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# Financial Management in ADB Sovereign Operations

01 May 2025

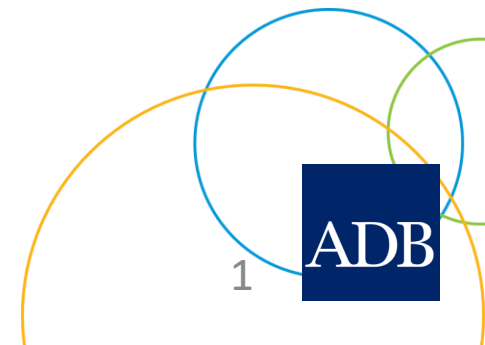
Islamabad, Pakistan



The ADB logo, consisting of the letters "ADB" in white serif font on a dark blue square background. The logo is positioned in the bottom right corner of the slide, with decorative vertical lines in green and blue extending upwards from the square.

# Agenda

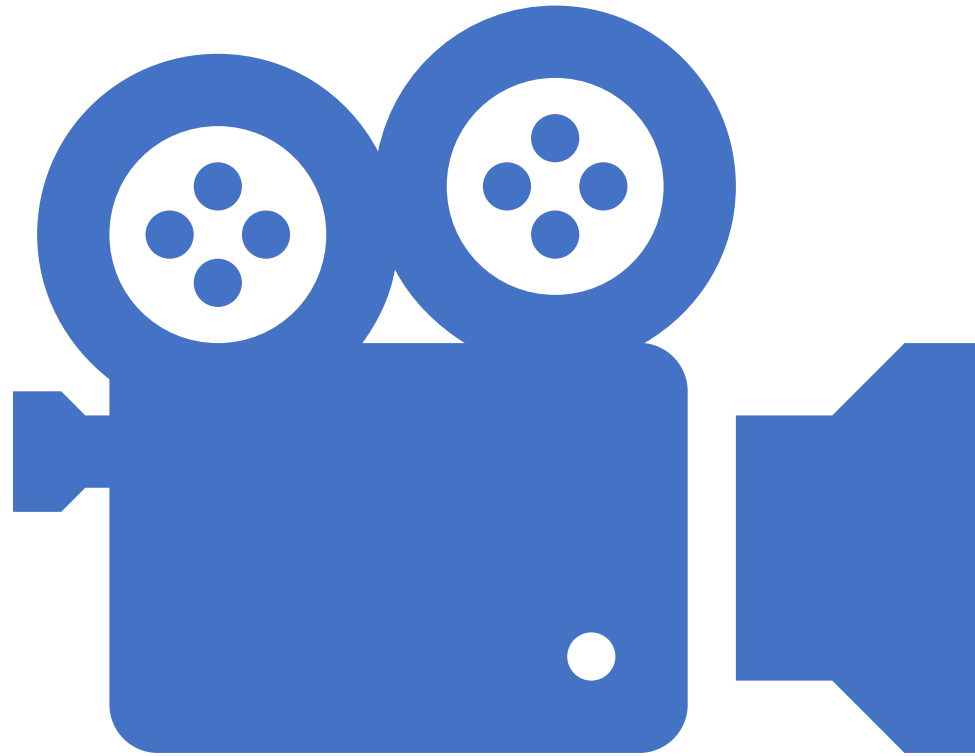
1. Financial Due Diligence and ADB Project Cycle
2. FM during Project Implementation
3. Financial Reporting Requirements
4. Audit Requirements
5. Asset Management and Financial Sustainability
6. Project Closure
7. Knowledge Check
8. eLearn Tools
9. Open Q&A Session





# 1. Financial Due Diligence and ADB Project Cycle

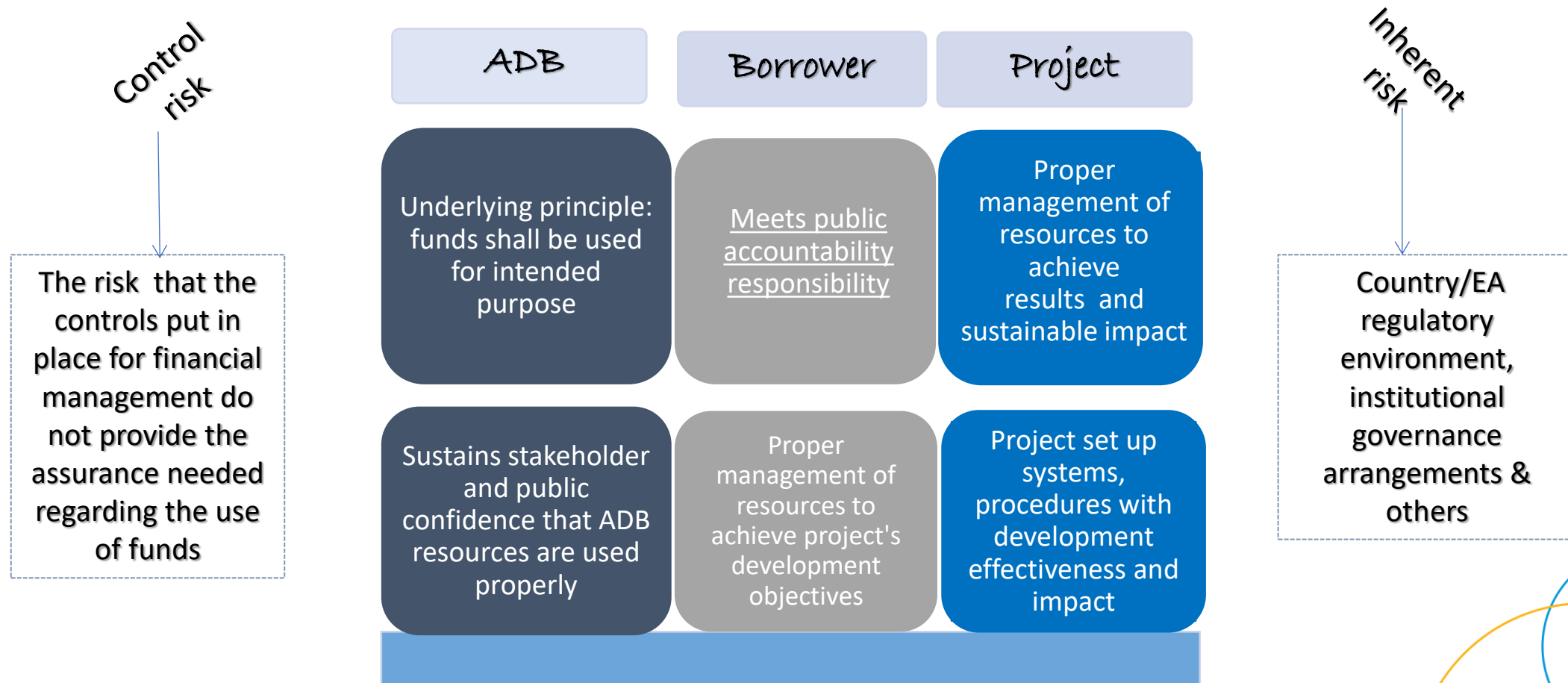
# Risks and Consequences of Poor Financial Management



