

Greater Colombo Urban Transport Development Project (Outer Circular Highway Project) Phase 1 - 2013.

The audit of the financial statements of the Greater Colombo Urban Transport Development Project (Outer Circular Highway Project) Phase 01 for the year ended 31 December 2013 was carried out under my direction in pursuance of provisions in Article 154 (1) of the Constitution of the Democratic Socialist Republic of Sri Lanka. This Project was initiated with the grant amounting to Rs.417 million equivalent to Japanese Yen 580 million received for detailed design study on the Outer Circular Highway to the city of Colombo under an agreement entered into between the Japan International Cooperation Agency (JICA) and the Democratic Socialist Republic of Sri Lanka (GOSL) on 20 February 2011. The Loan Agreement No.SL- P89 had been entered into between former Japan Bank for International Co-operation (JBIC) and the Democratic Socialist Republic of Sri Lanka on 28 March 2007 to construct 11 kilometres highway from Kottawa to Kaduwela (Phase 01). Two subsequent Loan Agreements (SL-P91 and SL-P101) had been entered into between the GOSL and JICA on 29 July 2008 and 22 March 2011 respectively to construct 8.9 kilometres of the highway from Kaduwela to Kadawatha (Phase II).

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreements of the Project, the Ministry of Highways, Ports and Shipping (MOHP & S) is the Executing Agency and the Road Development Authority (RDA) is the Implementing Agency of the Project. The objectives of the Project are;

- (a) To construct an expressway in the outskirts of Colombo which connects with the Southern Expressway and other national roads radiating from Colombo city in order to mitigate traffic congestion in the Colombo Metropolitan Region and enhance connectivity with other regions, thereby of the country.
- (b) To mitigate traffic congestion in the Colombo Metropolitan Region to enhance connectivity with other regions by constructing a highway in the outskirts of Colombo that will link to major roads and the Southern Expressway thereby contributing to the strengthening of economic development among the regions in Sri Lanka.

The estimated total cost of the Project was Rs. 72,924 million and out of that, a sum of Rs. 52,007 million equivalent of Japanese Yen 46,974 million was agreed to be financed by the JICA. The construction of the highway under Phase 1 was scheduled to be commenced in May 2008 and expected to be completed within 48 months by April 2012. However, the contract had been awarded only on 22

October 2009 and expected to be completed only for 11 kilometres within 42 months by the year 2013. Further, the contract for construction of the highway under Phase II had been awarded to another contractor on 22 October 2009 and was expected to be completed within 36 months by 23 December 2013. However, this part had been treated separately and operated under another Project Monitoring Unit (PMU) with effect from 05 September 2011 according to the letter dated 25 April 2012 of the Department of Management Services issued on the request made by the Road Development Authority. The Section from Kottawa to Kaduwela (Phase 01) was completed and opened to the traffic on 08 March 2014.

1.3 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Generally Accepted Accounting Principles. This responsibility includes: designing, implementing and maintaining control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error, selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

2. Scope of Audit and Basis of Opinion

My responsibility is to express an opinion on these financial statements based on my audit. Audit opinion, comments and findings in this report are based on review of the financial statements presented to audit and substantive tests of samples of transactions. The scope and extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitations of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes the examination on a test basis of evidence supporting the amounts and disclosures in financial statements and assessment of accounting policies used and significant estimates made by the management in the preparation of financial statements as well as evaluating their overall presentation. I have obtained sufficient information and explanations which to the best of my knowledge and belief were necessary for the purpose of my audit. I therefore believe that my audit provides reasonable basis for my opinion. The examination also included such test of systems and controls, transactions, assets, liabilities and accounting records as deemed necessary to assess the following.

- (a) Whether the systems and controls were adequate from the point of view of internal control so as to ensure a satisfactory control over Project management and the reliability of books, records, etc. Relating to the operations of the Project.

