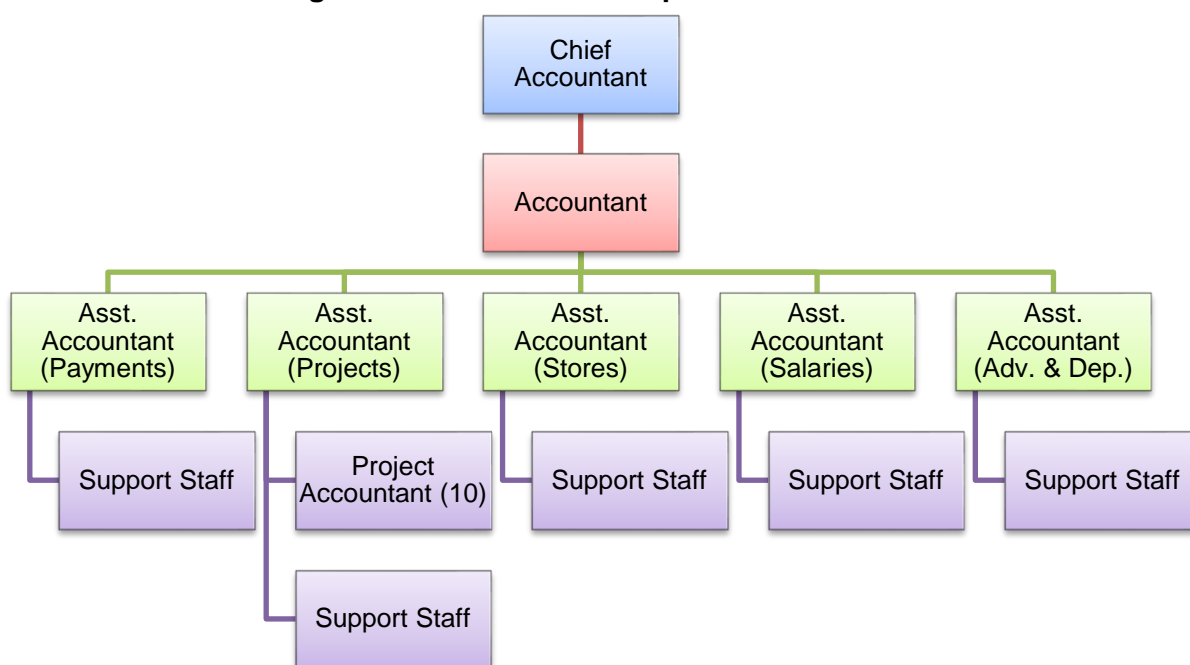
Source: MMDE

32. The Chief Accountant, Accountant and Assistant Accountants are qualified accountants. Other supporting staff are currently undertaking accountancy programs and/or undergraduate studies, diplomas in accountancy except for 3 staff members that are employed as clerks/messengers.

#### B. Mahaweli Authority of Sri Lanka

33. The chief financial executive of MASL is the Chief Accountant. He is assisted by the Accountant who is engaged in day-to-day finance operations of the institution. The Chief Accountant reports directly to the Director (Finance) as well as to MASL's DG and additional DG.

34. There are five Assistant Accountants reporting to the accountant that are responsible for key functional, administrative and operational areas of the MASL, 10 Project Accountants at each project manager's office, and 14 other support staff reporting to assistant accountants.

**Figure 8: MASL Finance Department Structure**

Source: MASL

35. The 10 Project Accountants report to the Assistant Accountant (Projects) and are based in each of MASL's 10 Project Manager's offices. These accountants are responsible for generating payment vouchers for projects, obtaining approvals from the head of the regional office (typically a qualified engineer) and sending them to head office for payments.

36. The Chief Accountant, Accountant, Assistant Accountants as well as Project Accountants at regional offices are qualified accountants. Other supporting staff are currently undertaking accountancy related programs, undergraduate studies and/or diplomas in accountancy related studies except for 5 staff members that are employed as clerks/messengers.

