

## **Provincial Road Project – Uva Province - 2015**

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The audit of financial statements of the Provincial Road Project – Uva Province 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 4.09(b) of the Loan Agreement No. 4630 LK dated 11 January 2010 entered into between the Democratic Socialist Republic of Sri Lanka and the International Development Association.

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

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According to the Loan Agreement of the Provincial Road Project, Uva, Eastern and Northern Provincial Councils 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 access to socio-economic centers in the Uva, Eastern and Northern Provinces through the sustainable management of improved road infrastructure. According to the Project Appraisal Document, the estimated total cost of the Project – Uva Province is US\$ 67.2 million equivalent to Rs.7,592 million and out of that US\$ 60 million equivalent to Rs. 6,800 million was agreed to be financed by the International Development Association. The Project commenced its activities on 31 March 2010 and completed on 31 March 2015. However, the financial statements of the Project for the year ended 31 December 2015 had been prepared and presented for audit.

### **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 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**

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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 identifications of the purchases made out of the Loan, etc.,
- (d) 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.
- (e) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement,
- (f) Whether the funds, materials and equipments supplied under the Loan had been utilized for the purposes of the Project,
- (g) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project,

- (h) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles,
- (i) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (j) 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 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 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 (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

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### 2.2.1 Non - compliance with Laws, Rules and Regulations

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Pay As You Earn Taxes aggregating Rs.251,216 had not been recovered from 08 officers of the Project and remitted to Commissioner General of Inland Revenue.

## 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 of funds, 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 according to the Loan Agreement		Allocation made in the Budget Estimate for the period under review	Funds utilized			
	US\$ million	Rs. million		US\$ million	Rs. million	US\$ million	Rs. million
IDA	60.00	6,800	1,109	2.62	348.93	54.34	6,762.25
GOSL	7.20	792	203	-	121.33	-	827.28
<b>Total</b>	<b><u>67.20</u></b>	<b><u>7,592</u></b>	<b><u>1,312</u></b>	<b><u>2.62</u></b>	<b><u>470.26</u></b>	<b><u>54.34</u></b>	<b><u>7,589.53</u></b>

According to the above information, out of the total allocation of US\$ 60 million made to implement the activities of the Project, only US\$ 54.34 million representing 90.6 per cent had been utilized at the end of the period of the Project.

### **3.2 Physical Progress**

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According to the initial work plan of the Project, 150 kilometres of 06 provincial roads in Uva Province were expected to be rehabilitated. However, the scope of the rehabilitation works had been reduced upto 121.77 kilometres subsequently. According to the information received, all the road rehabilitation works and road maintenance contracts offered by the Project under 94 packages had been completed as at 31 December 2014. Further, an additional allocation of Rs. 10.36 million had been made in 2014 to erect 54 bus shelters in 04 provincial roads rehabilitated under the Project and such works had also been completed as at 31 December 2014.

### **3.3 Contract Administration**

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The following observations are made.

- (a) Out of 06 provincial roads rehabilitated by the Project, the defects in the road surfaces and drainage systems at several locations of Galauda- Kandeketiya-Karametiya Road and Haggala McDonald Road had been revealed at the site visits made by the auditors, due to application of improper practices for road rehabilitation purposes.
- (b) The Project had taken action in 2014 to construct 54 bus shelters at 04 provincial roads at a cost of Rs.257,250 each. The defects such as constructions deviated from the specifications and cracks of the floor surfaces of 22 bus shelters etc, had been revealed at the site visits made by the auditors on 21 March 2016.

### **3.4 Matters highlighted in the previous audit reports remained unresolved**

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According to the agreement entered into with the Consultant, transport facilities to be provided by the Project for the staff of the Consultant and 15 motor vehicles were expected to be deployed thereon. However, the Project had provided 25 motor vehicles and additional cost of Rs.50.5 million had been incurred thereon. However, action had not been taken by the Project to identify the parties responsible and investigate the reasons thereto.

### **3.5 Matters of Contentious Nature**

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The road rehabilitation works under Galauda- Kandaketiya- Karamatiya Road had been offered to a contractor with foreign joint venture at a cost of Rs. 767.33 million which was 32 per cent below than the Engineer's Estimate, without calling further information from the bidder to confirm the feasibility of the road rehabilitation works. It was further

observed that the joint venture agreement had also not been registered in Sri Lanka. However, the contractor had filed an arbitration case and claimed a sum of Rs.729 million to resolve the disputes arisen with the Project on price escalation and time extension for 736 days requested by the contractor. Out of the total amount claimed, a sum of Rs 32.80 million had been settled by the Project in December 2013. However, the contractor had made an appeal to an Arbitration Tribunal and according to the decision of the Tribunal made on 06 August 2015, the Project had been ordered to pay another sum of Rs.471.61 million to the contractor. The Project had taken action as at 31 December 2015 to obtain the legal opinion and seek opportunities to refer the case to the Commercial High Court.

### **3.6 Closure of the activities of the Project**

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The following observations are made.

- (a) According to the feasibility studies of the Project, it was expected to reduce the travel time of the roads rehabilitated under the Project to enable to improve the level of community transportation system within the Uva Province. However, action had not been taken by the Uva Provincial Council to assess the travel time before and after the rehabilitation of roads and revise the time tables of community service buses under the purview of the Provincial Council.
- (b) Eventhough the activities of the Project had been closed as at 31 March 2015, action had not been taken by the Project and the Executing Agency to hand over the assets to the respective parties and prepare wind up accounts as at 31 December 2015.