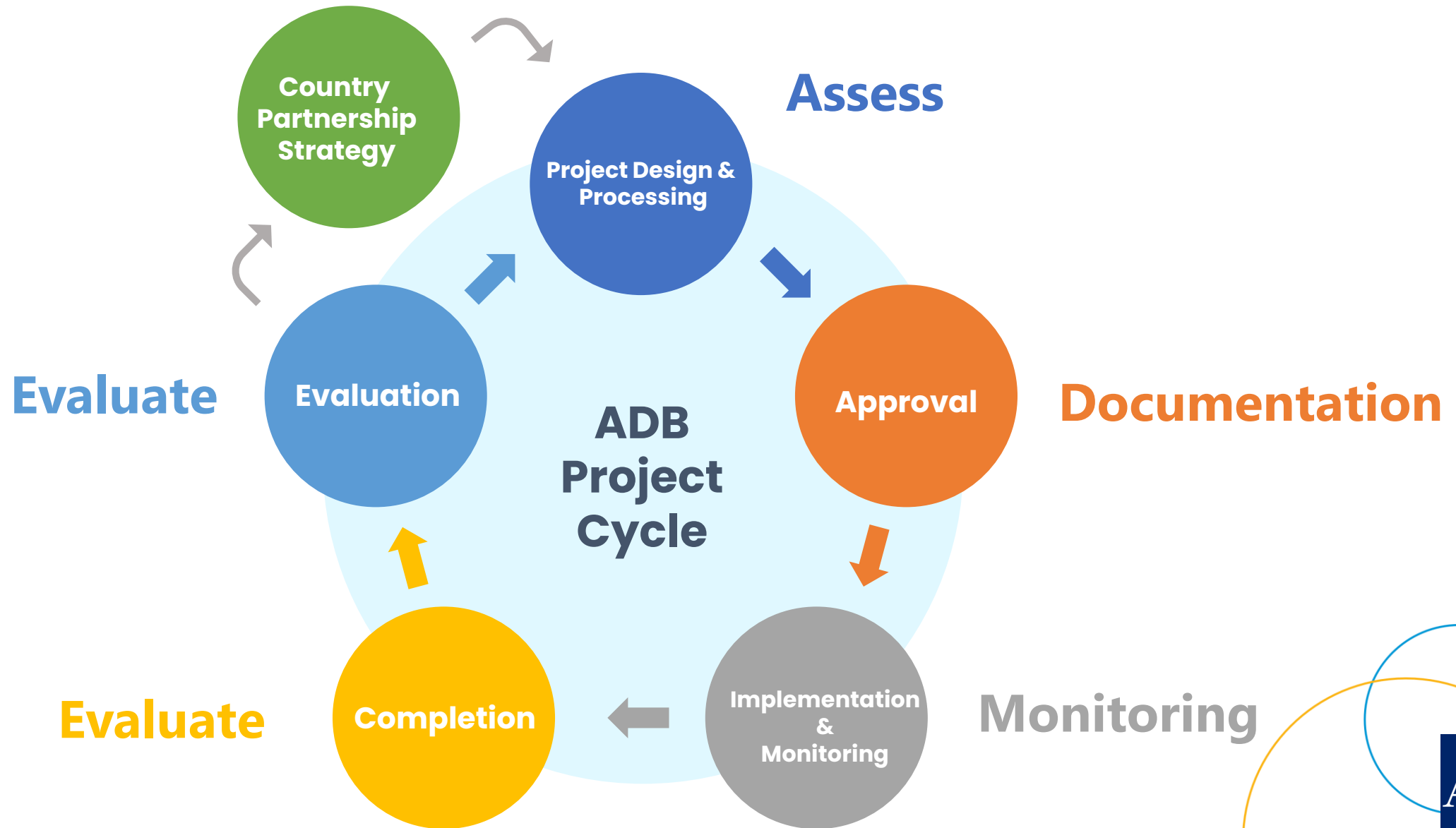


# FM Risk Framework

## Fiduciary Mandate and Associated Risks



# FM during Project Cycle



# What are the two types of risks that can affect financial management?

- A. Inherent Risk and Control Risk
- B. Operational Risk and Market Risk
- C. Credit Risk and Liquidity Risk
- D. Strategic Risk and Compliance Risk
- E. All of the above

# True or False

The ADB Project Cycle includes stages such as Project Design & Processing, Approval, Completion, Evaluation, Implementation & Monitoring, and Country Partnership Strategy

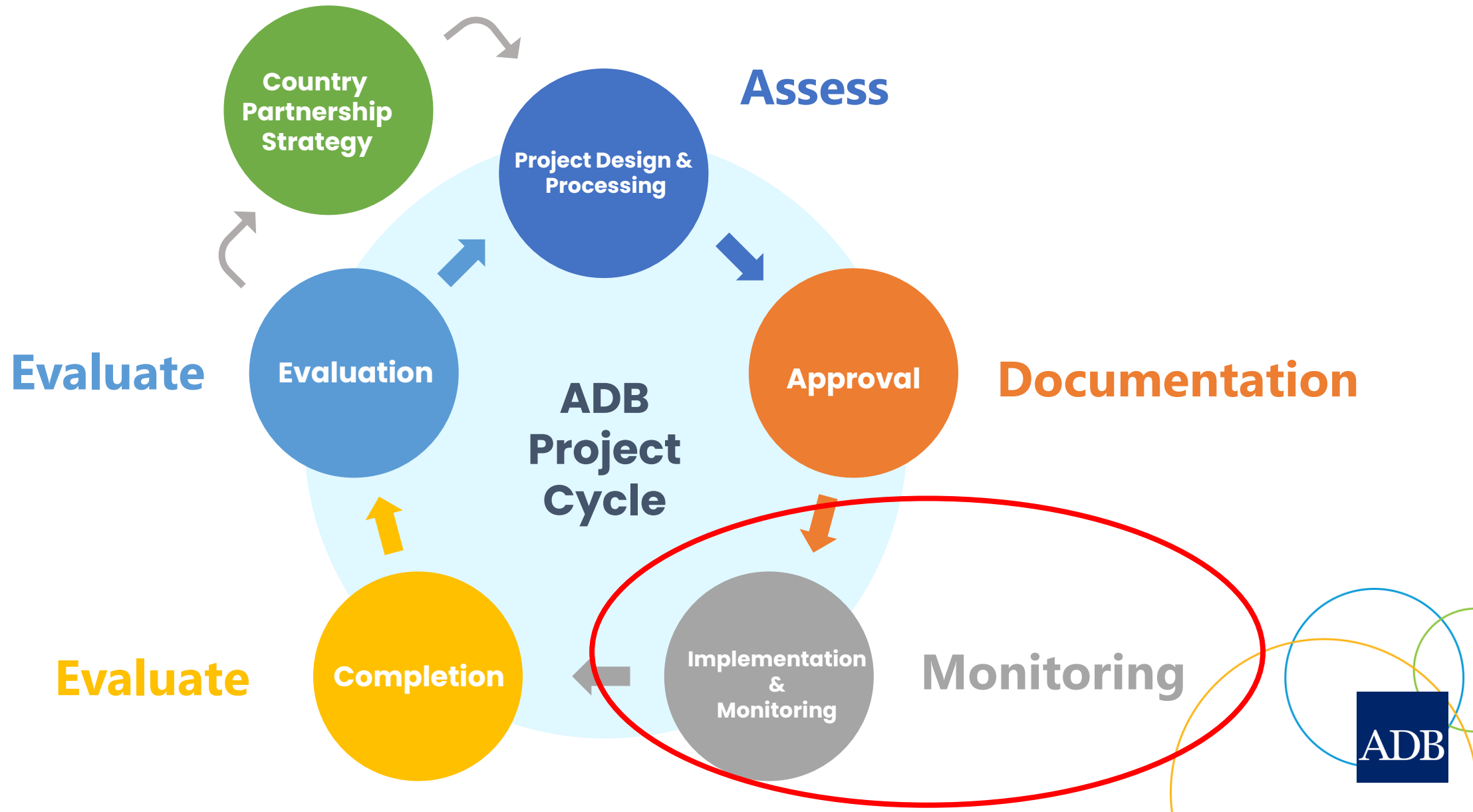


## 2. FM during Project Implementation

# ADB Initiatives

- In-country capacity building workshops/trainings
- Regular coordination with EA/IAs and the auditor to avoid audit delays and improve the quality of audit submissions
- Develop and engage technical capacity support to strengthen the capacity of EA/IA
- Frequent field visits to conduct consultation, supervision missions
- Harmonization with other donor partners in the country

# FM during Project Cycle



# Which of the following is an initiative taken by ADB to improve financial management during project implementation?

- A. In-country capacity building workshops/trainings
- B. Regular coordination with EA/IAs and the auditor to avoid audit delays
- C. Developing and engaging technical capacity support
- D. Frequent field visits to conduct consultation, supervision missions
- E. All of the above



### 3. Financial Reporting Requirements

# Legal Basis – where to find the specific requirements?

- Legal Agreements:
  - Loan or Grant Agreement
  - Project Agreement
  - Schedule attached to the agreements – Financial Covenants/matters
- Project Administration Manual (PAM) or Facility Administration Manual (FAM)
- Addendum or Amendment to the above documents (if any)
- Standard Audit Terms of Reference (TOR)

# ADB's Financial Reporting and Audit Requirements



[Explainer video](#)




# Financial Reporting Requirements

**Periodic**



**Quarterly  
Progress  
Report**

**Annual**




**APFS**

**Annual**



**AEFS**

**Annual**



**Financial  
covenants**

# Progress Report

## Frequency

- monthly, quarterly, semi-annual or annual based on PAM

## Contents:

- **Institutional** – overview of FM structure, changes in staff strength, and key changes in FM systems and processes, if any.
- **Financial progress** – current and cumulative expenditure against budget; current and cumulative funds flow. Include an explanation of variances above 5%.
- **FMAP** – update on compliance with FM action plan.
- **Audit** – update on the external audit process.
- **Issues/ Challenges and Solutions** – highlight key issues in FM and plans to address those issues; update on actions taken to address issues/comments highlighted in the last APFS review by ADB.

