

Integrated Road Investment Program (i-Road) - 2020

The audit of financial statements of the Integrated Road Investment Program for the year ended 31 December 2020 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. 3171- SRI (SF) for Tranche- 1 dated 05 November 2014, the Loan Agreement No. 3221- SRI and 3222 SRI (SF) for Tranche- 2 dated 28 May 2015 and the Loan Agreement No. 3325- SRI and 3326 SRI (SF) for Tranche- 3 dated 11 December 2015 and Loan Agreement No. 3610- SRI (SF) for Tranche- 4 dated 15 December 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 reported to Parliament appear in this report.

1.2 Implementation, Objectives, Funding and Duration of the Program

According to the Loan Agreements of the Program, then the Ministry of Higher Education & Highways, presently the Ministry of Highways is the Executing Agency and Road Development Authority is the Implementing Agency of the Program. The objective of the Program is to enhance the road accessibility between rural communities and socio economic centers. The long term impact is to increase transport efficiency of national and provincial roads. As per the Loan Agreements, the estimated total cost of the Program was US\$ 906 million equivalent to Rs. 117,780 million and out of that US\$ 800 million equivalent to Rs 104,000 million was agreed to be financed by the Asian Development Bank. The balance amount of Rs.13,780 million is expected to be financed by the Government of Sri Lanka. The financing plan of the program consists of six Tranches under Multi Tranche Financing Facility and out of that 04 separate loan agreements amounted to US\$ 557 million had been with the donor as at 31 December 2020. The Program had commenced its activities on 01 June 2014 and scheduled to be completed by 30 September 2024.

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 Program as at 31 December 2020 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 the 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 scepticism 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 Program.
- 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 Deficiencies

No	Accounting Deficiencies	Amount Rs.	Responses of the Management	Auditor's Recommendations
(a)	Contrary to Paragraph 36 of Sri Lanka Public Sector Accounting Standard No. 05, exchange differences arisen in foreign operations had not been recognized under net assets of the program.	158.33 million	Noted to rectify it when the preparation of succeeding year Program Financial Statement.	Exchange differences arisen in foreign operations should be recognized under net assets of the program.
(b)	Although 544 rural and national roads with the length of 2,231.3 km had been handed over to the Road Development Authority as at 31 December 2020, the cost thereon had not been recognized as assets in line with Sri Lanka Public Sector Accounting Standard 01.	Cannot be ascertained.	The cost of construction of individual roads could be correctly given only after the above taking over process completed.	Assets should be recognised in line with Sri Lanka Public Sector Accounting Standard 01.
(c)	Contrary to Sri Lanka Public Sector Accounting Standard No.08, the provisions had not been made for outstanding payments against 08 interim payment certificates as at 31 December 2020.	58.95 Million	Interim Payment Certificates relating to the period of 2020 have been received and paid in 2021.	Provisions should be made in line with the Sri Lanka Public Sector Accounting Standard No.08.
(d)	Eventhough rehabilitation works of 07 packages had been entirely completed, the provision had not been made for the Performance Based Maintenance in the financial statements as at 31 December 2020.	Cannot be ascertained.	It is noted to make provision for the Performance Based Maintenance in the Financial Statements from the year 2021.	Provisions should be made in line with the Sri Lanka Public Sector Accounting Standard No.08.

2.2 Unreconciled Balances

Value as per Financial Statements Rs.	Value as per corresponding records Rs.	Differences Rs.	Response of the Management	Auditor's Recommendation
Rs.5,806.1 million	As per General Treasury Rs.7,132.43 million As per External Resources Department Rs.6,698.44 million	1,326.33 million 892.34 Million	The reconciliations will be submitted to the audit, from the year 2021 onward.	Need to discuss with relevant parties and should minimize the differences.

