

## **Southern Road Connectivity Project - 2022**

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The audit of financial statements of the Southern Road Connectivity Project for the year ended 31 December 2022 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 ii Section 2.09 of the Loan Agreement No.3027- SRIdated27 May 2014 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank. My comments and observations which I consider should be reported to Parliament appear in this report.

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

According to the Loan Agreement the Ministry of Ports and Highways, presently, the Ministry of 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 33 kilometers of the roads linked to the southern Highway.

As per the Loan Agreement, the estimated total cost of the Project amounted to US\$ 95 million equivalent to Rs.12,248 million and out of that US\$ 70 million equivalent to Rs.9,025 million was agreed to be financed by the Asian Development Bank. The balance amount of US\$ 25 million equivalent to Rs.3,223 million agreed to be finance by the Government of Sri Lanka.

The Project had commenced its activities on 27 May 2014 and scheduled to be completed by 30 December 2018. However, the date of completion of the activities of the Project had been extended up to 31 December 2022.

### **1.3 Opinion**

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2022 and its cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

### **1.4 Basis for Opinion**

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the section of Auditor's Responsibilities for the Audit of the Financial Statements appeared in my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

### **1.5 Responsibilities of management and those charged with governance for the Financial Statements**

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Public Sector Accounting Standards and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Those charged with governance are responsible for overseeing the Project's financial reporting process.

## **1.6 Auditor's Responsibilities for the audit of the Financial Statements**

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 internal control of the project.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with those charged with governance regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

## 2 Comments on Financial Statements

### 2.1 Accounting Deficiencies

Accounting Deficiency / Audit Issue	Amount Rs. million	Response of the Management	Auditor's Recommendations
The provision had not been made for the interest payable amounting to Rs.314 million for the delay in payment of statutory compensation of Rs.1019 million to land owners as at 31 December 2022.	314	Land Acquisition Compensation (Rs. 1.2 billion) and Interest payable (0.5 billion) amount of completed vouchers have been handed over to the Land Division of Road Development Authority by the end of September 2022 and recorded in RDA financial statements as a liability.	Adhere to the Sri Lanka Public Sector Accounting Standard

### 2.2 Non Compliance with Laws, Rules and Regulations

No	Reference to the Laws Rules and Regulations	Non Compliance/Audit Issue	Response of the Management	Auditor's Recommendations
(a)	Section 4.3.1 of the procurement Guidelines and the finance Circular No. 2/2002 dated 07 August 2012.	When comparing the BOQ items in the engineer estimate of the SRCP/CP - 5 package and the items under the interim payment certificate No 21, it was observed that 32 work items valued at Rs.324.94 million were not fully attended and 26 work items valued at Rs.825.22 million were partially attended by the contractor due to the engineer's estimates of the contract packages had not been prepared in accurate manner.	Works items of the Engineering Estimate, prepared for the Original scope of work could not be fully attended.	Action should be taken to prepare the Engineer Estimate in accurate manner.
(b)	Section 8.13.4 of the Government procurement Guidelines 2006.	43 work items valued at Rs.643.65 million had been exceeded the approved work quantity limits in the BOQ. As a result of that, the total cost estimate of the project had not been prepared according to the supplementary 14 of the procurement manual.	The Original Contract has to revise and with the approval of MPC, and ADB concurrence the Contract Sum was revised.	Action should be taken to prepare the BOQ in accurate manner.

### 3. Physical Performance

#### 3.1 Physical Progress of the Activities of the Project

Component	Activity	As at 31 December 2022		Audit Issue	Reasons for delays
		Expected physical performance percentage	Performance achieved percentage		
Contract Package-05	Road Construction	100%	86%	Actual progress of the Project activities were behind the targeted progress.	COVID -19 pandemic, delay in land acquisition, economic crisis and scope change.

#### Response of the Management

Delay of physical progress of CP -05 contract package is mainly due to COVID 19 pandemic other than the delay in land acquisition, economic crisis and scope change.

#### Auditor's Recommendations

Action need to be taken to expedite the road rehabilitation activities as per the work plan

