

## FINANCIAL MANAGEMENT ASSESSMENT

### A. Background

1. The financial management assessment (FMA) was conducted in accordance with the Guidelines of the Asian Development Bank (ADB) for the *Financial Management and Analysis of Projects* (2005), the *Financial Due Diligence: A Methodology Note* (2009), and the *Financial Management Technical Guidance Note* (2015). The FMA considered the financial management capacity of the Public Health Engineering Department (PHED) of the Government of West Bengal (GOWB) in its role as the executing and implementing agency for the proposed West Bengal Drinking Water Sector Improvement Project (WBDWSIP), including funds-flow arrangements, staffing, accounting and financial reporting systems, financial information systems, and internal and external auditing arrangements.

2. The major risk factors identified by financial management assessment that need to be addressed include:

- (i) limited experience of PHED in implementing and managing externally funded projects may cause the delay in implementation of WBDWSIP;
- (ii) inadequate staff in the accounts and finance sections of project management unit (PMU) may hamper the timely preparation and submission of periodic financial reports;
- (iii) internal audit system in PMU needs strengthening so there are no backlogs in preparation of project financial statements; and
- (iv) not having an approved tariff or user charge structure for water supply in the state as of September 2017 may constrain the medium and long-term financial sustainability of PHED and project *gram panchayats*.

3. Despite the highlighted risks, the financial management arrangements are satisfactory considering the proposed and ongoing actions of PHED. In addition, the project management consultants (PMCs) will support the PMU, and the three design, supervision, and institutional support consultants will support the three project implementation units (PIUs), in enhancing their and the project *gram panchayats*' financial management capacity. The overall risk assessment for the proposed financing is *moderate*. The action plan for mitigating the foreseen risks includes the following measures:

- (i) extending full training and capacity building support with the help of PMCs for enhancing the financial management capacity of PHED and the PMU;
- (ii) strengthening the accounts and finance divisions of the PMU by engaging qualified staff for the timely preparation of financial reports;
- (iii) strengthening the internal audit process by appointing qualified staff or outsourcing to experienced audit firms; and
- (iv) issuance of the government order on asset management and service delivery framework (ASMDF) and implementation of the same, which contains the water tariff structure and regular tariff revisions, before the completion of the project.

## B. Introduction

4. This FMA was conducted in accordance with the *Guidelines for the Financial Management and Analysis of Projects* (2005), the *Financial Due Diligence: A Methodology Note* (2009), and the *Financial Management Technical Guidance Note* (2015) of the Asian Development Bank (ADB).<sup>1</sup>

5. The FMA considered the financial management capacity of PHED of the GOWB in its role as the executing and implementing agency for the proposed WBDWSIP, along with its PMU, including funds-flow arrangement, staffing, accounting and financial reporting system, financial information system, and internal and external auditing arrangements.

6. A key aspect of the FMA is evaluating the risks associated with the financial arrangements of the project. ADB's principal concern is to ensure that the project funds are used economically and efficiently for the purposes intended. In support of this, it seeks assurance that the financial management system of the implementing agency can report on the source and use of the project funds. The assessment was based on the results of the FMA questionnaire, discussions with officials from the GOWB, PHED, and *gram panchayats*, and information available through various reports.<sup>2</sup>

## C. Brief Project Description

7. The project aims to provide safe, reliable, and continuous drinking water as per the Government of India's standard to about 2.6 million people in selected arsenic, fluoride, and salinity affected areas of Bankura, North 24 Parganas and South 24 Parganas, and Purba Medinipur districts of the state of West Bengal. The impact of the project will be drinking water security ensured in selected districts of West Bengal (Vision 2020, PHED, and National Sub-Mission for Arsenic and Fluoride Removal, Ministry of Drinking Water and Sanitation).<sup>3</sup> The outcome will be sustainable, resilient, and inclusive drinking water service delivered in project districts.

8. The project has the following outputs: (i) Output 1: climate resilient drinking water infrastructure constructed; and (ii) Output 2: institutions and capacity of stakeholders for drinking water service delivery strengthened.

