

## **Extension of Southern Expressway Project - 2016**

-----

The audit of financial statements of the Extension of Southern Expressway Project for the year ended 31 December 2016 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 Loan Agreements of PBC No.(2014) 27 Total No.(321), PBC No.(2015) 38 Total No.(381), GCL No.(2014) 17 Total No.(520) and GCL No.(2014) 18 Total No.(521) of dated 16 September and 23 December 2014 and 07 April 2016 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 Agreements of the Project, then Ministry of Higher Education and Highways presently, the Ministry of Highways & Road Development and Petroleum Resources is the Executing Agency and Road Development Authority is the Implementing Agency of the Project. The main objective of the Project is to develop the road network of Sri Lanka by extending of 96 kilometres of the Southern Expressway from Matara to Hambantota to facilitate for the developments of Hambantota area as an international hub. The estimated cost of the Project amounted to Rs.311,075 million and out of that US\$ 1,708 million equivalent to Rs.218,438 million was agreed to be provided by the Export Import Bank of China for the civil works and supervision consultancy purposes. The construction works of 03 sections of the Expressway had been commenced in January 2016 and the construction works of other section had been commenced in October 2016. It was expected to complete the construction works in January 2019.

### **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 followings.

- (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, etc.
- (d) Whether the funds, materials and equipment supplied under the Loans 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 Sri Lanka Public Sector Accounting Standards,
- (g) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (h) Whether the financial covenants laid down in the Loan Agreements had been complied with.

## **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 paragraphs 2.2 of this report. I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2016 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2016 in accordance with Sri Lanka Public Sector Accounting Standards.
- (b) the funds provided had been utilized for the purposes 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 Agreements had been complied with.

## 2.2 Comments on Financial Statements

### 2.2.1 Accounting Deficiency

A sum of Rs 931 million payable to the Consultants of the Project as at 31 December 2016 had not been brought to the financial statements for the year under review.

### 2.2.2 Non - Compliance with Laws, Rules and Regulation

Even though the payments aggregating Rs. 1,084 million not approved either by the Project Director or the Executing Agency as required by the Financial Regulation 137 had been shown as accrued expenses in the financial statements of the year under review.

## 3. Financial and Physical Performance

### 3.1 Utilization of Funds

Certain significant statistics relating to the financing, budgetary provision for the year under review and the utilization of funds during the year under review and up to 31 December 2016 are shown below.

Source	Amount agreed for financing in the Loan Agreement		Allocations made in the Budget	Funds utilized	
	US\$ million	Rs. million	Estimate for the year under review	during the year under review	up to 31 December 2016
	US\$ million	Rs. million	Rs. million	Rs. million	Rs. million
Export Import Bank of China	1,708	220,042	40,626.60	31,784.80	46,588.70
Government of Sri Lanka	121	15,588	5,400.00	4,535.00	11,818.30
Hatton National Bank	63	8,181	-	1,785.50	1,785.50
	<u>1,892</u>	<u>243,811</u>	<u>46,026.6</u>	<u>38,105.30</u>	<u>60,192.50</u>

### 3.2 Physical Progress

According to the Technical Audit Report issued by the University of Moratuwa on 28 April 2015, the Economic Internal Rate of Return of the construction of extension for Southern Expressway with 04 lanes had remained at negative 11.10 per cent. However, the construction works of the extension of Expressway with 04 lanes had been divided under 04 sections, namely Matara to Beliatta, Beliatta to Wetiya, Wetiya to Andarawewa and Mattala to Hambantota via Andarawewa and awarded to 03 foreign contractors in 2014 under unsolicited contract packages. According to the information received, the activities of the construction of the Expressway had remained at the preliminary stages as at 31 December 2016. The following further observations are made thereon .

- (a) As a general feature, the scope of works of the contracts had been changed regularly. Therefore, Viaduct Bridges had been introduced from 6.50 kilometre to 10.30 kilometre of the Expressway from Matara to Beliatta instead of the embankments proposed in the initial designs. However, the impacts on cost escalations thereon had not been measured and disclosed by the Project.

- (b) The site supervision of the construction works of the section from Matara to Beliatta of the Expressway had been awarded to a state owned corporation in September 2014 and terminated in September 2015. It was observed that a sum of Rs 24.84 million had been paid using the savings of other donor funded project called Northern Road Rehabilitation Project. However, the civil construction works had been commenced only on 19 January 2016 thus proved that neither the guidance of the Consultants had been sought nor site supervision on the construction works carried out by the Consultant.

### **3.3 Human Resources Management**

The approved cadre of the Project consisted with 226 positions including a Project Accountant, 13 Project Engineers and 36 Management Assistants. However, the Project Monitoring Unit had deployed 04 Project Accountants, 13 Project Engineers and 36 Management Assistants additionally without being obtained the approval of the Department of Management Services.

### **3.4 Matters in Contentious Nature**

The following further observations are made.

- (a) It was observed that a quarry pit of 40 metres in length and 23 metres in depth of the Section from 8+250 kilometre to 8+500 kilometre of the Expressway from Mattla to Hambantota had not been identified at the initial stage of land surveying of the Expressway eventhough 13 Land Acquisition and Resettlement Consultants had been deployed and remuneration aggregating Rs 386.67 million had been paid them as at 31 December 2016. Subsequently, it was decided by the Project to embank the quarry pit at an estimated cost of Rs 380.66 million.
- (b) It was observed that a sum of Rs 266.61 million had been paid to the contractor eventhough a Gravel Compaction Pile tests carried out for 41,970 linear metres at the Section from Matara to Beliatta was reported as failed.
- (c) The costs on obtaining performance bond aggregating Rs.128.42 million had been spent by the Project, contrary to the section 4.2 of the general condition of the contract.
- (d) According to the Bill of Quantities No 103 (2) of the contract agreement, the contractors are allowed to re-export the machineries and equipment imported for construction purposes. However, no mechanism had been introduced to identify the machineries and equipment expected to be re-export by the contractors .

### **3.5 Issues on Land Acquisition Activities**

According to the information furnished to the audit, the land acquisition process was commenced on 21 May 2014 and scheduled to be completed on 19 November 2014. However, no records had not been maintained by the Land Acquisition Division of the Road Development Authority on plots of lands acquired by the respective Division for extension of Southern Expressway.

### **3.6 Issues on Financial Control**

The Fixed Assets Register required to be maintained as per Financial Regulation 454 and 751 had not been properly maintained by the Project.