

## **Northern Road Connectivity Project -2017**

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The audit of financial statements of the Northern Road Connectivity 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 read in conjunction with Section 4.05 of Article IV of the Loan Agreement No.2639-SRI dated 27 August 2010 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank.

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

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According to the Loan Agreement, then Ministry of Ports and Highways, presently the Ministry of Highways and Road Development is the Executive 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 Project activities at the national level. The objective of the Project is to rehabilitate and improve 170 kilometres of national roads in the Northern and North Central Provinces. As per Loan Agreement, the initial estimated total cost of the Project amounted to US\$ 146 million equivalent to Rs. 16,790 million and out of that US\$ 130 million equivalent to Rs. 14,950 million was agreed to be financed by the Asian Development Bank. Further, the Asian Development Bank had agreed to provide US\$ 68 million equivalent to Rs. 8,840 million under the additional financing Loan Agreement No. 2890 SRI (SF) of 31 May 2013, out of which US\$ 34 million equivalent to Rs. 4,420 million had been allocated to Provincial Road Development Authorities of the Northern Province and North Central Provinces. In addition, US\$ 30 million equivalent to Rs. 3,900 million had also been allocated by the Asian Development Bank under the Loan Agreement No.2891 SRI of 31 May 2013 to national roads highways in the Northern and North Central Provinces. The Project commenced its activities under the initial Loan Agreement on 22 October 2010 and had been completed by 31 December 2015. The activities of the Project under additional financing arrangements were commenced on 13 May 2013 and scheduled to be completed by 31 December 2017.

### **1.3 Responsibility of the Management for the Financial Statements**

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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**

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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. 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 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 Loans etc.
- (d) Whether the withdrawals under the Loans had been made in accordance with the specifications laid down in the Loan Agreements.
- (e) Whether the funds, materials and equipment supplied under the Loans 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 the 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 Agreements had been complied with.

## **1.5 Basis for Qualified Audit Opinion**

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My opinion is qualified based on the matters describe in paragraph 2.2 of this report.

## **2. Financial Statements**

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### **2.1 Opinion**

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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 opening and closing balance, withdrawals from and replenishments to the Imprest Accounts had been truly and fairly disclosed in the books and records maintained by the Project and the balances as at 31 December 2017 had been satisfactorily reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,
- (d) the Statements of Expenditure submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreements,
- (e) the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (f) the financial covenants laid down in the Loan Agreements had been complied with.

## **2.2 Comments on Financial Statements**

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### **2.2.1 Accounting Deficiencies**

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The following observations made in this regards.

- (a) Eventhough civil works under the contracts awarded by the Project had been completed as at 31 December 2015, the value of such works amounting to Rs. 21.57 million had continuously shown as work-in-progress in the financial statements.
- (b) The value of motor vehicles transferred to the Road Development Authority amounting to Rs.276.33 million had been erroneously shown in the financial statements as Rs. 284 million.

### 3. Financial and Physical Performance

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#### 3.1 Utilization of Funds

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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 Agreements		Allocation made in the Budget Estimate for the year under review	Funds utilized		
	US\$ million	Rs million	Rs million	during the year 2017 Rs million	up to 31 December 2017 US\$ million	Rs million
ADB						
- 2639	130	14,950	86.00	81.56	127.28	16,103.77
- 2890	34	4,420	450.00	409.70	28.19	3,911.74
- 2891	30	3,900	-	246.83	22.69	3,077.27
GOSL	-	2,080	25.30	10.92	0.58	74.95
<b>Total</b>	<b><u>194</u></b>	<b><u>25,350</u></b>	<b><u>561.30</u></b>	<b><u>749.01</u></b>	<b><u>178.74</u></b>	<b><u>23,167.73</u></b>

#### 3.2 Physical Progress

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According to the information received, the rehabilitation works of 10 national roads in Northern and North Central Provinces with the length of 170 kilometres under 10 packages including 03 years performance based maintenance works of 03 rehabilitated national roads had been completed even as at 31 December 2015. Further, the works contracts for rehabilitation of other 02 national roads awarded in 2015 by utilizing the savings on rehabilitation of roads in the Northern and North Central Provinces under the initial Implementing Plan and the additional financing arrangements had been completed as at 31 December 2016. In addition to that, a new contract had been awarded on 28 April 2017 to rehabilitate a section of Kandy - Jaffna Road from Rambewa to Medawachchiya with the length of 9.64 kilometres and physical progress of the contract was remained at 49 per cent as at 31 December 2017.

#### 3.3 Matters in Contentious Nature

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The following observations are made.

- a) The contracts at an estimated cost of Rs. 232.19 million had been awarded to maintain 20 national roads, out of 22 national roads rehabilitated by the Project in addition to the contract awarded to rehabilitation. It was observed that contract for the maintenance of 11 national roads for the period of 03 years whilst 09 other national

roads for the period of 05 years had been awarded without considering the fact that the completion of the period of the Project as at 31 December 2017.

- b) According to the information received, the office buildings and staff quarters constructed by the Project at a cost of Rs. 90.1 million at Oddusudan, Mulliwaikkal and Madu Junction had been transferred to the Road Development Authority as at 31 December 2017. However, the information relating to the dates of transfer and the parties undertaken such properties etc, had not been made available for audit and as a result, the existence and usage of those properties for intended purposes could not be examined by the audit.

### **3.4 Uneconomic Transactions**

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It was observed that the contractors who engaged in road rehabilitation works of the Project were allowed to import motor vehicles directly for the use of their activities. Therefore, 37 motor vehicles procured at a cost of Rs.284 million from 2013 to 2016 had been transferred to the Road Development Authority whilst other 10 motor vehicles procured at a cost of Rs. 89.6 million remained at the Project Monitoring Unit as at 31 December 2017. The following observations are made thereon.

- a) The Project had taken action to hire 02 motor vehicles during the year under review in addition to the above mentioned 10 motor vehicles. According to the lease agreements, the maximum limit of 2,500 kilometres per month per motor vehicle is required to be run. It was observed that a sum of Rs. 3.66 million had been spent by the Project as at 31 December 2017 on running of 59,484 kilometres with the shortage of 17,316 kilometres.
- b) Further, the Project had taken action to procure another motor vehicle at a cost of Rs. 14.05 million on 24 April 2017 and necessity of a new motor vehicle could not be determined in audit as the period of Project was scheduled to be closed as at 31 December 2017.

### **3.5 Extraneous Activities of the Project**

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It was observed that a printer and other accessories had been procured at a cost Rs.2.89 million for the use of the Road Development Authority and not directly related to achieve the objectives of the Project.