HLB MARKA AUDIT

COMMUNITY DEVELOPMENT AND INVESTMENT AGENCY "SUSTAINABLE VILLAGES IN THE KYRGYZ REPUBLIC" PROJECT

MANAGEMENT LETTER ON CONDUCTED AUDIT

FOR THE PERIOD FROM 1 JANUARY 2020 TO 31 DECEMBER 2020

Bishkek-2021

"Sustainable Villages in the Kyrgyz Republic" Project

Community Development and Investment Agency (ARIS)
102, Bokonbaeva Street,
Bishkek, the Kyrgyz Republic

Dear Madams and Sirs,

In accordance with our contract, on 8 February 2021, we completed auditing the financial statements of the "Sustainable Villages in the Kyrgyz Republic" Project (the 'Project') for the period from 1 January 2020 to 31 December 2020, prepared by the Community Development and Investment Agency (ARIS) and implemented in accordance with the Loan Agreement concluded between the Government (GKR) of the Kyrgyz Republic and the Islamic Development Bank (IDB).

In accordance with the Terms of Reference (scope of work), attached to the contract on auditing services, hereby we present this Letter in addition to the Auditor's report on the Project's financial statements you had provided us with.

The Letter includes comments and observations on accounting records, systems and controls and it also includes the aspects affecting the Project implementation which were audited during our engagement.

Independence of the engagement team members

The audit was conducted in accordance with:
- Terms of Reference (scope of work), which is an integral part of the Contract on audit;
- International Standard on Auditing 800 (Revised) "Special Considerations - Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks", adopted by the International Federation of Accountants (IFAC);
- International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code).

The International Standards on Auditing require that we comply with ethical requirements and demands for independence. In the appointment of the engagement team to audit the financial statements of the Project, we have confidence that the team meets ethical standards and independence requirements that allowed us to do the job, based on the principles of impartiality and objectivity.

Overall audit strategy

Our commitment was to perform the audit in accordance with the Loan Agreement concluded between the Government of the Kyrgyz Republic and the Islamic Development Bank ('IDB') hereinafter referred to as the "Contracting parties".

Audit of the Project financial statements is an expression of reasonable assurance regarding the fair presentation of the financial statements of the Project. The audit was conducted by sampling in the amount provided by the source accounting documents in accordance with the approved audit program. In order to be able to express reasonable assurance, we planned and performed the audit in such a way as to reduce the audit risk to an acceptably low level. For this purpose, we have studied the Project and its environment, including internal control, on the basis of which we identified and evaluated the risks of material misstatement in respect of which we fulfilled the relevant procedures. The audit planning

allowed us to assign the necessary resources and the timing of audit procedures. There were no discrepancies between the assigned resources and the timing of the audit. The task of this engagement included the expression of an opinion by the auditor:

a) whether all of the Project's sources of funds and their uses reported by the ARIS in its financial statements, including the Statement of Sources and Uses of Funds for the audited period, occurred in reality ('actuality'), were true ('accuracy') and eligible ('eligibility');

b) whether the cash flows of the Special Accounts, as well as supporting documents and information provided with it, can truthfully rely on the support of the Applications for replenishment in accordance with the requirements described in the Agreement;

c) that the appropriate supporting documents and reports on the Project are properly kept and there is clear correlation between the accounting data and the reports presented to the Islamic Development Bank;

d) that the internal control system (ICS) includes all corresponding policies and procedures adopted by the ARIS to support proper implementation of the Project tasks that means ordered and effective performance including safety of assets, prevention and reveal of facts of fraud and errors, accuracy and completeness of accounting records, as well as timely preparation of the financial statements;

e) that measures are taken to ensure the Project's assets integrity;

f) whether during the reporting period the ratio of financing and expenditures at the expense of the Islamic Development Bank, the Islamic Solidarity Fund for Development with a view to reimbursement and the Government of the Kyrgyz Republic, established in the Loan Agreement, were observed.

'Eligibility' means that the funds provided as the loan have been spent in accordance with the Loan Agreement terms paying proper attention to economy and efficiency and only for the purposes aimed at the Project financing.

Accounting policies

The ARIS is responsible for the selection and use of appropriate accounting policies. In our opinion, the accounting policies selected by ARIS are adequate and applicable to the Project's activities. The significant accounting policies are described in Note 2 to the Project financial statements.

We have noted that during the reporting period, the Project did not carry out any operations for which there is an insufficiency of regulatory standards. We also note that the financial statements in all material respects do not contain circumstances and events related to a different period.

Auditor's adjustments

The International Standards on Auditing require that we aggregate all known and proposed adjustments, revealed during the audit, except for insignificant adjustments, about which relevant managers were informed. All the adjustments proposed by the auditors were imported into the financial statements.

Financial information on the Project's expenditures

The amount of expenses that was the subject of this audit is USD 3,909,944.67. The cost cover ratio was 91% (USD 3,167,049.21). This ratio represents the total expenses sampled by us, expressed as a percentage of the total expenses that were the subject of the verification.

Subsequent events

After the approval of these financial statements, no events happened, which could affect the amounts presented in the financial statements.