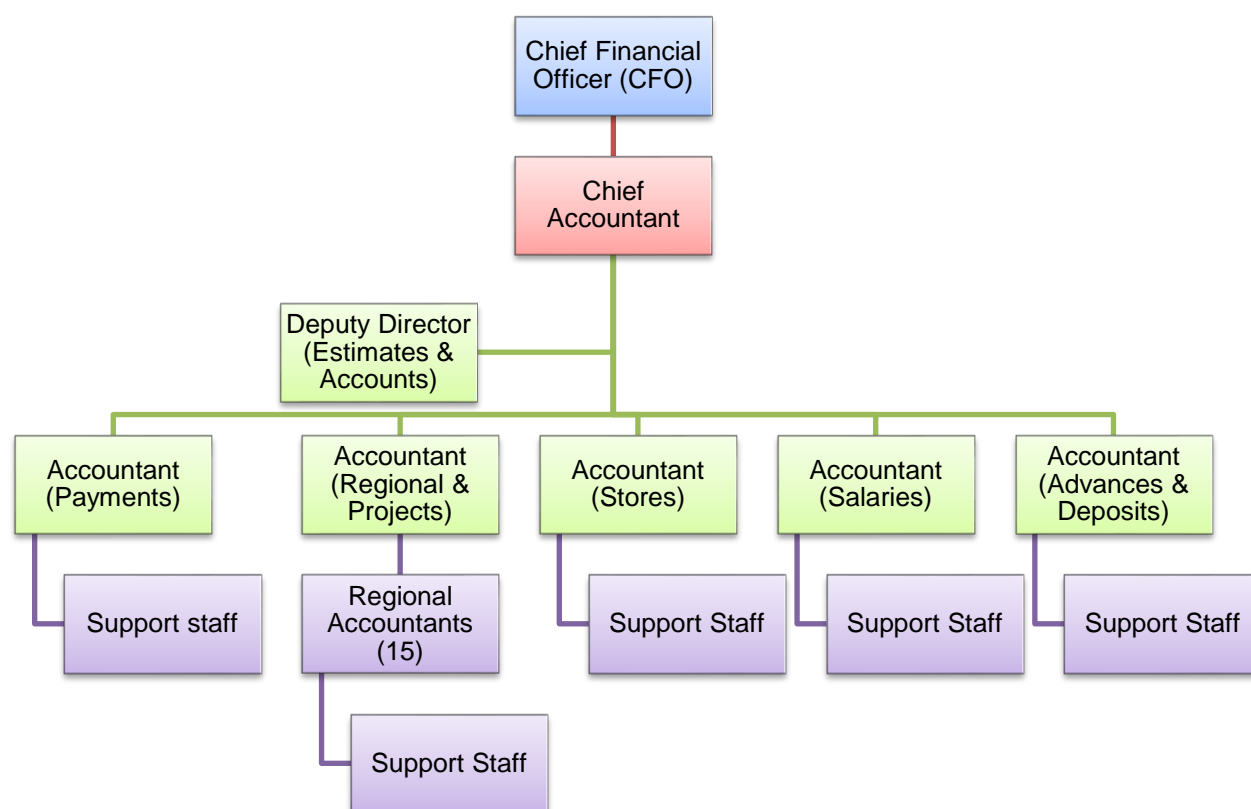
### **C. Department of Irrigation**

37. The chief financial executive of the DOI is the Chief Financial Officer (CFO). She is assisted by the Chief Accountant, who is engaged in day-to-day finance operations of the institution.

38. There are five Accountants reporting to the Chief Accountant. The Deputy Director comes under the supervision of the Chief Accountant. In addition there are 15 other regional accountants in each of the DOI's regional offices and 8 support staff.

39. The CFO, Chief Accountant, Deputy Director and 5 main Accountants as well as 15 regional accountants are qualified accountants. Other supporting staff are currently undertaking accountancy programs and/or undergraduate studies, diplomas in accountancy or related studies except for 2 staff members that are employed as clerks/messengers.



**Figure 9: DOI Finance Department Structure**

Source: DOI

40. In the regional and projects department, there are regional accountants based in each of the DOI's 15 regions. These regional accountants are responsible for generating payment vouchers for projects, obtaining approvals from the head of the regional office (typically a qualified engineer) and sending them to head office for payments.

41. Based on meetings and discussions with the Finance Departments of the MMDE, MASL and DOI, payment approvals for past and current foreign-funded projects, as well as locally funded projects, and fund disbursements both appear to function well. However, training and workshops in ADB's disbursement, procurement and financial reporting guidelines will be required in relation to the program. These workshops and training programs are best conducted locally at regional office level, which will ensure all regional staff members follow ADB's procedures, guidelines and best practices during the program. It is also recommended to conduct routine training programs and workshops at the head office combining all regional accountants and head office financial staff on a regular basis, at least on a half yearly basis, on ADB guidelines and instill ADB's best practices.

#### **IV. ACCOUNTING AND IT SYSTEMS**

42. Accounts of MMDE, MASL and DOI are prepared in accordance with Sri Lankan Accounting and Auditing Standards and the financial year corresponds with the normal calendar year ending to 31<sup>st</sup> December. These institutions maintain its accounts under a modified cash basis of accounting. Under this modified cash accounting, capital expenditures for fixed assets are accounted at cost, but depreciation is not provided in the accounts while its expenditure and income are recorded on cash basis.

43. Despite MASL's efforts in the preparation of financial statements, the absence of a comprehensive set of basic financial statements (i.e. profit and loss account, balance sheet and a cash flow statement) is of some concern. However, MMDE, MASL and DOI prepare comprehensive Appropriation Accounts with detailed notes on an annual basis. Typically, all institutions that report to the Treasury do not prepare full financials. The government has already identified this weakness and the Treasury is expected review and revise the present system, albeit it is difficult to define an exact timeframe.

44. The Appropriation Account records actual recurrent expenditures (divided into operational and development activities) and capital expenditure (also divided into the same activities) with comparison to the budget. A variation analysis is also provided along with explanations to provide justifications for both over and under expenditure.

45. A statement of claims under foreign reimbursable aids is included as a separate note in Appropriation Account. This is a very useful statement, which provides details of payments and claims relating to foreign-funded projects. It is recommended that these institutions maintain a separate note and a statement to monitor payments and claims relating to the investment program. Appropriation Account notes structure has the flexibility to introduce such additional notes.

46. MMDE, MASL and DOI's accounting systems use a common platform called CIGAS which is employed by most government institutions reporting to the Treasury. CIGAS has been the core accounting system and it seems to function well. It is an on-line fully integrated system that has established direct links with any regional offices of the institutions. In addition to the Appropriation Account, the CIGAS system generates and uploads monthly reports to the Treasury. Even though there are few limitations in the present IT system, these are not seen as major issues that would have an impact on the proposed investment program.

47. The Treasury is currently reviewing the existing system and is likely to augment the system across its Ministries and Departments. This will bode well for the investment program as the new system is likely to introduce separate modules to monitor and report foreign financed projects in more detail. Exact implementation date, however, cannot be established as yet.

## V. FINANCIAL PLANNING AND BUDGETING

48. In Sri Lanka, the Treasury reviews and finalizes annual budgets for all government departments through the relevant ministries. Once budgets are finalized, the Treasury through the Finance Minister (typically the President of Sri Lanka) presents the budget to the parliament usually in October/November each year. Once the parliament approves the budget, usually after three to four rounds of budget debates, the Treasury distributes the final budget by the beginning of each year to relevant ministries and institutions.