## D. Country and Sector Financial Management Issues

9. The Country Policy and Institutional Assessment for transparency, accountability and corruption in the public sector rating (1 = low to 6 = high) in India was last reported by the World

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<sup>1</sup> ADB. 2005. *Financial Management and Analysis of Projects*. Manila. <https://www.adb.org/sites/default/files/institutional-document/31339/financial-governance-management.pdf>; ADB. 2009. *Financial Due diligence: A Methodology Note*. Manila. <https://www.adb.org/sites/default/files/institutional-document/33540/files/financial-due-diligence.pdf>; ADB. 2015. *Financial Management Technical Guidance Note*. Manila.

<sup>2</sup> *Gram panchayat* is the village-level (the first tier) of the local administrative body of the Government of West Bengal. Average population under the project *Gram Panchayats* range from 16,000 to 26,000.

<sup>3</sup> Government of West Bengal. Public Health and Engineering Department. 2011. *Vision 2020: To Provide Safe, Sustainable and Adequate Water Supply to All Humans and Livestock by 2020*. Available from <http://wbphed.gov.in/activities/vision-2020/>; Government of India. Ministry of Drinking Water. 2016. National Sub-Mission for Arsenic and Fluoride Removal, Ministry of Drinking Water and Sanitation. Available at <http://www.mdws.gov.in/national-sub-mission-guidelines-provide-safe-drinking-water-remaining-arsenic-and-fluoride-affected>

Bank at 3.6 in 2012.<sup>4</sup> Transparency, accountability, and corruption in the public sector assess the extent to which the executive can be held accountable for its use of funds and for the results of its actions by the electorate and by the legislature and judiciary, and the extent to which public employees within the executive are required to account for administrative decisions, use of resources, and results obtained. The three main dimensions assessed here are the accountability of the executive to oversee institutions and of public employees for their performance, access of civil society to information on public affairs, and state capture by narrow vested interests.

10. The main findings of the assessment of India's public expenditure and financial accountability are:<sup>5</sup>

- (i) **Assessment of the impact of public financial management.** The adoption of rule-based fiscal management by enacting the Fiscal Responsibility and Budget Management Act (2003) helped in monitoring aggregate fiscal indicators, but its impact on the actual practice of financial management is not clear. The budgeting system in India is conventional and input-based, and more concerned with basic financial compliance, but this has not resulted in establishing an effective fiscal discipline. The absence of a multi-year perspective in expenditure planning, lack of robust macroeconomic forecasting on which to base the budget, and inherent weaknesses in adhering to the procedures laid down in constitutional and legal provisions have negatively affected public financial management (PFM) outcomes;
- (ii) **Aggregate fiscal discipline.** Important weaknesses of the PFM system that limit fiscal discipline include (a) absence of a multi-year perspective in the expenditure planning that indicates future year commitments; (b) lack of effective fiscal risk assessment at an aggregate level; (c) unevenness and a late spike in the annual spending pattern; (d) surrendering of money at the end of the fiscal year in an annual lapsable budget cycle due to a lack of effective program management in budget implementation; (e) absence of a hard budget constraint; and (f) weak internal control and internal audit system. While external audit in the country is well established and facilitates the legislature in exercising control over the executive, the process of scrutiny of the audit reports has deteriorated, adversely affecting its effectiveness; and
- (iii) **Strategic allocation of resources.** The strategic allocation of resources in India is affected by the lack of well-developed sector strategies based on government objectives, developing and costing of programs to achieve those objectives, and linking the resource allocation to the priorities specified in sector strategies. The cash accounting followed by the government does not have the capacity to reveal the full outlays either on a program or a project. In the existing budgeting system, performance information is not included to improve strategic resource allocation.

11. Recent developments include the government's 2012–2013 Finance Bill that, as part of expenditure management reforms, introduced amendments to the 2003 Fiscal Responsibility and Budget Management (FRBM) Act,<sup>6</sup> which has the overall purpose of reducing the fiscal deficit. A provision for the 'Medium-term Expenditure Framework Statement' has been added to the Act to provide greater certainty in the multi-year budgeting framework. Also, 3-year rolling targets for expenditure indicators are to be prepared annually to provide certainty of allocation to ministries

<sup>4</sup> World Bank. 2012. *The World Bank's Country Policy and Institutional Assessment*. Washington D.C. Available at <http://data.worldbank.org/indicator/IQ.CPA.PUBS.XQ>.

