

## EXECUTIVE SUMMARY

### A. Introduction

Republic Act (R.A.) 6234 dated June 19, 1971 created Metropolitan Waterworks and Sewerage System (MWSS) to ensure an uninterrupted and adequate supply and distribution of potable water for domestic and other purposes at just and equitable rates. Based on its original Charter, the MWSS has jurisdiction, supervision and control over all waterworks and sewerage systems within Metro Manila, the entire province of Rizal and a portion of Cavite. R.A. No. 8041 or the National Water Crisis Act of 1995 and implemented by Executive Order No. 286 on December 6, 1995 and Executive Order No. 311 on March 20, 1996 allowed the MWSS to enter into arrangements that will result in the involvement and participation of the private sector in any or all of the segments, operations and/or facilities of the MWSS.

On February 21, 1997, the retail distribution of water was privatized through the Concession Agreement (CA) entered into with Manila Water Company, Inc. (East Zone) and Maynilad Water Services, Inc. (West Zone) while on January 15, 2016, the Luzon Clean Water Development Corporation entered into a CA with MWSS for the Bulacan Bulk Water Supply Project (Province of Bulacan).

Currently, the Chairman of the MWSS Board of Trustees is PLTGEN Reynaldo V. Velasco (Ret.) PhD., who is also the concurrent Officer-in-Charge Administrator of MWSS Corporate Office. The Chief Regulator of the MWSS Regulatory Office is Atty. Patrick Lester N. Ty.

### B. Scope and Objectives of Audit

The audit covered the examination, on test basis, of the accounts and transactions of the MWSS for CY 2020 and 2019 and was conducted in accordance with the International Standards of Supreme Audit Institutions.

The audit was conducted to determine (a) the level of assurance that may be placed on the Management's assertions on the financial statements, to enable the Auditor to render an opinion on the fairness of presentation of the financial statements; (b) the propriety of transactions and compliance with existing rules and regulations as well as Management's policies; and (c) the extent of the implementation of prior years' audit recommendations.

### C. Financial Highlights

#### Financial Position

|             | 2020            | 2019<br>(As restated) | Increase<br>(Decrease) |
|-------------|-----------------|-----------------------|------------------------|
| Assets      | 217,440,289,534 | 58,559,345,409        | 158,880,944,125        |
| Liabilities | 169,228,708,999 | 11,193,367,307        | 158,035,341,692        |
| Equity      | 48,211,580,535  | 47,365,978,102        | 845,602,433            |

## Results of Operations

|                                 | 2020            | 2019            | Increase<br>(Decrease) |
|---------------------------------|-----------------|-----------------|------------------------|
| Revenue                         | 2,580,822,917   | 4,180,994,412   | (1,600,171,495)        |
| Current Operating Expenses      | (1,436,061,156) | (1,617,452,879) | (181,391,723)          |
| Surplus from Current Operations | 1,144,761,761   | 2,563,541,533   | (1,418,779,772)        |
| Other Non-Operating Income      | 14,365          | 92,800,986      | (92,786,621)           |
| Gains                           | 403,766,880     | 294,423,192     | 109,343,688            |
| Losses                          | (946,050)       | (17,878,619)    | 16,932,569             |
| Income Tax Expense              | (14,530,467)    | (11,983,161)    | 2,547,306              |
| Net Surplus                     | 1,533,066,489   | 2,920,903,931   | (1,387,837,442)        |

The increase in total assets pertains to the initial recognition of the *Concession Assets* acquired and/or developed by the concessionaires after the commencement of the Concession Agreement in 1997 amounting to P194.872 billion with the related accumulated depreciation of P37.020 billion or a net carrying amount of P157.853 billion; and the increase in liability pertains to the corresponding increase in the *Deferred Service Concession Revenue* account which represents the unearned portion of the revenue arising from the exchange of assets between the MWSS and the Concessionaires by the end of the service concession agreement amortized yearly over the economic substance of the arrangement. This was the subject of an audit observation and one of the bases for the adverse opinion for CYs 2020 and 2019.

Further, the decrease in the Revenue account pertains to the decline in the concession fees received from the Concessionaires that are intended for MWSS loan amortization and payments to contractors/suppliers amounting to P1.226 billion and P434 million, respectively.

