



Asian Development Bank

19 November 2009

Dr. Anup K. Pujari  
Joint Secretary (MI)  
Department of Economic Affairs  
Ministry of Finance  
North Block, New Delhi  
India

Facsimile Number: (91-11) 2309-2039

Dear Dr. Pujari:

**Loan No. 2528-IND: North Eastern Region Capital Cities Development Investment Program—Project 1 – FINANCIAL REPORTING AND AUDITING REQUIREMENTS**

1. This letter is to ensure your timely compliance with the loan covenants and the quality of financial information as required by ADB. Please refer to ADB's Handbook for Borrowers on the Financial Governance and Management of Investment Projects Financed by the ADB ([http://www.adb.org/Documents/Handbooks/Borrowers\\_Fin\\_Gov\\_Mgt\\_Investment/default.asp](http://www.adb.org/Documents/Handbooks/Borrowers_Fin_Gov_Mgt_Investment/default.asp)) for guidance.
2. ADB, by its Charter, is required to ensure that the proceeds of any loan made, guaranteed, or participated in by ADB are used for the purposes for which the loan was approved. ADB requires accurate and timely financial information from its borrowers to be assured that expenditure was for the purposes stated in the loan agreement.
3. For this particular loan, the requirements are stipulated in Section 4 and Schedule 5 of the Loan Agreement dated 4 August 2009 between ADB and India and Sections 2.09 and 2.10 of the respective Project Agreements. Please provide copies of the Loan / Project Agreements to the Executing Agencies (EAs) and the auditor(s), together with a copy of this letter.
4. The following are the main requirements:
  - (i) ADB requires the EAs to maintain separate project accounts and records exclusively for the Project to ensure that the loan funds were used only for the objectives set out in the Loan or Project Agreements. The project accounts comprise the following:
    - Statement of Accounting/Financial Policies
    - Statement of Income/Cash Receipts
    - Statement of Expenses/Cash Payments
    - Cash Flow Statement
    - Imprest Account Statement
    - Statement of Expenditures (SOE), and
    - Notes to the Financial Statements

Please refer to Attachment 1 for the purpose of each accounting statement. We will send a typical format for each statement in due time.

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The first set of project accounts to be submitted to ADB covers the fiscal year ending 31 March 2010. As stipulated in the Project Agreement, they are to be submitted up to nine months after the end of the fiscal year. For this loan, the deadline is by 31 December 2010.

- (ii) The accounts and records for the project are to be consistently maintained by using sound accounting principles. Please stipulate that your external auditor is to express an opinion on whether the financial report has been prepared using international or local generally accepted accounting standards and whether they have been applied consistently.

ADB prefers project accounts to use international accounting standards prescribed by the International Accounting Standards Committee. Please advise your external auditor to comment on the impact of any deviations, by the EAs from international accounting standards.

- (iii) Please ensure that your external auditor specifies in the Auditor's Report the appropriate auditing standards they used, and direct them to expand the scope of the paragraph in the Auditor's Report by disclosing the key audit procedures followed. Your external auditor is also to state whether the same audit procedures were followed for all supplementary financial statements submitted.

ADB wishes that auditors conform to the international auditing standards issued by the International Federation of Accountants. In cases where other auditing standards are used, request that your external auditor to indicate in the Auditor's Report the extent of any differences and their impact on the audit.

- (iv) The external auditor's opinion is also required on whether
- the proceeds of the ADB's loan have been utilized only for the project as stated in the Loan Agreement;
  - the financial information contains data specifically agreed upon between India and ADB to be included in the financial statements;
  - the financial information complies with relevant regulations and statutory requirements;
  - compliance has been met with all the financial covenants contained in the Loan or Project Agreements;
  - Imprest Account/Second Generation Imprest Account(s) funds have been correctly accounted for; and
  - documents and controls on the use of the SOE procedure are adequate.

Please refer to Attachment 2 for a model Audit Opinion for a non-revenue earning project.

- (v) The Auditor's Report is to clearly state the reasons for any opinions that are qualified, adverse, or disclaimers.
- (vi) Actions on deficiencies disclosed by the external auditor in its report are to be resolved by the Ministry of Finance and/or the EAs within a reasonable time. The external auditor is to comment in the subsequent Auditor's Report on the adequacy of the corrective measures taken by the Ministry of Finance and/or the EAs.

5. ADB also requires auditors to provide a Management Letter with reference to the EA. This is a report on the internal controls and operating procedures of the entity, covering all aspects included during the normal course of the audit. This should be submitted together with the audited project accounts.

6. Compliance with these ADB requirements will be monitored by review missions and during normal project supervision, and followed up regularly with all concerned, including the external auditor.

