

Second Integrated Road Investment Program (i-Road II) - 2019

The audit of financial statements of the Second Integrated Road Investment Program (i-Road II) for the year ended 31 December 2019 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 4.03 of Article IV of the Loan Agreement No. 3579 SRI and Loan Agreement No.3580 SRI(COL) dated 22 November 2017 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank. My comments and observations which I consider should be report to Parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Program

According to the Loan Agreements, then Ministry of Higher Education and Highways, presently the Ministry of Highways is the Executing Agency and the Road Development Authority is the Implementing Agency of the Program. The objective of the Program is to enhance the 3,400 km road accessibility between rural communities and socio economics centres. The long term impact is to increase transport efficiency of 340 km national and provincial roads. The activities of the Program are implemented under 05 components namely civil works, consultancy works, project management unit, utility shifting, taxes, interest and commitment chargers. As per the Loan Agreements, the estimated total cost of the Project amounted to US\$ 1,084.60 million equivalent to Rs. 184,382 million and out of that US\$ 900 million equivalent to Rs. 153,000 million was agreed to be financed by Asian Development Bank. The balance amount of Rs.31,382 million is expected to be financed by the Government of Sri Lanka. The Program commenced its activities on 20 July 2018 and scheduled to be completed by 19 July 2028.

1.3 Opinion

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Program as at 31 December 2019 and of 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 this 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.

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

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 Non-Compliance with Laws, Rules and Regulations

No	Reference to the Rules and Regulations	Non-compliances	Impacts	Responses of the Management	Auditor's Recommendations
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	Sub Clause 4.2 of the General Condition of the Contract	The separate pay items had been made in the Bill of Quantities on road rehabilitation works by allowing contractors to quote the cost of providing performance guarantees. Accordingly, a sum of Rs.85.64 million had been paid additionally to the contractors of Uva Province to reimburse the cost of performance security bonds obtained by the contractors.	Undue advantage for contractors.	If this amount is not provided in the BOQ as a separate item, the Bidder could include the Cost within the other BOQ items. As the Contract was awarded based on Quoted Contract Price (substantially lowest evaluated Contract Price). This amount cannot be considered as a loss. However, Sub Clause 4.2 of General Condition was amended in packages of Eastern, Northern and Western Provinces. Accordingly, pay item in the BOQ was removed.	The review of Bill of Quantities needed to be done by the Procurement Specialist and the Technical Evaluation Committee, before issuing the bidding documents.
	Sub Clause 14.6 of the Particular Condition of Contract	The Engineer shall not be bound to issue an Interim Payment Certificate less than 1.5 per cent of the value of the contract. However, it was observed that 130 instances in Uva Province where evaluation of Interim Payment Certificates below than the required threshold up to 31 December 2019.	Overrunning of cost on evaluation of interim payment.	There was a decision by the Employer to approve payment below the minimum specified (1.5) to improve the cash flow of the Contractor as the provision in the Condition of Contract is not a mandatory. This decision is made based on the fact that not making payment may further affect	It is required to adhere with the thresholds stipulated in the condition of contract in order to minimize the costs, time and undue favours for the

the progress of the works. However, contractors. action has been taken to adhere to the Contractual Clauses except under special circumstances.

3. Physical Performance

3.1 Physical Progress of the activities of the Program

No	Component	Audit Observations	Impacts	Responses of the Management	Auditor's Recommendations
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(a)	Rehabilitation of National Roads	According to the initial plans, the road rehabilitation works of 340 km of national roads and 3,400 km of rural roads in Northern, Eastern, Uva and Western Provinces were expected to be rehabilitated during the period of the Program. However, out of that rehabilitation works, only 1,041.96 km of rural roads in Uva Province, 845.57 km of rural roads in Eastern Province and 1,036.26 km of rural roads in Northern Province had only been awarded as at 31 December 2019. Accordingly, the rehabilitation works of remaining 476.21km of rural roads and none of the national roads had been awarded even up to 31 December 2019.	Possible increase of costs due to delays in commencement of construction works.	As at 15 June 2020, total 3,629.25 Kms of roads have been selected and awarded including 700 Kms roads in the Western Province. Initially 800 of roads were selected in Western Province and during the time of bidding 100 Km were omitted since they had been already rehabilitated under different programs. Additional National Roads will be identified to cover the balance.	Necessary action should be taken to comply with the original plan and complete the rehabilitation works of National Roads along with the rural roads.
(b)	Rehabilitation of Rural Roads	(i) Out of awarded rehabilitation works of 1,041.96 km of rural roads in Uva Province, only 210.1 km had been	Possible increase of costs due to delays in	The Construction works of the Packages of Uva Province commenced on 20 July 2018. Out of awarded	Necessary action should be taken to speed up the

completed as at 31 December 2019. Further it was observed that the construction progress of 07 contract packages in Badulla district and 02 contract packages in Monaragala district were far behind the expected target as at 31 December 2019. As a result of this slow physical progress, the contractors would not be able to complete the construction works before the due date of completion.

- (ii) Out of awarded rehabilitation works of 845.57 km of rural roads in Eastern Province, only 9.8 km had only been completed as at 31 December 2019.

completion of construction works.

Possible increase of costs due to delays in completion of construction works.

of Rehabilitation works in Uva Province, 210.1 Km had been completed as at 31 December 2019 and the completed length is 287.22 Km as at 31 May 2020. Poor Progress is observed in nine Packages.