2.3 Non-compliance with Rules and Regulations

No	Reference to the Rules and Regulations	Non-compliances	Responses of the Management	Auditor's Recommendations
(a)	Sub clause 14.6 of the Particular Condition of Contract.	The minimum amount of Interim Payment Certificate to be submitted by the contractor was 1.5 per cent of the accepted contract value. However, 67 instances were observed where evaluation of Interim Payment Certificates under 20 packages below than the required threshold.	The reasons such as Covid-19, adverse weather, material shortages etc. may result in causing additional cost to the contractors. If we adhere to original conditions the contractors' cash flow will be affected, and they will not be able to achieve even lower progress.	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 contractors.
(b)	Sub clause 4.2 of the General Condition of the Contract.	Although the Performance Securities should be provided by the contactors at their own cost, it was observed that a separate pay item had been made in the Bill of Quantities under Preliminary and General Items to be able to claim to the contractors. Accordingly, a sum of	If this amount is not provided in the BOQ as a separate item, the bidders could include that cost in the overhead of the other BOQ items. However, General Condition was amended and that pay item in the BOQ was removed in packages of Eastern, Northern and Western Provinces.	The review of Bill of Quantities needed to be done by the Procurement Specialist and the Technical Evaluation Committee, before issuing the bidding documents.

Rs.564.45 million had been paid additionally to the contractors to reimburse the cost of performance security bonds obtained by the contractors. Further, actions had not been taken to recover that amount from the contractors even up to 31 December 2020.

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| (c) | Sub Clause 15.3 of General Conditions of Contracts. | It had not been prepared the value at termination for KU4, KU5, PU2, PU3, R2 and G1 contract packages even up to 31 December 2020. | Valuation of Termination and Employer's claims have been prepared and forwarded pertaining to the Contract Packages PU2, PU3, KU3, KU4 & KU5. | Value at termination should be prepared at the right time. |
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3. Physical Performance

3.1 Physical Progress of the Activities of the Project

No	Component	Audit Issues	Responses of the Management	Auditor's Recommendations
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(a)	Awarding of road rehabilitation works of National and Rural Roads	Although the road rehabilitation works of 218.19 km of National Roads and 3,106.10 km of rural roads were expected to be rehabilitated during the period of the Program according to the initial plan, only 104.13 km of National Roads had been awarded as at 31 December 2020.	The Program has to decide on priorities of awarding Contracts, depending on budget allocation received during each year. Accordingly, the Project decided to change initial plan and delay awarding National Roads due to change of priorities.	Necessary actions should be taken to comply with the initial plan of the program and achieve the target with the period.
(b)	Completion of rehabilitation works of National and Rural roads.	The rehabilitation works of 2,203.87 km of rural roads had been completed and handed over to the Road Development Authority	The 12 Contracts had to be terminated due to poor performance and suspension of work by the Contractors as spelt in the Conditions of Contract.	All effort should be taken to achieve intended targets of the program.

as at 31 December 2020. Further, 1,000.43 km length of rural roads relevant to 12 contract packages had been abandoned as at 31 December 2020.

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| (c) | Completion of rehabilitation works of National and Rural roads. | Even though out of 12 abandoned contract packages, 03 contract packages had been terminated in the year 2019, no action had been taken to continue the balance works even by 31 December 2020. | Actions have been taken to re-bidding of 03 contract packages terminated in 2020. | All effort should be taken to achieve intended targets of the program. |
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3.2 Contract Administration

No	Audit Issues	Responses of the Management	Auditor's Recommendations
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(a)	Out of 12 abandoned contract packages, balance works of 05 contract packages had been re awarded to carrying out through this project during the year under review and the value of the re awarded contracts had been increased by Rs.5,007 million when compared with the original contract price.	Agreed that the termination and re-awarding of the 12 Contracts has additional cost to the Government. The Contracts were terminated due to poor performance by the Contractors.	Necessary actions should be taken to complete the construction without further delay.
(b)	A settlement agreement had been signed to complete the balance works of 04 abandoned contracts with the same failed contractor through the 100,000 km Rural Road Development Program during the year under review and the value of such contracts had been increased by Rs.580.14 million when compared with the original contract price.	Possible additional cost of price fluctuations and procurement process, Court injunction orders taken by the contractor to prevent from enforcing termination, awarding the balance work to another Contractor and encashment of bonds and guarantees, causing severe inconvenience to the public had been considered when awarding those contracts to the same contractor.	Necessary actions should be taken to complete the construction without further delay and additional costs.