#### 3.2 Contract Administration

No	Audit Issue	Response of the Management	Auditor's Recommendations
(a)	The KPI's had not been established to measure the output and outcome of the project operation. Therefore, the level of benefits to public from the project could not be verified in Audit.	The output of the project such as no of km done, no of bridges/culverts done length of retaining wall done, no of lane km done etc. is measured with respect to the original scope .	"SMART" KPI's should be introduced.
(b)	According to the revised scope of the Project, the road construction works had been scheduled to be implemented under 05 contract packages to rehabilitate 45.77 Km of 06 national roads in Colombo and Kalutara district. Even though contract package-3 had been completed at scheduled date, construction activities of the contract packages (CP) 1, 2 and 4 had been completed with delay of 248 days, 534 days and 689 days respectively. Although the progress had mentioned hundred percent completion, of CP-1 to CP-4 the roads had been completed substantially, the balance work at the CP-2,CP-3 and CP-4 was added to CP-5 package due to subsequent scope change in the	Only the surfacing and balance construction works of road section 23+400 to 28+180 of B-084 road and all works of road section 15+360 to 16+280 of A-004 road both under CP-2 were added to CP-5. However, no balance work of CP-3 and CP- 4 was added to CP-5. CP-5 Package was commenced on 29 <sup>th</sup> February 2020 and completed on 15 <sup>th</sup> November	Action should be taken to complete the works according to the Project scope.

construction. The rehabilitation works of the contract package - 5 commenced on 29 February 2020 and scheduled to be completed on 30 November 2021 was reported only 86 per cent physical progress as at 31 December 2022. The cost of balance works of the project amounting to Rs.2,536 million will be burdened to the government in future. In addition to that, balance work of package-5 had been planned to carry out from the I-Road project. However, there is no any agreement with the I-Road project for balance works up to now.

2022. When the country return to normal after August 2022 CP-5 project resumed works to complete balance works.

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| (d) | The contractor for the SRCP/CP 5 rehabilitation works of 12.45 km of Kirulapana to Godagama and Pamankada to Pokunuwita road had been commenced on 29 February 2020 at a cost of Rs.4,215 million and scheduled to be completed on 21 August 2021. However, the period of contract had been extended by the Project up to 30 June 2022 by granting of 853 days of time extension to the contractor condition of contract. Further, it was observed that, the contractor had claimed Rs.160 million relating to cost of time extension of 177 days and project had approved that claim without considering contractor poor performance. | The commencement of the CP-5 package was on 29-02-2020 and the COVID-19 pandemic was experienced in Sri Lanka from March 2020 up to September 2021. Therefore, the project has to grant EOT for the Contractor since the situation experienced during the contract period is beyond the control of both the Employer and Contractor. | Corrective action should be taken to minimize the additional cost.                   |
| (e) | According to the variation approval letter dated 17 May 2022, the total sum of the variation limit approved as Rs.519 million, however according to the interim payment certificate No 21, (CP-5) the project had made actual variations of to Rs.525 million. Due to that, the actual variation amount had been exceeded the approved variation limit by Rs.5.57 million due to weakness of contract administration.  | Agreed<br>When the works of Variation Orders are carried out, some estimated quantities have exceeded.   | Action should be taken to comply with the approved variation limits.                 |
| (f) | Even though the contractor interim payment certificate No 29 released SRCP/CP-3 was submitted on 24 June 2019 for the payment of Rs.248.6 million, the Project had been settled that amount on 05 July 2022 with 3 years delay. As a result, the contractor had claimed interest of Rs.46.9 million for the delayed period. It was observed that, the delay in settlement of contractor payment had been affected to overrun the project cost.   | Agreed.<br>When the constructions are in progress, some practical requirements lead to scope change identified. So, the contract amount has to be revised in this regard.  | Action should be taken to settle the payments on time without paying delay chargers. |

### 3.3 Issues relating to the Land Acquisition

No	Audit Issue	Response of the Management	Auditor's Recommendations
(i)	According to the information made available, it was scheduled to acquire 8,499 plots of land including 1,562 plots of land owned to the Government and out of that compensation of Rs.8,249 million had been paid under the section 17 of the Land Acquisition act. Further, the additional payments amounting to Rs.3,223 million had been made under the decision of the Land Acquisition and Resettlement committees. In addition, a sum of Rs.899 million had been recorded as interest on delays in settlement of compensation up to 31 December 2022. Moreover, the value of outstanding vouchers value at Rs.1714 million had been handed over to the RDA at the end of the year under review. However, no any plot of land had been registered under section 44 of the Land Acquisition act as at 31 December 2022 due to poor supervision of the land acquisition process.	Not Agreed.  However, the amount paid for interest on delays in the settlement of compensation is Rs.403.09 million. Registration of land lots under section 44 of the Land Acquisition Act is progressing at the Divisional Secretarial office together with the Ministry of Land. The land acquisition process involves several government institutions and they cannot be directed by the project beyond a limit.	Action should be taken to accelerate the compensation process to minimise additional cost.
(ii)	Although the project had acquired 8,503 land lots, some land lots (Kirulapana to Homagama) are not utilized for construction work.	Agreed.  Once the land acquisition is started it cannot be interrupted without diverting back to the original owners with their consent.	Action should be taken to divert unused lots of land.