- (b) Whether adequate accounting records were maintained on a continuing basis to show the expenditure of the Project from the funds of the Government of Sri Lanka and the lending agency, the progress of the Project in financial and physical terms, the assets and liabilities arising from operations of Project, the identifications of purchases made out of the Loans, etc.
- (c) Whether withdrawals under the Loans had been made in accordance with the specifications laid down in the Loan Agreements.
- (d) Whether the funds, materials and equipment supplied under the Loans had been utilized for the purposes of the Project.
- (e) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (f) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles.
- (g) Whether satisfactory measure had been taken by the management to rectify the issues highlighted in my previous year audit report and
- (h) Whether financial covenants laid down in the Loan Agreements had complied with.

3. Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, except for the effects of the adjustments arising from the matters referred to in paragraph 5 of this report, I am of opinion that;

- (a) The Project had maintained proper accounting records for the year ended 31 December 2013 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2013 in accordance with Generally Accepted Accounting Principles,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the opening and closing balances, withdrawals from and replenishments to the Special Dollar Account during the year ended 31 December 2013 had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2013 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,

- (d) satisfactory measures had been taken by the management to rectify the issues highlighted in previous year audit report, and
- (e) the financial covenants laid down in the Loan Agreements had been complied with.

4. **Financial Statements**

4.1 **Financial Performance**

According to the financial statements presented and information made available, the expenditure of the Project for the year ended 31 December 2013 amounted to Rs. 8,136 million and the cumulative expenditure as at 31 December 2013 amounted to Rs. 25,631 million. The following statement shows a summary of the expenditure for the year under review, the preceding year and the cumulative expenditure as at 31 December 2013.

Description	Expenditure incurred during the year ended 31 December		Cumulative Expenditure as at 31 December 2013
	2013	2012	
	Rs.	Rs.	Rs
Property, Plant and Equipment	853,446	1,880,728	195,601,601
Project Management	735,312,127	765,433,941	3,428,752,172
Lands and Land Improvement	300,716,035	(766,217,867)	2,719,629,115
Civil Works	6,819,882,450	3,696,031,011	18,124,183,068
Consultancy	273,997,833	219,668,901	1,143,384,710
Research, Development and other Costs	5,560,897	(166,365)	19,751,990
	8,136,322,788	3,916,630,349	25,631,302,656

5.1 **Audit Observations**

5.1.1 **Accounting Deficiencies**

The following observations are made.

- (a) According to the Cash Flow Statement, the total funds disbursed under Loan No SLP – 89 had been shown as Rs. 3,342,223,619. However, the corresponding amount had been shown in the balance sheet as Rs. 3,218,959,948. The reasons for the difference of Rs. 123,263,671 had not been explained to audit.

- (b) According to the Interim Payment Certificates Nos. 23 and 24, a sum of Rs. 587,973,996 was payable to the contractors, whereas according to the Ledger Account it was shown as Rs. 554,694,447. The difference of Rs. 33,279,549 was not been explained to audit.
- (c) According to the contract agreements for Consultancy and Civil Works, the assets such as motor vehicles, equipment, furniture, etc. purchased by the Contractor, out of the project funds are the properties of the Project. However, it was observed that out of the assets purchased through the Interim Payment Certificates submitted by the contractor, assets valued at Rs. 27,291,475 only had been shown in the financial statements for the year under review.
- (d) Compensations on land acquisition had been overpaid by Rs. 600,000 due to the erroneous calculations.
- (e) Contrary to instructions given in the Section 8.3.9 of the Circular No. PED/12 dated 02 June 2003 of the Department of Public Enterprises of the General Treasury, a sum of Rs. 141,741,679 had been remitted to the Road Development Authority up to 31 December 2013 as overhead charges.

5.1.2 Unreconciled Control Accounts

The following observations are made.

- (a) The Current Account maintained by the Project with the Road Development Authority had shown a payable balance of Rs. 2,468,490 as at 31 December 2013. However, the related corresponding balance in the Current Account maintained by the Road Development Authority had been shown as Rs. 10,602,815 as at that date. Although the difference was identified, necessary adjustments had not made in the accounts.
- (b) The balance of Rs. 647,225,985 shown in the Current Account maintained by the Project had not been agreed with the balance of Rs. 646,654,827 of the Current Account of the Outer Circular Highway Project – (Phase II). The difference of Rs. 571,158 had been identified but it had not adjusted in the respective accounts.
- (c) According to the Loan Account maintained by the Project, the disbursed loan amount had shown as Rs. 3,218,959,948 as at 31 December 2013, whereas balance in the related account maintained by the General Treasury it had been shown as Rs. 3,284,007,431. The difference of Rs. 65,047,483 identified had not been adjusted in the respective accounts.

