

## **Improvement of National Road Network in Northern Province Project (Rehabilitation of 63 kilometres of Kandy- Jaffna Road) - 2014**

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The audit of financial statements of the Improvement of National Road Network in Northern Province Project (Rehabilitation of 63 kilometres of Kandy- Jaffna 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 201002 dated 09 September 2010 entered into between the Democratic Socialist Republic of Sri Lanka and the Export-Import Bank of China.

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

According to the Loan Agreement of the Project, then Ministry of Ports and Highways, presently the Ministry of Higher Education 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 rehabilitation and improvement of 63 kilometres of Kandy-Jaffna Road (A09) from 122 kilometre post to 230 kilometre post. As per the Loan Agreement, the estimated cost of the Project was US\$ 83.5 million and out of that US\$ 71 million was agreed to be financed by the Export-Import Bank of China. The preliminary works of the Project was commenced on 01 June 2010 and rehabilitation and improvement works of the Road had been commenced on 07 February 2011. The activities of the Project were scheduled to be completed by 06 October 2013. However, the activities of the Project were continued up to 31 December 2014.

### **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 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.
- (d) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.
- (e) Whether the funds, materials and equipments supplied under the Loan had been utilized for the purposes of the Project.
- (f) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (g) Whether the financial statements had been prepared on the basis of Sri Lanka Accounting Standards.
- (h) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (i) 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 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 Accounting Standards,
- (b) the funds provided had been utilized for the purpose for which they were provided,
- (c) 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 of Financial Statements**

### **2.2.1 Accounting Deficiency**

A special Loan of Rs.2.49 million obtained during the year under review from Road Development Authority had not been separately recognized and disclosed in financial statements. The liability of the Loan had not been settled even as at 31 December 2014.

### **2.2.2 Lack of Evidence for Audit**

As a practice, value of assets such as vehicles, equipments, furnitures etc., procured by the contractor and consultant, out of Loan proceeds were not recognized separately and brought to accounts of the Project. Further, according to the information made available, the assets valued at Rs.35.92 million which included in the value of civil works had been transferred to the Line Ministry during the year under review. However, such assets procured by the contractor and the Consultant and other assets included in the value of civil works which were subsequently transferred to the Line Ministry could not be verified in audit due to lack of Register of Fixed Assets and other details relevant for verifications.

### 2.2.3 Non - Compliance with Laws, Rules and Regulations

The overhead cost amounting to Rs.1.367 million had been recovered by the Road Development Authority contrary to the Section 8.39 of the Circular No. PED/12 dated 02 June 2003 of the Department of Public Enterprises. Further, the bonus and medical allowance of Rs. 233,254 had been paid to the staff of the Road Development Authority attached to the Project which was not permitted in terms of the Section 8.6 of the said Circular. Eventhough the above instances of non – compliance were highlighted in my previous audit reports, such practices were continued even during the year under review without taking remedial actions.

## 3 Financial and Physical Performance

### 3.1 Utilization of Funds

Certain significant statistics relating to the financing of funds, budgetary provision for the year under review and the utilization of funds during the year under review and up to 31 December 2014 are shown below.

Source	Amount agreed for financing according to the Loan Agreement		Funds utilized			
			during the year 2014		up to 31 December 2014	
	US\$	Rs.	US\$	Rs.	US\$	Rs.
	million	million	million	million	million	million
Export-Impo Bank of China	71.00	8,153.20	5.70	746.05	70.98	8,568.61
GOSL	12.50	1,832.81	0.27	35.30	11.04	1,794.95
	83.50	9,986.01	5.97	781.35	82.02	10,363.56

### 3.2 Physical Progress

According to the information received, the rehabilitation works of the Road had been substantially completed before the expected date and the rehabilitated roads were handed over to the Road Development Authority on 06 August 2013.

### 3.3 Contract Administration

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The following observations are made.

- (a) Eventhough the defects liability period of the road works was ended as at 06 August 2014, the site inspections made by the auditors in August 2015 had revealed that several cracks in the road surface at the chainage from 131 + 100 kilometre to 131 + 106 kilometre of the Road. Further, cracks were appeared at the head and wing walls of the culvert No. 123/1 and the concrete slab of the culvert No. 132/1 of the Road. In addition, a crack was appeared between the interface of the approach slab of the bridge No.230/3 and the Asphalt concrete of the Road. It was observed that the Project had not taken action to observe such defects as enable to rectify by the contractor during the defects liability period.
- (b) It was observed at the site inspections that the road bend at the chainage of 131 + 060 kilometre at right hand side was not properly designed and reconstructed. The width of section of the road had been reduced by 0.5 metre and as a result, road surface at this chainage had been damaged. Further, safety requirements had not been fulfilled due to lack of sign boards at the nearest locations, erasing of road edge line and center line due to narrowness of the road bend.
- (c) As per Clause No. 114 of the Volume 03 of the Technical Specification, the contractor is responsible to maintain carriageway and allocation amounting to Rs.21.12 million had been made in the Bill of Quantities for the respective works. However, the Statement of Completion submitted by the contractor had indicated that a sum of Rs.73.95 million had been spent by the contractor and furnished claims accordingly.