

Provincial Roads Project (Northern Province) - 2015

The audit of financial statements of the Provincial Roads Project (Northern Province) for the 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 Loan 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 Loan 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 Northern 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 Northern Province of Sri Lanka through the sustainable management of improved road infrastructure. As per the Loan Agreement, the estimated total cost of the Project was US\$ 21 million equivalent to Rs. 2,399.25 million and total amount was agreed to be provided 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 judgment, including the assessment of the risks of material misstatement of the financial statement, 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 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 Loan Agreement.
- (f) Whether the funds, materials and equipment 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.

1.5 Basis for Qualified Audit Opinion

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

2 Financial statement

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 adjustment arising from the matters referred to in paragraph 2.2 of this report, I am of 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 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,
- (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 Deficiency

The balance of the US\$ 312,599 equivalent to Rs 44.15 million remained in the Special Dollar Account had been refunded on 15 September 2015 to the Lending Agency, However, the balance of Rs. 41.98 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.

3. Financial and Physical Performance

3.1 Utilization of Funds

Certain significant statistics relating to the financing of funds, budgetary provision for the year under review and the utilization of funds during the period under review and up to 15 October 2015 are shown below.

Source	Amount agreed for financing in the Loan Agreement		Allocation made in the Budget Estimate for the year review	Funds utilized			
	US\$ million	Rs. million		US\$ million	Rs. million	US\$ million	Rs. million
IDA	21.00	2,399.25	773	4.63	617.83	20.68	2,509.95
GOSL	-	-	9	-	8.60	-	20.17
Total	<u>21.00</u>	<u>2,399.25</u>	<u>782</u>	<u>4.63</u>	<u>626.43</u>	<u>20.68</u>	<u>2,530.12</u>

3.2 Physical Progress

According to the information made available, 04 contract packages had been awarded by the Project to rehabilitate 12 provincial roads with the length of 60.64 kilometres even though it was expected to rehabilitate 100 kilometres approximately of the provincial roads in the Northern Province. The rehabilitation works of 06 roads of 23.07 kilometres under 02 packages had been completed with delays in period ranging from 150 days to 174 days as at 30 October 2013. The contracts awarded to rehabilitate the provincial roads under other 02 packages terminated in 2012 and rewarded to other contractors in 2013 had been completed as at 15 March 2015.

3.3 Contract Administration

The following observations are made.

- (a) It was observed that a contractor engaged in road rehabilitation works under Package -01 had made an arbitration claim amounting Rs. 6.7 million for the extension of time of 123 days. According to the information received, a sum of Rs 15.18 million had been paid during the period under review by the Project to settle the claim. Further, legal charges amounting to Rs 2.62 million had also been spent during the period under review by the Project for arbitration claims made by the contractors engaged for the rehabilitation works of roads under other 02 packages.

- (b) It was observed that the roads rehabilitated under the Package -02 by the Project had been taken over by the Provincial Road Development Department of the Northern Provincial Council with delays of 132 days without valid reasons. According to the Clause D-43 of the Condition of Contract, the rehabilitated roads are required to be taken over within 07 days.
- (c) It was observed that the variation of the scope of works of the roads had been approved by the Project Director without consulting either the Technical Evaluation Committee or the Consultant. Therefore, the scope of the works on rehabilitation of culverts of Uduvil – Sandilipay Road under the Package 3R valued at Rs 12.34 million representing 73 per cent of works which originally estimated had been curtailed. Further, the construction works of retaining walls of Madathivu Road under Package 5R valued at Rs 10.38 million representing 44 per cent of works which originally estimated had also been curtailed with the approval of the Project Director .
- (d) The site visits made by the audit officer on 15 May 2016 had revealed that cracks at the several locations of the road surfaces of the Kondavil-Irupalai Road and Thiruneli – Puththur Road of which the road rehabilitation works completed in October 2013. Thus, it provided evidence on quality failures of the road rehabilitation works.

3.4 Closure of the Activities of the Project

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 inventory items and prepare wind up accounts and Project Completion Report as at 31 October 2015.