<sup>5</sup> Assessment of India Public Expenditure and Financial Accountability Public Financial Management Performance Assessment Report, March 2010 by National Institute of Public Finance and Policy, New Delhi.

<sup>6</sup> Ministry of Finance (2012b): "Finance Bill—Chapter VI, Amendments to the Fiscal Responsibility and Budget Management Act, 2003".

and departments over the medium-term to help undertake resource allocations for prioritized schemes.

12. **Public financial management of the Government of West Bengal.** The PFM framework of the State of West Bengal is strong. All departments follow the national and state laws including (i) General Financial Rules (2017);<sup>7</sup> (ii) West Bengal Financial Rules (1979); (iii) West Bengal Treasury Rules (2005); and (iv) Delegation of Financial Power Rules (1977). The regular statutory external audit is done by the Office of the Comptroller and Auditor General of India (Supreme Audit Institution of India). All officers and employees abide by the conditions of ethics as prescribed in the GOWB's published gazettes: *The West Bengal Financial Rules* (1979), *The Delegation of Financial Power Rules* (1977), and *The West Bengal Service Rules* (1971).

13. **Financial management risks.** The GOWB introduced the West Bengal Fiscal Responsibility and Budget Management Act in July 2010 and amended it in February 2011 fixing the rolling fiscal targets for fiscal years (FY) 2010–2015. The Act aimed to bring direction and prudence in fiscal management and improve fiscal stability by the progressive elimination of revenue deficit and reduction in fiscal deficit, accompanied by prudent debt management consistent with fiscal sustainability and greater transparency. The GOWB also introduced a comprehensive budgeting system, a treasury management system, and introduced a financial management information system to systematize their budget processes and procedures throughout the public administration, including PHED. Given the financial management framework in the state of West Bengal, there are no significant financial management risks that need to be addressed in the coming years.

14. The GOWB is largely complying with various financial rules, procedures, and directives of the public financial management framework. Subsidiary Rule 330A under the West Bengal Treasury Rules stipulates that for grants provided for specific purposes, departmental officers should obtain the utilization certificates from the grantees within 1 year from the date of release of the grant and, after verification, should forward to the Principal Accountant General.

## E. Project Financial Management System

15. **Overview.** PHED was created as an independent full-fledged department following the Home Department's Notification No. 16664-AR dated 2 September 1987. Main activities of PHED are related to the rural and urban water supply. In the urban water supply sector, the activities of PHED are mostly limited to areas of the state outside Kolkata Metropolitan Area. As per the Rules of Business of GOWB,<sup>8</sup> PHED controls the water supply and sanitation-related budget of the GOWB and implements programs on water supply and sanitation services.<sup>9</sup> The head of the department is the additional chief secretary/principal secretary who is a senior administrative officer from the Indian Administrative Services Cadre. The head of the technical and the execution wing is the engineer in chief. PHED is headquartered in Kolkata (the capital city of West Bengal) and has offices in every district town, with officers posted in the various blocks under the district administration.

<sup>7</sup> General Financial Rules 2017 replaced General Financial Rules 2005.

<sup>8</sup> Government of West Bengal, Public Works Department. 1964. *Rules of Business*. Kolkata.

<sup>9</sup> The allocated Major Head of Account for PHED are 2215 – Water Supply and Sanitation, and 4215 – Capital Outlay on Water Supply and Sanitation. Government of West Bengal. Year. *Rules of Business*. Kolkata.

16. For the implementation of the project, the GOWB created the PMU, three PIUs, appointed the project director to head PMU, and expects to complete full staffing of PMU and PIUs by June 2018.

17. **Experience of managing externally financed projects.** As of 2017, PHED is implementing the West Bengal Piped Water Supply Project in Purulia valued at \$200 million and funded by the Japan International Cooperation Agency. The project faced problems in the original scope and design and is redesigning the raw water source necessary for implementation. In 2002 and 2012, the GOWB and Kolkata Municipal Corporation successfully executed the ADB-funded Kolkata Environmental Improvement Project. The Kolkata Environmental Improvement Investment Program, funded by ADB, is under implementation (2014–2023); Kolkata Municipal Corporation and the Municipal Affairs Department, GOWB, are the implementing agencies.

