

Northern Road Rehabilitation Project for rehabilitation of 84 kilometres of Jaffna - Point Pedro Road Puttur - Meesalai Road, Jaffna - Kankasanturai Road and Jaffna - Palali Road - 2014

The audit of financial statements of the National Road Network in Northern Province Project for rehabilitation and improvement of 84 kilometres of Jaffna - Point Pedro Road, Puttur - Meesalai Road, Jaffna - Kankasanturai Road and Jaffna - Palali Road for the year ended 31 December 2014 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. This Project is implemented as per the Loan Agreement No.BLA 201004 dated 09 September 2010 entered into with the Democratic Socialist Republic of Sri Lanka and the Export-Import Bank of China.

1.2 Implementation, Objective, Funding and Duration of the Project

According to the Loan Agreement of the Project, then Ministry of Ports and Highways presently the Ministry of Highways and Higher Education is the Executing Agency and the Road Development Authority is the Implementing Agency of the Project. The Road Development Authority is responsible for the management and coordination of the Project activities at the national level. The objective of the Project is to rehabilitate and improve of 84 kilometres of Jaffna-Point Pedro Road, Puttur-Meesalai Road, Jaffna-Kankasanturai Road and Jaffna-Palali Road. As per the Loan Agreement, the estimated total cost of the Project is US\$ 88.7 million and out of that US\$ 75.4 million or 85 per cent was agreed to be financed by the Export-Import Bank of China. The preliminary activities of the Project was commenced on 01 December 2010 and the contract was effected from 09 June 2011. The rehabilitation works of the roads were scheduled to be completed by 08 December 2013. The road works had been completed and handed over to the Road Development Authority 01 October 2013. However, the financial statements of the Project for the year ended 31 December 2014 had been presented for audit.

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 controls so as to ensure a satisfactory control over Project Management and the reliability of books, records etc. relating to the operation of the Project.
- (b) 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 identification of the purchases made out of Loan etc.
- (c) Whether the funds, materials and equipments supplied under the Loan had been utilized for the purposes of the Project.
- (d) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (e) Whether the financial statements had been prepared in accordance with Sri Lanka Public Sector Accounting Standards.
- (f) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (g) Whether 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 2014 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2014 in accordance with Sri Lanka Public Sector Accounting Standards,
- (b) the funds provided had been utilized for the purpose for which they were provided,
- (c) the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (d) the financial covenants laid down in the Loan Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Non – Compliance with Laws, Rules and Regulations

The following instances of non-compliance highlighted in my previous audit report had been continued even during the year under review without taking remedial actions.

- (a) Payment of mobilization advances amounting to Rs.3,055.5 million on 30 per cent of total contract value of which included provisional amounts and allocations for contingencies aggregating Rs.882.65 million, contrary to the Section 5.4.4 of the Government Procurement Guidelines.
- (b) Bonus and allowance for medical encashment aggregating to Rs. 111,344 paid to the employees of the Road Development Authority attached to the Project, contrary to the Sections 8.3.9 and 8.6 of the Circular No PED/12 dated 02 June 2003 of the Department of Public Enterprises.
- (c) Calculation of remunerations for the employees of the Road Development Authority attached to the Project based on a formula introduced by the Road Development Authority, contrary to the Circular No.33 of 05 April 2007 of the Department of Management Services. In this connection, remuneration aggregating Rs.12.81 million had been paid up to 31 December 2013 without being obtained a proper authority.

2.2.2 Un-reconciled Balances

According to the financial statements, the proceeds of Loan received during the year under review amounted to Rs.2,805.6 million whereas the statements of the External Resources Department and a summary report prepared by the Project Monitoring Unit corresponding balance had been shown as to Rs.2,318.43 million. The difference of Rs.487.17 million had not been reconciled.

3. Financial and Physical Performance

3.1 Utilization of Funds

According to the information made available, certain significant statistics relating to the financing of the Project and the utilization of funds for the year under review and as at 31 December 2014 are shown below.

Sources	Amounts agreed to be financed in the Loan Agreement		<u>Funds utilized</u>		during the year 2014 as at 31 December 2014	
	<u>US \$</u> million	<u>Rs.</u> million	<u>Rs.</u> million	<u>US \$</u> million	<u>Rs.</u> million	
China Export – Import Bank	75.40	10,185.00	2,805.63	74.75	9,281.87	
GOSL	13.30	1,968.75	44.82	14.60	1,905.55	
	<u>88.70</u>	<u>12,153.75</u>	<u>2,850.45</u>	<u>89.35</u>	<u>11,187.42</u>	

3.2 Physical Performance

According to the information received, the rehabilitation and reconstruction of the roads had been substantially completed and the rehabilitated roads were handed over to the Road Development Authority on 01 October 2013.

3.3 Contract Administration

The following observations are made.

- (a) According to the quality test reports of the Consultant, the Asphalt laid in the 04 roads were not agreed with the technical specifications to meet required quality. As a result, a sum of Rs.323.04 million had been deducted from the claims presented by the contractors. According to the instructions of the Consultant, the compaction degree mentioned in the technical specifications had been reduced up to 92 per cent from 96 per cent and a sum of Rs.61.84 million of deduction made had been repaid to the contractor. According to the provisions of the consultancy agreement, the Consultant is not permitted to change the specifications unless the employer gives such decisions to the

Engineer in writing. However, the action had not been taken by the Project to call the explanation from Consultant for altering of the specifications and approving the refunds.

- (b) According to the information made available, savings amounting Rs. 2,053 million whilst additional works valued at Rs.3,484 million had been reported at the completion of civil works thus indicated that the Bill of Quantities had been prepared by the Project without making proper ground surveys and actual requirements. Although the works related to the installation of 723 street lamps at the sides of 4 roads had been included in the Bill of Quantities, cable installation and power supply connection to street lamps had been ignored. Thus, the variation orders valued at Rs. 41.90 million had to be approved.

3.4 **Transaction with contentions Nature**

The following observations are made.

- (a) According to the Statement of Completion, a sum of Rs. 515.46 million had been paid for demolition and rebuilding of properties eventhough the provisional allocation amounting to Rs.15 million had only been made in the Bill of Quantities for that purpose. Further, it was observed that the contractors had not directly involved for the demolition and rebuilding activities and payments had been made to the third parties. However, the payment details had not been made available for audit.
- (b) Eventhough the following activities were not directly related to the original scope of works of the Project, such activities had been carried out by the Project through variation orders.

<u>Description</u>	<u>Amount spent</u> Rs. million
Construction of access roads to the Jaffna Fort and Thuraiappa Stadium	39.49
Signal light system at Hospital junction in Jaffna	5.32
Specialized works in Kilinochchi town	63.38