

Provincial Roads Project – (Eastern Province)- 2015

The audit of financial statements of the Provincial Roads Project – (Eastern Province) for the accounting period from 01 January to 15 October 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 Financing Agreement No. 4630 LK dated 11 January 2010 entered into between the Democratic Socialist Republic of Sri Lanka (GOSL) and the International Development Association (IDA).

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Financing Agreement of the Provincial Roads Project, then Ministry of Local Government and Provincial Councils, presently Ministry of Provincial Councils and Local Government is the Executing Agency and the Eastern Provincial Council is the Implementing Agency of the Project. The main objective of the Project is to improve access to socio-economic centers in the Eastern Province through the sustainable management of improved road infrastructure. As per the Project Appraisal Document, the estimated total cost of the Project was US\$ 20 million equivalent to Rs.2,000 million and the total amount was agreed to be financed by the International Development Association. The Project commenced its activities on 31 March 2010 and scheduled to be completed by 31 March 2015. However, the activities of the Project had been continued up to 15 October 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 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 15 October 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 Financing 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 Financing Agreement had been complied with.

1.5 Basis for Qualified Audit Opinion

My opinion is qualified based on matters described in paragraph 2.2 of this report.

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, except for the effects of the adjustments arising from the matters referred to in paragraph 2.2 of this report, I am of the opinion that,

- (a) the Project had maintained proper accounting records for the period ended 15 October 2015 and the financial statements give a true and fair view of the state of affairs of the Project as at 15 October 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 had been truly and fairly disclosed in the books and records maintained by the Project and balance as at 15 October 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 Financing 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 Financing Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following accounting deficiencies are observed in audit.

- (a) The balance of the US\$ 296,524 equivalent to Rs 41.88 million remained in the Special Dollar Account had been refunded on 29 September 2015 to the Lending Agency. However, the balance of Rs. 39.82 million of the Special Dollar Account had been shown as a current asset of the financial statement of the Project as at 15 October 2015.
- (b) According to the decision of the Adjudicator on dispute on rates applied for the determination of payments to the contractor involved on construction of 02 bridges located at Malwatta-Surippodai Road, the Project was directed to settle a sum of Rs. 40.04 million. However, the Project had made an appeal for the above decision. The contingency liability thereon had not been disclosed in the financial statements.

3. Financial and Physical Performance

3.1 Utilization of Funds

Certain significant statistics relating to the financing, budgetary provisions for the period under review, utilization of funds during the period under review and the cumulative expenditure as at 15 October 2015 are shown below.

Source	Amount agreed to be financed according to the Loan Agreement		Allocation made in the Budget Estimate for the year under review	Fund utilized			
				during the period under review		as at 15 October 2015	
	US\$ million	Rs. million	Rs. million	US\$ million	Rs. million	US\$ million	Rs. million
IDA	20	2,000	247	1.44	192.70	18.91	2,515.90
GOSL	-	-	20	0.01	1.92	0.10	14.22
Total	<u>20</u>	<u>2,000</u>	<u>267</u>	<u>1.45</u>	<u>194.62</u>	<u>19.01</u>	<u>2,530.12</u>

3.2 Physical Progress

The following observations are made.

- According to the initial plan of the Project, it was expected to upgrade and rehabilitate 100 kilometres of the provincial roads in the Eastern Province. Out of that, only 38.35 kilometres of 11 provincial roads in Ampara District of the Eastern Province had been upgraded and rehabilitated during the period of the Project.
- As a response to the request made by the Secretary of the Ministry of Provincial Councils and Local Government, the International Development Association had informed by the Letter of 19 November 2014 to terminate rehabilitation works of the rural roads under the Package EP-08 due to time constrain. However, the Project had awarded contracts on 12 November 2014 to rehabilitate 03 rural roads under the Package No. EP-08 at a total estimated cost of Rs.143.44 million, without the approval of the Lending Agency. Further, the quality of the roads expected to rehabilitate under this Package was remained questionable, as the consultancy service agreement for the road rehabilitation works was ended on 30 November 2014.

3.3 Matters in Contentious Nature

The Arbitral Tribunal had instructed to the Project on 07 July 2015 to take appropriate action to retain a sum of Rs.132.08 million from the proceeds of the Loan allocated under the Package EP-01 to meet any possible expenses on Arbitral proceedings on construction of 02 bridges located at Malwatta-Surippodai Road. However, the Project had not taken action to obtain an

approval from the International Development Association and retain funds for the arbitration proceedings. It was observed that a sum of Rs 2.39 million had been spent during the year under review, out of the contribution of the Government of Sri Lanka to meet the expenses on arbitration proceedings.

3.4 Closure of the Activities of the Project

The following observations are made.

- (a) The Consultant's Office of the Project had handed over several laboratory equipment such as Sieves, Electric Ovens, Compression Testing Machine, Asphalt Centrifuge Extrater and Electronic Scales etc on 26 January 2015 to the Executive Engineer's Office of the Provincial Road Development Department in Ampara. The respective equipment was remained idle from the date of handing over of the assets at the premises of Executive Engineers Office.
- (b) Eventhough the activities of the Project had been completed as at 15 October 2015, actions had not been taken by the Project to prepare and present financial statements for winding up purposes.