### D. Auditor's Opinion

The Auditor rendered an adverse opinion on the fairness of presentation of the financial statements of MWSS for the year ended December 31, 2020 and 2019 due to the following:

1. Service Concession Assets (SCA) and Deferred Service Concession Revenue with carrying amounts of P157.852 billion and P156.884 billion, respectively, as at December 31, 2020 are not supported with details and supporting documents, and the 2019 financial statements are materially misstated due to non-restatement of the opening balances of net assets/equity accounts which adversely affected the faithful representation of the said accounts in the financial statements for 2020 and 2019, contrary to International Public Sector Accounting Standards (IPSASs) 1, 3 and 32;
2. Various errors and deficiencies in the Property, Plant and Equipment (PPE) account with carrying amount of P20.437 billion contrary to the pertinent provisions of IPSASs 1, 17 and 21, resulting to material misstatements of PPE and other affected accounts by undetermined amounts, which include the following: a) incomplete physical inventory of Property, Plant and Equipment (PPE) with carrying amount of P20.437 billion and non-submission of Physical Inventory Report (PIR) for CYs 2019 and 2020; b) absence of certificates of titles and proofs of ownership of land assets totaling P4.668 billion; c) non-existent, dilapidated, non-operational and/or abandoned Office Building and Other structures amounting to P5.117 billion as reported in CY 2018 PIR still carried in the books without impairment loss; and d) non-adjustment of Construction in Progress

consisting of completed projects to PPE amounting to P156.551 million;

3. Doubtful collectability of various dormant receivables amounting to P4.255 billion, without provision for impairment loss, contrary to IPSAS 26 resulting to misstatement of receivables and related accounts by undetermined amounts; and
4. Assets and liabilities amounting to P574.475 million and P884.548 million, respectively, included in various assets and liabilities accounts in the financial statements as of December 31, 2020 were unaccounted and undocumented, contrary to IPSASs 1 and 21 and the Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities, resulting to misstatement of assets by undetermined amount and liabilities by P884.548 million.

For the above-mentioned observations which caused the issuance of an adverse opinion, we recommended that Management require:

1. *On Service Concession Assets/Deferred Service Concession Revenue*

- a. Finance Department to submit the pertinent reports and records requested to substantiate the initial recognition of Service Concession Assets (SCA) and Deferred Service Concession Revenue as enumerated in Part 2 of this report;
- b. Finance Department to restate the opening balances of net assets/equity accounts in the prior period financial statements presented on comparative basis with the current year financial statements and provide the required disclosure on the adoption of IPSAS 32; and
- c. Finance Department to perform a thorough analysis and validation of the Service Concession Assets and regularly monitor the subsequent events affecting the PPE accounts, upgrade on existing assets, impairment and depreciation of the SCA, including the General Administrative Equipment (GAE).

2. *On Property, Plant and Equipment*

- a. Asset Management Department (AMD) to conduct complete annual physical inventory and submit the CY 2020 Physical Inventory Report (PIR) and Inspection and Inventory of Unserviceable Properties (IIRUP) with identification and description of turned-over GAEs from the concessionaires and with analysis and reconciliation with the Accounting records
- b. AMD to account and secure the land titles in MWSS's name and institute procedures on proper safekeeping and custody of the land titles and determine the ownership of the 23 land titles under the custody of MWSS that were not recorded in the books;
- c. Finance Department to provide allowance for impairment losses to reflect the recoverable amount of the inexistent, dilapidated, non-operational and/or abandoned Office Building and Other structures with carrying amount of P5.117 billion;
- d. AMD and Finance Department to identify the decommissioned and abandoned deep wells with the structures thereon and determine the carrying amount of said properties for the recognition of impairment loss in the books as warranted; and

- e. Finance Department to reclassify the cost of completed projects to the appropriate PPE accounts and recognize the related depreciation expense reckoned from the date that the assets became operational;

### 3. *On Receivables*

Finance Department to:

- a. Provide allowance for impairment losses on the dormant Receivables to reflect the recoverable amounts;
- b. Analyze the dormant receivable accounts to determine if they are qualified for write-off under COA Circular No. 2016-005 and accordingly, request for authority to write-off from the Commission on Audit;
- c. Submit an updated report on the arbitration of the disputed claims with MWSI amounting to P4.048 billion together with all the supporting legal documents;
- d. Formulate a schedule of payment for the Guarantee Deposits and Debt Service and impose the collection of the amounts due from the Concessionaires;
- e. Analyze and reconcile the receivable account from the two Concessionaires and if a shortfall of collection is found, immediately enforce collection of the amount advanced by the MWSS to pay the matured loans; and
- f. Send demand letters on the Receivables from government agencies and Inactive Raw Water customers amounting to P5.005 million and P1.519 million, respectively.

