

Saudi Funded Road Network Improvement Project - 2018

The audit of financial statements of the Saudi Funded Road Network Improvement Project for the year ended 31 December 2018 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 provisions in the Loan Agreement No. 9/574 dated 30 October 2012 entered into between the Democratic Socialist Republic of Sri Lanka and the Saudi Fund for Development. My comments and observations which I consider should be reported to the Parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement, then Ministry of Ports and Highways, presently the Ministry of Highways is the Executing Agency and Road Development Authority is the Implementing Agency of the Project. The objective of the Project is to rehabilitate and improve 131.50 km of 06 road sections in the Central, Eastern, Sabaragamuwa, Western and North Western Provinces. As per the Loan Agreement, the estimated total cost of the Project amounted to US\$ 81.75 million equivalent to Rs.10,628 million and out of that US\$ 60 million equivalent to Rs.7,800 million was agreed to be financed by Saudi Fund for Development. The Project commenced its activities on 03 June 2013 and scheduled to be completed by 05 August 2020.

1.3 Qualified Opinion

In my opinion, except for the effects of the matters described in the Table 2.1 of my report, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2018 and its cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting standards.

1.4 Basis for Opinion

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

1.5 Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Public Sector Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Project ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Program or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Project's financial reporting process.

The Project is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared by the Project.

1.6 Auditor's Responsibilities for the audit of the Financial Statements

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 internal control of the Project.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with those charged with governance regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

2. Comments on Financial Statements

2.1 Accounting Deficiency

Accounting Deficiency -----	Impact -----	Responses of the Management -----	Auditor's Recommendation -----
Nine projects are being conducted under the Miscellaneous Foreign Aided Project and the Project Monitoring Cost of all those projects amounting to Rs. 69.9 million had been shown in the financial statements of the project as at 31 December 2018. It was observed that, the Project had not been used proper basis for the apportionment of expenditure among each project. Hence, the relevant expenditure for this project could not be recognized.	Overstatement of assets and liabilities.	Noted and action will be taken to divide the PMU expenditure among each project from year 2020 onward.	Actual cost incurred for the project and the liabilities arisen need to be accounted.

3. Physical Performance

3.1 Physical progress of the activities of the Project

Component -----	Audit observation -----	Impact -----	Responses of the Management -----	Auditor's Recommendations -----
Rehabilitation and Improvement of Roads	The completion of the project had been delayed, due to all the six roads of it had not been commenced together. Therefore, out of Rs.70 million which incurred as project management cost, Rs.15.5 million had been incurred for the period from January 2016 to 2018 after completion of the first section.	Possibility to increase the cost of the project due to poor planning.	After completion of 6 contract packages there was a loan balance and decided to improve Naula Town section from 53+740km to 58+000km on Kandy – Jaffna Road which is originally included in Naula Dambulla section. Hence PMU was unable to commence all project together.	Action should be taken to speed up the balance rehabilitation of roads works.

3.2 Contract Administration

Audit Issue	Impacts	Responses of the Management	Auditor's Recommendations
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(a). An activity plan should be prepared before implementing a new projects for road rehabilitation. However, such a plan had not been prepared for the rehabilitation and improvement to Kandy-Jaffna road section from 53+740 to 54+990. Further, noted that the contract period is expected to complete on 03 August 2020, but respective periods of loan agreements had been extended only up to 30 January 2020.	Possibility to incomplete whole rehabilitation works of the roads if the loan agreement is not extended.	The said road section (Naula town) was included in original works programme under improvement of Naula – Dambulla Road section when prepare the Procurement plan. Action has been taken to extend loan validity period.	Action should be taken to extend loan validity period.
(b). Eventhough 982 plots of land scheduled to be acquired for the Project, 98 plots of land had only been acquired by paying compensation amounting to Rs. 53 million as at 31 December 2018.	Possibility to increase the interest costs on compensation, due to delays in settlements of claims.	Agreed	Need to take prompt actions to settle the compensation and avoid additional costs thereon.
(c). A sum of Rs 38.7 million had been claimed as an interest by the contractor due to delayed payments by 272 days for the variation order value at Rs.312.9 million of Kandy-Jaffna road section from Alawathugoda to Palapathwela. Further, contractors had submitted IPC delay payment interest claims of Rs. 7.6 million and Rs. 8 million related to Kandy-Jaffna road section of Alawathugoda to Palapathwela and the other section from Palapathwela to Naula respectively.	Possibility to increase the total project cost.	According to the General Conditions of Contract, Contractor is entitle for the delay payments. Interest payments have not been paid due to top management decision and the Contractor disputed the same.	Prompt action should be taken to minimize unnecessary costs.

- (d). Six contract packages at Possibility to Total cost of variation Need to evaluate
 estimated cost of Rs.8,031 million misuse funds orders and EOT claims whether realistic
 for the rehabilitation and due to is Rs. 1194.41 million estimations are
 improvement works were made. unrealistic which is less than 25% made in future.
 However, the total contracts estimations. contingencies allow in
 awarded prices was only Rs.6,955 the estimates. The
 million or lower than 13 per cent varied works while
 of the estimated cost. Thus, doing construction
 unrealistic and over estimations works is unavoidable
 were observed. Further, the due to unforeseen
 project had paid an aggregated situation of ground
 sum of Rs.1,194 million condition and other
 for variations and extension of institutional delays
 time claims, due to poor planning when carryout land
 of the rehabilitation and acquisition.
 improvement works of those
 roads.