# FM Reporting and Performance Management



Project Implementation => **Implement Agreed Arrangements**

Audited Project Financial Statements

Auditor's Opinion on use of loan proceeds

Management Letter

Audited Entity Financial Statements

Auditor's Opinion on compliance with financial covenants

Financial information in project progress report

**Annually, 6 months after fiscal year end**

**Annually, 6 months after fiscal year end**

**Annually, 6 months after fiscal year end**

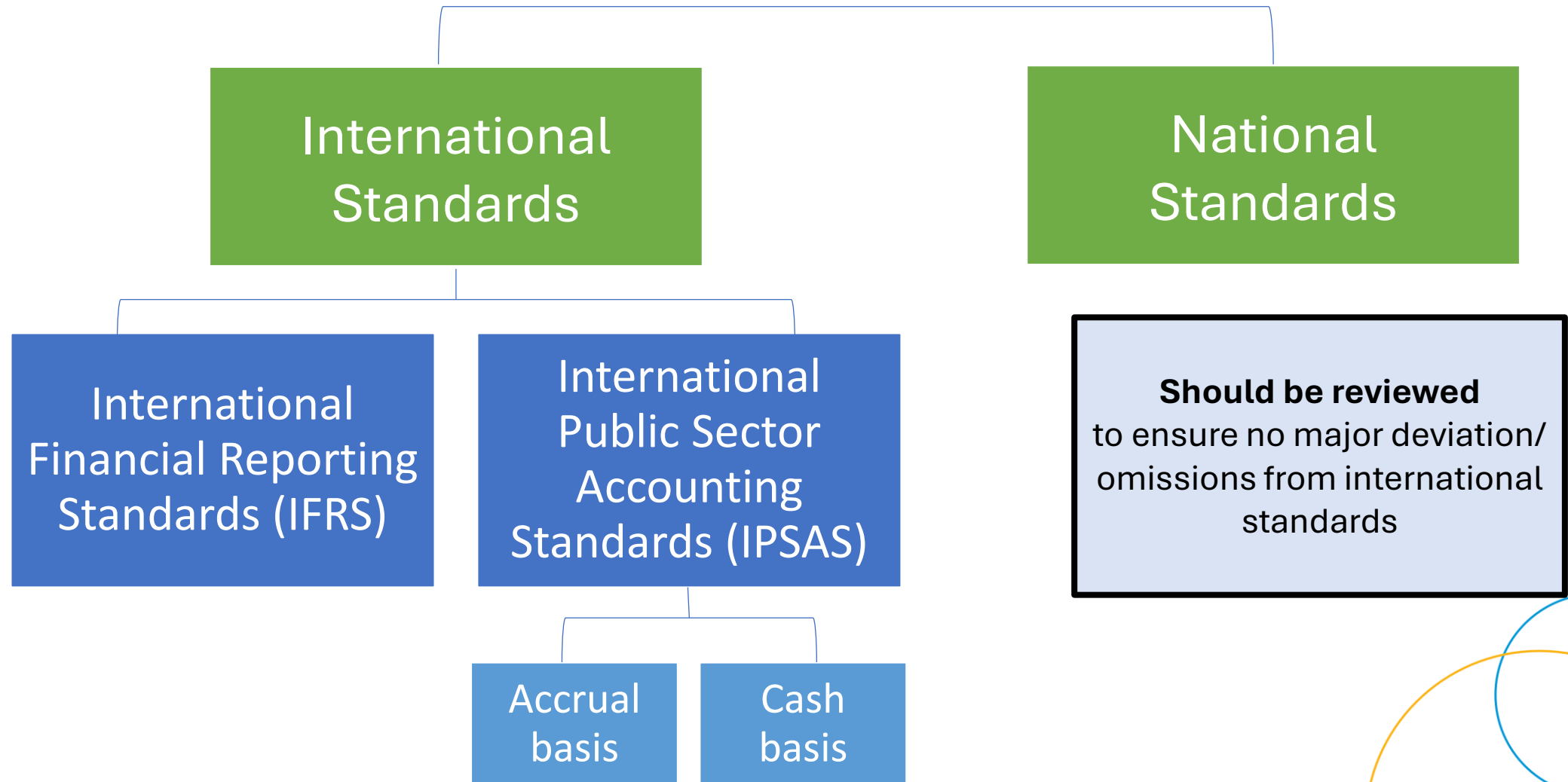
**12 months after fiscal year end or within 1 month of their approval by the relevant authority, whichever is earlier**

**Annually**

**Monthly/quarterly/semi-annually, as indicated in PAM**

# Project Accounting standards

Accounting Standards acceptable to ADB



# Project Accounting standards - IPSAS

The International Public Sector Accounting Standards, or IPSAS, for public sector entities are a set of internationally recognized standards that allow governments worldwide to provide robust, understandable, and comparable financial reporting.

## IPSAS Accrual Basis

Transactions are recorded when revenues are earned and expenses are incurred

## IPSAS Cash Basis

Receipts and expenditures are recorded when cash is received or paid out

# Financial statements: ADB's review



**Quality** to be assessed, are all statements complete, including the fixed asset schedule, plus comparatives



**Budget utilization** (if IPSAS) – link to Annual Workplan and Budgeting (AWPB)



**Cash balances** – adequate compared to usage, reconciled to ADB records and designated account statements



**Management responsibility** statement to be included.

# Requirements for Project Financial Statements



## Clear Presentation

- Funds received by sources – all project funds
- Expenditure category
- Current year, previous year, and cumulative figures (from the second year of reporting until the financial closing date)
- Reconcile ADB disbursements with ADB records



## Complete and all key components

- Complete statements
- Significant Accounting Policies
- Notes to FS
- Signed and dated
- Notes on use of government counterpart contribution
- Notes on project assets management
- Notes on financial covenants compliance
- Reconciliation with ADB systems

# Financial Statements Basis of Preparation



## Cash Basis

- Statement of cash receipts and payments
- Statement of Budgeted vs. Actual Expenditures
- Statement of Advance Account\*
- Statement of Expenditures\*
- Significant accounting policies and explanatory notes
- Any additional schedules (e.g., summary of assets, reconciliation with ADB's disbursement data)

# Financial Statements Basis of Preparation



## Accrual Basis

- Statement of financial position
- Statement of financial performance
- Statement of cash flows
- Statement of changes in net/assets/ equity/ fund\*
- Statement of advance account\*
- Statement of budgeted vs actual expenditures
- Summary statement of expenditures\*
- Significant accounting policies and explanatory notes
- Any additional schedules

# Complete FS Presentation

## Financing Sources and Expenditure Categories

### C. Detailed Cost Estimate by Financier (\$ million)

Item	ADB								Total Cost
	ADF Loan		ADF Grant		EDB Loan		Government		
	Amount	% of Cost	Amount	% of Cost	Amount	% of Cost	Amount	% of Cost	
A. Investment Costs <sup>a</sup>									
1 Toktogul turbine-generator units 1 and 3 replacement	38.88	40.00%	25.66	26.40%	32.65	33.59%	-	0.00%	97.19
2 Civil structure refurbishment	4.50	60.00%	3.00	40.00%	-	0.00%	-	0.00%	7.50
3 Dam Monitoring System	-	0.00%	1.70	100.00%	-	0.00%	-	0.00%	1.70
4 Consulting Services									
a. Business process assessment and management modernization	-	0.00%	5.00	100.00%	-	0.00%	-	0.00%	5.00
b. Project management and individual consultants	-	0.00%	4.00	100.00%	-	0.00%	-	0.00%	4.00
c. Public information program	-	0.00%	0.40	100.00%	-	0.00%	-	0.00%	0.40
d. Corporate financial audit for eight power and heat companie	-	0.00%	1.20	100.00%	-	0.00%	-	0.00%	1.20
e. Project financial statement audit for EPP and MOE	-	0.00%	0.13	100.00%	-	0.00%	-	0.00%	0.13
Subtotal (A)	43.38	37.04%	41.09	35.08%	32.65	27.88%	-	0.00%	117.12
B. Taxes and Duties <sup>b</sup>	-	0.00%	-	0.00%	-	0.00%	23.90	100.00%	23.90
Total Base Costs (A+B)	43.38	30.76%	41.09	29.14%	32.65	23.15%	23.90	16.95%	141.02
C. Contingencies <sup>c</sup>									
Physical Contingency	10.41	48.44%	6.08	28.29%	5.01	23.31%	-	0.00%	21.49
Price Contingency	4.86	48.36%	2.83	28.16%	2.34	23.28%	-	0.00%	10.05
Subtotal (C)	15.27	48.41%	8.91	28.25%	7.35	23.30%	-	0.00%	31.54
D. Financial Charges During Implementation <sup>d</sup>	1.35	55.33%	-	0.00%	-	0.00%	1.10	44.92%	2.44
Total (A+B+C+D)	60.00	34.29%	50.00	28.57%	40.00	22.86%	25.00	14.28%	175.00
% of Total Project Cost	34.29%		28.57%		22.86%		14.28%		

ADB = Asian Development Bank, ADF= Asian Development Fund, EDB = Eurasian Development Bank

Source: Consultant and Asian Development Bank estimates.

