Landslide Disaster Protection Project - 2017

The audit of financial statements of the Landslide Disaster Protection Project for the year ended 31 December 2017 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 under the Loan Agreement No. SL-P 109 dated 14 March 2013 entered into between the Democratic Socialist Republic of Sri Lanka and the Japan International Cooperation Agency.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement of the Project, then Ministry of Ports, Highways and Shipping, presently Ministry of and Highways and Road Development is the Executing Agency and Road Development Authority is the Implementing Agency of the Project. The objective of the Project is to mitigate landslide disaster of national roads by implementing appropriate countermeasures in highland areas in the Central, Uva and Sabaragamuwa Provinces, thereby contributing to the economic and social development and enhance the security of the road network and safeguard the lives of people including road users and residents. As per the Loan Agreement, the estimated total cost of the Project amounted to Japan Yen 9,841 million equivalent to Rs.14,754 million and out of that, Japan Yen 7,619 million equivalent to Rs.11,423 million was agreed to be provided by the Japan International Cooperation Agency. The Project commenced its activities on 05 July 2013 and scheduled to be completed by 31 March 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 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 etc.

(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 equipment 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 Public Sector 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 2017 and the financial statements give a true and fair view of the state of affairs of the

Project as at 31 December 2017 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 Agreement had been complied with.

2.2 Comments on Financial Statements

2.2.1 Accounting Deficiencies

The following accounting deficiencies were observed in audit.

(a) A sum of Rs. 76.5 million payable to the Contractor as at 31 December 2017 and reimbursement of Economic Service Charges Tax and income tax on payments made to the foreign Consultants aggregating to Rs.2.44 million had not been brought to the financial statements of the Project.

(b) It was observed that the fixed assets procured at a cost of Rs 14.87 million under the package - 02 of the Project for the use of the local Consultant and the offices of Resident Engineer in Bandarawela and Site Engineer in Badulla had not been accounted under property, plant and equipment in the financial statements of the Project.

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 2017 are shown below.

Source	Amount agreed for financing in the Loan Agreement		Allocation made in the Budget Estimate for the year under review	Funds utilized during the year under review		Funds utilized as at 31 December 2017	
	JPY million	Rs. million	Rs. million	JPY million	Rs. million	JPY million	Rs. million
JICA	7,619.00	11,423.00	1,270.00	911.47	1,212.79	1,405.53	1,826.17
GOSL	2,222.00	3,331.00	278.00	105.53	140.41	203.32	263.03
	9,841.00	14,754.00	1,548.00	1,017.00	1,353.20	1,608.85	2,089.20

According to the above information, out of total allocation of Yen 7,619 million equivalent to Rs.11,423 million made by the Lending Agency, only a sum of Yen 1,405.53 million equivalent to Rs.1,826.17 million representing 16 per cent of the total allocation had been utilized as at 31 December 2017 after lapse of 03 ½ years from the commencement of the activities of the Project.

3.2 Physical Progress

The contracts for the execution of countermeasures at 16 locations in Central, Uva and Sabaragamuwa provinces for road disaster management had been awarded at an estimated cost of Rs.6,094.48 million on 01 March 2017 under 02 packages and the construction works were scheduled to be completed on 21 March 2019. According to the work plans of the Project , the physical progress of 24.5 per cent and 38.12 per cent was required to be achieved under the package 01 and package 02 respectively by 31 December 2017 and progress of 1.95 per cent and 34.88 per cent had been achieved respectively as at that date. Eventhough the contract agreement for execution of countermeasures had been entered into on 24 March 2017 with a contractor under the package 01, the construction works at Ramboda, Theligama, Pitawala and Ginigathena sites had not been commenced even as at the date of audit inspection made on 12 September 2018. Further, the slow progress had been reported on construction works under other 09 sites as at 31 December 2017.

3.3 Contract Administration

The following observations are made.

(a) The construction works at Keppetipola and Toppass sites awarded to a state owned Corporation at an estimated cost of Rs.357 million under the package -01. It was revealed at the physical site visits made in October 2018 that the construction works were continued by the contractor through a sub contractor who involved in construction works under package 02 of the Project, as a joint venture partner .

(b) According to the Cabinet Memorandum No. 13/0076/504/005 of 16 January 2013, the Project should implemented countermeasure works of "A" class national roads in the highland areas. However, contrary to the above policy, an AB class road in Nawalapitiya area had been selected under the package - 01 to implement countermeasure works at an estimated cost of Rs.412.65 million.

(c) According to the information received, the contracts for construction of 10 drainage wells had been awarded at an estimated cost of Rs.490.44 million in Nawalapitiya, Kahagalla and Lunugala areas as countermeasures for the prevention of landslides under the Project and the sites scheduled to be handed over to the property owners after completion of the construction works. However, no arrangements had been made with regard to the maintenance of the wells in sustainable manner .

(d) The Rock Bold countermeasures for construction works had been applied in mitigation works carried out at Diyagala in Nawalapitiya and a sum of Rs.62.5 million had been spent thereon during the year under review . However, a part of the construction had been collapsed due to the heavy rain and therefore, the methodology applied as a protective measure had remained questionable.

(e) It was observed at the site inspection that the tap lines for overflowing water from the drainage well located at the Lunugala of Peradenya- Badulla- Chenkalady Road had been fixed without allocating protective area between the road and water line. However, actions had not been taken to prevent the probable damages that could be occurred to the system thereon.

(h) The Project had taken to spread hydro seeding, as a countermeasure for landslides of 11 areas at an estimated cost of Rs.43.77 million and out of that a sum of Rs 3.07 million had been spent as at 31 December 2017 to spread hydro seeding in Lunugala area . The site inspection made in September 2018 had revealed that the local grass had been grown in the area of spreading of hydro seeding and thus it evident the hydro seeding was not a successful alternative for counter measuring purposes.

3.4 <u>Matters in Contentious Nature</u>

The Project had been allocated a sum Rs.09 million, out of a Loan obtained by the Road Development Authority from Licensed Specialized Bank in 2014. However, no action had been taken to settle the Loan even at the end of the year under review.

3.5 <u>Issues on Financial Control</u>

The following observations are made.

(a) According to the Sub clause No. 14.6 of the conditions of the contract agreements, the minimum amount of an interim payment certificate had been determined as 02 per cent of the agreed contract amount for the evaluation purposes . However, 09 interim payment certificates submitted during the year under review had remained below the prescribed amount, due to the poor physical progress of the construction works.

(b) According to the contract agreements signed with 02 contractors, sums of Rs.90.34 million and Rs.89.50 million had been estimated for lump sum payments under general expenses for the package- 01 package -02 respectively without considering the nature of the payments and requirements. Out of that estimates, a sum of Rs.167.6 million had been claimed by 02 contractors up to 30 June 2018.

(c) The Project had not taken action to obtain exemption for local taxes, and as a result, the Value Added Tax amounting to Rs.204 million had been paid by the Project during the year under review on the payments made to the contractors. Further, income tax amounting to Rs.2.42 million and Pay-As-You-Earn Tax amounting to Rs.3.37 million had to be borne by the Project during the year under review on behalf of the Consultant.

3.6 <u>Human Resources Management</u>

It was observed that 02 local Consultants had been appointed in July 2017 even though no such a post had not been approved by the Department of Management Services.