

Pro -Poor Eastern Infrastructure Development Project

1. 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 2 of this report, I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2010 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2010 in accordance with Generally Accepted Accounting Principles,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the withdrawals from and replenishments to the Special (Yen) Account during the year ended 31 December 2010 had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2010 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,
- (d) the statement of expenditure (SOE) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement,
- (e) satisfactory measures had been taken by the management to rectify the issues highlighted in my previous audit report, and;
- (f) the financial covenants laid down in the Loan Agreement had been complied with.

2. Financial Statements

2:1 Financial Performance

According to the Financial Statements presented and information made available, the expenditure of the Project for the year under review amounted to Rs.2,573,697,860 and the cumulative expenditure as at 31 December 2010 amounted to Rs.5,380,039,837. The following statement shows a summary of expenditure for the year under review and the preceding year and the cumulative expenditure as at 31 December 2010.

Category of Expenditure	Expenditure for the year		Cumulative expenditure as at 31 December 2010
	ended 31 December		
	<u>2010</u>	<u>2009</u>	
	Rs.	Rs.	Rs.
Fixed Assets	57,915	105,300	104,673
Work in Progress	2,394,840,957	1,622,754,746	4,876,231,213
Consultancy	178,798,988	176,688,736	503,703,951
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	2,573,697,860	1,799,548,782	5,380,039,837
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2.2 Special (Yen) Account

According to the financial statements and information made available, the operations of the Special (Yen) Account during the year under review and the balance as at 31 December 2010 are given below.

<u>Particulars</u>	<u>SLRs.(MN)</u>	<u>SLRs.(MN)</u>	<u>Yen (MN)</u>
Balance as at 01 January 2010		2,928.9	2,410.2
Less: Withdrawals	1,585.4		1,219.9
Foreign Exchange Gain	<u>(255.8)</u>	1,329.6	-
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Balance as at 31 December 2010		<u>1,599.3</u>	<u>1,190.3</u>

3. Audit Observations

Following observations are made.

3.1 Accounting Deficiencies

- (i) The foreign exchange gains / losses arising from the transactions of the Foreign Aid Account in the year under review had not been computed and disclosed in the accounts.
- (ii) Even though the Project had been commenced in the year 2006, a sum of Rs.1,321,098 representing the overhead expenses of the Road Development Authority in respect of the year 2005 had been reimbursed to the Road Development Authority from the Project funds in the year 2008. That transaction had not been settled even during the year 2010.
- (iii) A sum of Rs.17,756,097 had been received in the year 2010 from the National Water Supply and Drainage Board for carrying out repairs to the excavations and damage caused to the roads developed by the Project in the process of Laying water mains. Out of this amount a sum of Rs.2,937,763 or 16.55 per cent only had been utilized for the purpose. The balance sum of Rs.14,818,334 or 83.45 per cent had been transferred to another imprest account without being utilized for the Project activities.

- (iv) Even though the amounts payable to the contractor and the consultant totaling Rs.200,145,615 had been adjusted to the Foreign Aid Receivable Account in the year 2009, that amount had been adjusted again in the accounts for the year 2010 as well. As such the Foreign Aid Account and the amount payable to the contractor and consultant had been overstated by a sum of Rs.200,145,615.
- (v) Even though a sum of Yen 24,533,397 had been paid to the contractor in December 2010, the Project had accounted the same value in the accounts erroneously and as a result an overstatement of Yen 24,533,397 was observed in Foreign Aid Receivable Account and Contractors Account .
- (vi) Provision for accrued expenses for the year under review had been overstated by Rs.280,000 due to the adjustment of same amount paid to a supplier.

3.2 Contract Administration

3.2.1 Payments to Contractors

Following observations are made.

(a) Road Reconstruction

Even though the civil works of the road section should have been completed by 31 December 2010 in accordance with the contract agreement, work valued at Rs.273,421,407 relating to 139 items of the Bill of Quantities had not been carried out. It was represented 8.8 per cent of the total cost of the contract. The reasons therefor were not made available to audit.

(b) Construction of the Kallady Bridge

A sum of Rs. 5 million had been paid on 23 February 2011 on the Interim Payment Certificate of the construction of the Kallady Bridge for December 2010 and January 2011 submitted by the contractor. The following observation is made in that connection.

Even though a period of 10 months had elapsed by 31 January 2011 since the commencement of work on the bridge, only 75 per cent of the contract activities relating to 20 per cent advance payment of the contract value

amounting to Rs. 162,693,913 had been completed by the contractor. In view of the delays resulting from the lack of efficiency it is doubtful whether work commensurate with the advance paid will be done during the contract period of 18 months.

- (c) Sums totaling Rs.575,000 had been paid to 06 Engineers of the Road Development Authority for the preparation of fresh designs for the Kallady Bridge. The sum payable to the Consolidated Fund on the fees obtained by rendering services to another institution or individual by utilizing the knowledge gained by Public Officers while in Government Service had not been recovered in terms of Section 2 of Chapter IX of the Establishments Code.