49. With respect to MMDE, MASL and DOI, in May/June of each year, the Finance Department requests all departmental heads and regional offices to submit their expected expenditure for the ensuing year. The estimates are consolidated and discussions are held with all the departmental heads to contain the total expenditure within the estimated budget for the ensuing year. Upon final review by the head of finance and the DG/Secretary, draft budgets are submitted to the Treasury by August each year. Several rounds of discussions then take place with the Treasury to finalize the budget to be presented to the parliament. The entire budgeting process normally takes about four to six months including parliament's approval.

**Figure 10: Annual Budgets of MMDE (including MASL) and DOI (2012-2016)**

Head No	Description	2012	2013 Revised Budget	2014 Estimate	2015 2016 Projections		2013 - 2016 Total
<b>152-</b>	<b>Minister of Irrigation and Water Resources Management</b>						
	<b>Operational Activities</b>	103,168	124,795	226,955	236,771	245,302	833,823
	Recurrent Expenditure	89,872	108,770	118,955	126,571	133,102	487,398
	Capital Expenditure	13,297	16,025	108,000	110,200	112,200	346,425
	<b>Development Activities</b>	24,702,243	33,408,300	42,125,420	63,303,200	66,721,445	205,558,365
	Recurrent Expenditure	1,868,880	2,054,980	2,133,070	2,197,500	2,373,225	8,758,775
	Capital Expenditure	22,833,362	31,353,320	39,992,350	61,105,700	64,348,220	196,799,590
	<b>Total Expenditure</b>	<b>24,805,411</b>	<b>33,533,095</b>	<b>42,352,375</b>	<b>63,539,971</b>	<b>66,966,747</b>	<b>206,392,188</b>
	Recurrent Expenditure	1,958,752	2,163,750	2,252,025	2,324,071	2,506,327	9,246,173
	Capital Expenditure	22,846,659	31,369,345	40,100,350	61,215,900	64,460,420	197,146,015
<b>282-</b>	<b>Department of Irrigation</b>						
	<b>Operational Activities</b>	368,769	414,975	420,885	442,210	461,940	1,740,010
	Recurrent Expenditure	337,517	373,350	377,735	389,710	396,240	1,537,035
	Capital Expenditure	31,252	41,625	43,150	52,500	65,700	202,975
	<b>Development Activities</b>	6,279,471	7,736,930	12,473,300	9,262,060	4,957,120	34,429,410
	Recurrent Expenditure	1,002,264	1,062,900	1,126,300	1,154,060	1,165,920	4,509,180
	Capital Expenditure	5,277,207	6,674,030	11,347,000	8,108,000	3,791,200	29,920,230
	<b>Total Expenditure</b>	<b>6,648,239</b>	<b>8,151,905</b>	<b>12,894,185</b>	<b>9,704,270</b>	<b>5,419,060</b>	<b>36,169,420</b>
	Recurrent Expenditure	1,339,781	1,436,250	1,504,035	1,543,770	1,562,160	6,046,215
	Capital Expenditure	5,308,459	6,715,655	11,390,150	8,160,500	3,856,900	30,123,205
	<b>Grand Total</b>	<b>31,453,651</b>	<b>41,685,000</b>	<b>55,246,560</b>	<b>73,244,241</b>	<b>72,385,807</b>	<b>242,561,608</b>
	<b>Total Recurrent</b>	<b>3,298,533</b>	<b>3,600,000</b>	<b>3,756,060</b>	<b>3,867,841</b>	<b>4,068,487</b>	<b>15,292,388</b>
	<b>Total Capital</b>	<b>28,155,118</b>	<b>38,085,000</b>	<b>51,490,500</b>	<b>69,376,400</b>	<b>68,317,320</b>	<b>227,269,220</b>

*Note: MMDE include MASL budget since MASL is considered as an institution of MMDE*

Source: Ministry of Treasury

50. As shown in **Figure 10**, MMDE's (which includes MASL) and DOI's budgets have been categorized in two main cost activities: operational and development. In addition, operational and development budgets have been further divided according to the nature of the expenditure: recurrent and capital.

51. Operational activities include all recurrent administration and establishment expenses of the head office and regional offices as well as any capital expenditure relating to acquisition of plant, property and equipment. Development activities include administration and maintenance costs of all irrigation schemes. Capital expenditure under development activity is the main cost element of MMDE, MASL and DOI and includes all development capital costs of new reservoir projects as well as major, medium and minor irrigation systems and other development projects and programs.

52. Changes to the budget allocation for government organizations at the Parliament are unusual since the Treasury has already made reallocations to the budget after detailed reviews and several rounds of discussions. Therefore, obtaining approval from the Treasury is the most important step in the Budget Approval process for MMDE, MASL and DOI.

53. Based on MMDE, MASL and DOI's previous experience with the Treasury and the budgeting process, the recurrent expenditure budget, which accounts to approximately 7% of total expenses of the 2014 budget, is typically approved without much difficulty. This is due to the fact that these expenses are estimated based on past trend taking in to consideration the recurrent nature of such costs. For majority of these costs such as salaries, rent, electricity, vehicle maintenance etc. organizations have a commitment and an obligation and therefore seeking approval from the Treasury is relatively straightforward. O&M costs relating to on-going and existing development projects are also included under recurrent cost category along with any forecast O&M for future projects in the pipeline.

54. MMDE (which includes MASL) and DOI's capital expenditure budgets have two areas (i) operational and (ii) development. Operational capital expenses account for less than 1% of the total capital expenditure budget for 2014, and include expenses such as improvements to buildings and structures and vehicle acquisition costs. Development costs, which accounts for 99% of the capital expenditure budget, and about 93% of entire budget for 2014, is the largest item and include capital costs relating on-going and planned projects. Obtaining approval from the Treasury for Development Capital Expenditure has been a problem in the past due to the lack of fund allocation to MMDE, MASL and DOI by the central government and insufficient priority to water and irrigation related projects.

