

Metro Colombo Urban Development Project -2017

The audit of financial statements of the Metro Colombo Urban Development 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 II (B.3) of Schedule 2 of the Loan Agreement No.8145 – LK dated 18 May 2012 entered into between the Democratic Socialist Republic of Sri Lanka and the International Bank for Reconstruction and Development (IBRD).

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement of the Project, Ministry of Megapolis and Western Development is the Executing Agency and Urban Development Authority, the Sri Lanka Land Reclamation and Development Corporation and the Colombo Municipal Council are the Implementing Agencies of the Project. The objectives of the Project are to reduce flooding in the catchment of the Colombo water basin, strengthen the capacity of Local Authorities in the Colombo Metropolitan Area, improve and maintain local infrastructure and services through selected demonstration investments. As per the Loan Agreement, the estimated total cost of the Project amounted to US\$ 321 million equivalent to Rs.42,031.74 million and out of that US\$ 213 million equivalent to Rs. 27,890.22 million was agreed to be financed by the International Bank for Reconstruction and Development. The Project commenced its activities on 10 July 2012 and scheduled to be completed by 30 June 2017. Subsequently, the period of the Project had been extended up to 30 June 2020.

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 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 identification of the purchases made out of the Loan etc,
- (d) Whether the opening and closing balances, withdrawals from and replenishments to the Special (Dollar) Account 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.
- (e) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.
- (f) Whether the funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (g) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (h) Whether the financial statements had been prepared on the basis of Generally Accepted Accounting Principles.
- (i) Whether the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (j) Whether financial covenants laid down in the Loan Agreement 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, 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 Generally Accepted Accounting Principles,
- (b) the funds provided had been utilized for the purpose for which they were provided,
- (c) the opening and closing balances, withdrawals from and replenishments to the Special (Dollar) Account had been truly and fairly disclosed in the books and records maintained by the Project and the balance as at 31 December 2017 had been satisfactory reconciled with the accounting records of the Central Bank of Sri Lanka as at that date,
- (d) the Statement of Expenditure submitted could be fairly relied upon to support the applications for reimbursement in accordance with the requirements specified in the Loan Agreement,
- (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 covenant laid down in the Loan Agreement had been complied with.

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 | Funds utilized | | | |
|--------------|---|-------------------------|---|----------------------|---------------------|------------------------|----------------------|
| | | | | during the year 2017 | | up to 31 December 2017 | |
| | US\$ million | Rs. million | Rs. million | US\$ million | Rs. million | US\$ million | Rs. million |
| IBRD | 213 | 27,890.22 | 3,000 | 14.34 | 2,347 | 87.70 | 12,198 |
| GOSL | 108 | 14,141.52 | 1,177 | 7.59 | 1,177 | 25.70 | 3,691 |
| Total | <u>321</u> | <u>42,031.74</u> | <u>4,177</u> | <u>21.93</u> | <u>3,524</u> | <u>113.40</u> | <u>15,889</u> |

According to the above information, only a sum of US\$ 87.70 million equivalent to Rs.12,198 million representing 41 per cent of the total allocation of US\$ 213 million equivalent to Rs.27,890.22 million made by the Lending Agency had been utilized after lapse of 5 ½ years of the period of the Project as at 31 December 2017. It was observed that possibility of utilization of balance of the allocation of US\$ 125.3 million equivalent to Rs.15,692.22 million during the rest of the period of 3 ½ years is remained in doubt, as a comprehensive detailed action plan had not been prepared and implemented by the Project.

3.2 Physical Progress

According to the information received, the Project had taken actions to implement 56 programmes under Components of the Flood and Drainage Management and Supporting the Local Authorities in Metro Colombo Region. With regard to the above programmes, 44 contracts had been awarded as at 31 December 2017 at an estimated cost of Rs.13,843 million and out that the activities related to 34 contracts had been completed at the end of the year under review, after delaying a considerable periods leading to extend of the period of the Project by further 03 years. The physical progress of the remaining 10 construction contracts had remained at a range from 10 per cent to 87 per cent at the end of the year under review. The following observations are made thereon.

- (a) Slow Progress ranging from 13 per cent to 90 per cent had been reported as at 31 December 2017 on reconstruction of drainage system of Kynscy Road, construction of drainage canal at Devi Balika Vidyalaya, development works at Madiwela East and Kollonnawa Urban Council area, due to delays on shifting of utility services and failures of the contractors. Such construction works were expected to be completed by 31 December 2017.
- (b) Construction works of Ambatale and St. Sebastian South Pumping Stations, a canal diversion and flushing gate at Kollonnawa, Bio Diverting Park at Kotte Rampart, Liner Park at Beira Lake, storm water drain at Sounders Place and rehabilitation works of Norris Canal expected to be completed at the end of the year under review at a cost of Rs.14,377 million under the Component of Flood and Drainage Management had not been commenced even as at 31 December 2017, due to the

delays application of procurement system and lack of proper coordination between the Implementation Agencies.

- (c) The construction works of new drop structure and flood gate under the contract on Improvements to Madiwela East Diversion (Stage- I) had not been completed even as at 30 June 2018, even though the respective works scheduled to be completed by November 2017.