3.2.2 Supervising Consultant

A Joint Venture Consultancy Company had been appointed in the year 2007 for the procurement of consultancy services from foreign and local consultants for the Project at the agreed costs of Yen 228,600,000 and Rs.180,200,000 respectively. Out of that, the actual cost of foreign and local consultancy alone, exclusive of incidentals and contingencies amounted to Yen 216,254,710 and Rs.166,542,411 respectively.

Following observations are made in this regard.

- (a) The Document Specialist who had been assigned with 6 months service period commencing from June 2007 had served for one month only up to the end of December 2010. As such it was not possible to ensure in audit as to whether the required service had been obtained as he had served only for one month. The balance sum of Yen 13,838,470 Out of Yen 16,551,470 allocated for that purpose, represented 84 per cent of the allocation. As such it was not possible to be satisfied in audit that the documents relating to the Project had been prepared properly and the related activities of the Document Specialist had been performed properly as expected by the Project.
- (b) Even though the officers had not been recruited for 07 posts in the consultancy service, a sum of Rs.22, 702,579 for 161 man months had been shown in the Bill of Quantities. As such, it was not possible to satisfy in audit that the work of the contractor which should have been inspected by those officers had been performed properly.

3.3 Payments made from the Consolidated Fund on Activities Contrary to the Project

The following observations are made in this connection.

- (a) A sum of Rs.11,975,941 being the expenditure on road improvements payable to the contractors from the foreign loan and a sum of Rs.957,152 which had been paid to the Road Development Authority as cost of labour included in the project estimate and a sum of Rs.1,767,000 spent on the purchase of water pipes for laying under the main road of Kattankudy Town which were not included in the Project Estimate had been spent out of the Consolidated Fund. The reasons therefore were not made available while the Treasury concurrence for that had not been obtained.
- (b) A sum of Rs.454,897 had been paid to a private transport company in connection with the transport activities of the Private Secretary to the Minister of Transport which was not related to the Project activities.

4. Financial and Operating Review

4.1 Financial Review

4.1.1 Utilization of Funds

	Amount agreed to be provided as per agreement		Budget for the year 2010	Utilization of Funds for the year 2010	Funds utilized up to 31 st December 2010
	Yen (Mn)	Rs (Mn)	Rs (Mn)	Rs (Mn)	Rs (Mn)
JBIC	4,460	4,756	1,790.0	1,630.8	4,716.3
GOSL	-	1494	241.9	241.9	591.3
	<u>4,460</u>	<u>6,250</u>	<u>2,031.9</u>	<u>1,872.7*</u>	<u>5,307.6*</u>

* These amounts differ from the amounts shown in paragraph 4.1 of this report due to exclusion of advances and accrued expenditure.

4.2 Operating Review

4.2.1 Performance

According to the Loan Agreement, the reconstruction of the 100 kilometer road between Akkaraipattu and Tirikkandumadu and the construction of a new bridge at Kallady costing Rs.6,250 million to be completed within 30 months (913 days) had been awarded on 06 December 2007 for a sum of Rs.3,806,804,232 exclusive of tax to the China Overseas Engineering Company. In view of the low level of the performance of the contract, the construction of the Kallady Bridge had been abandoned by the Company with the concurrence of the Executing and Implementing Agencies of the Project. In consequence, a sum of Rs.700 million had been deducted from the contract amount of the company and the contract for the construction of the bridge at a cost of Rs.813,469,566 to be completed within 540 days from 01 April 2010, had been awarded on 25 March 2010 to the State Development and Construction Corporation.

Following observations are made in this connection.

- (a) Even though the scope of the original contract had been reduced, two further extensions of 184 days had been granted by 31 December 2010 instead of reducing the contract period for the reconstruction of the roads section.
- (b) An increase of Rs.113,469,566 was observed in the new contract price relating to the construction of the bridge and the Project had agreed with the lending institution to settle that amount from the expected exchange gain during the Project period. In the event of inability to complete the contract with the available funds during the period the GOSL will have to bear the additional cost.
- (c) The expected progress as at 31 December 2010, on the new contract for the construction of the Kallady Bridge in 18 months from 01 April 2010 to 30 September 2011 had been 26.08 per cent as against the actual progress of 8.2 per cent.
- (d) According to the work plan and the notes to the progress of the contractor included in the Progress Report for December 2010, the decrease in the progress of the main items between the expected and the actual progress was ranging from 0.08 per cent to 29.04 per cent.

4.2 .2 **Physical Performance**

Physical Performance of the road and Kallady bridge were 99.81% and 8.2% against the planned activities of 100% and 26.08% respectively as at 30 September 2010. Details are as follows.

Contract	Revised contract value	Actual expenditure as at 31 December 2010	Expected progress as at 31 December 2010 (%)	Actual physical progress as at 31 December 2010 (%)
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	Rs (Mn)	Rs (Mn)		
	-	-	-	-
1. Reconstruction of 64km from 364km to 427km of A4 road and 36km of A15 road	3106.804	2906.614	100	99.8
2. Construction of Kallady bridge	813.469	59.387	26.08	8.2