55. It is expected that capital costs relating to the investment program will form a part of MMDE's Development Capital Expenditure budget from 2015 onwards (not included in the Figure 10). As evidenced from the past, MMDE, MASL and DOI usually experiences a high level of scrutiny and can face difficulties in getting development capital budgets approved by the Treasury, especially for new projects. Accordingly, in order to ensure the implementation of the investment program within its allocated timeframe, while safeguarding the program's features and without having to compromise on quality, it is vital that the Treasury extends a firm commitment to prioritize the investment program and to fully allocate the necessary funding requirement to MMDE during the annual budgetary process.

56. The current process of fund disbursement seems satisfactory based on the experience of past and on-going foreign and locally funded projects executed by MMDE and implemented by MASL and DOI. Requests for funds from IAs are typically sent to the Treasury through

MMDE. The Treasury acknowledges the request by releasing funds without any major delays if the claims and payment requests are within the budget allocation. It is expected a similar fund disbursement process will continue for the ADB program.

57. Even though there are basic KPIs set by the agencies in the past, it is recommended that MMDE review its existing framework to update the KPIs using ADB's knowledge and best practices based on previous projects done in the region to track physical progress with financial disbursements of projects and programs. This will enable effective decision-making, planning and allocation of resources and funds. MMDE should track and report physical progress of the projects and link them to financials in a more effective, organized and standardized manner. This could be implemented internally (using MS Excel for instance) without incurring major cost and could be accommodated as a training initiative to support the investment program.

58. A 5-year Corporate Plan is also another important planning document for any organization. During the FMA of MMDE, MASL and DOI, only MASL appeared to give prominence to the 5-year Corporate Plan, which is updated yearly. MASL's Corporate Plan outlines its objectives, identifies its challenges and provides useful insights to its vision for the next 5 years. Although both MMDE and DOI have basic Corporate Plans, these are not as detailed as MASL's document. Accordingly, it is recommended that MASL's Corporate Plan to be reviewed and introduce ADB's best practices and guidelines, which can then be used as a template for MMDE and DOI. This also can be done as a training initiative to support ADB's investment program prior to its implementation.

## **VI. FINANCIAL REPORTING, MONITORING AND AUDIT**

59. MMDE, MASL and DOI's financial reporting and monitoring is performed monthly. Expenditure is incurred and recorded at the departmental and regional levels and at month end, each department and region uploads the monthly expenditure along with the variance analysis to the system through the CIGAS.

60. At MASL, the Chief Accountant's office consolidates its head office and regional monthly financial statements and submits to MMDE. The Chief Accountant at MMDE then prepares consolidated monthly financials of MMDE and uploads to the Treasury through the CIGAS. In terms of DOI, the CFO's office at DOI prepares consolidated monthly expenditure statements and submits directly to the Treasury through MOI using the online CIGAS system.

61. If the expenditure for one cost category exceeds the budget, transfers can be made from other cost category budgets as long as overall expenditure remains under the budget ceiling. The Chief Accountants at MMDE and MASL, and the CFO at DOI, are required to obtain approval for such adjustments from the Treasury. In most cases, approvals are sought after the event when transfers are made between budget items as long as total expenditure is within the predetermined limit. If however, the budget limit is exceeded, Treasury approval is required prior to the event.

62. Similar to the case of over-spending, MMDE, MASL and DOI are also required to submit details of any under-spending/savings at the end of the year. This is seen as a good practice since under-spending could mean either weak budgeting or delays/non-payments from the Treasury.

63. As shown below, based on the past analysis of expenditure, actual recurrent expenditure are by and large in line with the budget. Actual capital expenditure are however, appear to be less than the budget in most instances across MMDE, MASL and DOI.

**Figure 11: Recurrent and Capital Expenditure (Actuals vs. Budget)**

LKR (in 000s)	2011 Budget	2011 Actual	2011 Variance	2012 Budget	2012 Actual	2012 Variance	2013 Budget	2013 Actual	2013 Variance
<b>MIWRM &amp; MASL</b>	<b>6,795,594</b>	<b>1,322,146</b>	<b>-33%</b>	<b>6,170,515</b>	<b>4,805,411</b>	<b>-5%</b>	<b>3,533,095</b>	<b>0,980,272</b>	<b>-8%</b>
Recurrent Expenditure	998,825	976,302	-1%	2,031,065	1,958,752	-4%	2,163,750	2,120,475	-2%
Capital Expenditure	4,796,769	345,844	-37%	4,139,450	2,846,659	-5%	1,369,345	859,797	-8%
<b>DOI</b>	<b>7,975,555</b>	<b>4,457,221</b>	<b>-19%</b>	<b>8,455,825</b>	<b>6,648,239</b>	<b>-21%</b>	<b>8,151,905</b>	<b>7,505,913</b>	<b>-8%</b>
Recurrent Expenditure	254,125	222,624	-3%	302,375	339,781	3%	436,250	416,705	-1%
Capital Expenditure	7,721,430	4,234,597	-22%	8,153,450	6,308,458	-26%	7,715,655	7,089,208	-9%
<b>Total</b>	<b>14,771,149</b>	<b>7,779,367</b>	<b>-28%</b>	<b>14,626,340</b>	<b>11,453,650</b>	<b>-9%</b>	<b>11,685,000</b>	<b>8,486,185</b>	<b>-8%</b>
Recurrent Expenditure	1,252,950	1,198,926	-2%	2,333,440	2,298,533	-1%	2,600,000	2,537,180	-2%
Capital Expenditure	11,518,199	4,580,441	-32%	12,292,900	9,155,117	-10%	9,085,000	5,949,005	-8%

Source: MMDE, MASL and DOI

64. Amongst other factors, one of the main reasons for under-utilization of capital expenditure budget is due to delays in fund releases by the Treasury. Even though the Treasury allocates a capital budget at the beginning of each year, due to fund constraints and re-prioritization of projects by the government, the Treasury ends up reallocating funds to its Ministries from time to time during the course of the year. This results in delays as well as amendments to implementation schedules of projects.