Disagreements with management

We have met fruitful collaboration on the part of the management and the staff during our audit. To get better understanding we had full access to the documents which were necessary for our auditing. We have not had any disagreements with the management.

Review of the auditor previous reporting period recommendations

During the course of our audit, we reviewed the audit recommendations for the previous reporting period. Below we suggest that you familiarize yourself with the results of our review.

Observation	***Recommendations***	**ICS state as of the date of the audit**
For 2019:		
During the audit, we noted cases when the Project Coordinator approved the applications for payments to consultants earlier than the Project's engineer and the executor - consultant himself approved them. Also, in some cases, the Coordinator approved the acts of services performed, prepared for the reporting months before the end of the period for the provision of services.	The Project management shall establish additional control over the preparation and approval of documents. ***Management comments*** *According to the work plan, the consultant completed all the activities planned for the month by the approved date of the report.*	The Project management has established additional controls over the execution and approval of epy documents. The 2019 observation has been fixed.

Significant internal control weaknesses

During the audit, we have noted some areas related to the work of the internal control system and other operational units that we present for your consideration. All comments and recommendations were discussed with the Financial Manager in order to improve the efficiency of the operating system and the internal control system. Appendix A to this Letter reveals such shortcomings.

We have tested the procedures which were sufficient to provide a known assurance that:
- The funds of the Project were used in accordance with the terms of the Agreements concluded with the Project Executors, with due regard to economy and efficiency and only for the purpose of financing the Project;
- The necessary supporting documents and reports on the Project are kept in full;

In general, the funds received for the Project were used in accordance with the budget items. The factual expenses were incurred and paid.

Management representations

During the audit we requested representations from management concerning various issues related to the financial reporting. These representations are contained in the letter of representation from the management of ARIS.

Use of this Letter

This Letter has been prepared exclusively for the purposes specified in the aforesaid objectives and solely for confidential use by the ARIS and IDB, and solely for the purpose of its submission to the Parties for

consideration in accordance with the requirements envisaged by the Loan Agreement. This Letter should not be used for any other purposes, and may not be distributed to any third parties.

This Letter has been prepared only based on the Project financial statements, stated above in paragraph "Overall audit strategy", and does not apply to any other project financial statements of the ARIS.

In conclusion, we would like to express our appreciation to the management and staff members of the Project for their support and assistance rendered in the process of our audit.

If you would like to discuss any issues of this Letter in more detail, please do not hesitate to contact us.

Truly yours,

Director
HLB MARKA AUDIT LLC

A.M. Asylbekova

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Appendix A to the Management Letter

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1. **Monitoring, including inventory of property supplies and construction and installation works** **8**

1. Monitoring, including inventory of property supplies and construction and installation works

As part of the audit of the financial statements for 2020 of the "Sustainable Villages in the Kyrgyz Republic" Project, on January 13, 2021, we carried out the monitoring procedures, including an inventory of property supplies and construction and installation works in the following construction sites:

- Construction of a roadside complex on the territory of Boroldoy Aiyl Aimak
- Construction of an elementary school for 100 places in the village. Novomikhaylovka, Chym-Korgon Ail Okmotu
- Construction of a gym in the village. Chaldovar, Frunzensky Ayil Okmotu
- Construction of a kindergarten for 50 children in the village. Rovnoe, Kurpuldok Aiyl Okmotu
- Construction of the building of the Group of Family Doctors No. 3 p. Chaldovar Frunzensky Aiyl Okmotu
- Extension of the resuscitation department, the premises of the entrance group and the overpass to the building of the reception department of the hospital in the city of Kara-Balta, Zhayil district.

Observations

In the process of the monitoring the construction sites, we noted the following:

1) In the act of completed works on the construction of the Sports Hall in the village of Chaldovar from "Ulan Stroy Company" LLC it is indicated:
- paragraph 2.6.17 "Installation of centrifugal pumps" for the amount of KGS 2,000
- paragraph 2.6.23 "Purchase and installation of curtains in shower rooms" 4 units*1,200 soms = KGS 4,800.

The indicated items were available in the act, but at the time of monitoring were not identified.

Recommendations

The Project management shall establish additional control over the execution of all positions specified by contractors in the acts of works performed.

Management comments

Concerning the construction of the Sports Hall in the village of Chaldovar. At the time of delivery of the Certificate of completed works of the completed object in operation to the Department of State Expertise, all centrifugal pumps and curtains were installed by the contractor organization "Ulan Stroy Company" LLC. After putting the object into operation and acceptance of the balance Frunzenskiy Ayil Okmotu, the gym began to operate for the safety of centrifugal pumps and the shower curtain was removed to storage in the warehouse Ayil Okmotu, because the Ayil Okmotu was not resolved water supply facility. According to the terms of the Framework Agreement signed between ARIS and Aiyl okmotu "Item 10. Ayil Okmotu) provides connection to external networks (mains, water, sewer, etc.)".
At the time of the survey, the subject has not been connected to the water supply due to the fact that all funds Ayil Okmotu today frozen due to the Covid-19, quarantine measures and Ayil Okmotu cannot execute events for drilling of drinking water for the facility.
In March 2021, Ayil okmotu promises to complete the above-mentioned measures to provide water supply to the facility and install the above-mentioned materials and equipment according to the design.