6. Financial and Operating Review

6.1 Utilization of Funds

According to the financial statements and information made available, certain significant statistics relating to the financing of the Project, budgetary provisions and the utilization of funds up to the end of the year under review are shown below.

<u>Loan</u>	<u>Amounts agreed to be financed in the Loan Agreements</u>		<u>Funds Utilized as at 31 December 2013</u>	
	<u>JPY Mn</u>	<u>Rs. Mn</u>	<u>JPY Mn</u>	<u>Rs. Mn</u>
Loan P- 89	21,917	24,547	26,167	21,806
Loan P- 91	-	-	14	12
Loan P- 101	-	-	147	123
GOSL	8,920	8,109	7,382	6,152

	30,837	32,656	33,710	28,093 *
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* This amount differs from the amount shown in paragraph 4.1 of this report due to non inclusion of accrued expenditure.

6.2. Physical Performance

6.2.1. Physical Progress of the Phase 01 of the Expressway.

According to the progress reports of the Project for the year ended 31 December 2013, the actual progress achieved by the Project was 90 per cent as against the 100 per cent progress targeted for the year under review, thus indicating that actual progress had been behind targets by 10 per cent. Extension of time for construction works from Section 27 + 560 kilometre to Section 18 + 100 kilometre and Section from 18 + 100 kilometre to Section 17 + 500 kilometre of the highway had been granted.

6.2.3 Contract Administration

The following observations are made.

- (a) According to the Public Finance Circular No.2/2012 of August 2012, estimates for all procurements should be made by considering all the matters to ensure the

accuracy of the total cost of the procurement. However, it was observed that cost of Civil Works amounting to Rs. 2,891,143,073 pertaining to 83 variation orders had been included and other 03 variation orders valued at Rs. 52,947,744 had been withdrawn from the initial estimates. This situation would lead to a number of disputes and unfavourable effects to the Project. Further the approval from the Cabinet Appointed Tender Board had not been obtained for such scope variations.

(b) It was observed that the total cost of the contract had exceed by 20 per cent due to changes in the scope of work with the introduction of interchanges for the highway. The following observations are made in this connection.

- (i) The interchange at Athurugiriya which was not included in original design of the highway had been carried out under the Phase I of the Project. This construction had been carried out as a separate contract awarded to the same contractor. However a contract agreement had not been signed for that purpose. The recommendations of the Secretary of the Line Ministry that should be obtained according to paragraph 2 of Public Finance Circular No.2/2012 of August 2012 had not been obtained for the construction of interchange at Aturugiriya at a cost of Rs. 2,077,069,589.
- (ii) Further, the consent of the Project in terms of Clause 59.1 of the Conditions of Contract had not been obtained by the Contractor for the pavement construction works and laying of asphalt wearing course at the interchange at Athurugiriya which were not estimated at the initial stages and carried out by a sub-contractor. The cost amounting to Rs. 11,067,453 had been claimed and under a variation order.
- (iii) The construction works of the Interchange at Kotalawala was planned under Phase II of the highway. However, a temporary interchange constructed at cost of Rs. 84,657,425 had been constructed due to delays in construction of the permanent interchange and charged to the cost to the Phase I of the highway. Construction contract for temporary interchange at Kottawa had been awarded to the State Engineering Corporation on 13 November 2013. However, the respective works had been carried out by a sub-contractor without the approval of the Project.
- (iv) The construction of the interchange at Kottawa was planned for completion before the commencement of the Southern Expressway (STDP). However, a temporary interchange had been built under a variation order at a cost of Rs. 258,918,579 by the Project due to delays in construction of permanent interchange. It was observed in audit that if the Project had properly planned to construct the interchange at the initial stage, the expenditure

incurred for the temporary interchange could have been saved. However, the temporary interchange had been demolished and new permanent interchange had been built by the Project at a cost of Rs. 928,993,187. Further, the permanent interchange was required to be constructed within 24 months according to the Conditions of the Contract had been completed after 36 months. The liquidated damages thereon amounting to Rs.16.91 million had not been charged. According to the explanations of the Secretary to the Ministry of Highway, Ports and Shipping, as the temporary interchange was constructed and the, Road Development Authority could operate the highway without any loss of income in spite of the delay of construction of the permanent interchange. Therefore, liquidated damages were waived off.