65. In order to ensure the successful implementation of the investment program, it is vital that the Treasury provides a firm commitment to MMDE, MASL and DOI to allocate the fund requirement and release funds without any significant delays. Based on an understanding of the national importance of the investment program and discussions held to-date in the government, it is anticipated that the Treasury will fully cooperate and provide the funding requirement. However, it is recommended to obtain Treasury commitment formally to ensure fund allocation and disbursements given experiences MMDE, MASL and DOI has encountered in the past.

66. After the close of each financial year, the Chief Accountants of MMDE and MASL, as well as the CFO at DOI, are required to prepare detailed financial statements. These are very comprehensive documents with detailed notes to the accounts and details of expenditure and income if any. Once reviewed and finalized, these are submitted to the Treasury and to the Auditor General (AG).

67. The accounts of MMDE, MASL and DOI are subject to an external audit by the AG or by such officers who are authorized by the AG's office. All institutions, including MMDE, MASL and DOI, that are audited by the AG are required to submit financial statements to AG's office by 31<sup>st</sup> March of the subsequent year. The AG's office then conducts an annual audit of the accounts. He submits the final audit report to the Treasury and issues a summary to the Parliament through the Treasury. The AG's office typically issues this report to the Treasury by September/October of the subsequent year with findings corresponding to the previous financial year. Most recent audited opinions of MMDE, MASL and DOI do not indicate any significant financial issues.

68. In addition to the annual audit by the AG, MMDE, MASL and DOI each have an in-house Chief Internal Auditor (CIA) that conducts regular internal audits. This unit operates as an independent department headed by a qualified accountant. Each of the units directly reports to the head of the institution, for instance at MIRWM the CIA reports directly to the Secretary, MMDE and at MASL and DOI the CIA reports directly to their respective DGs.

69. Each of the CIA's offices at MMDE, MASL and DOI appear to be adequately staffed with 15-30 employed in each CIA's office. The CIA's unit typically operates in teams of 3 to 4 that are sent to regional offices and head office departments for comprehensive audits (once a year) and for spot audits (once or twice a year). In addition to the CIA being a qualified accountant, team leaders of the CIA office are also qualified accountants. The CIA office ensures that the departments and regional offices comply with policies, requirements and regulations of the institution. The office also conducts examination and analysis of fiscal procedures, checking and verification of accounts and expenditures.

70. In addition to the AG's audit and internal audits, the AG shall also carry out a separate audit of the ADB-financed investment program in accordance with ADBs guidelines. In addition, the CIAs at MMDE, MASL and DOI shall also ensure that the internal audit annual plan covers a separate audit for the investment program including at least two spot audits per year along with an annual comprehensive audit.

71. The Treasury has identified DOI as a "Department" and therefore has allocated a separate cost center code to DOI (number 282). MMDE's cost code is 152 (refer to Figure 10). Accordingly, the Treasury presents both MMDE and DOI's budgets separately. Further, DOI being a "Department" has certain advantages over MMDE's "Institutions" such as MASL. Similar to DOI, MASL has large operations in the country and has several large projects under its purview. The investment program will also contribute towards the prominence of MASL. Therefore, it is suggested to explore the possibility of categorizing MASL as a "Department" and to allocate a separate cost center number to MASL.

## **VII. FINANCIAL PERFORMANCE**

72. For the purpose of analyzing MMDE's financial performance, MASL's financials have also been included in MMDE's financials. DOI's financials are separate.

### **A. Ministry of Mahaweli Development and Environment and Mahaweli Authority of Sri Lanka**

73. Summarized in **Figure 12** are MMDE's (including MASL's) actual expenses for 2011, 2012 and 2013, along with forecast estimates for 2014, 2015 and 2016. The information presented has been extracted from Treasury forecasts and MMDE's (and MASL's) actuals. Forecast estimates below exclude the investment program.

**Figure 12: MMDE Financials (including MASL)**

LKR (in 000s)	2011 Actual	2012 Actual	2013 Actual	2014 Estimate	2015 Estimate	2016 Estimate
<b>Recurrent Expenditure</b>	<b>1,976,302</b>	<b>1,958,752</b>	<b>2,120,475</b>	<b>2,252,025</b>	<b>2,324,071</b>	<b>2,506,327</b>
Operational Activities	8,813	8,872	106,595	18,955	26,571	33,102
Development Activities	897,489	868,880	2,013,880	2,133,070	2,197,500	2,373,225
<b>Capital Expenditure</b>	<b>9,345,844</b>	<b>22,846,659</b>	<b>28,859,797</b>	<b>40,100,350</b>	<b>51,215,900</b>	<b>54,460,420</b>
Operational Activities	1,877	3,297	4,743	108,000	110,200	112,200
Development Activities	323,967	22,833,362	28,845,054	39,992,350	51,105,700	54,348,220
<b>TOTAL</b>	<b>11,322,146</b>	<b>24,805,411</b>	<b>30,980,272</b>	<b>42,352,375</b>	<b>53,539,971</b>	<b>56,966,747</b>
<b>TOTAL in USD mn</b>	<b>87.1</b>	<b>190.8</b>	<b>238.3</b>	<b>325.8</b>	<b>488.8</b>	<b>515.1</b>