18. **Funds flow arrangements.** ADB will provide United States dollar loans to the Government of India, which (through Comptroller of Aid Accounts and Audit, Department of Economic Affairs) will on-lend to the GOWB on back-to-back terms and conditions in the rupee equivalent of the loan proceeds. The GOWB will receive the loan for the implementation of the project based on the proposed arrangements. The GOWB will create appropriate budget heads under the PHED's Demand Code Number 45 for allocation of the ADB loan funds and for allocation of the GOWB's counterpart funds for the execution by PHED. The PMU will implement the project and be responsible for the spending of the allocations under the budget heads.

19. **Staffing.** PHED is staffed with engineers, skilled staff, assistants, and computer operators, among others, at its various divisions, circles, and field offices. In year 2017, the PHED was running short of officers and staff due to positions falling vacant after the retirement of staff, which has affected its performance. Nevertheless, the quality of officers is high, and they are skilled in designing, executing, and managing major projects. As per the Vision 2020,<sup>10</sup> PHED has plans to create new positions and deploy resources to improve its performance.

20. PHED will staff the PMU with an adequate number of officers (either on deputation from other sections or by professionally engaging them), skilled accountants, project management specialist, and other experts as and when required. Under the guidance of the project director, [who] proposes a dedicated PMU, three PIUs, and a project finance and accounting unit (PFAU) for the implementation of the project. The project management consultants (PMC) and the design, supervision, and institutional support consultants will also assist the PMU, PIUs, and PFAU in managing the project. As of April 2018, PHED is in the process of creating the PFAU and expects to appoint the financial management specialists in PHED for support to the implementation of the project by December 2017. Until then, ADB's grant-funded consultants will continue supporting the PMU and PIUs.

21. **Accounting policy and procedures.** PHED maintains its accounts under the single-entry method and adopts the cash-basis of accounting based on the Government Accounting Rules (GAR, 1990).<sup>11</sup> The accounts of the project will be maintained under the guidelines issued in Letter No. 5/2/2010-ADB-I dated 2 September 2013, by the Department of Economic Affairs, Multilateral Institutions Division and the Comptroller and Auditor General (C&AG), of the Government of India. The guidelines direct the financial reporting templates that all ADB-assisted projects in India need to maintain.

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<sup>10</sup> Government of West Bengal. Public Health Engineering Department. 2011. *Vision 2020: To provide Safe, Sustainable and Adequate Water Supply to All Humans and Livestock in West Bengal by 2020*. Kolkata.

<sup>11</sup> Government of West Bengal. Finance Department. 1990. *Government Accounting Rules*. Kolkata.

22. **Segregation of duties.** The organizational system of PHED ensures adequate segregation of duties, with the works division responsible for ordering, the administration division responsible for receiving, and the accounts division responsible for payments. In the division, all important activities like authorization, recording, payments, and reconciliations are segregated and carried out by different officers. PHED created the PMU as a separate and distinct cell, wholly responsible for the implementation of the project.

23. **Budgeting division.** The annual financial statement (the budget), which is a statement of the estimated receipts and expenditure of the state in respect of a financial year, is laid before the Legislature under Article 202 of the Constitution of India. The Controller General of Accounts, Ministry of Finance, Government of India, in consultation with the C&AG of India has issued the list of major and minor heads of accounts of receipts and disbursements of the central and state governments. The GOWB through its finance department prepares its annual budget and lay it before the legislature of GOWB. The accounts division of PHED obtains information from other divisions and prepares the departmental budget. The engineer-in-chief is responsible for the departmental budget preparation, which the principal secretary and the minister-in-charge approve. PHED then submits the departmental budget to the Finance Department of GOWB for approval and the Finance Department consolidates and places before the Legislative Assembly for voting and approval. The budget of the project using the specified budget heads will follow the same procedure. The project director will be responsible for preparing the budget for the project, which he shall submit to the engineer-in-chief, PHED, for approval.

