

## **Northern Road Connectivity Project Additional Financing – Provincial Component - 2015**

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The audit of financial statements of the Northern Road Connectivity Project Additional Financing – Provincial Component for the year ended 31 December 2015 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 of Article (iv) of the Loan Agreement No. 2890-SRI(SF) dated 19 November 2012 entered into between the Democratic Socialist Republic of Sri Lanka (GOSL) and the Asian Development Bank (ADB).

### **1.2 Implementation, Objectives, Funding and Duration of the Project**

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According to the Loan Agreement of the Northern Road Connectivity Project – Additional Financing, the Provincial Road Development Department of Northern Provincial Council and the Provincial Road Development Authority of North Central Provincial Council are the Implementing Agencies and then Ministry of Local Government and Provincial Councils, presently the Ministry of Provincial Councils and Local Government is the Executing Agency of the Project. The objective of the Project is to improve the road connectivity within the Northern Province and between the Northern region and the Southern region of Sri Lanka. The Project shall comprise:

#### **Part B. Rehabilitation and Replacement**

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Rehabilitation of about 50 kilometres of provincial roads and rehabilitation and/or replacement of selected bridges in the Northern Province.

#### **Part C. Rehabilitation and Replacement**

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Rehabilitation of about 70 kilometres of provincial roads and rehabilitation and/or replacement of selected bridges in the North Central Province.

As per the Project Administration Manual, the estimated total cost of the Project is US\$ 33.67 million equivalent to Rs.4, 377 million and out of that US\$ 28.9 million equivalent to Rs.3,757 million was agreed to be financed by the Asian Development Bank. The Project commenced its activities on 31 May 2013 and scheduled to be completed by 30 June 2018.

### **1.3 Responsibility of the Management for the Financial Statements**

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Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Public Sector Accounting Standards 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**

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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 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 identification of the purchases made out of the Loan etc.
- (d) Whether the Statements 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) Whether the opening and closing balances and withdrawals from and replenishments to the Special (Dollar) Account had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2015 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date.
- (f) Whether withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.

- (g) Whether the funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (h) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (i) Whether the financial statements had been prepared on the basis of Sri Lanka Public Sector Accounting Standards.
- (j) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (k) Whether the financial covenants laid down in the Loan Agreement had been complied with.

## **2. Financial Statements**

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### **2.1 Opinion**

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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 2015 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2015 in accordance with Sri Lanka Public Sector Accounting Standards,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the opening and closing balances and withdrawals from and replenishments to the Special (Dollar) Account during the year ended 31 December 2015 had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2015 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka (CBSL) as at that date,
- (d) the Statements 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) 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.

### 3. Financial and Physical Performance

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#### 3.1 Utilization of Funds

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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 2015 are shown below.

Source	Amount agreed for financing in the Loan Agreement		Budgetary Provision for the year under review	Funds utilized			
				during the year 2015		up to 31 December 2015	
	US\$ million	Rs. million	Rs. million	US\$ million	Rs. million	US\$ million	Rs. million
ADB	28.90	3,757	1,398	10.20	1,332	23.10	3,009.25
GOSL	4.77	620	224	0.98	127	2.13	276.54
	<u>33.67</u>	<u>4,377</u>	<u>1,622</u>	<u>11.18</u>	<u>1,459</u>	<u>25.23</u>	<u>3,285.79</u>

#### 3.2 Physical Progress

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The following observations are made.

- (a) According to the Implementation Plan of the Project, 07 provincial roads in Anuradhapura District with the length of 75.65 kilometres, 04 provincial roads in Killinochchi District with the length of 24.11 kilometres and 02 provincial roads in Mulathivu District with the length of 24.49 kilometres were expected to be rehabilitated during the period of the Project. Out of that the rehabilitation works of all provincial roads in Anuradhapura District, 02 provincial roads in Kilinochchi District and 01 provincial road in Mulathivu District had been completed as at 31 December 2015.
- (b) The contract for rehabilitation works of Vattapalai-Keppaipilavu Puthukudiriyurpu Road of 12.85 kilometres in Mulathivu District had been awarded in 26 November 2015, after lapse of 2 ½ years from the date of commencement of the activities of the Project and physical progress of 12.5 per cent had only been shown as at 31 May 2016. According to the progress reports, the rehabilitation works of 02 Main Canal Roads at Akkarayankulam in Kilinochchi District which commenced on 31 December 2014 had shown a physical progress of 45.5 per cent as at 31 May 2016.

### **3.3 Contract Administration**

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The following observations are made.

- (a) The site visit made by the auditors on 02 March 2016 revealed that the surface and road shoulders at several locations of Kirigollewa- Heeralugama and Yakawewa- Mahakoongaskada Road in Anuradhapura District which were running over the reservoir dams were severely cracked and damaged, as a result of improper earth fillings and soil compaction etc, done without surveying the ground situation. It was further observed that the shoulders of the several locations of Kennedy Road and Approach Road to Cattle Farm in Northern Province had also been damaged and washed off, due to improper soil compaction. Further, the site inspection made on 11 April 2016 had revealed that more than 50 per cent of turf works of the Oddusuddan- Puthukudiyiruppu- Mathalan Road in Northern Province was failed due to improper up keeping of the contractor, eventhough a sum of Rs. 8.19 million had been paid thereon.
  
- (c) According to the contract agreements, the roads rehabilitated under the Project are required to be maintained by the respective contractors for further 05 years period after handing over the roads to provincial road authorities. However, there was no proper mechanism stipulated in the contract agreements to monitor road maintenance works and make payments thereon.

### **3.4 Matters in Contentious Nature**

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The following observations are made.

- (a) The Provincial Project Management Unit of the North Central Province had deployed 03 officers of the North Central Provincial Council since 2014 with the approval of the Governor for the North Central Province, contrary to the provision made in the Circular No. 33 of 05 April 2007 of the Department of Management Service. The allowances of 1/6 of the monthly salary of the permanent posts aggregating to Rs. 305,908 had been paid them during the year under review.
  
- (b) The rehabilitation works of 10 provincial roads, out of 13 provincial roads had been almost completed and handed over to the Provincial Road Authorities as at 31 December 2015. However, the operations of the Project are scheduled to be continued up to 30 June 2018, as determined in the Loan Agreement. It was observed that there was no proper action plan to implement the activities to be carried by the Project and designated purposes of continuing operations of the Provincial Project Management Units during the remaining period of the Project.