

Eastern and North Central Provincial Road Project - 2014

The audit of financial statements of the Eastern and North Central Provincial Road Project for the year ended 31 December 2014 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 read in conjunction with Section 4.04(a) of Article IV of the Loan Agreement No. 2546 – SRI (SF) dated 22 October 2009 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement of the Eastern and North Central Provincial Road Project, the Provincial Road Development Department of the Eastern Provincial Council and the Provincial Road Development Authority of the North Central Provincial Council are the Implementing Agencies of the Project and the responsibility for the execution of the Project is assigned to then Ministry of Local Government and Provincial Councils, presently the Ministry of Provincial Councils and Local Government. The objectives of the Project are to improve the transport system in the Eastern and the North Central Provinces by rehabilitating and improving provincial roads enhancing project management capabilities of Eastern Provincial Road Development Department and North Central Provincial Road Development Authority and improving the physical resources of the offices of Eastern Provincial Road Development Department. As per the Loan Agreement, the estimated total cost of the Project is US\$ 78 million and out of that US\$ 70 million or 89.74 per cent was agreed to be financed by the Asian Development Bank. The balance sum of US\$ 8 million or 10.26 per cent should be financed by the Government of Sri Lanka. The Project commenced its activities on 20 March 2009 and scheduled to be completed by 30 June 2014. The period of the Project had been extended up to 15 March 2015.

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 and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

1.4 Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements. 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 judgement, 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 Project'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 Project's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management as well as evaluating the overall presentation of the financial statements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion. The examination also included such tests 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 the Project management and the reliability of books, records etc. relating to the operations of the Project.
- (b) Whether the expenditure shown in the financial statements of the Project had been satisfactorily reconciled with the enhanced financial reports and progress reports maintained by the Project.
- (c) 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 the operations of the Project, the identifications of the purchases made out of the Loan etc.
- (d) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.
- (e) Whether the funds, materials and equipments supplied under the Loan had been utilized for the purposes of the Project.
- (f) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (g) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles.
- (h) Whether the opening and closing balances, withdrawals from and replenishments to the Imprest Fund Account had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2014 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date,
- (i) Whether the Statements of Expenditure (SOEs) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement,
- (j) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and

- (k) Whether financial covenants laid down in the Loan Agreement had been complied with.

2. Financial Statements

2.1 Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2014 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2014 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 Imprest Fund Account during the year ended 31 December 2014 had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2014 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,
- (d) the Statements of Expenditure (SOEs) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement,
- (e) the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (f) the financial covenants laid down in the Loan Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following accounting deficiencies were observed in audit.

- (a) The assets such as 02 motor vehicles and research equipments procured at a cost of Rs.13.38 million and Rs.9.74 million respectively in 2013 and other equipments procured for the use of Auditorium of North Central Provincial Road Development Authority at cost of Rs. 9.74 million in 2014 through Interim Payments Certificates submitted by the contractors had been accounted under the civil works instead of being accounted as the properties of the Project.

(b) The replenishments made during the year amounting to Rs. 312.28 million shown in the financial statements was not agreed with the corresponding amounts of Rs.272.71 million and Rs.193.77 million shown in the records maintained by the Department of External Resources and Central Bank of Sri Lanka. The Project had not taken action to reconcile the balances.

3. Financial and Physical Performance

3.1 Utilization of Funds

Certain significant statistics relating to the financing, budgetary provision for the year under review and the utilization of funds during the year under review and up to 31 December 2014 are shown below.

Source	Amount agreed for financing in the Loan Agreement		Allocations made in the Budget Estimated for the year under review	Funds utilized			
	US\$ million	Rs. million		during the year 2014		up to 31 December 2014	
	US\$ million	Rs. million	Rs. million	US\$ million	Rs. million	US\$ million	Rs. million
ADB	70	7,980	728	4.12	540	55.56	7,279
GOSL	08	912	121	0.92	121	7.93	1,040
	78	8,892	849	5.04	661	63.49	8,319

Eventhough the period of the Project had been extended by 09 months and 95 per cent of the entire period of the Project had been lapsed as at 31 December 2014, only 80 per cent of Loan proceeds had been utilized.

3.2 Physical Progress

According to the Progress reports of the Project, the road rehabilitation works of 19 provincial roads in the North Central Province and 17 provincial roads in the Eastern Province had been completed as at 31 December 2014 and handed over to the Provincial Road Development Authorities functioned under the respective Provincial Councils.

3.3 Contract Administration

According to the contract agreements, the maintenance works of the roads rehabilitated under the Project was required to be carried out by the contractor for the next 03 years. However, the requirements of the maintenance of roads rehabilitated had not been highlighted in the Engineer's Estimates adequately and as a result, the bidders had quoted lower rates for road maintenance activities in their bid documents. The test check carried out in this connection had revealed that the allocations ranging from 0.25

per cent to 2.31 per cent of the total contract sum had been only made for the maintenance of 19 roads rehabilitated under the Project in the North Central Province.

Further, the site visits made by the auditors in May and August 2015 had revealed the subsidence of the roads at several locations and other defects at the road shoulders of Pothana – Ihalagama Road, Gurugalhinna-Ellapothana- Walahawiddawewa Road, Parasangawewa –Katukeliyawa Road and Oyamaduwa- Thanthirimale Road rehabilitated by the Project in the North Central Province. According to the explanation of the Project Director, the road maintenance works after completion of the rehabilitation works had not been satisfactorily implemented by the contractors and as a result, defects were appeared in several locations of the roads.

Thus evident that the contractors had not involved with road maintenance works due to inadequate allocations in the bid documents for road maintenance purposes. Further, it indicated that the Project had not taken action effectively to monitor the contractors during the defect liability periods and take remedial action to ensure the quality of the roads in sustainable manner.