24. The budget approvals and the actual payments are monitored through the integrated financial management information system. The budget, the actual spending, and the issuance of utilization certificates are audited by the Internal Audit Department of GOWB and by the Office of the Comptroller and Auditor General of the Government of India.

25. **Payments.** PHED makes payments against invoices and other supporting documents submitted for payments to the accounts division. There is an established procedure for making payments through the Treasury of the GOWB. All payments follow the provisions of (i) the West Bengal Financial Rules (1979, as amended until date); (ii) the West Bengal Treasury Rules (2005); and (iii) the Delegation of Financial Power Rules (1977, as amended until date). The payments for the project will follow the same established procedure.

26. **Cash and bank.** PHED operates bank accounts through the treasury of the GOWB. The accounts division of PHED is responsible for reconciliation with accounting records and treasury records. All receipts and payments for the project will be through the treasury against the codified account heads that the Finance Department will allow for the implementation of the project. The PFAU of the project will be responsible for preparing withdrawal applications, accounting for all payments, receipts of loan funds, and reconciliation between Treasury and release of funds by the Reserve Bank of India.

27. **Safeguard of assets.** The records of PHED's fixed assets are maintained at the executing divisions and circles. PHED maintains adequate asset registers (tools and plants register) and available procedures guide the annual verification of the assets. Assets are not covered by insurance policies. Reconciliation of records after the annual verification with asset registers or the control accounts does not always take place. Adequate asset registers shall be maintained by the PMU, and its PFAU will be responsible for maintaining detailed records of capital work in progress and assets completed under the project.

28. **Contract management and accounting.** The officers at sub-divisions, districts, and zones are responsible for maintaining all records of PHED related to contracts, procurement, and accounts. For the project, the PMU shall maintain all records including accounting records, and contracts, which will enable ADB and PHED to monitor contracts effectively, and details of related payments.

29. **Internal audit.** PHED does not prepare separate financial statements. All receipts and payments by PHED get accounted in the GOWB's Annual Financial Statements using the established account heads and codes. The Finance (Internal Audit) Department of GOWB conducts the internal audit of PHED on a periodic basis.<sup>12</sup> The audit follows the timeline that the Finance Department specifies for internal audit in each department. It is understood there are no regular internal audits of the GOWB departments.

30. PHED will strengthen the internal audit process by appointing qualified staff or deploying firms of auditors to carry out a risk-based internal audit annually on project financial statements to ensure the establishment of internal controls as per ADB's guidelines.

31. **External audit.** The Accountant General (Accounts and Entitlement) of the GOWB compiles the accounts of receipts and disbursements. The latest accounts available from the auditor general are for the fiscal year (FY) 2015–2016. The Office of C&AG of India is responsible for the audit of the GOWB, including PHED, under Article 151(2) of the Constitution. This includes an audit of all operations that PHED manages. This audit report concerning the entire GOWB is placed before the State Legislature. The latest completed and published audit report by the C&AG is for FY2014–2015. PHED will report on the receipts and disbursements under the project using the established account heads and codes, which will get reflected in the Annual Financial Statements of GOWB. The C&AG will conduct the audit of PHED including the receipts and disbursements of the project.

32. The PFAU under PMU will prepare a separate set of annual financial statements for the implementation of the project only.<sup>13</sup> The C&AG will separately audit and report on the project annual financial statements within 6 months from the close of the financial year.

33. **Reporting and monitoring.** PHED prepares periodic reports as required for various schemes and projects. The PMU shall prepare quarterly progress reports for submission to ADB detailing the physical and financial progress of the project. The PMU will also create adequate structures for proper project performance monitoring and reporting. Reporting will be quarterly and annually. The financial reports shall compare actual expenditure with budget allocations. Variance analysis shall be undertaken for proper management of the budgetary control system.

34. **Information systems.** The accounting division of PHED uses computerized accounting systems developed for the Government Accounting System. It fulfills the present needs of PHED. For preparing separate financial statements for the project, the PMU will install an appropriate stand-alone accounting system for cash-based double entry system of accounting for the project's receipts and payments.