Yours sincerely,



Hun Kim  
Director, Urban Development Division *ABS*  
South Asia Department

Attachments: as stated

cc: DEA/MOF:  
Ms. Anuradha Thakur, Director (ADB-I), Fax No. +91-11-2309-2477  
Mr. S. Kumar Singh, Under Secretary (MI-VIII), DEA/MOF, Fax No. +91-11-2309-2229

National EA:  
Mr. A.K. Mehta, Joint Secretary, MOUD, Fax No. +91-11-2306-2477  
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Mr. A. Joshi, Director (UD), MOUD, Fax No. +91-11-2306-1137

State level EAs:  
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Mr. T. Bhutia, Commissioner-cum-Secretary, UDHD, Government of Sikkim, Fax No. +91 03592-202726  
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Mr. Bishwajit Dutta, Project Director, SIPMIU (Shillong), UAD, Government of Meghalaya,  
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Mr. Valbuanga, Project Director, SIPMIU (Aizawl), UP&PAD, Government of Mizoram,  
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Mr. R.K. Majumder, Project Director, SIPMIU (Agartala), UDD, Government of Tripura,  
Fax No. +91 0381 232 9301/5149

ADB:  
T. Kondo, Country Director, INRM, Fax No. +91-11-2687-0955

## Accounting Statements and Financial Reports

Accounting Statements	Non-Revenue-Earning Projects and Executing Agencies (PIUs)		Revenue-Earning Projects and Executing Agencies (PIUs)	
	Interim (PMRs)	Annual Audited	Interim (PMRs)	Annual Audited
Statement of Accounting/Financial Policies	...	✓	...	✓
Statement of Income (Cash Receipts)	✓	✓	...	...
Statement of Expenses (Cash Payments)	✓	✓	...	...
Cash Flow Statement	✓ note (i)	✓ note (i)	✓	✓
Imprest Account Statement	✓	✓	✓	✓
Statement of Expenditures (SOE)	✓	✓	✓	✓
Income Statement	These statements are usually not prepared, as most non-revenue-earning projects currently use the cash basis of accounting		✓	✓
Balance Sheet			✓	✓
Notes to the Financial Statements	✓ note (ii)	✓ note (ii)	✓ note (i)	✓ note (i)
Other Information	✓ note (iii)	✓ note (iii)	✓ note (iii)	✓ note (iii)

- (i) The content and format of Cash Flow Statements for non-revenue-earning projects (and EAs) will not necessarily conform to international accounting standards or to national accounting standards.
- (ii) The notes to the financial statements provide further breakdowns or explanations of the information provided in the main financial statements.
- (iii) The scope and nature of other information provided will be negotiated between ADB and the borrower.

## Statement of Accounting or Financial Policies

5.3.3.4. As discussed in section 5.2.3, and irrespective of whether the cash or accrual basis of accounting is used, a clear statement of the accounting or financial policies that underlie the accounting statements must be provided.

## Statement of Income (or Cash Receipts)

5.3.3.5. Shows the year's complete financial information, and cumulative data from project start-up to date. Where the cash basis of accounting is followed, the opening and

closing cash balances should be shown. ADB financing should be subdivided as follows when ADB disburses via SOE procedures: (i) by expenses category in the loan agreement, RRP or revisions thereto; (ii) disbursements via SOE; and (iii) other methods.

### Statement of Expenses (or Cash Payments)

5.3.3.6. Shows the year's financial information, and cumulative totals from project start-up to the current date. Where the accrual basis of accounting is used, this statement will include non-cash items, such as depreciation.

### Cash Flow Statement

5.3.3.7. The Cash Flow (or project funds) Statement should include:

- Sources of project financing (for example, ADB, Government contribution, etc.), and by methods of disbursement by ADB (for example, direct payment, imprest account, etc.)
- Uses of funds summarized under project disbursement categories as per the loan agreement (for example: equipment, civil works, consultant services and training, and "Other" which may be further subdivided following start of project implementation)
- The opening and closing cash balances; and
- In accordance with IAS 7, separate disclosure is required of funds that are not available for use, such as confirmed future commitments.

### Imprest Account Statement

5.3.3.8. This statement summarizes ADB's advances and replenishments, less amounts withdrawn by the project entity, showing the remaining cash balance in the Imprest Account.

5.3.3.9. Bank statements should be provided by each local bank that is selected to operate each imprest account, where these are in use for the project. Each bank statement should summarize the current year's advances and replenishments, interest earned on balances; less withdrawals for project expenditures. The first account is used to receive money from ADB for the credit of the "Project Imprest Account", and the second may be used by the project for local operating purposes ("Second Generation Imprest Account"). The Project Imprest Account is to be used to replenish the SGIA, when this is in use. It will be necessary to attach "Reconciliation Statements" to reflect in-transit items between ADB and the Imprest Account and between Imprest Account and the SGIA. (Replenishment made by ADB not yet received; and reimbursements to the SGIA

from the Imprest Account not yet received by it). The third financial statement is a detailed statement of transactions of the Imprest Account's Operating Account(s). This is to be generated by the EA, where the Imprest Account is used to make direct payments in local and foreign currency.

