

## **Badulla-Chenkaladi Road Improvement Project - 2018**

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The audit of financial statements of the Badulla-Chenkaladi Road Improvement Project for the year ended 31 December 2018 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 the Loan Agreements No. 1661P and 10/639 dated 26 June 2015 and 30 October 2015 entered into between the Democratic Socialist Republic of Sri Lanka and the OPEC Fund for International Development and the Saudi Fund for Development. 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 Agreements of the Project, then the Ministry of Higher Education and Highways, presently the Ministry of Roads and Highways is the Executing Agency and the Road Development Authority is the Implementing Agency of the Project. The objective of the Project is to improve the connectivity of Eastern Province with Uva Province and Central Province enabling the improvement of transportation and enhancing the economic activities in the region by rehabilitation of 147 kilometres of the road from Badulla to Chenkaladi of Peradeniya- Badulla-Chenkaladi Road. As per the Loan Agreements, the estimated total cost of the Project amounted to US\$ 140 million equivalent to Rs.18,200 million and out of that US\$ 60 million equivalent to Rs.7,800 million was agreed to be financed by the OPEC Fund for International Development and US\$ 60 million equivalent to Rs.7,800 million was agreed to be financed by the Saudi Fund for Development. The balance of US\$ 20 million is expected to be financed by the Government of Sri Lanka. The activities of the Project are expected to be completed by March 2019.

### **1.3 Qualified Opinion**

In my opinion, except for the effects of the matters described in the Table 2.1 Basis for my report, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2018, financial performance 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 of 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.

In preparing the financial statements, management is responsible for assessing the Project ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Program or to cease operations, or has no realistic alternative but to do so.

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

The Project is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared by the Project.

## **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 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 Deficiency

Accounting Deficiency	Impact	Response of the Management	Auditor's Recommendation
It was observed that the interest amounting to Rs.29.80 million payable on delays in settlement of compensation on lands acquired as at 31 December 2018 had not been brought to account.	Understatement of assets and liabilities.	This issue will be rectified in the financial statements of 31 December 2019.	Provisions need to be made as per Sri Lanka Public Sector Accounting Standards 08.

## 3. Physical Performance

### 3.1 Physical progress of the activities of the Project

Component	Audit Issue	Impact	Response of the Management	Auditor's Recommendation
Rehabilitation of Roads	The physical progress of road rehabilitation works from Badulla to Bibila had remained at a range of 21 per cent to 46 per cent as at 31 December 2018, even after lapse of 03 years from the commencement of the works.	Possible increase of costs due to delays in completion of construction works.	The Project completion time could be extended depending on the approved time extension.	Need to be influenced the contractors to achieve the time targets and avoid the cost increase and extension of the period of the contracts.

### 3.2 Contract Administration

The following observations are made.

	Audit Issue	Impact	Response of the Management	Auditor's Recommendations
(i)	Eventhough the Consultant of the Project had regularly commented on poor performance of the contractor who engaged in road rehabilitation works from Lunugala to Bibila, there was no remedial action	Total cost of the Project may increase and unnecessary delay in completion of the Project.	“Notice to correct” issued by the consultant to the contractor OFID package 03, as an initial step, under termination process as per the clause 15.1 of General Condition of contract subsequently there was a meeting arranged with	Need to take necessary action either to terminate or expedite the construction.

<p>taken according to the Section 15.2 of General Condition of Contract.</p>	<p>Ministry officials, consultant, contractor and Employer to review the status of the contract.</p>	<p>(ii) Eventhough a sum of Rs.368 million had been paid for respective works at once for the shifting of utility services such as electricity and water supply lines etc, it had not been carried out in timely manner.</p>	<p>Unnecessary cost and time will spend and total cost of the project may increase.</p>	<p>Payment were done to utility agencies before awarding the contract, in order to expedite the utility shifting.</p>	<p>Required to have a proper time plan from the respective parties to complete the works on timely.</p>
<p>(iii) The separate pay items had been made in the Bill of Quantities on road rehabilitation works allowing contractors to quote the cost of providing performance guarantees, contrary to the provisions made under the sub clause 4.2 of the General Condition of the Contract to obtain performance security bonds at cost of respective contractor. Accordingly, a sum of Rs.80 million had been paid additionally to the contractors to reimburse the cost of performance security bonds obtained by the contractors.</p>	<p>Undue advantage for contractors.</p>	<p>As per clause (4.2) under Performance Security in the General CoC, briefed that the contractor shall obtain (at his cost) a performance security, which is include in the contract agreement, the same contract agreement comprises of the BOQ, where the contractor asked to prize the above items separately. However, the priority documents among the set of contract documents as per the CoC, also the contractor's right for claiming the item, where contractor was asked to do so by the employer, under the BOQ provision, the general statement given CoC clause (4.2) is overruled.</p>	<p>Action should be taken to recover the over payment.</p>		
<p>(iv) According to the sub clause 14.6 of the Particular Conditions of the Contract, the certificate work done an</p>	<p>Overrunning of cost on evaluation of Interim Payment</p>	<p>The condition laid under minimum amount of IPC was relaxed by looking into various factors, including the rate of progress of</p>	<p>It is required to adhere with the thresholds stipulated in the condition of contract in order to minimize</p>		

<p>Interim Payment Certificate should be greater than 2 per cent of the Accepted Contract Amount. Contrary to that, five instances were observed where the IPC payments had been made an amount ranging from Rs.35 million to Rs.52 million.</p>	<p>Certificates.</p>	<p>works and Engineer's recommendation etc. Contractor submits monthly IPC's irrespective of the amount of IPC to the Engineer, then the Engineer keep it &amp; send to Employer, by Cumulating IPCs to reach minimum value for payment.</p>	<p>the costs, time and undue favouration for the contractors.</p>
<p>(v) According to the information received, 5,612 plots of land including 2,322 plots of crown land were expected to be acquired by the Project for road rehabilitation works and compensation payments amounting to Rs. 135 million related to 231 plots of land had been settled as at 31 December 2018.</p>	<p>Possibility to increase the interest costs on compensation, due to delays in settlements of claims.</p>	<p>38 (a) Gazette orders were issued in 20 times for separate sections from June 2012 to March 2016. And compensation payments commenced in year 2017.</p>	<p>Need to take prompt actions to settle the compensation and avoid additional costs thereon.</p>