

The audit of financial statements of the Greater Colombo Urban Transport Development Project (Outer Circular Highway Project) Phase II 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 is 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 2001. Further, the first Loan Agreement No.SL-P89 had been entered into between the former Japan Bank for International Co-operation (JBIC) presently the Japan International Cooperation Agency and the Democratic Socialist Republic of Sri Lanka on 28 March 2007 to construct 12 kilometres highway from Kottawa to Kaduwela (Phase I). Second Loan Agreement No.SL-P91 had been entered into between the GOSL and JICA on 29 July 2008 and third Loan Agreement No SLP 101 had been entered into between the GOSL and JICA on 22 March 2011 to construct 8.9 kilometres highway from Kaduwela to Kadawatha (Phase II). A separate Project Monitoring Unit (PMU) had been established according to the Letter dated 25 April 2012 of the Department of Management Services issued on the request made by the Road Development Authority on 05 April 2012. Therefore, these financial statements for Greater Colombo Urban Transport Development Project (Outer Circular Highway Project) Phase II for the year ended 31 December 2013 had been separated and presented financial statements accordingly.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement of the Greater Colombo Urban Transport Development Project (Outer Circular Highway Project) Phase II, then Ministry of Highways, Ports and Shipping presently, the Ministry of Highways, Higher Education and Investment Promotion is the Executing Agency and the Road Development Authority is the Implementing Agency of the Project. The objective of the Project is to construct a highway 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. According to the Loan Agreement, the estimated total cost of the Project is Japanese Yen 36,998 million equivalent to Rs. 44,880 million and out of that, Japanese Yen 25,513 million equivalent to Rs. 27,094 million was agreed to be financed by the Japan International Cooperation Agency. The construction of the highway under Phase II was scheduled to be commenced in May 2008 and was expected to be completed within 48 months by April 2012. However, the contract for construction of the highway under Phase II had been awarded to a contractor from the People's Republic of China on 22 October 2009 and was expected to be completed by March 2015. The value of the contract amounted to Rs. 66.7 billion.

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 internal 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 a 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 managements 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 a 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 the Project, the identifications of purchases made out of the Loan, etc.
- (c) Whether withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreements,
- (d) Whether the funds, materials and equipment supplied under the Loan 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 measures 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, and
- (c) 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.18,793,257,546 and the cumulative expenditure as at 31 December 2013 amounted to Rs.24,834,824,577. The following statement shows a summary of the expenditure for the year under review, expenditure for the preceding year and the cumulative expenditure as at 31 December 2013.

Description	Expenditure for the year ended 31 December		Cumulative Expenditure as at 31 December 2013
	2013	2012	
	Rs.	Rs.	Rs.
Property, Plant and Equipment	579,277	1,583,655	3,242,066
Land and Land Improvement	144,879,973	820,137,996	1,661,691,368
Project Management Expenses	54,403,206	96,630,020	160,036,875
Construction Cost	18,238,660,551	4,123,658,531	22,372,272,209
Consultancy	354,734,539	282,847,520	637,582,059
	<u>18,793,257,546</u>	<u>5,324,857,722</u>	<u>24,834,824,577</u>

5. Audit Observations

5.1 Accounting Deficiencies

The amounts shown in the Statements of Financial Position did not agree with the corresponding documents in several instances. The Project had identified such differences after being pointed out in Audit. However, the financial statements had not been rectified accordingly. Details of the instances observed in audit are given below.

- (a) According to the information collected, the compensation paid for Land Acquisition for Resettlement Activities amounted to Rs. 1,516,444,923. However, it was shown in the financial statements as Rs. 1,516,811,395, thus showing a difference of Rs. 366,472.
- (b) According to the financial statement, a sum of Rs. 18,792,678,370 had been spent on civil works in progress. However, the corresponding figure shown in the cash flow amounted to Rs. 24,115,952,439 due to an error in computation of cash flows from investing activities.
- (c) According to the statements of cash flow for the year under review, outflows on advance and prepayment amounted to Rs. 3,635,400. However, according to the Statement of Financial Position it was shown as Rs. 3,638,400.
- (d) According to the cash flow statement, funds disbursed during the year under review had been shown as Rs. 11,012,776,383. However, the corresponding amount shown in the Statement of Financial Position amounted to Rs. 10,740,594,665.
- (e) Payables amounting to Rs. 14,577,343 to the Local Consultants as at 31 December 2013 had been brought to account twice.
- (f) According to the Interim Payment Certificates the mobilization advances aggregating to Rs. 1,822,010,292 had been recovered as at 31 December 2013. However, according to the financial statement it was shown as Rs. 3,635,672,999.

