

Support to Colombo Urban Regeneration Project (SCURP) - 2022

The audit of financial statements of the Support to Colombo Urban Regeneration Project for the year ended 31 December 2022 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 3.4.3 of the Loan Agreement No. L 0081 A dated 25 April 2019 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Infrastructure Investment Bank (AIIB). 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, the Ministry of Urban Development and Housing is the Executing Agency and the Urban Development Authority is the Implementing Agency of the Project. The objectives of the Project are to improve housing condition of low - income communities and increase land use efficiency in Colombo through investment in the construction of affordable housing and redevelopment of land, with associated policy and system enhancements.

As per the Loan Agreement, the estimated total cost of the Project was US\$ 287 million equivalent to Rs 50,460 million and out of that US\$ 200 million equivalent to Rs.35,163.7 million was agreed to be financed by the Asian Infrastructure Investment Bank (AIIB). The balance amount of Rs 14,417.2 million is expected to be financed by the Government of Sri Lanka. Further, balance amount of US\$ 5 million equivalent to Rs. 879.1 million agreed to finance by the Private Partner.

The Project had commenced its activities on 22 July 2019 and scheduled to be completed by 30 June 2025. Further according to the revised loan agreement dated 01 July 2022, the Asian Infrastructure Investment Bank (AIIB) had changed the scope of original activities due to releasing the allocation of funds amounting to US\$ 70 million to the emergency health component.

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 2022 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 section of 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 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 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

No	Accounting Deficiency / Audit Issue	Amount Rs. million	Response of the Management	Auditor’s Recommendations
(a)	The work done value of Stadiumgama and Colombage Mawatha Projects up to 31 December 2022 had not been recorded as accrued basis. As a result of that the value of work done and payables to the contractors had been understated by that amount.	1,166.13	We will be following this from the year 2023.	Correct value should be accounted in the financial statement.

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| (a) | Advance payment of material at site had been accounted as working progress instead of been shown as current assets. As a result, working progress amount in the financial statement had been overstated by that amount. | 249.41 | We will be showing material at site under current assets from the year 2023. | Correct value should be accounted in the financial statement. |
| (b) | As per the Section 39(a) of Sri Lanka Accounting Standard 21, Parity adjustments relating to the foreign loan of the project had not been accounted in the financial statements as at 31 December 2022. | 301.36 | We have not been provided the Island accounts or breakup of it for reconciliation. | Action should be taken to reconcile the Parity adjustments. |

2.2 Non-Compliance with Laws, Rules and Regulations

No	Reference to the Laws Rules and Regulations	Non-Compliance/Audit Issue	Response of the Management	Auditor's Recommendations
(a)	Procurement Guidelines 2.3.1.(a) and (b) of 2006	The entity should satisfy with the initial environmental assessment, environmental impact assessment, social impact assessment and all other pre-procurement preparations related to the project and land acquisition and issues of compensation and resettlement including relocation of utilities and all other matters necessary for smooth implementation of the project have been fulfilled. However, it was observed that the project had started construction works contrary to the above Guide Line.	Preliminary Planning Clearance (PPC) for all six projects had been obtained from Urban Development Authority prior to commencing of the development works.	Procurement Guidelines should be followed.
(a)	Schedule 02-D of the Loan Agreement.	Environmental and social management framework and a policy framework had not been prepared and implemented until the date of audit on 30 March 2023. Furthermore, a resettlement action plan should be prepared and forwarded to the bank immediately, however action plan had not been prepared over 3 ½ years.	The Environmental and Social Management Framework (ESMP) and Resettlement Planning Framework (RPF) had been developed and submitted to AIIB to obtain approval.	Conditions of the Loan Agreement should be followed.

3. Physical Performance

3.1 Physical progress of the activities of the Project

Component	Activity	As at 31 December 2022		Delay/ Audit Issue	Reasons for delays	Response of the Management	Auditor's Recommendations
		Expected physical performance percentage	Performance achieved percentage				
(a)	Colombage Mawatha	74.28	52.26	The contract had been awarded to Maga Engineering Company at an estimated value of Rs.3595.56 million to construct 624 housing units on 01 June 2020. The project had planned to be spent Rs.1793.08 million as at 31 December 2022 and Rs.1902.03 million had been spent thereon. However, the project could not be completed the scheduled date of 24 August 2023.	Due to Covid 19 pandemic and economic crises and power cut.	Physical progress of the project was affected badly due to globally affected Corona 19 Pandemic and health guidelines issued by the health authority.	Construction works should be closely monitored in order to complete within the time frame.
(b)	Obesekarapu ra	Terminated on 29 March 2022		The Construction had been awarded to Subhasinghe Construction Company at an estimated value of Rs.1,981.85 million for the construction of 300 housing units, and the Construction work had been started on 5 May 2020 and expected to be completed on 21	Due to termination before completion the project.	Technical Evaluation Committee (TEC) was appointed to assist SCAPC for retendering and initial draft tender document has been completed and to be forwarded to AIIB for their comments.	Construction works should be closely monitored in order to complete within the time frame.

October 2022. However this project was terminated on 29 March 2022 due to poor performance and at that time only 14 percent had been achieved and Rs.300 million had been spent for that. However, the project and line ministry had not taken action to reward the construction works of Obeysekarapura housing Project even after laps of one year.