- (c) According to the Conditions of the Construction Contract, the Contractor should adhere to the quality assurance system for the road construction purpose and therefore, quality assurance staff should be planned and deployed by the Contractor. However, it was observed that the Contractor had not complied with the above requirement. Therefore, additional staff for quality assurance activities had been recruited by the Consultant of the Project and claimed an amount of Rs.7,258,126 through a variation order.
- (d) It was observed 13 Non-Conformance Product Notifications (NCPN) had been issued by the Consultant from July 2012 to December 2013 which were significant in the maintenance of the highway. But action had not been taken to rectify such notification requirements.
- (e) According to Clause 14.2 of the Condition of the Contract, the contractor is required to revise the work programme when granting extensions of time to complete the works. However it was observed that the contractor had not submitted a revised work programme to complete the works from 17+500 kilometre 27+560 kilometre.
- (f) According to Clause 56.1 of the Conditions of the Contract, the Engineer of the Contract should certify the measurements of actual work done. However, it was observed in audit that an overpayment of Rs. 68,703,786 had been made to the contractor on works carried out in three sections. Such overpayments had been recovered after three months providing additional financial benefits to the Contractor for over three months.

- (g) Although the rate of asphalt concrete for wearing course is Rs. 14,161 per ton as approved in the Bill of Quantities, the rate of Rs. 17,701 had been applied for payments for the Contractor, without explaining the reasons for variation.
- (h) Although proper compaction of asphalt concrete wearing course should be laid according to the Method Statement of Specification 406.3 (e), it was observed that payments had been made for poor standard wearing course in six occasions without considering the reports submitted by the Material Engineer employed by the Consultant.
- (i) As stipulated in the Clause 62.2 of the Condition of the Contract, the Interim Payment Certificates which exceed the value of Rs. 200 million should be taken in to consideration for the Technical Evaluation Committee. However six IPCs which did not exceed Rs. 200 million had been evaluated.
- (j) Asphalt laid according to the initial design for the construction of shoulders of the highway had been removed subsequently as it was not suitable and safe for the road users. Therefore, 2279 tons of asphalt laid had been removed subsequently, at a cost of Rs. 1,391,365. A new Asphalt layer had been applied at a cost of Rs. 48,677,164 and the payment was made under a variation order without a proper approval.

6.2.4 Lands Acquisition and Resettlement Activities of the Project

According to the financial statements, the Project had spent a sum of Rs. 2,719.6 million up to 31 December 2013 for acquisition of six lands 7.5691 hectares in extent to resettle the persons displaced due to Project activities .The following observations are made in this connection.

- (a) It was observed that the land acquisition and resettlement activities of the Project were expected to be completed at the end of December 2011. However, the land acquisition activities had been completed in Phase 01 of the highway by 99 per cent as at 31 December 2013 and only 70 per cent of the resettlement activities had been completed as at that date.
- (b) Although a sum of Rs. 13,472,204 had been paid as incentive to expedite the land acquisition activities, interest aggregating Rs. 174,492,185 had been incurred by the Project as at 31 December 2013 on delays in payment of compensations for the lands acquired.
- (c) A land at Kaduwela of 324.17 perches in extent had been acquired by the Project at a cost of Rs. 71,815,877 in 2009 for resettlement of displaced persons and subsequently a sum of Rs. 2,890,781 had also been spent for land development

activities. The acquired lands had been demarcated into 21 plots and out of that, 10 plots had remained idle even as at 30 December 2013 without taking an action to handover to the persons displaced.

6.2.5 Human Resource Management

The following observations are made.

- (a) According to the information made available, the Department of Management Services had approved to recruit 56 Persons for 24 posts for the Project Management Unit of the Project.