5.2 Un reconciled Control Accounts

The Register of Fixed Assets had not been updated and as a result, assets procured at a cost of Rs. 1,918,542 during the year under review had not been recorded in the Register of Fixed Assets.

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 and the utilization of funds up to the end of the year under review are shown below.

Source	Amount agreed to be provided in the Loan Agreements		Budgetary Provision for the year 2013	Funds utilized during the Year 2013	Utilization of Funds Up to 31 December 2013	
	JPY	Rs.	Rs.	Rs.	JPY	Rs.
	millions	millions	millions	millions	millions	millions
JICA - Loan P91	25,513	27,094	10,256	10,255	7,798	22,488
GOSL	11,485	17,786	389	389	503	1,161
	-----	-----	-----	-----	-----	-----
	36,998	44,880	10,645	*10,644	8,301	23,649
	=====	=====	=====	=====	=====	=====

* This figure did not agree with the amounts shown in paragraph 4.1 of the report as the payables at the year end had not been included.

6.2 Physical Performance

6.2.1 Physical Performance of the Phase II of the Expressway

According to the progress reports of the Project for the year ended 31 December 2013, the actual progress achieved had been 44 per cent as against the amended targeted of 68 per cent, thus indicating that actual progress remained behind the target. According to the explanation of the Secretary to the Ministry of Highways, Higher Education and Investment Promotion, the delays caused on construction of bridge over Kelani River unexpected variations on rock profile, re-designs of file caps and delays on approval received from Department of Irrigation for temporary bridges etc, had been the reasons for the low performance.

6.2.2 Contract Administration

The following observations are made.

- (a) As the bid value of Rs. 62.041 billion submitted by the contractor had exceeded the engineering estimate Rs. 31.334 billion pertaining to the construction of road section from Kaduwela to Kadawatha (8Kms) (Phase II) the Cabinet Ministers had decided to cancel the awarding of the contract on 06 October 2010. However, it was noted that contrary to the cabinet decision, the above bid was reconsidered and awarded on 25 November 2011 after reducing the bid price up to Rs. 44.88 billion. According to the information received, the Cabinet of Ministers at its meeting held on 25 November 2011 had granted the approval for second bid even though the rates applied either for engineering estimate or second bid had not been approved by the Supervision Consultant and the Technical Evaluation Committee.
- (b) According to the Engineer's Estimates, allocations aggregating Rs.120,728,000 had been made to procure 15 motor vehicles and 08 motor cycles under the category of preliminary expenditure. However, this allocation had been increased up to Rs.

153.54 million under other category for provisional sums to procure 21 motor vehicles and 12 motor cycles. However, actual cost amounted to Rs. 185.62 million and exceeded the allocation by a sum of Rs.32 million.

- (c) The Value Added Tax amounting to Rs. 19,884,107 incurred by the contractor had been reimbursed by the Project out of the Loan proceeds received. Further, the contractor had also claimed a sum of Rs. 6,900,740 as an interest on delay in the reimbursement.
- (d) Although provision in the initial Bill of Quantities for additional soil sample testing amounted to Rs. 3.3 million, the contractor had been paid a sum of Rs.53.79 million exceeding the initial provision for that activity by a sum of Rs.50.49 million.
- (e) According to the Interim Payment Certificate No. 30, a sum of Rs.159,173,175 had been paid to the contractor under provisional sum category for supplying and installation of 50 mm dia GI pipes, as a result of accessories for sonic logging test and supply and pumping of grouting materials which was necessary for sonic logging test which had not been included in Bill of Quantity under provisional sums.
- (f) Further, a sum of Rs. 138.28 million had been paid to the contractor for sonic logging test for pile integrity under provisional sum category, exceeding the Bill of Quantity value by 182 per cent, without an identifying item in the Engineering estimates or without approving specifications in the contract.
- (g) According to the Clause 60.2 of the Conditions of the Contract, the Interim Payment Certificates which exceed, the value of Rs. 200 million should be taken into consideration for evaluation. However, 02 Interim Payment Certificates valued at Rs. 143.5 million and Rs. 136.4 million had been taken in to evaluation purpose.
- (h) According to the Clause 60.5 of the Conditions of Contract 10 per cent of retention money should be deducted from Interim Payment Certificates. However, 5 per cent retention money had been deducted from Interim Payment Certificate – 20 and as a result, Rs. 464.7 million had been over paid to the contractor.