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<sup>12</sup> The Internal Audit Wing of the Finance Department of the Government of West Bengal was set up in November 1998 by a Finance Department Resolution no.7959-F dated. 20 November 1998. The responsibilities of the section include conducting internal audit and special audit in all departments, directorates of the state government and their subordinate and regional offices, and companies owned and controlled by state government undertakings.

<sup>13</sup> Using the guidelines issued in Letter No. 5/2/2010-ADB-I dated 2 September 2013, by the Department of Economic Affairs, Multilateral Institutions Division and C&AG applicable for all externally aided projects in India.

## F. RISK ASSESSMENTS

35. The financial management assessment considered two types of risks, (i) inherent risks, i.e., risks outside the direct control of the entity's financial management; and (ii) control risks, i.e., risks concerning the internal functioning and control of the entity's accounts division. The following key risks have been identified.

**Table 1: Financial Management Inherent and Control Risk Assessment**

Risk Type	Risk Assessment	Proposed Mitigation Measures
<b>A. Inherent Risk</b>		
1. Country-Specific Risks (India)	<p><b>Low</b></p> <ul style="list-style-type: none"> <li>The financial management capacity and auditing standard in India are sound</li> <li>India has a strong accounting profession, although the accounting is done on a cash basis in most levels of the government</li> </ul>	<ul style="list-style-type: none"> <li>Not applicable</li> </ul>
2. Entity-Specific Risks, Government of West Bengal (GOWB)	<p><b>Moderate</b></p> <ul style="list-style-type: none"> <li>There is a strong institutional mechanism and legislative framework for budgeting, accounting, and auditing in a time-bound manner</li> <li>However, there are no water user charges or tariff levied in the state of West Bengal. Costs related to water supply are covered by allocating revenues from tax revenues and other funds</li> </ul>	<ul style="list-style-type: none"> <li>The GOWB will issue a government order on the AMSDF to the project <i>gram panchayats</i> enabling them to levy regular water user charges on water supply to recover at least operation and maintenance (O&amp;M) costs</li> <li>Financial projections to identify realistic and appropriate user charges revisions need to be prepared</li> </ul>
3. Project-Specific Risks	<p><b>Substantial</b></p> <ul style="list-style-type: none"> <li>The Public Health Engineering Department (PHED) is responsible for rural water supply in the state of West Bengal. PHED meets O&amp;M costs out of budgetary allocations from the GOWB. <i>gram panchayats</i> coordinate with PHED for water supply within the <i>gram panchayat</i> jurisdiction. An earlier practice to levy water user charges on a monthly basis was discontinued as the collections became irregular. <i>Gram panchayats</i> maintain the water supply assets using the untied funds devolved and available</li> </ul>	<ul style="list-style-type: none"> <li>The GOWB issued a government order on 9 November 2017 on the asset management and service delivery framework (AMSDF) to the project <i>gram panchayats</i> enabling them to levy regular user charges on water supply to recover operational costs</li> <li>Establishment of a strong legal, institutional, and financial arrangement and agreement on sharing the O&amp;M costs between PHED and <i>gram panchayats</i></li> <li>Government commitment to the O&amp;M budget allocation at both PHED and <i>gram panchayat</i> levels</li> </ul>

