

Strategic Cities Development Project - 2021

The audit of financial statements of the Strategic Cities Development 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 Section II (B) (3) of the Financing Agreement No.5428-LK dated 12 September 2014 and Additional Financing Agreement No. 5800 – LK dated 20 July 2016 entered into between the Democratic Socialist Republic of Sri Lanka and the International Development Association. 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 Financing Agreement, then Ministry of Megapolis and Western Development, presently the Ministry of Urban Development and Housing is the Executing Agency and the Urban Development Authority is the Implementing Agency of the Project. The objective of the Project is to improve selected urban services and public urban spaces in the Participatory City Regions of Sri Lanka. The activities of the Project are implemented under four components namely Kandy City Region Urban Intervention, Galle City Region Urban Intervention, Jaffna City Region Urban Intervention and Project Management. As per the Financing Agreement, the estimated total cost of the Project was US\$ 257.08 million equivalents to Rs. 34,912.48 million and out of that US\$ 202 million equivalents to Rs. 27,507 million was agreed to be financed by International Development Association. The balance amount of Rs. 7,405.48 million is expected to be financed by the Government of Sri Lanka. The Project had commenced its activities on 05 May 2014 and scheduled to be completed by 31 December 2019. 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 02 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 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 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 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	Amount Rs. million	Response of the Management	Auditor's Recommendation
Parity adjustment made by the General Treasury during the period of the project had not been brought to the financial statements up to 31 December 2021.	2,650.53	Our adjustment are done with \$ accounts and project rupee account and not with the Treasury.	Corrected value should be shown in the financial statements.

2.2 Non-Compliance with Laws, Rules and Regulations

No	Reference to the Laws Rules and Regulations	Non-Compliance	Management Responses	Auditor's Recommendations
(a)	Financial Regulation of the Democratic Socialist Republic of Sri Lanka			
	(i) FR 757 and 760	The action had not been taken relating to shortage of 97 items belonging to 17 categories as shown in the Board of Survey report conduct for the year under review.	Agreed with observation but prevailed situation in the country was the reason for delay.	Corrective actions should be taken with regard to the shortages and losses observed in the Board of Survey.
	(ii) FR 770	Any action had not been taken relating to 33 disposed items belong to 14 categories as shown in the Board of Survey conducted for the year under review.	Agreed with observation and now this has been addressed.	Government Regulations should be followed.
(b)	Paragraph 9.3 of Management Services Circular No.1/2019 dated 15 March 2019	Project Steering Committee Meetings had not been held for the year under review as required by the Circular.	Prevailed situation in the country was the reason for this.	Circular instruction should be followed by the Project.
(c)	Procurement Guidelines			
	(i) Reference 2.8.4	The technical evaluation committee should be represented by a subject expert with a finance related background. As a result, the progress of the project was very slow, due to the lack of financial capacity of the contractor for the construction of warehouses and related facilities of the Galle Municipality.	Agreed. This has been brought to the top management to prevent such situations in the future.	Government Procurement Guideline should be followed by the Project.

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| (ii) Reference 1.2.1 and 2.4 | The Project had been terminated, due to the failure to fulfil the duty properly by the Technical Evaluation Committee and the Procurement Committee in selecting contractor for rehabilitation of Moraga Ela Main Canal and Temple by Pass in Gall. | Agreed | Government Procurement Guideline should be followed by the Project. |
| (iii) Reference 7.9.2 (j) | Two separate Technical Evaluation Committee reports have been prepared by the same Technical Evaluation Committee for same contract within 25 days period recommending two separate contactors based on two (original and revised) Engineers Estimate. After revision of the Engineer estimate in the mid of this bid evaluation process, even indicating the un-realisticness of the items, the same Technical Evaluation Committee recommended the previous unsuccessful contractor at same rates. | Agreed the observation but action has been taken with approved committee approvals. | Government Procurement Guideline should be followed by the Project. |
| (iv) Reference 3.9.1 | Software Development Platform – Development of an information technology platform for the bus operation management and transitional bus operation up to 31 December 2021.
a) Instead of calling for quotations for the value of Rs.18.7 million for painting the front side (Face) of 1,500 buses in terms agreements, the contract of pasting stickers fully on 02 buses and pasting stickers partially on 135 buses at the contract value of Rs.5 million, awardable to a one community based organizations | Agreed. | The answers of the Central Province Transport Service Authority regarding the non-compliances with the agreement should be obtained and submitted to the audit. |

in terms of circulars, had been awarded without evaluating other qualified community based societies.