<sup>a</sup> In 2015 prices.

<sup>b</sup> Include taxes and duties (10% custom duties and 12% value added tax) to be financed or waived by the Government of the Republic of Kazakhstan.

<sup>c</sup> Physical contingencies computed at 16% for turnkey contracts and at 5% for all other cost categories. Price contingencies computed following the ADB's cost escalation factors, a power purchase parity assumption has been made to compute exchange rate adjustments.

<sup>d</sup> Includes financial charges during construction on ADB loan at 1% per annum; and at 1% per annum of EDB loan, and 0.5% upfront commission on EDB loan.

# Notes to Financial Statements

General Information about the project

Summary of Accounting Policies

More information about the accounts in the FS

# Notes to Financial Statements

[NAME OF THE COUNTRY/IMPLEMENTING AND EXECUTING AGENCY]

[NAME OF THE ENTITY/PROJECT]

[ADB LOAN REFERENCE]

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED [YEAR END DATE]

1. Project Nature and Activities

1.1 *Description of the Project, the nature of activities, commencement and expected completion dates. Mention location, domicile, legal form, controlling IA/ EA, brief nature of the project outputs,*

Project description and activities

1.2 Give legislative framework

*Insert as relevant*

## 2.1 Statement of compliance

"Electric Power Plants" OJSC maintains separate books and records by funding source for all expenditures incurred on the project following International Public Sector Accounting Standards (IPSAS).

These special purpose project financial statements have been presented in accordance with the cash basis of accounting and the Financial agreements, to the extend applicable to these special purpose project financial statements and as agreed by the Project Executing Agency, the Government of Kyrgyz Republic, Asian Development Bank and Eurasian Development Bank.

Accounting framework

## 3. SIGNIFICANT ACCOUNTING POLICIES

3.1 Financial Statements

This comprises of the Statement of Receipts and Payments, the Statements of Expenditure by Category and Financier, the Statement of Disbursement and related notes and appendices to the financial statements

3.2 Basis of measurement

Financial statements have been prepared under the historical cost convention and on *[cash/ accrual]* basis of accounting

3.3 Changes in Accounting policies

*Describe changes in accounting policies, if any*

Significant accounting policies

# Noncash transactions reporting

(presentation of in-kind contributions by government counterpart financing to the project)

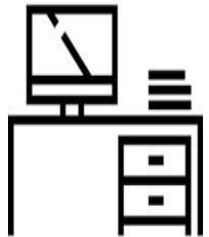


If it **can be measured** reliably, quantity and report as project expenditure in the APFS



If it **cannot be measured** reliably, disclose in the notes to the financial statements

# Presentation of In-Kind Contributions by government counterpart financing to the project



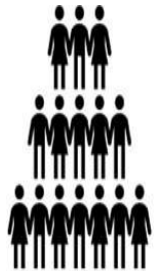
Office space



Utilities



Cash Basis:  
Disclose in the notes to financial statements



Salaries of  
project staff



Taxes and duties



Accrual:  
Quantifiable amount is presented as Source and  
Use of funds in the APFS

# True or False

The Annual AEFS and Periodic Quarterly Progress Report are part of ADB's Financial Reporting and Audit Requirements



## 4. Audit Requirements

# Basic Requirements - APFS



## Audited

- Independent auditor whose qualifications, experience are acceptable to ADB



## Accurate and Complete Submission

- Auditor's Opinions on
  - FS Presentation
  - Use of Proceeds
  - Compliance on the use of advance account / SOE
- Financial Statements
- Management Letter



## Form and Timeliness

- In English
- Compliance with acceptable accounting and audit framework
- Timely submitted

# Why Audited Financial Statements?

Accountability for use  
of public funds

Funds are used for the  
purposes intended

Due attention to  
economy  
and efficiency

To verify compliance  
with covenants

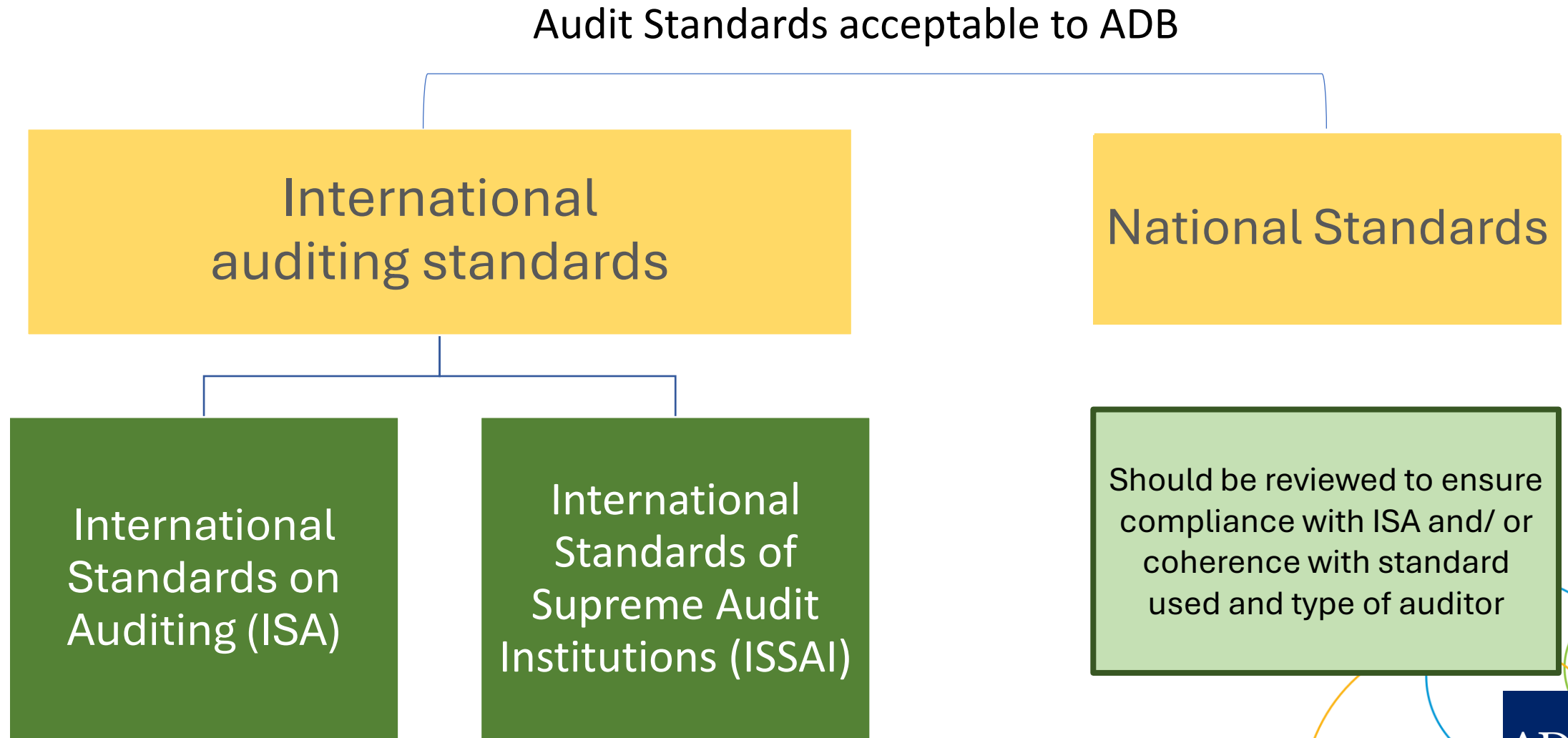
Reliable financial  
information

ADB's Access to  
Information Policy

# Responsibilities of the Borrower and the Auditors

	Borrower	Auditor
Preparation of PFS and management representation letter	✓	
Independent audit of the PFS		✓
Issuance of audit opinions (PFS, compliance with FC, and use of loan proceeds) and a management letter		✓
Submission of APFS, auditors' opinions, and management letters to ADB	✓	
Calculation of FC	✓	
Preparation of auditors' TOR	✓	
Agreement on the timeline, including submission timing to ADB	✓	✓

# Audit standards



## Specific Audit Opinion

What are the **specific audit opinions** required on a set of **project financial statements** submitted to **ADB**?