Source: MMDE, MASL and Treasury

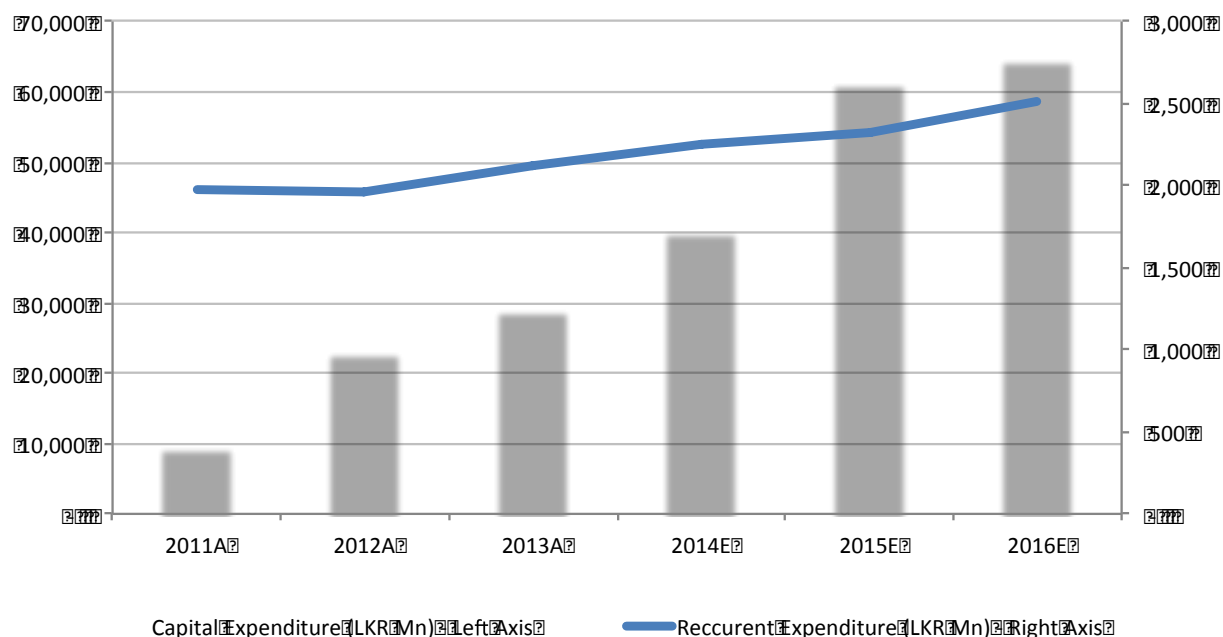
74. Recurrent expenditure as a percentage of total expenses has averaged 11% between 2011 and 2013 and has witnessed a 3.6% compound annual growth rate (CAGR). During 2014 to 2016, recurrent expenditure is expected to grow at a marginally faster rate of around 5.7% CAGR with a relatively steep 7.8% year-on-year growth estimated in 2016. Due to high levels of capital expenditure anticipated from 2014 onwards, recurrent expenditure as a percentage of total expenses is expected to average around 4% between 2014 and 2016.

75. The majority of recurrent expenditures relate to personnel costs, which include salaries and wages, overtime and holiday payments as well as allowances. For instance nearly 90% of the recurrent expenditure of the 2014 Budget is made up of personnel costs, which is consistent when compared to historical data from 2011 to 2013, as well as when compared with estimates for 2015 and 2016.

76. Other recurrent expenditures, which accounts for approximately 10% of the recurrent expenditure budget, includes electricity and water, fuel, stationary, travelling expenses and other administrative expenses.

77. Capital expenditure of MMDE accounts for the majority of the Ministry's expenses. During 2011 to 2013, on average 89% of total expenses were capital costs and in 2014 capital expenditure is estimated at 95% of MMDE's total expenditure budget. Between 2011 and 2013, capital expenses have grown at a rapid phase of around 75.7% CAGR and in 2014 it is anticipated to grow by 53% year-on-year.



**Figure 13: Recurrent and Capital Expenditure (SLRs million)**

Source: MMDE, MASL and Treasury

78. The majority of capital expenditures relate to reservoir projects and water systems. For instance, out of the SLRs 40 billion capital expenditure projected for 2014, SLRs 15 billion has been reserved to the “Uma Oya Diversion Project” co-funded by Iran and SLRs 13 billion allocated to the “Moragahakanda and Kalu Ganga Reservoir Project” co-funded by China, Kuwait and Saudi Arabia. The capital budget also includes capital expenditure relating to development activities, which entails administration and maintenance cost of reservoirs and water systems under the purview of MMDE and MASL.

79. Based on the past experience of implementing large projects especially funded by foreign countries, MMDE together with MASL appear to have sufficient financial management capacity to implement the proposed investment program. However, it is important that the capital expenditure budget for the investment program is prepared and reviewed in detailed to ensure timely disbursement of funds from the Treasury.

## **B. Department of Irrigation**

80. Due to the non-preparation of a full set of financial statements, only expenditure details are available within DOI. Summarized in Figure 14 are DOI’s actual expenses for 2011, 2012 and 2013, along with forecast estimates for 2014, 2015 and 2016. This information presented has been extracted from Treasury forecasts and DOI actuals. Forecast estimates below exclude the investment program.

**Figure 14: Financials Records of DOI**

LKR (in 2000s)	2011 Actual	2012 Actual	2013 Actual	2014 Estimate	2015 Estimate	2016 Estimate
<b>Recurrent Expenditure</b>	<b>1,222,624</b>	<b>1,339,781</b>	<b>1,416,705</b>	<b>1,504,035</b>	<b>1,543,770</b>	<b>1,562,160</b>
Operational Activities	89,551	93,517	96,220	97,735	98,710	99,240
Development Activities	33,073	40,264	47,485	51,263	54,060	56,920
<b>Capital Expenditure</b>	<b>5,234,597</b>	<b>5,308,458</b>	<b>5,089,208</b>	<b>11,390,150</b>	<b>11,160,500</b>	<b>11,856,900</b>
Operational Activities	4,699	5,125	5,783	11,315	11,250	11,570
Development Activities	350,463	386,610	969,906	765,000	827,500	981,200
Major Irrigation Systems	585,388	808,840	765,326	845,000	730,500	610,000
Minor & Medium Irrigation Systems	64,047	1,757	16,141	37,000	50,000	100,000
<b>TOTAL</b>	<b>6,457,221</b>	<b>6,648,239</b>	<b>6,505,913</b>	<b>12,894,185</b>	<b>12,704,270</b>	<b>13,419,060</b>
<b>TOTAL in US\$ mn</b>	<b>9.7</b>	<b>10.1</b>	<b>9.7</b>	<b>19.2</b>	<b>17.4</b>	<b>18.7</b>

