

Southern Road Connectivity Project - 2015

The audit of financial statements of the Southern Road Connectivity Project 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 Article IV Section 4.05 of Loan Agreement No. 3027 – SRI dated 27 May 2014 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

According to the Loan Agreement of the Project, then Ministry of Highways and Investment Promotion, presently the Ministry of Higher Education and Highways is the Executing Agency and Road Development Authority is the Implementing Agency of the Project. The objective of the Project is to improve national transport efficiency by upgrading and rehabilitating 32 kilometres of the Southern Highway Link Roads. As per the Loan Agreement, the estimated total cost of the Project amounted to US\$ 100 million equivalent to Rs.12,893 million and out of that US\$ 75 million equivalent to Rs.9,670 million was agreed to be provided by the Asian Development Bank. The Project commenced its activities on 27 May 2014 and scheduled to be completed by 31 December 2018.

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 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

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 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 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 Sri Lanka Public Sector Accounting Standards.
- (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 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 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 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

2.2.1 Accounting Deficiency

The Project Monitoring Unit of the Project had administered 02 other donor funded projects and overhead expenditure amounting to Rs.3.64 million incurred for all three projects had been charged to the Southern Road Connectivity Project without taking action to adopt a reasonable basis to absorb overhead expenditures proportionately.

3. Financial and 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 2015 are shown below.

Source	Amount agreed for financing in the Loan Agreement		Allocation made in the Budget Estimate for the year under review	Funds utilized			
	US\$ million	Rs. million		US\$ million	Rs. million	US\$ million	Rs. million
ADB	75 *	9,670	644.00	2.59	419.41	3.38	523.04
GOSL	25	3,223	466.86	3.29	466.78	3.30	468.06
	<u>100</u>	<u>12,893</u>	<u>1,110.86</u>	<u>5.88</u>	<u>886.19</u>	<u>6.68</u>	<u>991.10</u>

* According to the information received, allocation of US\$ 5 million had been transferred to the Project operated under the Loan No. 3028 SRI.

3.2 Physical Progress

The following observations are made.

- (a) According to the information received, 41 per cent of the rehabilitation works of 4.64 kilometres of Moratuwa –Piliyandala Road and Ratmalana– Mirihana Road had been completed as at 31 December 2015, eventhough 55 per cent of rehabilitation works were expected to be completed as at that date. Further, a sum of Rs 15.77 million had been paid to the Ceylon Electricity Board to relocate electricity lines along the Moratuwa –Piliyandala Road and such works had not been completed even as at 30 April 2016.
- (b) The rehabilitation works of 16.18 kilometres of Kirulapana – Godagama Road and Kesbewa – Pokunuwita Road and 10.37 kilometres of the road from Southern Expressway to Madurugoda had not been commenced even as at 30 June 2016.

- (c) Due to delay in implementation of the activities of the Project up to 31 December 2015, the commitment and interest charges amounting to Rs.16.16 million had been paid by the Project during the year under review.

3.3 Contract Administration

The following observations are made.

- (a) According to the contract administration requirements, the laboratories to be established by the contractor for quality assurance purpose within 60 days of the commencement of the rehabilitation works. However, the site inspection made by the auditors on 16 November 2015 had revealed that the laboratory established by the contractor for the rehabilitation works of Moratuwa – Piliyandala Road was not equipped with necessary testing equipment. Further, it was observed that the necessary calibration of time had not been done for Electric Thermometer and Marshall Ring used by the contractor.
- (b) According to the Clause 4.9 of the Condition of the Contract, the hard copies of Quality Management Assurances System to comply with the requirement of ISO 9000: 2000 Standard should be submitted by the contractor within 28 days of commencement of the contract. However, the contractor had not been completed the Quality Assurance Plan even as at the end of the year under review.
- (c) According to the information received, the key posts of Claim Specialist and Senior Quantity Surveyor of the staff of the Consultant were remained vacant up to 31 August 2015 and it indicated that the supervisory activities of the road rehabilitation works were not properly executed. As per the Clause No 4.4 (III) of the Consultancy Agreement, the Claim Specialist should review the guarantee bonds and insurance claims submitted by the contractor. However, a sum of Rs.12.55 million had been paid up to 31 December 2015 to the contractor for insurance coverage, security bonds etc, for the road rehabilitation works. Further, a sum of Rs. 89.28 million had been paid on 04 Interim Payment Certificates without being recommended by the Quantity Surveyor, as required by the Clause No.4.4.(III) of the Consultancy Agreement.

3.4 Financial Covenants not complied

According to the Clause 6.1 of the Condition of the Contract, the contractor is required to include gender information to ensure at least 20 per cent female participation for the road rehabilitation works. According to the progress reports, female participation for the rehabilitation works was remained at 6.5 per cent only at the end of the year under review.