However 03 Management Assistants, 04 Local Consultants, 01 Resettlement Consultant, 01 Design Consultant and 01 Transport System Analyst had been deployed by the Project for the respective posts which were not approved by the Department of Management Services, and a sum of Rs. 7,736,364 had been as salaries in the year under review.

- (b) The staff for the Project should be recruited in terms of the Management Services Circular No 33 of 05 April 2007 issued by the Department of Management Services of the General Treasury. Although cadre of the Project had been approved by the Department of Management Services 3 Management Assistants recruited outside the cadre without obtaining the relevant approval and remuneration amounting to Rs. 1,316,507 had been paid during the year under review.

- (c) According to paragraphs Nos. 2.2.4 and 2.2.7 of Circular No. 33 dated 05 April 2007 of the Department of Management Services, Staff recruitments should be made by calling for applications through notices published in national newspapers and appointments should be made on contract basis, not exceeding three years. However, all members of the Project Staff consisted of the officers released from the Road Development Authority had been recruited on temporary basis contrary to the above provisions.

- (d) Salaries of Road Development Authority employees attached to the Project had been paid on the formula introduced by the Road Development Authority contrary to the Circular No. 33 of 05 April 2007 issued by the Department of Management Services. In this connection a sum of Rs. 208,796,395 had been paid as salaries up to 31 December 2013 without adhering to the above instructions.

- (e) Although Road Development Authority employees attached to the Project are not entitle to receive bonus, medical allowances and Road Development Authority allowance, it was observed a sum of Rs. 3,405,403 had been paid as bonus and

medical allowance contrary to Sections 8.3.9 and 8.6 of the Circular No. PED/12 dated 02 June 2003 issued by the Department of Public Enterprises.

- (f) Several personnel had been recruited for the key posts of the Project such as Project Directors, Deputy Directors, Engineers, Accountants, Administrative Officers and Local Consultants from time to time during the period of 8 years. It was observed in audit that the Road Development Authority as an implementing agency as a practice, assign officers to the Project in order to provide experience in Project management and financial benefits for them, Hence the aspects of smooth functioning timely implementation and closely monitoring of the Project had become lesser priorities.
- (g) Four local consultants had been recruited without following the recruitment procedure and paid remuneration amounting to Rs. 642,423 up to 31 December 2013. According to the Job descriptions, the Consultants had not been assigned at any specific duties from which the outcome can be measured. But these Consultants had been entrusted with the work that had already been carried out by other staff officers of the Project. Therefore the beneficial impact and the contribution from those Consultants could not be ascertained in audit.

6.2.6 Utilization of Motor Vehicles

The motor vehicle fleet of the Project comprised 02 motor vehicles purchased out of the Project funds, 09 hired motor vehicles, a motor vehicle allocated by the Road Development Authority and 04 motor vehicles provided by the Contractor. Eight motor vehicles had been assigned to the officers who were not entitled to receive motor vehicle facilities in terms of Circular No 33(1) dated 20 December 2007 of the Department of Management Services.

6.2.7 Matters in Contentious Nature

The following observations are made.

- (a) Variation Orders valued at Rs. 2,907,895 had been approved for various purposes contrary to the objectives of the Project.
- (b) A sum of Rs. 14,741,679 had been remitted up to 31 December 2013 to the Road Development Authority as overheads contrary to the instructions given in Section 8.3.9 of the Public Enterprises Circular No. PED/12 dated 02 June 2003.
- (c) Six Engineers had participated 20 days workshop in Japan in March 2013 and had been paid a sum of Rs. 2,128,200 by Project and the officers who participated at

the workshop had not submitted the reports in terms of the Circular No. CA/1/1/16/1 dated 09 July 2010 of Secretary to in President.

- (d)** The Sub – Contractor had been paid Rs. 172,339,728 for the blasting and removal of 9218 m³ of hard rock at a rate of Rs. 18,696 for cubic meter at a section 18+002 kilometres to 18 + 110 kilometre. Further, the contractor had allowed to use 920m³ and out of that 143m³ had been used. The information relating to the usage or sale or disposal of balance rocks material had not been explained for audit.