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| (c) | The action had not been taken by the program to encash the performance bonds with the value of Rs.2,668.47 million relevant to 12 abandoned contract packages even by the end of the year under review. | The Contractors has taken Court Orders to prevent encashing Guarantee & bonds and litigation is in progress. Therefore, recovering of the amounts and claims on termination can only be finalized only after completion of litigation. | Action should be taken promptly by the Program to recover the outstanding balances. |
| (d) | Even though the lending agency had instructed to recover mobilization advance and refund to the lending agency related to the terminated contracts, the project had failed to recover the outstanding mobilization advances amount of Rs.1,830 million related to 8 terminated contract packages. Accordingly, the total unrecovered mobilization advances as at 31 December 2020 was Rs.2,793 million relevant to 12 packages including 04 abandoned packages. | The Contractors has taken Court Orders to prevent encashing Guarantee & bonds and litigation is in progress. Therefore, recovering of the amounts and claims on termination can only be finalized only after completion of litigation. | Action should be taken promptly by the Program to recover the outstanding balances. |
| (e) | Though the MA 03 and NE 03 contract packages had been completed in December 2018 and February 2020, Statement at Completion (SAC) had not been finalized even as at 31 December 2020. Further, performance based maintenances should be conducted by the contractor had not been revealed to the audit. | Statements at Completion (SAC) of the contract package MA03 and NE03 have been finalized in 2021. | Statements at Completion need to be prepared without delay. |
| (f) | Eventhough, G1 contract package had been terminated on 12 February 2019, the cost to completion had not been evaluated even up to 31 December 2020. | Cost to Completion of the G1 Contract package has been evaluated in 2021. | Cost to Completion need to be prepared without delay. |

- (g) Rs. 158.2 million had been incurred up to 31 December 2020 by the other two active contractors for the completion of the emergency works and to get the roads up to motorable condition related to abandoned 05 contract packages in North Western province in the year 2019.
- Variation Orders were issued for completion of immediately required balance works attending emergency safe works and making road sections motorable.
- Necessary action should be taken to recover the additional expenditure incurred from the respective contractors.

3.3 Observations made on site visits

No	Audit Issues	Response of the Managements	Auditor's Recommendations
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(a)	KL2 and KL3 contract packages in Kalutara District were only completed 35.15 per cent and 51.83 per cent and those had been abandoned in the year 2019. Further, without construction of shoulders and other structures it had only been asphalted several intervals of the roads and Rs. 772.84 million and Rs.747.47 million had been paid for those two packages respectively.	Those contracts had been terminated due to poor performance and suspension of work by the Contractor and re-bidding process is being followed at present. Further, the Contractor of this Contract has taken injunction order from the Courts.	Necessary actions should be taken to complete the task without further delay.
(b)	Even though prevailed culvert located at the chainage 3+700 of the Akkara 500 to Sagara Palansooriya road (ID 30) had been demolished for construction of a new culvert, it had not been even started up to the inspection date of 10 March 2021 due to abandonment of KL 03 contract package. It was observed that, users of the road had been faced inconvenience and had to accommodate a temporary solution by using a private land beside the road to link the road.	Those contracts had been terminated due to poor performance and suspension of work by the Contractor and re-bidding process is being followed at present. Further, the Contractor of this Contract has taken injunction order from the Courts.	Necessary actions should be taken to complete the task without further delay.
(c)	It was observed that rehabilitation of some roads were abandoned only after laying the ABC layer.	Those contracts had been terminated due to poor performance and suspension of work by the Contractor and re-bidding process is being followed at present. Further, the Contractor of this Contract has taken injunction order from the Courts.	Necessary actions should be taken to complete the task without further delay.

3.4 Extraneous Payments

Audit Issue	Response of the Management	Auditor's Recommendation
----- Commitment charges amounting to Rs.290.81 million had been paid uneconomically to the Lending Agency on undisbursed proceeds of the loan during the year under review and accumulated commitment charges were Rs.1,471.26 million as at 31 December 2020.	----- Payments of Commitment Charges are unavoidable, even though it is an uneconomical payment. But it can be minimized by achieving disbursement targets.	----- Action should be taken to minimize the unnecessary costs.