# Required Audit Opinions

## Required Audit Opinion

Auditor's  
opinion on  
financial  
statements

- Whether the financial statements were ***fairly presented***, or ***give a true and fair view*** of the project's financial position, financial performance and cash flows (fair presentation framework)

In our opinion, the accompanying project financial statements present fairly, in all material respects, the statement of cash receipts and payments, the statement of budgeted versus actual expenses, the statement of advance account and the statement of expenses and withdrawal schedule for the year ended December 31, 2021 in accordance with International Public Sector Accounting Standard "Financial Reporting Under the Cash Basis of Accounting" (the "IPSAS") issued by the International Public Sector Accounting Standards Board of the International Federation of Accountants and "Guidelines for the Financial Governance and Management of Investment Projects Financed by the Asian Development Bank" (the "ADB Guidelines").



In our opinion, the accompanied financial statements of "Naryn Rural Water Supply and Sanitation Development Program" Project and "Naryn Program Readiness" within the framework of the Multi-Sectoral Activities Support Fund (Activity 2) Project, present fairly, in all material respects, view of receipts and payments for the year ended on December 31, 2021 in accordance with the International Public Sector Accounting Standards under the cash basis of accounting (IPSAS).

# Required Additional Auditor's Opinion

## Additional auditor's opinion

- Auditor's opinion on the use of loan/grant proceeds
- Auditor's opinion on compliance with financial covenants , if any

In addition to the audit opinion on financial statements, in our opinion:

- (i) The Project financing is used only for purposes of the Project;

Opinion on the use of loan and grant proceeds

# Audit standards

- ISA 700 (revised) - wording on **True and fair** and **present fairly, in all material respects** to be enforced, key audit matters
- Modification of **opinion (qualified, adverse, disclaimer)** - use guidance in ISA 705/706 to consider if the audit opinion is reasonable, given the materiality of any issues raised.
- Qualified opinions may or may not be acceptable, depending on the nature of the issue, adverse/ disclaimers are generally not.

# Auditor's capacity:

## Qualifications of private auditors

- Objective and independent
- Comply with the local legislation
- Relevant audit licenses/permits from the local audit regulator, if applicable
- Conform to International Standards on Auditing (ISA)
- Demonstrate experience
- Have competent auditors with the necessary qualifications and capabilities

# Minimum requirements of an auditor's report

Title of the audit report

Addressee (executing agency and/or borrower

Identification of financial information audited

Management's responsibility

Auditor's responsibility

Expression of audit opinion (qualified, unqualified, disclaimer, adverse)

Auditor's signature

Date of audit report

Auditor's address

# Test Case

Missing  
EA  
addressee

Audit report should  
be issued each year

International Standards of Supreme  
Audit Institutions (ISSAI) are  
applicable

Should mention IPSAS

Audit report is not dated;  
Complete address not given

**AUDITOR'S REPORT**

We have audited the accompanying Financial Statements of the Project Command Area Development - output 2 & 3 Component of Project "Construction of Jalapur Irrigation Canal and its System" (ADB Loan No. 3599-PAK) for the financial years 2019-20- and 2020-21.

These Financial Statements are the responsibility of the management of the Project Management.


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 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 Project's policy is to prepare the accompanying statements in the format agreed between the Asian Development Bank and the Government of Punjab as noted in the Minutes of Negotiations for the Loan, on a cash receipts and disbursement basis in which cash is recognized when received and expenses are recognized when paid, rather than when incurred.

In our opinion, (A) the aforementioned Financial Statements and appended notes fairly present in all material respects the financial position of the Project as on 30-06-2021 and the results of its operations for the Financial Years 2019-20 and 2020-21 in conformity with IPSAS, applied on a basis consistent in all material respects with that of the previous year; (B) the project has utilized all proceeds of the loan of the ADB only for purposes of the Project as agreed between the Asian Development Bank and Government of the Punjab in accordance with the Loan Agreement; and no proceeds of the loan have been utilized for other purposes; and (C) the Project was in compliance as at the date of closing of the Financial Year with all financial covenants of the Loan Agreement.

Dated:  
Place: Lahore

  
(Muhammad Ejaz-ul Haq)  
Director General Audit Punjab  
Lahore

# Test Case

Project number  
missing

Should clearly  
mention financial  
covenants compliance

## AUDITOR'S REPORT TO THE MANAGEMENT

Ms. Ismat Tahira  
Secretary,  
Benazir Income Support Program  
F-Block, Islamabad

### Auditor's Report on the Social Protection Development Project (SPDP)

We have audited the accompanying Financial Statements of "Social Protection Development Project (SPDP)" under the Benazir Income Support Program, Loan No. 3837-PAK that comprise Statement of Receipts and Payments together with the Notes forming part thereof for the year ended 30<sup>th</sup> June, 2021.

### Management's Responsibility

It is the responsibility of the project management to establish and maintain a system of internal controls, and prepare and present the Statement of Receipts and Payments in conformity with the requirements of Cash Basis International Public Sector Accounting Standards (IPSAS), Financial Reporting under the Cash Basis of Accounting Standard.

### Auditor's Responsibility

The responsibility of the auditor is to express an opinion on the financial statements based on the audit conducted. We conducted our audit in accordance with the International Standards of Supreme Audit Institutions (ISSAIs). These standards require that we plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement. The audit process includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. It also includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall statement presentation. We believe that the audit evidence, we have obtained is sufficient and appropriate to provide a basis for audit opinion.

### Opinion

In our opinion

- a) The Financial Statements present fairly, in all material respects, the cash receipts and payments made by the project for the year ended 30<sup>th</sup> June, 2021 in accordance with Cash Basis IPSAS, Financial Reporting under the Cash Basis of Accounting Standard.
- b) The expenditure has been incurred in accordance with the requirements of legal agreements.

(Kamran Rashid Khan)  
DIRECTOR GENERAL  
Directorate General Audit (SSNs),  
Benevolent Fund Building, Zero Point, Islamabad

Dated: 14 June 2021

# Test Case

Missing  
EA  
addressee

Management  
responsibility para  
repeated

## AUDITOR'S REPORT TO THE MANAGEMENT

The Directorate General Audit Works (Federal), Islamabad has audited the accompanying Financial Statements, as of 30<sup>th</sup> June 2021, of the Project "Central Asia Regional Economic Cooperation Regional Improving Border Services (RIBS) Project", financed through Asian Development Bank Loans No. 3344-Pak and 3345-Pak.

The preparation of Financial Statements is the responsibility of the Management of the Project. The responsibility of Audit is to express an opinion on the accompanying Statements based on the Financial Attest.

The audit was carried out in accordance with the International Standards of Supreme Audit Institutions (ISSAI). The standards require the Audit to obtain reasonable assurance that the Financial Statements are free of material misstatements. This audit is based on a test check basis and includes findings, evidence supporting the amounts and disclosures in the Financial Statements. It also includes assessing the Accounting Principles used by the Management in preparing Financial Statements and significant estimates made by the Management. We believe that our audit provides a reasonable basis for our opinion.

The Management's responsibility is to prepare the accompanying statements on the format agreed between Asian Development Bank and the Government of Pakistan, on a cash receipts and disbursement basis in which revenue is recognized when received and expenses are recognized when paid.