### 4. *On Unreconciled/Unverified accounts*

Finance Department to provide allowance for impairment loss on the unaccounted and undocumented assets reported at P574.475 million and revert back the unaccounted and undocumented liabilities totaling P884.548 million to Accumulated Surplus/Deficit account.

## **E. Summary of Other Significant Audit Observations and Recommendations**

In addition to the above audit observations which were the bases for the rendition of an adverse opinion, the other significant audit observation and corresponding recommendations, the details of which are presented in Part II of this Report are as follows:

### ***MWSS Corporate Office***

1. The existence and validity of the Other Assets account amounting to P225.001 million cannot be ascertained due to the dormancy of the account and non-submission of supporting documents, hence, did not reflect the reasonable recoverable amounts, that affected the faithful representation of the asset accounts contrary to IPSASs 1 and 21.

Recommendations:

- a. Require the Finance Department to provide allowance for impairment losses to reflect the reasonable recoverable amounts;
  - b. Require the Finance Department to submit to the Commission on Audit a request for write-off of the dormant accounts, if the said accounts qualify for write-off;
  - c. Require the Legal Department to provide status of claims under government litigation, claims from AOs for cash shortage and garnished accounts; and
  - d. Require the Legal Department to identify all the persons liable for the necessary legal action of MWSS to recover its claims.
2. Unreconciled variance amounting P101.362 million between the book and bank balances of Cash in Bank account reported in the financial statements at P3.105 billion, due to non-preparation of Bank Reconciliation Statements (BRS) casts doubt on the validity and accuracy of the account balance contrary to paragraph 27 of IPSAS 1, COA Circular No. 2020-02, and Sections 74 and 122 of Presidential Decree (PD) No. 1445.

Recommendation:

Require the Finance Department to prepare and submit the periodic bank reconciliation statements for all the bank accounts and take up the necessary adjustments on the variances noted, including the closed PNB accounts with net amount of P171,964.10 to arrive at the correct balance of the Cash in Bank account.

***MWSS Regulatory Office***

1. The restricted fund amounting to P103.774 million intended for the payment of future arbitrations was recorded as non-current asset contrary to paragraph 76 (d) of IPSAS 1, thus affecting the fair presentation of the account in the financial statements.

Recommendation:

Require the Accounting Section to reclassify the restricted fund amounting to P103.774 million from Restricted Fund account to Cash and Cash Equivalents.

2. Lack of monitoring and appropriate action on the Notices of Disallowance (ND) with issued Notices of Finality of Decision (NFD) amounting to P78.509 million resulted to non-recovery of amounts due from persons liable for the said NDs contrary to Section 2.1 and Annex C of COA Circular No. 2020-002 and Section 7 of COA Circular No. 2009-006.

Recommendations:

- a. Require the Accounting Section to maintain and submit the subsidiary records of the persons liable for the subject NFD amounting to P78.509 million;

- b. Require the Accounting Section to reclassify the Due from Officers and Employees account amounting to P78.509 million to Receivables – Disallowances/Charges account;
- c. Require the Administration Department to formulate a policy on the settlement of disallowances with issued NFDs; and
- d. Cause the immediate recovery of the disallowances with issued NFD.

#### **F. Summary of Audit Suspensions, Disallowances and Charges**

Details are shown in Part II of this Report.

#### **G. Status of Implementation of Prior Years' Audit Recommendations**

MWSS Corporate Office - Out of the 145 audit recommendations, 14 were fully implemented, 28 were partially implemented and 103 were not implemented. The details are presented in the Status of Implementation of Prior Years' Audit Recommendations under Part III of this Report.

MWSS Regulatory Office - Out of the 18 audit recommendations, nine were fully implemented, one was partially implemented and 8 were not implemented. The details are presented in the Status of Implementation of Prior Years' Audit Recommendations under Part III of this Report.