### 3.4 Observations made on site visits

Audit Issue	Response of the Management	Auditor's Recommendations
Although, the project had paid Rs.93.95 million and Rs.43.24 million to the Ceylon Electricity Board and Sri Lanka Telecom respectively for relocating of electricity lines and telephone lines under SRCP/ CP-5 package, only 65 percent of electricity poles and 26 percent of transformers of the CEB had been completed and 74 percent of the telephone poles of the SLT had been	Agreed  Until the total estimated payment is done for both CEB and SLT, they will not start the work since for the contracting for the given scope of work.	Instructions should be given complete the works within the time frame and closely monitor the contractors' works.

done as at 31 December 2022. Further it was observed that the Project had paid Rs.100 million over the BOQ amount of Rs.36.8 million without having the proper approval.

### 3.5 Idle/ Unutilized/ Underutilized Resources

Audit Issue	Response of the Management	Auditor's Recommendations
<p>a) The loan agreement of the Project was signed on 27 May 2014 for US\$ 70 million and end on 31 December 2018, However, due to delay in the construction activities of the Project, the loan closing date had been extended by the funding agency several times up to 31 December 2022. Even though the loan closing date had been extended by the funding agency, the Project had failed to utilize total loan facility before the loan expiration due to the management inefficiency. It was observed that, a sum of US\$ 1.32 million equivalent to Rs.478 million had been failed to utilize by the Project.</p>	<p>Even though the ADB has approved to utilize loan balance, the condition that it can be applicable for the works up to 30-06-2022 has restricted that facility, despite the loan disbursement period being extended up to 31-12-2022. As a result, the loan was closed without utilizing the sum of US\$ 1.32 million.</p>	<p>Action should be taken to utilize the loan facility effectively.</p>
<p>b) It was observed that, despite there was an outstanding payment balance of Rs. 316.13 million as at 31 December 2022, the Project had failed to settle that amount from the remaining imprest balance and the total remaining imprest balance of Rs.154.76 million had been returned to the lending agency.</p>	<p>Agreed. After the ADB rejected the loan extension, the undisbursed loan balance has to be returned back to ADB.</p>	<p>Action should be taken to utilize the loan facility effectively.</p>
<p>c) Out of GOSL allocation of Rs.727 million under capital expenditure vote No.117-2-4-43-2105-17, the Project had utilized only Rs.126 million and allocation of Rs.601 million representing 83 percent had not been utilized during the year under review. Further it was observed that, allocation for the reimbursable foreign aid of Rs.30 million, the project had utilized only Rs.23 million and allocation of Rs.6 million representing 20 percent of the total</p>	<p>Even though the allocation of Rs.727 million has been granted for 2022, only Rs.120 million imprest received to settle the land acquisition-related payments and allocations for Reimbursable Foreign Aid vote (117-2-4-43-2506-14) for the year Rs.30 million and utilized Rs.23.7</p>	<p>Action should be taken to utilized total allocation effectively.</p>

allocation had not been utilized by the Project. Hence the cost of unfinished works of the Project will be burdened to the government in future.

million. This vote could be used for only six months due to the loan closure in June 2022 was not fully utilized.

- d) It was observed that Rs.311 million was paid as interest and commitment charges for the entire loan amount, However out of the total loan amounting to USD 70 million, a sum of USD 1.32 million had not been utilized by the Project and refunded to the lending agency. Accordingly, interest & commitment charges of Rs.5.8 million had been paid by the Project for the unutilized loan amount.

ADB has charged Rs.311 million as interest and commitment charges. That is the loan condition and it has been agreed upon at the time of granting the loan. This amount has to be fully charged by the end of 2019 without any consideration of whether the loan is fully used or not.

Action should be taken to utilize the loan fund effectively.

### 3.6 Matters in Contentious Nature

No	Audit Issue	Response of the Management	Auditor's Recommendations
(a)	The retention money amounting to Rs.210 million relevant to the contract package 5 had already been released to the contractor. However the outstanding works of this package had been decided to transfer to the I-Road project.	The completion of CP-5 package parallel with loan closure of SRCP loan, is not a decision of the Contractor but it is a decision of the Employer. there is no contractual obligation to retain retention money.	Instruction should be given to release the retention money after issuance of the completion report.
(b)	Delay damages amounting to Rs.31.95 million recovered from the contract package-1 under IPC 15 submitted on 19 June 2017 had been released to contractor on 10 October 2019. Further, it was observed that, delay damages amounting to Rs.14.14 million had been deducted from the contract package - 4 and recorded as liability in the financial statements as at 31 December 2022. The releasing of delay damages was a problematic issue in audit.	With the proper approval for EOT from the relevant authority, the recovered delay charges of the CP-1 package have been released subsequently. The contractor of the CP-4 package has not appealed yet for the EOT and hence the Engineer deducted delay damages have been recorded as a liability.	Effective action should be taken to claim delay damages as per the condition of contract.