3.3 Contract Administration

As a common feature, the weaknesses in contract administration such as inaccuracies of the designs prepared by the Consultants, regular changes of scope of works and designs, preparation of improper estimates etc. had directly influenced for the slow progress on achievement of the objectives of the Project. Details are given below.

- (a) The improvement works under of Madiwella East Diversion Scheme – Stage II, had shown slow progress, due to delays occurred on application of procurement process. Therefore, the improvement works had remained behind the target over 05 months as at 31 December 2017 and the cost of the contract amounting Rs. 100 million initially estimated had been increased upto Rs. 125 million without proper reasons.
- (b) It was observed that several requirements stipulated in the scope of the contract for construction of the Liner Park along Beira Lake- Stage I awarded at a cost of Rs.202 million such as submission of Timber Treatment Certificates for wood works done, preparation of Handbook for the maintenance gardens and furnishing of warranty certificate for bamboo plastic composite and Tensile Fabric etc. had not been fulfilled by the contractor, even though a sum of Rs.16.43 million had been paid thereon.
- (c) According to the specification, the visitors’ seats at the Linear Park at the Baire Lake were required to be made out of the timber called Kumbuk or Teak wood and allocation amounting to Rs. 7.86 million. However, the laboratory tests carried out by an independent party on samples picked by the auditors had proved that the respective visitors’ seats had not complied with the specifications and made out of other variety of timber.
- (d) The physical observations made on the construction of drainage system at Devi Balika Vidyalaya had proved that the precast concrete items, interlock blocks and iron bars used for the construction purposes were not complied with the quality requirement. It was further observed that there was no mechanism adopted for quality assurance purposes and payments amounting to Rs. 52.62 million had been made before laying the pre cast concretes.
- (e) As highlighted in my previous year report, no action had been made to assess the possible flood risks and environmental effects for the construction works of Bio-diversity Park at Beddagana planned with a view to mitigate the flood risk of the area. Further, the Bills of Qualities and Engineer’s Estimates thereon had been

prepared without conducting a proper study and overpayments amounting to Rs.92 million made thereon to the contractor, due to incorrect calculations of quantity of works done had not been recovered.

- (f) The contract for the construction of Crow Island Beach Park at Mattakkuliya had been awarded at an estimated cost of Rs.275 million on 23 September 2014 and expected to be completed by July 2015. However, it was revealed at the site visit that the construction activities were completed only on 31 December 2016, due to failures of contractors. Eventhough a sum of Rs. 183 million had been paid at the end of the year under review, 47 items included in the Bill of Quantities of the contract agreement had not been completed up to 31 December 2017.
- (g) According to the information received, the works under 19 contracts awarded by the Project at an estimated cost of Rs. 5,106 million had been completed as at 31 December 2017 at a cost of Rs.4,404 million and it evidenced that the Project had prepared unrealistic cost estimations thereon.
- (h) The test checks carried out on the work done reports produced by the Local Consultants deployed by the Project had revealed that majority of Consultant were involved in administrative works of the Project instated of involving in construction works of the Project, contrary to the Terms of Reference. The service periods of 03 Consultants had been extended by the Project since August 2017 for further 03 years and awarded 10 per cent of annual salary increment without evaluating their performances.

3.4 Human Resource Management

The following observations are made.

- (a) It was observed that 70 vacancies of key positions of the Project such as Senior Engineers and Technical officers had remained vacant for over a year and this situation had badly influenced for the smooth operations of the Projects activities.
- (b) The Project had deployed 50 officers of the Sri Lanka Land Reclamation and Development Corporation including 18 Engineers to implement activities under the contracts carried out by the Corporation and remuneration aggregating Rs.32.6 million had been paid them from January 2017 to May 2018. In addition 02 Consultants had been recruited and paid a sum of Rs.2.8 million during the year under review. However, the duty lists had not been issued enable to evaluate their performance.

3.5 Extraneous Activities

The following observations are made.

- (a) It was observed that the Project had hired a plot of land of 260 perches at Mattakkuliya to use as a motor vehicle and material yard and a sum of Rs.12.1 million had been spent for the period from August 2017 to July 2018. However, related works under new Mutwal Tunnel at Mattakkuliya had not been commenced even as at 31 July 2018.
- (b) A sum of Rs.4.28 million had been incurred during the year under review for installation of the granite plaques and opening ceremonies, which were not related to achieve the objectives of the Project.
- (c) It was observed that the Project had spent a sum of Rs.5.5 million during the year under review to hire 05 motor vehicles. Eventhough it was required to run 2,000 kilometres per month, an average utilization of a motor vehicle was remained at 549 kilometres per month during the year under review. Further, those vehicles had been assigned to 05 officers contrary to the Circular No. 01/2016 of 24 March 2016 of the Management Services Department.

3.6 Issues on Financial Controls

A Fixed Assets Register had not been prepared as per paragraph 42 of the Project Appraisal Document to record the fixed assets procured by the Project at a cost of Rs.1,940 million as at 31 December 2017.