In our opinion:

A. The aforementioned Financial Statements that were subject to audit, fairly present in all material respects the financial position of the Project "Central Asia Regional Economic Cooperation Regional Improving Border Services (RIBS) Project", financed through Asian Development Bank Loans No. 3344-Pak and 3345-Pak. for the period ended 30<sup>th</sup> June, 2021, in conformity with Cash Basis International Public Sector Accounting Standard.

B. The management of the Project has utilized all proceeds of the loan withdrawn from the Asian Development Bank only for the purposes of the Project as agreed between the Asian Development Bank and Government of Pakistan in accordance with the Loan Agreement; and no proceeds of the loan have been utilized for any other purposes.

Dated: 16<sup>th</sup> December, 2021  
Islamabad

(Iftikhar Ahmed Babar)  
Director General Audit Works (Federal)

# Auditing Arrangements

## Financing Audit Costs

- Audited project financial statements – eligible for ADB financing and should be included in the project cost estimates.
- Audited entity financial statements - eligible for ADB financing provided AEFS submission is required by ADB but
  - (i) the entity is not subject to audit by the laws of the borrower; or
  - (ii) the entity has been required to prepare entity financial statements by adopting a set of financial reporting standards acceptable to ADB

# Auditor's performance:

## Things to discuss with auditors

Importance of entry and exit meetings to discuss internal control issues

Monitoring of Risk-based time bound audit recommendations and management responses

Reporting deadlines to ADB

Auditing standards



To discuss with auditors

Responsibilities of auditor and management should be contained in audit opinion

# ADB's Recommendations for project audit reports (APFS)

- Any additional information in APFS should be reported in accordance with the provisions of adopted financial reporting framework and standards.
- Add page numbers and initials of the auditor on all pages of the APFS for identification purposes to ensure the comprehensiveness and authentication of the set of Financial statements audited.
- Provide a high-level analytical review of the cumulative utilization of funds based on budget versus actual comparison.
- APFSs may include high-level summary of project fixed assets.

# Requirements for Management Letter



- any weaknesses in the accounting and internal control systems
- details of any ineligible expenditure identified during the audit
- recommendations to rectify identified weaknesses
- management's comments on the audit recommendations
- the status of significant matters raised in previous management letters

## Common Issues with Management Letter

- Unresolved or recurring internal control issues
- No update on implementation of audit recommendations for previous year's internal control issues
- No Management's response on internal control issues raised

# Audited Project Financial Statements



Effectivity

Project  
implementation

Loan Closing

YEARLY APFS MUST BE SUBMITTED

# First APFS



# Non-submission of APFS

**If APFS is not  
received within 6  
months after the due  
date**

**ADB will withhold  
processing of  
requests for new  
contract awards  
and disbursement**

**When the APFS is not  
received within 12  
months after the due  
date**

**ADB may  
suspend the  
loan/grant**





# Recurring issues with APFS submission

Late submission

Project Financial  
Statements are not  
complete (do not  
include required data)

Audit Opinion not  
entirely in line with  
ISSAI/ ISA

Lack of separate  
opinion on the use of  
loan/grant proceeds

No breakdown by fund  
source

No management  
letter provided

No follow up of the  
implementation of the  
previous year's issues

No formal deferment  
submitted to and  
cleared by ADB for no  
submission

# Audited Entity Financial Statements

- Requirement
  - **Statutory/Regulatory Compliance** – if required by the developing member country's laws or regulations
  - **Project Monitoring** – as needed for monitoring project progress
- **Purpose**
  - to allow ADB to monitor the use of loan or grant proceeds; and
  - To satisfy itself of the ongoing financial viability and sustainability of the project and the executing or implementing agency.
- **Acceptable Accounting Standards**
  - the generally accepted accounting standards followed in the country or another standard, if agreed during project processing
- **Language:** English
- **Due Date:** within 1 month of their approval by the relevant authority or twelve months from fiscal year-end, whichever is earlier

# Audited Entity Financial Statements

## AEFS requirement in the Loan Agreement:

18. The Borrower shall cause the Implementing Entities to (a) provide their annual financial statements prepared in accordance with financial reporting standards acceptable to ADB; (b) have their financial statements audited annually by independent auditors whose qualifications, experience and terms of reference are acceptable to ADB, in accordance with auditing standards acceptable to ADB; (c) as part of each such audit, have the auditors prepare the auditors' opinion(s) on the financial statements and compliance with the financial covenants of the Loan Agreement; and (d) furnish to ADB, no later than 1 month after approval by the relevant authority, copies of such audited financial statements and auditors' opinion(s), all in the English language, and such other information concerning these documents and the audit thereof as ADB shall from time to time reasonably request.

# Financial Covenants

## Requirement for auditor's report on Financial Covenants

- Auditors' opinion on compliance with financial covenants in legal agreements
- Reasonable assurance opinion
- Auditor's confirmation on the compliance or noncompliance
- Calculation of numerical financial covenants (i.e. ratios)

# Financial Covenants

## Breach of Financial Covenants

- Breach of financial covenants can have **legal consequences**
- Noncompliance with covenants constitute an event of default and under financial reporting standards (and as mandated by international standards such as International Financial Reporting Standards), they will be fully disclosed, and the consequences of default will be given effect in the financial statements.
- The borrower and ADB should usually identify potential noncompliance at an early stage, and may mutually agree to **defer, restructure, or waive** some covenants if supported by sufficient basis and analysis of the changes in the circumstances which are **beyond the control of the borrower**.

# What are the basic requirements for APFS to be considered audited?

- A. Independent auditor whose qualifications are acceptable to ADB
- B. Accurate and complete submission
- C. Auditor's opinion on FS presentation, use of proceeds, and compliance
- D. All of the above

# True or False

Audited financial statements are important for accountability, verifying compliance with covenants, and providing reliable financial information



## 5. Asset Management and Financial Sustainability

# ADB and Financial Sustainability

- **ADB's fiduciary responsibility**
  - ✓ To ensure that all investment projects are subjected to the **highest standards of financial due diligence** so implementation complies with requirements for **economy and efficiency**
  - ✓ ADB's due diligence process for
    - Ensuring prudent use of ADB's resources
    - Identifying and mitigating risks to project and entity sustainability
- **ADB's Strategy 2030**
  - ✓ Achieve a **prosperous, inclusive, resilient, and sustainable Asia and the Pacific**

# For discussion

1. Why is financial sustainability important to you?
2. What are some key challenges facing your projects that may affect financial sustainability?
  - Asset management
  - Capacity and resources constraint
  - Information management system
  - Fiscal planning, budgeting and allocation
  - Other?

# Asset Management and Financial Sustainability

## What is Asset Management?

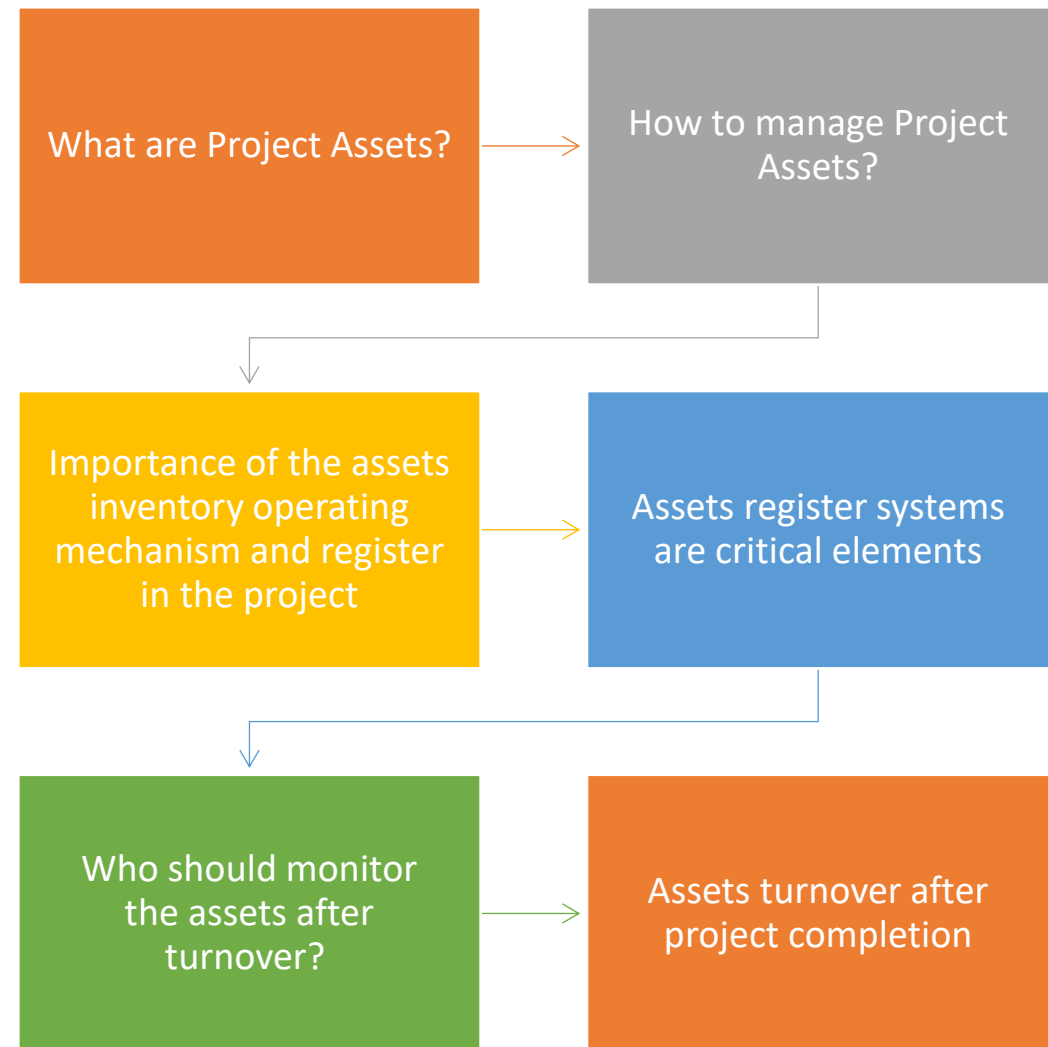
Deploying, operating, maintaining, upgrading and disposing of assets cost-effectively