Therefore, retendering process is in progress.

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It was proposed to build 700 housing units through this housing project, and contract had been awarded to China Railway Group (China Railway 25th Corporation LTD) at an estimated value of Rs. 4473 million. Construction work had started on 27 October 2020 and expected to be completed on 17 October 2023.

In addition, the Ministry had not taken any action in connection with the incurred loss of Rs.10.9 million due to ignoring the cash discount of Rs.43.3 million offered by a bidder during the bid evaluation in the year 2020.

Covid 19 pandemic and economic crises and power cut. Heavily affected by Corona 19 pandemic outbreak and economic crisis experienced during the past couple of years lead to date of completion of the project. Hence extension of time (EOT) may be envisaged. Corrective actions should be taken to expedite the remaining works.

(d)	Ferguson Road	76.61	6.88	Construction had been awarded to China Civil Engineering Corporation & China Railways 25, as at estimated value of Rs.4,511 million for constructing 750 houses. The contract commenced on 20 January 2021 and scheduled to be completed on 04 January 2024.	Covid 19 pandemic and economic crises and power cut.	Physical performance of the project was heavily affected by Corona 19 pandemic outbreak and economic crisis. Hence extension of time (EOT) may be envisaged.	Corrective actions should be taken to expedite the remaining works.
(e)	Madampitiya	32.76	14.89	Construction had been awarded to Thudawa Brothers Private Company at an estimated value of Rs. 4529.26 million for the construction of 700 housing units and contract started on 24 May 2020 and expected to be completed on 03 May 2024. Labour supervision and poor contractor supervision mainly affect to the poor progress of the contract.	Covid 19 pandemic and economic crises and power cut.	Physical performance of the project was heavily affected by Corona 19 pandemic outbreak and economic crisis. Hence extension of time (EOT) may be envisaged.	Corrective actions should be taken to expedite the remaining works.

3.2 Funds Utilization

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	Due to inefficiency fund utilization by the project, the cabinet had decided to reduce the loan amount by US\$ 70 million. As a result, project activities of phase 3 had been suspended and number of housing beneficiaries had been reduced by 1,272.	It has been decided to redirect USD100 million (USD70 Mn from SCURP and USD30 Mn from RLVMMMP) from the aforesaid two projects to procure essential pharmaceuticals and medical supplies.	Efficient fund management system needs to be implemented.
(b)	According to the original cost estimate GOSL contribution was US\$ 42 million. However it had been reduced by US\$ 14 million up to US\$ 28 million. Further, the private partner contribution for land redevelopment had been removed totally according to the revised agreement.	This is according to the Restructured loan agreement dated 1 July 2022 sent by ERD	Effective action should be taken to find the project financing sources.
(c)	The project had paid a commitment fee of Rs.372.39 million and interest of Rs.366.33 million up to 31 December 2022 and the project had only utilized US\$ 40 million out of the loan amount of US\$ 130 million due to poor performance of the project	Project was slowed down due to Covid during 2020, 2021 and financial crisis followed in 2022.	Funds should be utilized effectively within the scheduled project period.

3.3 Contract Administration

Audit Issue	Response of the Management	Auditor's Recommendation
A sum of Rs. 970.68 million had been paid more than the agreed contract amount for 4 projects in SCURP due to agreeing to pay various percentages in Dollar and Sri Lankan Rupees when paying to contractors on spot rate at the date of payment. Such an unfavourable condition include in contract agreement was a problematic issue in Audit.	A technical committee was appointed future action will be taken based on committee recommendations.	Immediate action should be taken to rectify the issue.

3.4 Idle/ Unutilized/ Underutilized Resources

Audit Issue	Response of the Management	Auditor's Recommendation
According to the project implementation manual it was expected to be developed 111.5 acres of land by the end of year 2022 under 11 land development projects of the component-2 however only 6 per cent of the expected target had been achieved at the end of the year under review.	Due to the economic condition of the country the Finance Ministry together with NPD directed to revisit the hiring of consultancy to optimize the funds allocation.	Action should be taken to achieve desired progress.

3.5 Matters in Contentious Nature

Audit Issue	Response of the Management	Auditor's Recommendation
Action had not been taken to obtain the certificates for the Ferguson Road Housing Project from the Sri Lanka Land Development Corporation, the National Building Research Institute, the Environmental Advisory Council, the Condominium Management Authority and the Urban Development Authority over 2 years.	The Environmental clearances and the building permit of Ferguson Road is delayed due to drainage and sewer clearance issue pertaining to the project and approvals are still pending.	Relevant approval should be obtained timely.

3.6 System and Controls

No	Audit Issue	Response of the Management	Auditor's Recommendation
(a)	The housing projects had not been registered as condominium properties. As a result, the expenses for the maintenance and operation of the housing schemes in future may be burden to the government.	According to the guidance of the Project Resettlement Policy Framework, it should be established Condominium Cooperation for each new housing scheme after the completion of resettlement.	Housing Projects should be registered as condominium properties.
(b)	The project had not identified low-income beneficiaries who are proposed for new housing schemes up to April 2023.	The PMU commence a new procurement process to hire a suitable consultancy service for Social Economic Base Line Survey.	Action should be taken to identify the proposed low-income beneficiaries.