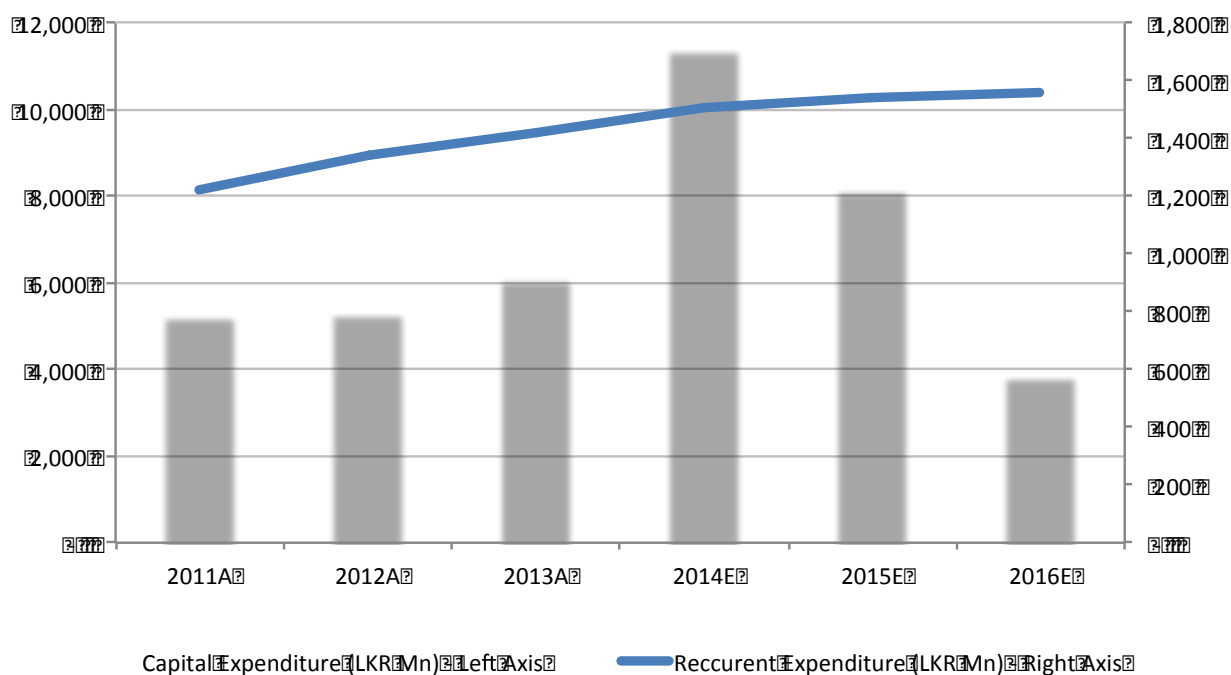
Source: DOI and Treasury

81. Recurrent expenditure as a percentage of total expenses of the DOI has averaged 19% between 2011 and 2013 and has experienced a 7.6% CAGR. During 2014 to 2016, recurrent expenditure is expected to grow at a comparatively lower rate of 3.3% CAGR despite a 6.2% year-on-year growth in 2014. Therefore, 2015 and 2016 recurrent costs appear to have been relatively understated.

82. The majority of recurrent expenditures relate to personnel costs, which include salaries and wages, overtime and holiday payments as well as allowances. For instance 90% of the recurrent expenditure of the 2014 Budget is made up of personnel costs, which is consistent when compared to historical data from 2011 to 2013, as well as when compared with estimates for 2015 and 2016. Average monthly staff cost per employee in 2014 is estimated around SLRs 23,000 or approximately \$180, which is in line with market rates prevailing in the country.

83. Other recurrent expenditures, which accounts for approximately 10% of the recurrent expenditure budget of DOI, includes electricity and water, fuel, stationary, travelling expenses and other administrative expenses. These expenses have experienced an increase of 9% CAGR from 2011 to 2013, while a 5% CAGR is expected between 2014 and 2016. Based on the historical trend analysis, DOI's estimates seem marginally optimistic. However, the impact on DOI's overall financials of any adverse movements is not likely to be material.

84. Capital expenditure of DOI accounts for the majority of the department's expenses. During 2011 to 2013, 81% of total expenses of DOI were capital costs and in 2014 capital expenditure is estimated at 88%. Between 2011 and 2013, capital expenses have grown at 7.9% CAGR and in 2014 it is anticipated to grow by 87% year-on-year.

**Figure 15: Recurrent and Capital Expenditure (SLRs million)**

Source: DOI and Treasury

85. The majority of capital expenditures relate to major, minor and medium irrigation systems. For instance, in 2014, 84% of the capital cost budget has been allocated towards development of irrigation systems. Out of the SLRs 9.6 billion irrigation development expenditures projected for 2014, SLRs 5 billion has been reserved to develop a new irrigation system “Yan Oya Project”. Planned investments for such large-scale projects have resulted in an 87% growth in total capital expenditure estimate for 2014 year-on-year.

86. DOI’s 2014 major irrigation program includes 18 projects, including the above captioned Yan Oya Project. Out of these 18 projects, 8 projects will continue into the subsequent year with a majority of the investments earmarked for the Yan Oya Project (SLRs 3.1 billion) and the Moragahakanda Reservoir (SLRs 1.2 billion) together which represent more than 50% of the capital expenditure budget planned for 2015. From the 8 projects in 2015, 4 are expected continue further in to 2016 where there is an overall capital expenditure budget of SLRs 3.8 billion out of which SLRs 1.8 billion is allocated to develop new irrigation systems.