## Why is it important?

- Operational Efficiency
- Risk Management
- Financial Performance
- Compliance and Accountability
- **Sustainability and long-term planning**
- Value maximization

# Project Assets Management



# What are the Project Assets?

Tangible Assets



Physical Assets

**Example**

Roads, building, plants, equipment,  
vehicles, computers etc

Intangible Assets



Non-Physical Assets

**Example**

Rehabilitation of roads/building

# Asset Management and Financial Sustainability

How to manage assets? **Asset Register**

## Registration of Asset

- Name and description of the asset
- Current location
- Acquisition date and cost
- Insurance and warranty details
- Maintenance details
- Depreciation model and salvage value

# Asset Management and Financial Sustainability

## Registration of Asset

- Name and description of each asset
- Current physical location
- Acquisition date and cost
- Insurance and warranty details
- Maintenance details
- Depreciation model and salvage value

To ensure accurate asset turnover to the entity and exit strategy at the end of the project

To include value of the asset in audited financial statements

To ensure proper amortization

To calculate and ensure sufficient replacement cost

To ensure sufficient O&M budget

Necessary for efficient management of project resources to realize maximum value, sustainability and long-term goal of the project

# Asset Management and Financial Sustainability

## Ownership, Registration, and Operation & Maintenance

Project Asset Examples	Ownership	Register	Operation and Maintenance	Monitoring, O&M after project completion
Roads, Plants, buildings, school, hospitals, rehabilitation of those assets	<b>States and transfer to the concerned state entity</b>	PMU	PMU	<b>Transferred to State Entities</b> After the resolution of PMU, O&M is turned over to the state entity, and registered in the balance sheet of the state
Equipment, laptops, office furniture, vehicles	States or line ministries and then transferred to <b>concerned parties</b> (e.g. schools and hospitals)	PMU then transferred to concerned parties	Concerned parties (e.g. schools and hospitals)	<b>Concerned parties</b> Concerned parties own them and continue O&M of the assets.

# Asset Management and **Financial Sustainability**

Financial covenants are:



Legally-binding



Measurable



Monitorable

**Financial performance indicators that help to objectively assess the financial performance of an executing and/or implementing agency.**

**They are incorporated into ADB project legal agreements (Schedule 4)**

# Financial Covenants and Financial Sustainability: revenue generating projects

One time compliance and continuous compliance

- One-time compliance

**Example** Conversion of convert existing government loans into equity

- Continuous compliance

**Example** Financial ratio covenants



# Asset Management and **Financial Sustainability**

## Examples of Financial Ratio Covenants

Accounts receivable  
number of days and  
collection efficiency  
ratios

Cash operating cost  
recovery ratio

Current ratio

Debt service coverage  
ratio

Debt-to-equity ratio

Self-financing ratio

# Key to Effective Financial Covenants

Ownership of the covenants by the borrower/EA/IA at the design stage

Diligent annual monitoring and reporting to ADB and proactive discussion during review mission on any potential non-compliance

Collaborative approach between the borrower and ADB to identify non-compliance due to the circumstances which are beyond the control of the borrower

# Implication of Non-compliance to Financial Covenants

Financial Covenants are legally binding

Breach of financial covenants can have legal consequences including trigger of default event

The borrower and ADB should identify potential non-compliance at an early stage and discuss to avoid project delay

# Delay in Project Implementation and Financial Sustainability

Delay in project implementation affects financial sustainability of a project due to the impact on Return on Investment

- Increase in recurrent cost
- Additional investment cost

# What is the importance of asset management in financial sustainability?

- A. Operational Efficiency
- B. Risk Management
- C. Financial Performance
- D. All of the above





## 6. Project Closure

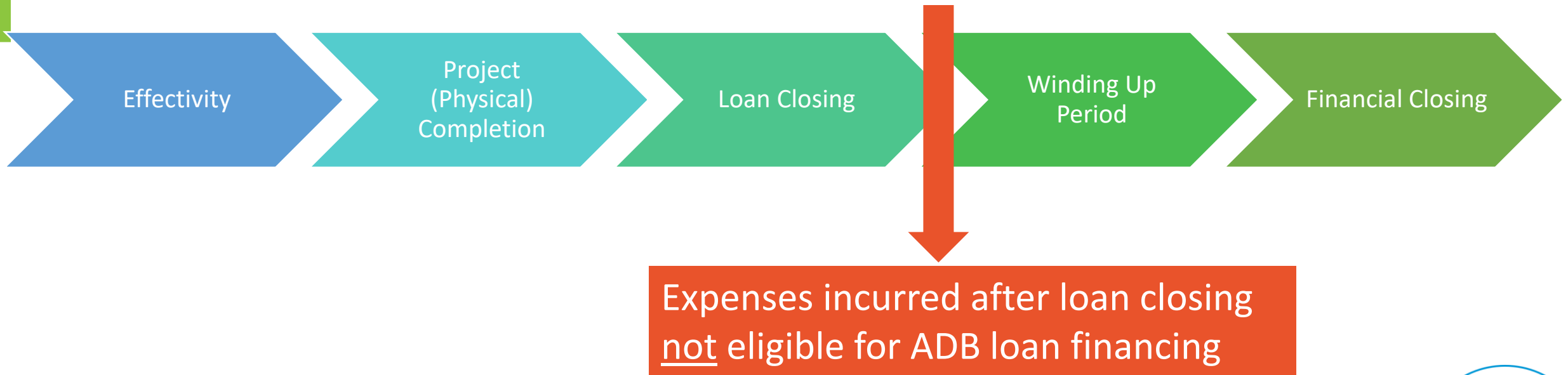
# FM in Project completion and Loan Closure



[Explainer video](#)



# Final APFS



# Requirements for Final APFS



Final APFS should include all payments until the project financial closure.



The final payment to audit should be also included into the APFS



If undisbursed eligible expenditures are recognized as of the loan closing date, disclosed in the notes to the accounts as of the loan closing date, and audited, APFS should state that no further APFS would be required.



May cover a partial year or a longer period up to 18 months

For accrual accounting: accrue the value of expenditures incurred up to loan closing date

For cash accounting: include disbursements to be made after loan closing date in notes to FS

# Discussion: Troubleshooting the Final Audit

As of loan or grant closing date:

- Final PFS has been prepared
- Some incurred expenditures are unpaid
- Final withdrawal application not submitted

What should be done?