Construction commenced on 25 September 2019. Before commencing the physical work, there were a lot of preliminary work to be finalized and completed. As such the completion of the volume of the physical works was less at the end of December 2019. Besides, the monsoon seasons started in November 2019 and continued up to end of January 2020. All the Contractors had fully mobilized as planned; however, they were unable to achieve the target progress by the 31December.

construction works and to achieve the objectives within the targeted period.

Necessary action should be taken to speed up the construction works and to achieve the objectives within the targeted period.

3.2 Contract Administration

No	Audit Issues -----	Impacts -----	Responses of the Management -----	Auditor's Recommendations -----
(a)	As per Particular Conditions of Contracts, the ownership of the equipment which was procured under the Bill of Quantities should be transferred to the contractor at the end of the Program. However, an amount of Rs. 98.42 million and Rs.178.95 million for equipment and Lab equipment had been paid as lump sum basis to meet the cost thereon as at 31 December 2019. Further, Rs. 44.23 million had been made as maintenance of lab equipment up to 31 December 2019. It may indicate that, an undue advantage had been given to the contractor as contractor is owning equipment at the end of the Program.	Undue favouration made to the contractor.	When the ownership of the assets reverts to the Contractor at the end of Contract period, the Contractors take into account the residual values of the particular assets and a reduced bid value could be expected. Hence, there was no adverse impact to the Project.	As a general practice, the respective assets are retained by the employer Therefore, the cost of the contract under this program is required to be reduced, compared with the cost of other contract packages awarded by other Donor funded projects
(b)	Loss of Rs.28.7 million had been incurred by Programe as at 31 December 2019 in respect to BA 4 and BA 5 contract packages, due to the rate discrepancies took place among Engineer estimates, bid documents and Bill of quantities by given wrong interpretation of items. The Procurement Committee or Technical Evaluation Committee had not been properly evaluated those documents in line with the Sub Clause 2.4 and 2.6 of the Government Procurement Guidelines.	Probable losses due to weaken contract administration.	The price bids were checked for followings: 1). arithmetic corrections 2). High rate items for unbalanced bid and under estimated work items. 3). Abnormally low bid The TEC evaluated the price bids in accordance with the guidelines as mentioned above. Evaluation guidelines provides a provision to minimize the risk of unbalance bids by increasing the performance security. This was not considered as the item is not an early work item. Evaluated bid price of the contracts BA4 and BA5 were found	Action should be taken promptly by the Program to recover the loss.

reasonable. The SCAPC and the TEC evaluated the bids within the provision of the ADB's evaluation guidelines.

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| <p>(c) Contrary to the Sub Clause 54 of the Contract Agreement for Consultant's Services, Rs.1.19 million had been paid to provide accommodation for the international staff (team leader) through contract package BA06 from September 2018 to December 2019.</p> | <p>Probable losses due to weaken contract administration.</p> | <p>Consultant sought a clarification before the submission of the proposal, regarding long term per diem for international staff. Employer informed all the short listed Consultants that accommodation and transport shall be provided for the Team Leader through the civil work contracts, in reply to their clarification. Accordingly, Consultants had submitted their proposals. Therefore, the payment of Rs.1,199,524 has been paid for the period from September 2018 to December 2019 as per contract.</p> | <p>Action should be taken to amend the Consultancy agreement if all parties agreed to the decision.</p> |
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3.3 Observations made on site visits

No	Audit Issues -----	Impacts -----	Responses of the Management -----	Auditor's Recommendations -----
(a)	According to the Sub clause 103.1 of Particular Conditions of Contracts, the contractor should take necessary measures for the safety of traffic and third parties. Even though an amount of Rs.7,545,000 and Rs.2,050,600 had been made to the contractor for the respective item relating to BA 2 and BA6 packages, it was observed during the site inspection on 25 February 2020 that the above safety measures were not properly followed	Though the cost incurred for the maintain traffic safety of the roads, possible caused to unsafety of General public	Contractor had been paid by obtaining joint inspection Report for the Traffic Safety and Control item. Accordingly, payment is done to the amount of work done monthly. If the contractor has done satisfactory work, full payment is certified and paid. If there are any short comings in safety arrangements at the site, payment is deducted proportionately for the pay items. Time to time the	Necessary action should be taken to maintain traffic safety of the respective roads.

in the site either by contractor or third party. It may be caused to unsafety of General public and project staff. and project staff. Engineer issued non-compliance notice in this regard to get this corrected.

According to Sub Clause 103.2.2 of Particular Specifications of the Conditions of contracts, the contractor should commence the routine maintenance works of roads to maintain the roads in good motorable condition. However, based on the physical inspection carried out on 25 February 2020, it revealed that the above maintenance works had not been carried out by the contractors and Rs.4,685,800, Rs.9,046,383 and Rs.3,162,635 had been paid relating to BA 02, BA 06 and BA 05 contract packages as at 31 December 2019. This situation will cause more inconvenience and lead to accidents to the General Public.

Though the cost incurred for the routine maintain of the roads, possible caused to more inconvenience and lead to accidents to the General Public.

Payments have been made according to the completed length of maintenance works, as per the Engineer's recommendation. Time to time the Engineer issued non-compliance notice in this regard to get this corrected.

Necessary action should be taken to carried out routine maintenance works smoothly.

3.4 Extraneous Payments

Audit Issue -----	Impact -----	Response of the Management -----	Auditor's Recommendation -----
Commitment charges amounting to Rs.206.03 million had been paid uneconomically to the Lending Agency as at 31 December 2019 on undisbursed proceeds of the Loan.	The allocation would not be utilized for intended purpose.	Commitment Charges on unutilized balance are applicable after the effective date of the Loan as per the Loan agreement. As such this is not an uneconomical payment.	Action should be taken to minimize the unnecessary costs.