87. In addition to the 18 major projects mentioned above, DOI has another 9 minor and medium projects in the pipeline for 2014. From these 9 projects, 3 are expected to continue in 2015 and only 1 is expected in 2016. It should be noted, however, that out of the total capital expenditure budget only around 5% relates to the development of minor and medium irrigation projects.

88. The capital budget also includes capital expenditure relating to development activities, which entails administration and maintenance cost of irrigation schemes and systems under the purview of DOI. During 2011 to 2013, such expenditure accounted to approximately 28% of the total capital budget which is expected to average 30% between 2014 and 2016.

89. Based on the past experience of implementing large projects, DOI appears to have sufficient financial management capacity to implement the proposed investment program. In 2014, DOI has been allocated approximately \$90 million capital budget as new investments for 27 schemes, as well as to operate and maintain existing portfolio of irrigation systems. Considering the future projects in the pipeline are also reducing from 2015 onwards, DOI should have spare capacity to effectively implement new projects. However, it is important that the capital expenditure budget for the investment program is prepared and reviewed in detailed to ensure timely disbursement of funds from the Treasury.

## VIII. RISK ASSESSMENT OF MMDE, MASL AND DOI

Area of Assessment	Risk Rating	Risk Assessment	Mitigation Measures
Country Specific Inherent Risks	M	Most government departments that report to the Treasury, including MMDE, MASL and DOI do not prepare full sets of financial statements.	Treasury has realized the importance of maintaining and preparation of the full sets of financial statements.  The Treasury is currently conducting a detailed study with the view of implementing new guidelines albeit it is difficult to predict an exact time frame.
Entity and Project Specific Inherent Risks	M	Even though the MMDE, MASL and DOI have implemented foreign-financed projects, lacks the direct expertise in implementing ADB projects.	The investment program requires a detailed Procedure Manual as well as adequate training on ADB's policies and guidelines.  Finance Staff and Regional Office staff directly engaged with the ADB project needs additional workshops and training programs.
<b>Overall Inherent Risks</b>			<b>M</b>

Area of Assessment	Risk Rating	Risk Assessment	Mitigation Measures
Implementing Agency Control Risks	N	MASL and DOI have implemented foreign projects in the past and it appears that both MASL and DOI have sufficient capacity to implement the proposed investment program.	
Fund Flow Control Risks	S	MMDE has executed large-scale foreign funded projects and both MASL and DOI have previous experience in implementing foreign projects in the past through the use of Imprest Accounts. A similar fund flow process is expected for the investment program. However, as	It is recommended to obtain a firm commitment from the Treasury to MMDE, MASL and DOI to release capital funds required by the investment program without any undue delays and to prioritize the investment project for fund

Area of Assessment	Risk Rating	Risk Assessment	Mitigation Measures
		seen in the past, the Treasury has the tendency to re-prioritize projects resulting in delays for planned projects.	disbursements.
Staffing Control Risks	N	MMDE, MASL and DOI, including their finance departments and their regional offices, are adequately staffed to implement the ADB-financed investment program.	Training on ADB specific policies and guidelines are required.
Accounting Policies and procedures Control Risks	N	MMDE, MASL and DOI follow Sri Lanka Accounting and Auditing Standards which are adequate. However, depreciation is not considered in accounts due to the mix of cash and accrual based accounting methods.	Treasury is currently in the process of addressing this issue. Once the Treasury implements new accrual based accounting system, MMDE, MASL and DOI have expressed the willingness to adopt to the new system.
Internal Audit Control Risk	N	MMDE, MASL and DOI's Internal Audit functions well.	Need to ensure Internal Audit's annual audit plan include a separate audit of the investment program. Minimum of 2 spot audits per year and an annual comprehensive audit is recommended at each MMDE, MASL and DOI levels.
External Audit Control Risk	N	AG's office currently conducts MMDE, MASL and DOI's annual audit which is adequate and audit opinions are generally free of any major issues	
Budgeting Control Risk	S	<p>It is evident from past performance that the MMDE, MASL and DOI generally under-spends the capital expenditure budget. One of the reasons is inaccuracy in forecasting capital costs.</p> <p>Other than MASL, MMDE and DOI's 5 year Corporate Plans are not comprehensive and are not updated frequently. Corporate Planning exercise should be done with extensive participation which will improve accuracy of estimates.</p>	<p>MMDE, MASL and DOI need to ensure expenditures are estimated accurately.</p> <p>Recommended to improve MASL's 5 year Corporate Plan with ADB best practices and use as a template for MMDE and DOI to be updated at least annually. This can be done as a training exercise prior to implementation of the investment program.</p>
Reporting and Monitoring Control Risk	M	MMDE, MASL and DOI's reporting and monitoring function does not include comprehensive set of KPIs and does not have the ability to track physical progress of projects and link them to financials.	It is recommended to introduce a system to track physical progress of projects and link to financials as well as to introduce KPIs in monthly reports. This can be done as a training exercise prior to implementation of the ADB-financed investment program.

Area of Assessment	Risk Rating	Risk Assessment	Mitigation Measures
		Treasury has not provided MASL a separate cost center code.	<p>Separate note recommended in appropriation accounts to report and monitor the investment program.</p> <p>MASL having a separate code will ensure efficient monitoring and planning. This will also enable MASL to approach the Treasury directly for urgent matters.</p>
Information Systems Control Risk	N	MMDE, MASL and DOI currently operates the CIGAS system, which is employed by departments reporting to the Treasury. This system appears adequate for implementing the investment program and monitoring its expenses.	
<b>Overall Risks</b>			<b>S</b>

\* H = High, S = Substantial, M = Moderate, N = Negligible or Low.