# Troubleshooting the Final Audit

## **Under accrual accounting:**

No problem! Unpaid expenditures and pending WAs accrued into PFS

## **Under cash accounting:**

1. Add to notes IF these can be reliably estimated
2. Extend the final reporting period up to 6 months



# Disclosure of Estimated Expenditures

## Preparation of the Final Audited Project Financial Statements under the Cash Basis of Accounting Sample Note to the Audited Project Financial Statements

Note **XX**: Other Information: Total Estimated Expenditures at Loan Closing Date

The total estimated project expenditures **as of (reporting date)** amounts to **PKRxxx**. Of this amount, **PKRxxx** refers to amounts specified in the invoices, contracts, and other documents that are paid after the reporting date, and which amounts related to funding of the expenditures incurred and committed **as of (loan closing date)**

**Table 1: Schedule of Total Estimated Project Expenditures**  
**In PKR millions**

		Estimated Expenditures paid subsequent to reporting date		Total Estimated Expenditures incurred up to reporting date
	Expenditures Recorded and Paid up to (reporting date)	ADB	Government	
Audit fees	0.00	3.00		3.00
Civil works	100.00	17.00	30.00	147.00
Consulting services	100.00	20.00	10.00	130.00
Project Management	50.00		10.00	60.00
<b>Total</b>	<b>250.00</b>	<b>40.00</b>	<b>50.00</b>	<b>340.00</b>

# Project Completion Report

## FM at Project Completion

**Borrower performance on FM**

**Project cost at completion**

**EA/IA Completion Report**

**Financial Revaluation and Sustainability Analysis**

# Project Completion Report

## FM monitoring and reporting



### **FM performance by borrower**

Analyzing APFS and AEFS  
review observations in  
assessing FM performance



### **Lessons learned and recommendations**

Identifying issues and  
providing solutions in FM  
for future design of projects

# What should be included in the final APFS?

- A. All payments until the project financial closure
- B. Final payment to audit
- C. Undisbursed eligible expenditures recognized as of the loan closing date
- D. All of the above



# 7. Knowledge Check

# 1. What areas are covered under ADB's financial due diligence?

- A. FM capacity of EA/IA to manage the project
- B. Financial viability of the project (i.e., revenues are more than expenses)
- C. Financial sustainability of the project (i.e., assets created can be maintained)
- D. EA/IA can prepare withdrawal applications and project financial statements
- E. All of the above

## 2. True or False

Financial due diligence is the sole responsibility of ADB's Financial Management Specialist

# 3. Match the mitigation actions with weakness

## Description of Weakness

Delayed submission of audited financial statements

Executing agency does not maintain original supporting documents, and there is no document retention policy

Weak control over inventory can lead to theft or misappropriation, inability to construct or operate the project.

## Mitigation actions

Introduce inventory accounting, control over issue and utilization, physical verification and reconciliation.

Implement automated accounting system/ ERP which will significantly improve the financial statements preparation

At the project level, initiate procedure for safe custody of original supporting documents including safe storage, and retention period, access control, etc. Initiate policy dialogue to persuade the management to adopt a similar policy for the enterprise.

## 4. True or False

Financial due diligence for grant-financed projects is not necessary since ADB does not expect the money back.

## 5. Who is responsible to prepare annual unaudited project financial statements?

- A. Auditor
- B. Executing Agency or Implementing Agency
- C. Borrower representative
- D. Jointly Executing Agency/Implementing Agency and Auditor

## 6. What is the alternative approach if in-kind contributions cannot be measured reliably?

- A. Email ADB that it cannot be measured
- B. Disclose in the notes to the financial statements
- C. Approach an actuary to get estimate
- D. Ask the auditor to include it in the management letter

## 7. True or False

Management letter is written by the Project Director and submitted to ADB annually.

## 8. True or False

Periodic financial reports and QPRs submitted to ADB **needs** to be audited.

## 9. The following are acceptable accounting and reporting frameworks to ADB, except

- a) International Public Sector Accounting Standards
- b) International Financial Recording Standards
- c) International Financial Reporting Standards
- d) National Accounting Standards

10.

1. Project financial statements should follow the cost category as presented in the legal agreement(s) and project administration manual

2. Funding sources should be identifiable in the project financial statements

- a) Both statements are TRUE
- b) Both statements are FALSE
- c) Only statement 1 is TRUE
- d) Only statement 2 is TRUE



# 11. In addition to the opinion on the project financial statements, ADB requires specific opinion on :

- a) Compliance with Safeguards covenants
- b) Use of loan or grant proceeds for purposes intended
- c) Compliance with the agencies internal control policies
- d) Use of accounting software in accordance with ADB standards

## 12. True or False

Final financial statement should include all expenditures incurred up to loan closing date



## 8. eLearning tools for ADB FM requirements

# Comprehensive FM eLearning for EA/IA



Go to "[eLearn.adb.org](https://eLearn.adb.org)"  
Search by "[financial management](#)"

## *Financial Management in ADB-Financed Sovereign Operations for Executing/Implementing Agencies*

- For executing and implementing agencies' management and project FM staff as well as FM consultants and auditors.
- Provides fundamental knowledge on financial management requirements in ADB-financed sovereign operations throughout the project cycle
- Can be taken based on interest (project design and/or project implementation)
- Focuses on the **responsibilities of the borrowers** in the core elements of financial due diligence, financial reporting and auditing, and monitoring during implementation and project completion.

# Cost Estimates



*The e-Learn module on Cost Estimates is a preparatory course*

- To gain basic understanding of the importance of robust project cost estimates, its guiding principles and detailed components.

Go to "[eLearn.adb.org](https://eLearn.adb.org)"  
Search by "[cost estimates](#)"

# Cash Basis IPSAS



Go to “[eLearn.adb.org](https://eLearn.adb.org)”  
Search by “[IPSAS](#)”

## *Cash Basis IPSAS for ADB Project Financial Reporting*

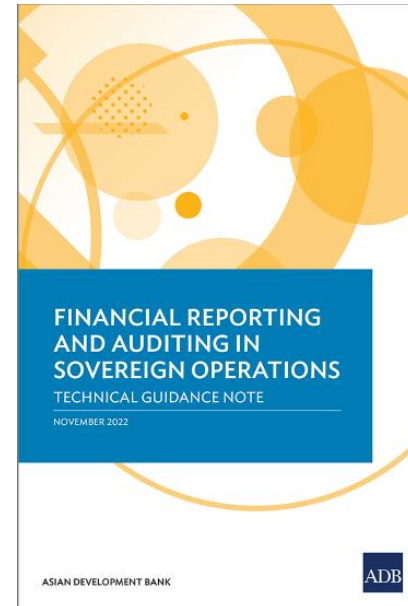
- For those who have, or plan to have, a key role in the preparation of Project Financial Statements (PFS) for submission to the Asian Development Bank (ADB)
- Provides the knowledge and skills to prepare PFS in accordance with the requirements of ADB.

# Technical Guidance Notes



<https://www.adb.org/sites/default/files/cost-estimation-sovereign-operations.pdf>

<https://www.adb.org/sites/default/files/financial-reporting-auditing-sovereign-operations.pdf>

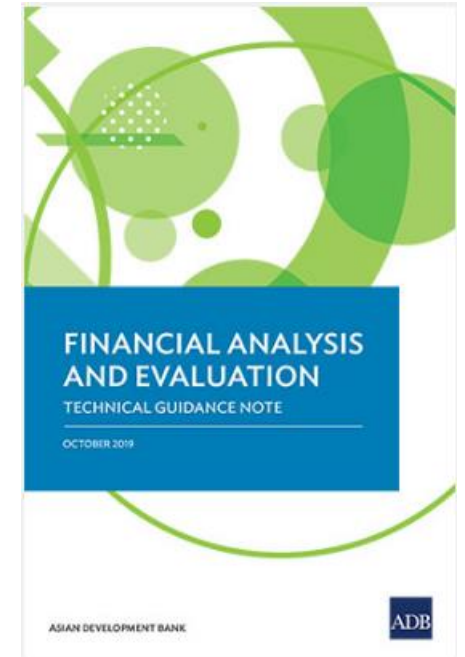


Financial Management Technical Guidance Note

<https://www.adb.org/sites/default/files/page/82468/financial-management-assessment.pdf>

May 2015

Financial Management Assessment



<https://www.adb.org/sites/default/files/institutional-document/535126/financial-analysis-evaluation-guidance-note.pdf>





# Q&A SESSION



# Thank You!

## Training Evaluation

*Thank you for your participation in the Financial Management Training. We would appreciate your feedback! Please rate your training experience below. The survey will take approximately 5-10 minutes to complete.*

Feedback Form - Financial  
Management Training Islamabad.

01 May 2025



<https://forms.office.com/r/jNsja0Mk1w>

ADB