



Republic of the Philippines
COMMISSION ON AUDIT
Commonwealth Avenue, Quezon City, Philippines

INDEPENDENT AUDITOR'S REPORT

THE BOARD OF TRUSTEES

Metropolitan Waterworks and Sewerage System
Katipunan Road, Balara
Quezon City

Report on the financial statements

We have audited the accompanying financial statements of the Metropolitan Waterworks and Sewerage System, which comprise the statement of financial position as at December 31, 2014, and the statement of comprehensive income, statement of changes in equity, and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with generally accepted state accounting principles in the Philippines and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Philippine Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in

the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Qualified Opinion

The accuracy and existence of the two accounts, Land and Land Improvements, and Building & Structures with carrying value of P19.226 billion and P27.788 billion respectively, were not ascertained due to incomplete inventory taking required under Section 102 of PD 1445 and COA Circular 80-124.

Also included in the Building & Structures account was Other Structures with carrying value of P27.577 billion which was not accurately stated due to:

- a. Capitalizing borrowing costs incurred after the completion of the project with an aggregate cost of P269.68 million, inconsistent with PAS 23;
- b. Recognizing depreciation charges only on the period the asset was reclassified to the PPE account and not when the asset was used as required under PAS 16, resulting in an understatement of P218.733 million; and
- c. Inclusion of the cost of consultancy services for the feasibility study and preliminary design of Angat Water Utilization and Aqueduct Improvement Project (AWUAIP) Phase II incurred in CY 2005 in the amount to P18.50 Million, contrary to PAS 38.

Of the balance of Other Receivables at P5.832 billion, the amount of P5.110 billion or 88% were not recognized as liabilities by the Concessionaires including dormant account totaling P296.825 million; hence its collection was doubtful.

For Accounts Receivable of P1.118 billion and P95.247 million representing amount collectible from Maynilad Water Services Inc. (MWSI) for penalties on delayed payment of concession fee, and of borrowing cost, respectively, the account, *Other Deferred Credits*, a liability account, was credited instead of the appropriate income account. This erroneous entry made in CY 2007 remained uncorrected as at December 31, 2014.

Dropping from the books of accounts of various land accounts totaling P267.207 million was not adequately documented to prove the validity thereof.

Qualified Opinion

In our opinion, except for the effects of the matters described in the Basis for Qualified Opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of Metropolitan Waterworks and Sewerage System as at December 31,

2014, and of its financial performance and its cash flows for the year then ended in accordance with generally accepted state accounting principles in the Philippines.

Emphasis of Matter

We draw attention to Note 24 to the Financial Statements, which describes the uncertainties related to the lawsuits or claims by third parties against MWSS which are either pending in courts or under negotiations. No provision for contingency is recognized in the financial statements since the outcome of said lawsuits are not presently determinable.

Likewise, we draw attention to Note 26 to the Financial Statements which discloses that the System has unreconciled balances in the asset and liability accounts which were taken up as one comprehensive unreconciled account. At year-end, 42 General Ledger accounts with net amount of P353.825 million remained unreconciled with the Subsidiary Ledger and unverified for lack of supporting documents.

Other Matter

The CY 2014 audit disclosed significant audit observations, other than those used as basis for qualified opinion:

- a. Among the foreign loans under the Long-Term Liabilities of MWSS was JBIC/OECF loan (Loan #PH110) of P1.275 billion for which no loan payment was remitted to the Bureau of Treasury despite the collections made from the Concessionaires amounting to P1.614 billion. This was attributed to the unresolved issue between MWSS and the Bureau of Treasury on whether the said is a liability of MWSS, or an equity of the Government to MWSS.
- b. The Cash and cash equivalents in the amount of P2.212 billion remained insufficient to cover the unpaid foreign loans already billed by the Bureau of Treasury and all recognized Trust Accounts, aggregating P2.455 billion at year-end. The Cash and cash equivalents already include the amount of P1.924 billion representing collections from the Concessionaires for the payment of the said foreign loans.

Also, the collections for the payment of its foreign loans totaling P1.803 billion were not restricted since no separate account for the subject collections was maintained in the books of MWSS.

Report on the Supplementary Information Required Under BIR Revenue Regulation No. 15-2010

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information on taxes, duties and license fees in Note 25 to the financial statements is presented for purposes of filing with the Bureau of Internal Revenue and is not a required part of the basic financial statements. Such information is the responsibility of management. The information has been subjected to the auditing procedures applied in our audit of the basic financial statements.

Emphasis of Matter

We draw attention to Note 24 in the Financial Statement which disclosed that the Bureau of Internal Revenue (BIR) assessed MWSS' withholding tax for year ending December 31, 2009. MWSS received Preliminary Collection Letters and Final Notice before Seizure on February 20, 2015, February 23, 2015 and March 23, 2015 respectively. BIR serve a Warrant of Garnishment upon Maynilad Water Services, Inc (MWSI) and Manila Water Company, Inc. (MWCI) on MWSS' receivable accounts, and such other property in the possession and control of the concessionaires. BIR lifted the Garnishment from MWSI and MWCI replacing them with MWSS's assets in the custody of the Development Bank of the Philippines (DBP) on April 29, 2015. MWSS filed Petition for Review (Ad Cautelam with Urgent Motion to Suspend Tax Collection) to the Court of Tax Appeals on May 20, 2015.

COMMISSION ON AUDIT

EYREN MARANAN - YULDE

OIC - Supervising Auditor

June 9, 2015