6.2.3 Consultancy Contract

The following observations are made.

- (a) According to the Supplementary Agreement for Consultancy, the Resident Engineer, the Electrical Engineer and the Planning Engineer are received to be recruited for implementing the activities of the Project. However, such posts remained vacant up to July 2014.
- (b) Further, 04 Engineers to be required to recruited under original Consultancy Agreement had not been recruited up to July 2014.

- (c) According to the Construction Contract Specification No. 102, a sum of Rs.287.01 million had been allocated to the contractor for the supply of office and residential facilities for the Consultant Engineer at the inception of the Project activities and Rs. 163.30 million had been paid thereon up to June 2013. However, the residential facilities had been provided after 1 ½ years of the commencement of the Project Activities. According to the Conditions of Contract No.49.4, the amount related to months which residential facilities not provided is required to be deducted, the payments amounting to Rs. 71.16 million for the entire period had been paid to the Contractor.
- (d) Although facilities are available to provide residential facilities to 13 Consultant, such facilities had been provided to 07 Consultants only. The allowances of Rs. 13,000 for each officer had been provided monthly, since June 2013 for other six Consultants.

6.2.4 Matters of Contentious Nature

The following observations are made.

- (a) According to the Loan Agreements the effective date of Loan had been in March 2009. However, proceeds of loans had been disbursed since January 2012. As a result the commitment charges amounting to Rs. 29,402,050 had been paid by the Project to the Lending Agency.
- (b) Encashment of leave amounting to Rs. 1,478,514 and claims for medical insurance amounting Rs.424,737 and allowance of Rs.3,501,406 had been paid to the employees of the Road Development Authority attached to the Project, contrary to the Sections 8.3.9 and 8.6 of the Circular No. PED/12 dated 02 June, 2003 of the Department of Public Enterprises.
- (c) A sum of Rs.21.2 million had been spent by the Project for activities which were not directly related to the objectives of the Project. Further, such payments had been made as variation of the construction work without obtaining relevant approvals.
- (d) Four Consultants had been employed by the Project without the approval of the Department of Management Services. Further, the terms of references had not been issued to them, even though remuneration aggregating Rs. 6.84 million had been paid to them during the year under review.

6.2.5 Lands Acquisition and Resettlement Activities

According to the financial statements, the Project had spent a sum of Rs. 1,661.7 million up to 31 December 2013 for acquisition of lands 1.3286 hectares in extent of for resettlement of the persons displaced due to Project activities. Further, the land acquisition and resettlement activities of the Project were expected to be completed by the end of December 2013. Even though 94 per cent of the land acquisition activities had been completed under Phase II of the Highway 70 per cent of the resettlement activities only had been completed as at 31 December 2013.

6.2.6 Human Resources Management

The following observations are made.

- (a) According to paragraphs Nos. 2.2.4 and 2.2.7 of the Circular No. 33 dated 05 April 2007 of the Department of Management Services, staff recruitment should be made by calling for applications through national newspapers and appointment should be given on contract basis for period not exceeding three years. However, all members of the Project staff including the officers released from the Road Development Authority had been recruited on temporary basis contrary to the provisions of the above circular.
- (b) Even though the Department of Management Service had approved a carder of 35 for the Projects, only 24 had been required by the Project and 11 posts had been vacant during the year under review.

6.2.7 Utilization of Motor Vehicles

The fleet of motor vehicles of the Project comprised 03 hired motor vehicles and 05 motor vehicles provided by the contractor. It was observed that 06 motor vehicles had been assigned to the officers who were not entitled for vehicle facilities in terms Circular No 33(1) dated 20 December 2007 of the Department of Management Services.