### Statement of Expenditures (SOE)

5.3.3.10. The Statement of Expenditures (SOE) procedure is an ADB reimbursement procedure that does not require submission of supporting documentation. The SOE form should include certification, confirming existence of registration for mobilization and secured advances/deposits. The ADB Loan Disbursement Handbook describes the use of this method and associated reporting and auditing procedures.

### Income Statement and Balance Sheet

5.3.3.11. These statements may not be necessary where cash accounting is used. These statements are described in section 4.3.4 (*Preparing Financial Tables*).

### Notes to Financial Statements

5.3.3.12. The EA should provide Notes to the financial statements. These should be explanatory notes and/or supplementary financial statements that analyze or qualify important heads of account, or that present the information in conformity with generally accepted accounting practices of the country.

5.3.3.13. For example, if Statements are prepared on a "cash basis", information may be required from the EA to convert key items to an "obligation" or "accrual" basis and ADB, therefore, may seek details relating to obligations (unpaid commitments and accounts receivable) in supplementary statements. Similarly, details may also be required to distinguish between transactions relating to capital (development) investments and operating expenditures.

### Other Information

5.3.3.14. ADB wishes to receive financial reports on a project that illustrate both performance in the fiscal year under review and accumulated transactions from project commencement particularly with regard to sources of funds and expenditures for assets and inventories.

5.3.3.15. Reporting practices in some government entities require only disclosure of annual financial transactions against annual budget authorizations. Therefore, in order

to monitor performance from start-up throughout the project's implementation period, the reported results of project transactions and financial performance data for previous fiscal years should be included as memorandum entries in a current fiscal year's Statement of Income (or Cash Receipts) and Statement of Expenses (or Cash Payments).

5.3.3.16. Alternatively, the reported results of prior years may be included in the annual financial statements as of the last day of the reporting fiscal year, that summarizes and classifies all receipts and expenditures relating to the project from its commencement. In addition, the accumulated sources or provision of funds for the project in the ratio agreed upon between the borrower and ADB should be disclosed in the Notes to the financial statements.

### 5.6.3.1. Model Audit Opinion for a Non-Revenue-Earning Project

To: Borrower (or designated agency)

We have audited the accompanying financial statements (pages \_\_\_\_ to \_\_\_\_ ) of the \_\_\_\_\_ Project financed under the Asian Development Bank Loan # \_\_\_\_\_ as of December 31, 20\_\_\_\_, and for the year then ended.

These financial statements are the responsibility of the management of the \_\_\_\_\_ EA.

Our responsibility is to express an opinion on the accompanying statements based on our audit.

We conducted our examination in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of misstatement. Our audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our audit also includes assessing the accounting principles and significant estimates made by management, as well as evaluating the overall statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The \_\_\_\_ (EA's) policy is to prepare the accompanying statements in the format agreed between the Asian Development Bank and the Government of \_\_\_\_\_ as noted in the Minutes of Negotiations for the Loan, [on a cash receipts and disbursements basis in which cash is recognized when received and expenses are recognized when paid, rather than when incurred] / [on an accruals basis in which expenses are recognized when incurred and revenue is reported when income is due.]

In our opinion, (A) the aforementioned financial statements and appended notes that were also the subject of the audit, fairly present in all material respects the financial position of the \_\_\_\_\_ project as at \_\_\_\_\_ 20\_\_ and the results of its operations for the year ended \_\_\_\_\_ 20\_\_, in conformity with \_\_\_\_\_ accounting standards, applied on a basis consistent in all material respects with that of the previous year; (B) the [Borrower] [EA] has utilized all proceeds of the loan withdrawn from the Asian Development Bank only for purposes of the Project as agreed between the Asian Development Bank and [the Borrower] in accordance with the Loan Agreement; and no proceeds of the loan have been utilized for other purposes; and (C) the [Borrower] [EA] was in compliance as at the date of the balance sheet of the year of audit with all financial covenants of the Loan Agreement.



In addition:

- (a) (1) With respect to Statements of Expenditures, adequate supporting documentation has been maintained to support claims to the Asian Development Bank for reimbursements of expenditures incurred; and (2) which expenditures are eligible for financing under Loan Agreement No. \_\_\_\_\_.
  - (b) (1) The Imprest Accounts (page \_\_) give a true and fair view of the receipts collected and payments made during the year ending \_\_\_\_\_; and (2) these receipts and payments support Imprest Account liquidations/replenishments during the year.
- [(a) and (b), above, are to be provided where the Loan Agreement requires separate Imprest Account and Statement of Expenditures audits and audit opinions.]