

Southern Road Connectivity Project - 2021

The audit of financial statements of the Southern Road Connectivity Project for the year ended 31 December 2021 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 Article II Section 2.09 of the Loan Agreement No.3027- SRI dated 27 May 2014 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 Project

According to the Loan Agreement of the Project, the 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 improve National transport efficiency by upgrading and rehabilitating 33 km of the roads linked to the Southern Highway. As per the Loan Agreement, the estimated total cost of the Project amounted to US\$ 95 million equivalent to Rs.12,248 million and out of that US\$ 70 million equivalent to Rs.9,025 million was agreed to be financed by the Asian Development Bank. The balance amount of US\$ 25 million equivalent to Rs.3,223 million agreed to be finance by the GOSL. The Project commenced its activities on 27 May 2014 and scheduled to be completed by 30 December 2018. However, the date of completion of the activities of the Project had been extended up to 31 December 2021.

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 2021 and its cash flows for the year then ended in accordance with Sri Lanka Public Sector Accounting Standards.

1.4 Basis for Qualified 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.

Those charged with governance are responsible for overseeing the Project'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 the 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 Deficiencies

| Accounting Deficiency / Audit Issue | Amount Rs. million | Management Response | Recommendation |
|--|-----------------------|--|---|
| The provision had not been made for the interest payable amounting to Rs. 68 million (approximately) for the delay in settlement of statutory compensation of Rs. 205 million to the land owners as at 31 December 2021. | 68 | Disclosed under the note to the financial statement. | Need to identify and record interest of Rs.68 million relating to the compensation payable of Rs.205 million shown in the financial statement as at 31 December 2021. |

2.2 Non Compliance with Laws, Rules and Regulations

| No | Reference to the Laws Rules and Regulations | Non Compliance/Audit Issue | Management Response | Auditor's Recommendation |
|-----|---|--|--|--|
| (a) | Section 8.13.4 of the Government Procurement Guidelines 2006. | The total cost of Contract Package-02 was Rs. 3,064 million and Rs. 510 million or 20 per cent by the total contract value had been provided for contingency provision. According to the Section of the Government Procurement Guide 2006, the necessary approval should be taken to exceed the contract value, however Rs 1,573 or 51 per cent from the total contract value had been incurred without such approval. | Relevant recommendation of the TEC, PPC approval and ADB concurrence has been obtained by the PMU. | The variation should be approved by the appropriate PC assisted by the appropriate TEC as per the revised total cost estimate. |

3. Physical Performance

3.1 Physical Progress of the Activities of the Project

| Component | As at 31 December 2021 | | Audit Issue | Reasons for delays |
|---------------------|-------------------------------|----------------------|---|-------------------------------|
| | Expected physical performance | Performance achieved | | |
| | percentage | percentage | | |
| Contract Package-05 | Original program- 100 | 59 | Actual progress of the Project activities was behind the targeted progress. | COVID -19 pandemic situations |
| | Revised program- 84 | 78 | | |

Response of the Management

Delay of physical progress of CP -05 contract package is mainly due to COVID 19 pandemic other than the delay in land acquisition, delay in utility shifting and the scope change.

Auditor's Recommendations

Action should be taken to expedite the completion of road rehabilitation activities on the targeted days to avoid additional costs due to delays and to avoid inconvenience to the general public.

3.2 Contract Administration

| No | Audit Issue | Response of the Management | Auditor's Recommendations |
|-----|---|---|---|
| (a) | The Construction work of Packages 1, 2 and 4 of the 05 Contract Packages for the reconstruction of 40.2 km of National Highways in the Colombo and Kalutara Districts was completed after a considerable delay. Accordingly, the delay charges of Rs. 31.95 million had been charged from Contract Package 1 on 19 June 2017 and released to the Contractor on 10 October 2019. In addition, a delay charges of Rs. 14.18 million levied on Package 4 had been shown in the Financial Statement as a liability to be released to the Contractor in future as at 31 December 2021. | Agreed. Contract Packages 01, 02, 04 and 05 Completed with delay of the above contract packages are mainly due to delay in land acquisition, delay in utility shifting and the scope change. The contractor was not in a position to control situations like these and therefore reasonable EOT had to be granted. Delay charges amounting to Rs. 14.18 million had been deducted from the contractor of package 4 recorded as a liability until the EOT is approved. | Action need to be taken to complete the road rehabilitation activities on targeted dates. |

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|-----|--|---|--|
| (b) | According to the information, a sum of Rs.248.6 million related to the final payment submitted by the contractor on 24 June 2019 under interim payment certificate No 29 had not been settled by the lending agency due exceeding the total contract cost over original contract amount. Therefore, this amount had been remained as outstanding liability about 2 ½ years even as at 31 December 2021. As a result, the contractor had claimed of Rs.46.9 million as interest for the delayed period and thereby total unsettled balance had been increased to Rs.310.6 million as at 31 December 2021. | Agreed. When the constructions are in progress, some practical requirements leads to scope change raised. So, the contract amount has to be revised in this regard. With the mutual understanding with the contractor, the above requirements have to be fulfilled before the contract period expired, subject to the revision of contract sum. | Need to settle the contractor liability without delay as per contract agreement to eliminate the interest cost. |
| (c) | GOSL allocation of Rs.200.21million representing 95 per cent of the total under Capital expenditure Vote No.117-2-4-43-2506-17 of the Project and allocation of Rs.286 million representing 14 per cent of the total relating to foreign loan had not been utilized during the year under review due to slow progress works of the Project. | Agreed. Extra allocation amounting to Rs. 200 million has been approved to settle the contract bill for vote no 2-4-43-2056-17. But, it was not processed, due to time limitations. Underutilization of foreign vote allocation (14%) has been recorded due to slow progress of the project with effect of COVID 19 pandemic in 2021. | The constructions works of the Project should be properly executed to utilize total loan before expiration of the loan facilities. |

3.3 Issues relating to the Land Acquisition

Audit Issue

According to the information made available, it was scheduled to acquire 8,499 plots of land including 1,562 plots of land owned to the Government and out of that compensation amounting to Rs.8,418 million had been paid under the section 17 of the Land Acquisition act. Further, the additional payments amounting Rs.3,210 million had been made thereon under the decision of the Land Acquisition and Resettlement committees. In addition, a sum of Rs.649 million had been paid as interest on delays in settlement of compensation up to 31 December 2021. However, no any plot of land had been registered under section 44 of the Acquisition act as at 31 December 2021.

Response of the Management

Agreed. Payment for land compensation process is in progress for the remaining plots of lands based on the availability of fund. Interest payment has been done end of 2021 and due interest payment for the acquired lands has to be fully settled before register under Sec 44 of Land Acquisition Act.

Auditor's Recommendations

Action need to be taken to accelerate the compensation payment and transfer the ownership of lands to the RDA.