- (d) The Public Finance Circular No.01/2021 of 29 September 2021 of the Secretary to the Treasury
 - i) Section 2.1

When awarding direct contracts to Community Based Organizations, an eligible Community Based Organization should be selected after verifying the qualifications by a three-member committee consisting of two representatives nominated by the Head of the Department and the Divisional Secretary of the area. The relevant contractual rural development society had not been selected by such committee.

Procurement of contract was done with the approvals of world bank and relevant procurement committees.

The answers of the Central Province Transport Service Authority regarding the non-compliances with the agreement should be obtained and submitted to the audit.

Section 2.7

In terms of the above Circular, the Head of the Department, the relevant District Secretary or the Divisional Secretary should ensure that, the contract works of these Community Based Organizations are carried out according to the proper standards and necessary technical supervision is undertaken during the entire period of the project implementation. However, it had not been done accordingly.

As per the memorandums operating procedure has been outlined.

The answers of the Central Province Transport Service Authority regarding the non-compliances with the agreement should be obtained and submitted to the audit.

3. Physical Performance

3.1 Physical Progress of the Activities of the Project

No	Component	As at 31 December 2021		Delay/Audit Issue	Response of the Management	Auditor's Recommendations
		Expected physical performance percentage	Performance achieved Percentage			
(a)	Flood Control System in the City of Galle	100%	Zero	The construction works of 16 flood control drainage systems in the city of Galle had not been commence and required lands for the works had not been acquired as per the plans. Thus, it was observed that situation had been directly affected to performance of the project and to the flood controlling activities.	Agreed. This has been brought to the notice of Ministry and expects to address the situation.	Sound and effective project management system should be implemented in order to achieve the project objectives through completion of project activities according to the scheduled project time period.
(b)	Rehabilitation of Moragoda Ela Main Canal & Temple Bypass in Galle	100%	20%	The contract had been awarded at a cost Rs. 844.9 million on 06 March 2017 and scheduled to be 07 September 2019. Initial construction contract was completed total length of 4,250 m. However, the contract had been terminated on 11 April 2019, due to poor physical progress of 20% reported as at date. Further, contractor had violated environmental and social safeguards provisions.	Agreed.	-Do-

(c)	Rectification works contract for Rehabilitation of Moragoda Ela Main Canal & Temple Bypass in Galle (0+000 to 1 + 850)	100%	72%	<p>(i)The total contract price of the 4,250 meter long Moragoda Canal was Rs. 736.03 million and the rectification of only 1,850 meters was given to a new contractor for Rs.462.6 million. Accordingly, due to the incomplete length of the canal, the public will not be able to reap its full benefits. However, the land acquisition for the entire length of the main canal had been completed and Rs. 397.6 million had been paid.</p> <p>(ii)Moragoda Ela main Cannel Rehabilitation work in some area was not able carry out, due to the lack of sufficient land spaces to operate the construction machines. As contractor could not carry out cost of Rs.112 million pre-cast piling work. Acquisition of lands without being conducted a proper evaluation was the main reason for above situation, the project had to re- awarded for pre-cast piling works.</p>	Agreed	-Do-
(d)	Construction of Warehouse and Related Facilities at Galle Municipal Council	100%	90%	<p>This contract was awarded on 24 April 2019 at a cost of Rs.135.65 million and construction period was 270 days. However, extension of time (EOT 3) 113 days recommended by the project and also several time requested from the contractor to submit realistic programme had not been submitted. Hence, contract had been terminated with affected from 23 May 2022.</p>	Agreed.	-Do-

(e)	Rehabilitation and Improvements to Jaffna Ponnalai Point Pedro Road (AB 21) From Chainage 1+830 km to 14+600 km	100%	76%	The construction had been awarded at a cost of Rs. 1,110.15 million on 12 August 2019 and expected to be completed by 15 May 2021. Lack of timely supervision by the consultant was directly affected for the delays. Eventhough Extension of Time had also been granted, they could not complete full length of (km) the road.	Agreed	-Do-
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3.2 Contract Administration

