

Pro-poor Eastern Infrastructure Development Project - 2013.

The audit of financial statements of the Pro-poor Eastern Infrastructure Development Project for the year ended 31 December 2013 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 (8) of the Loan Agreement No.SLP/87 dated 28 March 2006 entered into between the Government of the Democratic Socialist Republic of Sri Lanka (GOSL) and the Japan Bank for International Co-operation (JBIC). The JBIC merged with the Japan International Corporation Agency (JICA) with effect from 01 October 2008.

1.2 Execution, Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement of the Pro-poor Eastern Infrastructure Development Project, the Ministry of Highways, Ports and Shipping is the Executing Agency of the Project and the Road Development Authority (RDA) is the Implementing Agency of the Project. The objectives of the Project are to restore economic foundation of the under developed eastern local economy and reduce the regional economic disparity by improving access within and outside of the Project areas through reconstruction of deteriorated and partly Tsunami affected national road between Akkaraipattu and Thirukkondiamadu including construction of a new Kallady Bridge in Batticaloa. According to the Loan Agreement, the estimated total cost of the Project is Japanese Yen 4,460 million. The Project commenced its activities in 2006 and was scheduled to be completed by September 2010. Subsequently, the Project period was extended up to 15 September 2013. However, the Project activities had been continued up to 31 December 2013.

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. This responsibility includes; designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies, and making accounting estimates that are reasonable in the circumstances.

2. Scope of Audit and Basis of Opinion

My responsibility is to express an opinion on these financial statements based on my audit. Audit opinion, comments and findings in this report are based on a review of the financial statements presented to audit and substantive tests of samples of transactions. The scope and extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitations of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes the examination on

a test basis of evidence supporting the amounts and disclosures in financial statements and assessment of accounting policies used and significant estimates made by the management in the preparation of financial statements as well as evaluating their overall presentation. I have obtained sufficient information and explanations which to the best of my knowledge and belief were necessary for the purpose of my audit. I therefore believe that my audit provides a reasonable basis for my opinion. The examinations also included such tests of systems and controls, transactions, assets, liabilities and accounting records as deemed necessary to assess the following.

- (a) Whether the systems controls were adequate from the point of view of internal control so as to ensure a satisfactory control over the Project Management and the reliability of books, records, etc. relating to the operations 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 operation of the Project, the identification of purchases made out of the Loan etc.
- (c) Whether withdrawals under the Loan had been made in accordance with the specification laid down in the Loan Agreement.
- (d) Whether funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (e) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (f) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles.

3. 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 5 of this report, I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2013 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2013 in accordance with Generally Accepted Accounting Principles,

- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the Statement of Expenditure (SOE) submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement,
- (d) satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and:
- (e) the financial covenants laid down in the Loan Agreement had been complied with.

4. Financial Statements

4.1 Financial Performance

According to the financial statements presented and information made available, the expenditure of the Project for the year under review amounted to Rs. 500,395,458 and the cumulative expenditure as at 31 December 2013 amounted to Rs. 7,510,101,696. The following statement shows a summary of expenditure for the year under review and the preceding year and the cumulative expenditure as at 31 December 2013.

Category of Expenditure	Expenditure for the year ended 31 December		Cumulative Expenditure as at 31 December 2013
	2013	2012	Rs.
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	Rs.	Rs.	
Non- Current Assets	136,538	-	136,538
Work-in-progress	445,695,635	6,150,036,481	6,595,732,116
Consultancy Fees	47,318,437	743,802,052	791,120,489
Project Management Unit Expenditure	<u>7,244,848</u>	<u>115,867,705</u>	<u>123,112,553</u>
Total	<u>500,395,458</u>	<u>7,009,706,238</u>	<u>7,510,101,696</u>

5. Audit Observations

5.1 Accounting Deficiencies

The following accounting deficiencies were observed.

1. The Project had not maintained separate set of books and records so as to identify the total cost incurred for rehabilitation of individual roads under the Project.

2. Even though the constructions of Colombo-Ratnapura- Wellawaya- Batticaloa Road, Batticaloa - Thirukkandimadu-Trincomalee Road and Kallady Bridge had been fully completed and handed over to the Project as at 15 September 2013, the total cost aggregating Rs. 7,509,965,158 consisting of consultancy fees and Project Management Unit expenditure incurred for the above construction works had been shown in the financial statements as work- in- progress.

3. The Project Management Units of other three foreign funded projects are located in a same office building. However, all expenses aggregating Rs. 6,420,120 incurred for water, electricity, telephone, transport charges, fuel expenses and insurances charges relating to those Projects had been charged to this Project without being ascertained separately and charged to individual Projects.

6. Financial and Physical Performance

6.1 Utilization of Funds

Certain significant statistics relating to the financing of funds, budgetary provisions for the year under review and utilization of funds during the year under review and the cumulative expenditure as at 31 December 2013 are shown below.

Source	Amount agreed to be financed		Allocation made in the Annual Budget	Amount utilized during the year under review	Amount utilized as at 31 December 2013	
	J.Yen Mn	Rs. Mn.	Rs. Mn	Rs. Mn	J.Yen Mn	Rs. Mn
JICA	4,460	6,158	-	-	4,837	6,205,604
GOSL	-	1,532	88,476	88,476		1,027,843
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Total	<u>4,460</u>	<u>7,690</u>	<u>88,476</u>	<u>88,476</u>	<u>4,837</u>	<u>*7,233,447</u>

- * This amount differs from the amount shown in paragraph 4.1 of this report due to exclusion of provision for gratuities, retention money and accrued expenditure.

6.2 Physical Performance

The contract for construction of Kallady Bridge had been awarded without evaluating the capacity and past experience of the bidders properly. As a result, the contract awarded for construction of bridge to the first contractor at Rs. 700 million had been terminated subsequently due to poor performance. The construction works had been completed by an other contractor at a cost of Rs. 1,389.5 million which represented 95 per cent increase from the original contract value. As a result, the consultancy fees amounting to Japanese Yen 228,600,000 equivalent to Rs. 326,392,260 according to the first contract agreement had been revised as Japanese Yen 321,318,914 equivalent to Rs. 459,196,960 which represents 29 per cent increase from the consultation fee included in the original contract.