Risk Type	Risk Assessment	Proposed Mitigation Measures
	<ul style="list-style-type: none"> <li>• Under the project, PHED will supply water up to overhead storage reservoirs, and <i>gram panchayats</i> will be responsible for distribution, house connections, and metering. <i>Gram panchayats</i> will levy a flat monthly user charge for the operation of assets developed under the project's AMSDF</li> <li>• If there is a delay in levying water user charges or if the GOWB decides not to levy any user charge, <i>gram panchayats</i> may have financial difficulties in covering O&amp;M costs</li> </ul>	
<b>Overall Inherent Risk</b>	<p style="text-align: center;"><b>Moderate</b></p> <p>While entity-specific risks exist, these risks might be mitigated through implementation of the AMSDF and efforts of the GOWB, PHED, and other related government administrative units with the support of ADB. The GOWB needs to support PHED and <i>gram panchayats</i> in achieving financial sustainability by implementing and continuing the water user charge structure and implementing user charge revisions on a regular basis</p>	
<b>B. Control Risk</b>		
1. Implementing Entity	<p style="text-align: center;"><b>Low</b></p> <ul style="list-style-type: none"> <li>• PHED is a full-fledged department of the GOWB under a Minister-in-Charge</li> <li>• PHED is currently implementing one JICA-financed project and has handled several projects financed by the Government of India and the GOWB</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> </ul>
2. Flow of Funds and Budget Allocation	<p style="text-align: center;"><b>Moderate</b></p> <ul style="list-style-type: none"> <li>• The GOWB will receive ADB loans in Indian rupees from the Government of India</li> <li>• The GOWB will allocate ADB loans and its counterpart funds to PHED using the established budgetary mechanism</li> <li>• Disclosure of funds flow, allocation, and yearly utilization will be available in a transparent manner in the public domain as a part of the disclosure requirements</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> </ul>
3. Staffing	<p style="text-align: center;"><b>Low (PHED)</b></p> <ul style="list-style-type: none"> <li>• All officers within PHED are permanent staff but are transferable within the divisions for regular rotation of duties</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> </ul>

Risk Type	Risk Assessment	Proposed Mitigation Measures
	<ul style="list-style-type: none"> <li>• Staff within the accounts division of PHED are from the Finance Department of the GOWB</li> </ul> <p style="text-align: center;"><b>Significant (PMU)</b></p> <ul style="list-style-type: none"> <li>• The GOWB created the PMU and three PIUs under PHED for the project. PHED appointed the project director and few engineers for the PMU</li> <li>• The GOWB is yet to complete staffing of other sections of the PMU including the PFAU and the other two PIUs</li> <li>• Delays in staffing the PMU, PFAU, and PIUs may hamper the effective implementation of the project</li> </ul>	<ul style="list-style-type: none"> <li>• The GOWB needs to fill the necessary positions and deploy officers before the loan effectiveness</li> </ul>
4. Accounting Policies & Procedures	<p style="text-align: center;"><b>Moderate</b></p> <ul style="list-style-type: none"> <li>• PHED follows the government accounting system and PMU will follow the same system for the project</li> <li>• The PMU will also prepare separate annual project financial statements for the projects and report as per the agreement with ADB.</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> </ul>
5. Internal Audit	<p style="text-align: center;"><b>Substantial</b></p> <ul style="list-style-type: none"> <li>• The Finance (internal audit) Department of the GOWB is entrusted the internal audit of all departments of the GOWB, including PHED</li> <li>• As of September 2017, the practice of internal audit is irregular in the GOWB including PHED</li> </ul>	<ul style="list-style-type: none"> <li>• PMU will appoint qualified staff or hire firms of auditors to carry out the risk-based internal audit of the project</li> </ul>
6. External Audit	<p style="text-align: center;"><b>Low (PHED)</b></p> <ul style="list-style-type: none"> <li>• PHED does not prepare separate financial statements. All receipts and payments are accounted by PHED using the established account heads and codes</li> <li>• The GOWB's Annual Financial Statements, including financial statements of PHED, are prepared by the Accountant General (Accounts and Entitlement) of the GOWB</li> <li>• The Comptroller and Auditor General are responsible for the external audit of the GOWB as a</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> </ul>