No	Audit Issues	Management Responses	Auditor's Recommendations
(a)	The contract of rehabilitation and improvement of 3.39 km of Dharmashoka Mawatha, Kandy had been awarded for Rs.796.42 million on 07 July 2016 and expected to be completed on 07 July 2018. Subsequently, the contract had been abandoned halfway on 14 June 2019 and a sum of Rs. 405 million had been paid for construction works completed until then. Further, balance works had been awarded for 2 contractors at a cost of Rs.512 million. As a result, an additional amount of Rs. 121.5 million had to be incurred by the Project, due to abandonment of the contract halfway.	Agreed	After being evaluated the current progress, corrective action should be taken to expedite the remaining contract work.
(b)	Out of the loan of US\$ 202 million agreed to be granted by the World Bank, a total amount of US\$ 92 million comprising US\$ 65 million allocated to construction of the Kandy Multimodal Transport Terminal (KMTT) and US\$ 27 million as expected savings as at 31 December 2021 had been cancelled, due to failure in reaching the targets expected by the Project as at the end of the year under review. As such, it was revealed in audit that benefits expected by the Project could not be reached.	Agreed	Sound and effective contract management system should be implemented in order to achieve the project objective through completing project activities according to the entire physical plans of the project.

3.3 Utilization of Funds

No	Audit Issues	Management Responses	Auditor's Recommendations
(a)	According to the information received, out of total funds of Rs.30,300 million equivalent to US\$ 202 million provided by the Lending Agency, a sum of Rs.14,567.64 million equivalent to US\$ 72.14 million representing 65.6 per cent had only been utilized after lapse of 7 ½ years from the date of the commencement of the project.	Agreed. Prevailed situations have resulted in lower utilization of original funds.	Action should be taken to monitor the Action Plans and budget as a Project's performance controlling and fund management instruments.
(b)	A sum of Rs. 925 million provided to the Strategic Cities Development Project – Kandy, Galle under the object code 12-02-07-08-2506 (17) by the Ministry of Urban Development and Housing had been transferred to the Project – Jaffna. However, the said entire amount had been saved without utilizing for the relevant purpose.	Disagree. Major part of this utilized subsequently from Jaffna vote.	A control system should be implemented to limit the fund transfers among other projects.
(c)	A sum of Rs.1,300 million provided to the Strategic Cities Development Project – Kandy, Galle under the object code 123-02-07-08-2506(12) by the Ministry of Urban Development and Housing had been transferred to the Strategic Cities Development Project – Jaffna. However, 51 per cent of the said amount had been saved without utilizing for the relevant purpose.	This has not affected the project work and changes were made from different votes due to change in funding source.	A control system should be implemented to limit the fund transfers among other projects.

3.4 Idle/ Unutilized/ Underutilized Resources

Audit Issue	Management Response	Auditor's Recommendation
Only 08 laptops out of 16 laptops received for the project operation center related to the software development platform to develop an information technology platform for bus operation management have been used. The remaining 08 computers worth Rs. 1.2 million had not been used.	This was an on-going project and assets will be utilized in future	Project cost should be incurred according to the principal of economic efficiency.

3.5 Issues related to the Environmental Matters

No	Audit Issues	Management Responses	Auditor's Recommendations
(a)	Pasaiyoor Pocket Parks in Jaffna City Planning Phase - 02		
	<p>i) The site was selected without conducting a feasibility study to develop the park. As a result, the livelihood of the villagers who were traditionally engaged in fishing activities had been severely affected and it was observed that there is no suitable environment for tourists and beneficiaries to spend their leisure time in the park.</p>	<p>It was proposed as a Neighbourhood park.</p>	<p>Sound Environmental Management System should be introduced.</p>
	<p>ii) A fence was not fixed for the safety of the users of this park and no system has been prepared for waste disposal. Therefore, waste was scattered around the lagoon. It was observed that the surrounding coastal ecosystem is being damaged through this.</p>	<p>Safety hand rails and little bins were fixed and handed over the asset now.</p>	<p>Sound Environmental Management System should be introduced.</p>