Risk Type	Risk Assessment	Proposed Mitigation Measures
	<p>whole, including PHED. The latest completed audit of the GOWB by the Comptroller and Auditor General is for FY2014–2015</p> <p style="text-align: center;"><b>Low (PMU)</b></p> <ul style="list-style-type: none"> <li>• PMU will prepare separate project annual financial statements using the existing guidelines applicable for all externally aided projects in India</li> <li>• The Comptroller and Auditor General will audit and report on the project annual financial statements of the project</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> </ul>
7. Reporting and Monitoring	<p style="text-align: center;"><b>Low (PHED)</b></p> <ul style="list-style-type: none"> <li>• PHED maintains a management information system as required under reporting and monitoring formalities</li> <li>• PHED's budget, accounting, and audit information are available in the public domain as necessary under the disclosure requirements</li> </ul> <p style="text-align: center;"><b>Moderate (PMU and PIUs)</b></p> <ul style="list-style-type: none"> <li>• The PMU needs to prepare quarterly and annual progress reports for reporting financial and physical progress of the project</li> <li>• Proper project monitoring systems are required for producing the desired reporting structure of the project</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> <li>• The reporting and monitoring formalities required for the project need to be established as part of the project implementation</li> </ul>
8. Information Systems	<p style="text-align: center;"><b>Low (PHED)</b></p> <ul style="list-style-type: none"> <li>• The system in operation suits the PHED's requirements. A backup procedure is also in place</li> </ul> <p style="text-align: center;"><b>Moderate (PMU)</b></p> <ul style="list-style-type: none"> <li>• The PMU will install the necessary systems for recording and reporting of project activities</li> <li>• The financial reporting system will have links to the financial information systems of individual projects</li> </ul>	<ul style="list-style-type: none"> <li>• Not applicable</li> <li>• Not applicable</li> </ul>
<b>Overall Control Risk</b>	<p style="text-align: center;"><b>Moderate</b></p> <p>Some financial management risks are recognized, but not all of them are substantial. However, delays in staffing the PMU and establishing appropriate internal controls may hamper the effective implementation of</p>	

Risk Type	Risk Assessment	Proposed Mitigation Measures
	the project. The initial support and capacity development for PHED and PMU staff on ADB procedures will be implemented with the support of qualified and experienced PMC.	

ADB = Asian Development Bank, AMSDF = asset management and service delivery framework, GOWB = Government of West Bengal, JICA = Japan International Cooperation Agency, operation and maintenance = O&M, PFAU = project finance and accounting unit, PHED = Public Health Engineering Department, PIU = project implementation unit, PMU = project management unit.

## G. STRENGTHS AND WEAKNESSES

36. **Strengths.** A significant strength of the financial management systems of PHED is that they have experience in handling large-scale projects with substantial values. In addition, PHED has an established legal, institutional, and monitoring framework available for budgeting, accounting, and auditing.

37. **Weaknesses.** The following weaknesses in the financial management system have been identified and need to be addressed:

- (i) limited experience of PHED in implementing and managing externally funded projects may cause delays in the implementation of the project;
- (ii) inadequate staff in the accounts and finance sections of the PMU may hamper the timely preparation and submission of periodical financial reports;
- (iii) weak internal audit system in the PMU may result in backlogs in the preparation of project financial statements; and
- (iv) lack of overall water tariff structure in the state may constrain the medium and long-term financial sustainability of PHED and project *gram panchayats*.

## H. PROPOSED TIME-BOUND ACTION PLAN

38. The actions agreed and set out in Table 2 are noted as an action plan to address issues that the financial management assessment identified in the PMU.

**Table 2: Time-Bound Action Plan**

Area	Current Scenario	Risk	Mitigation Measures	Responsibility	Target Date
Managing externally assisted projects	Limited experience of PHED in implementing and managing externally funded projects	This may cause delays in the effective implementation of the project	Extending full training and capacity building support, developing a manual, and conducting periodic workshops with the help of PMCs to enhance the financial management capacity of PMU and PIUs	PHED	April 2018
Staffing	Inadequate staff in the accounts and finance	This will hamper the timely preparation and submission of	Strengthening the accounts and finance sections of the PMU and PIUs	PHED	June 2018

Area	Current Scenario	Risk	Mitigation Measures	Responsibility	Target Date
	sections of the PMU	periodical financial reports	by engaging qualified staff for the timely preparation of financial reports		
Internal audit	Need to strengthen internal audit system in the PMU	This may result in backlogs in the preparation of project financial statements	Strengthening the internal audit process by appointing qualified staff or outsourcing to experienced audit firms	PHED	June 2018
Financial Sustainability	No overall approved water user charges or tariff structure in the state	This may constrain PHED and <i>gram panchayats</i> from achieving medium and long-term financial sustainability	Implementing a water user charge structure and regular user charge revisions by the project GPs through the asset management and service delivery framework	PHED <i>gram panchayats</i>	September 2020

PHED = Public Health Engineering Department, PMC = project management consultants, PMU = project management unit, WBDWSIP = West Bengal Drinking Water Sector Improvement Project.