

## Southern Transport Development Project - 2016

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The audit of the amalgamated financial statements of the Southern Transport Development Project for the year ended 31 December 2016 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. The Project was implemented under the Loan Agreements No. 1711-SRI(SF), No. 2413-SRI, No. SL-P-70, No.SL-P-92, NDF 324, No.BLA201011 and No.BLA201012 entered into between the Democratic Socialist Republic of Sri Lanka , the Asian Development Bank, Japan Bank for International Corporation , Nordic Development Fund Loan and Export Import Bank of China.

### 1.2 Implementation, Objective, Funding and Duration of the Project.

According to the Loan Agreements of the Southern Transport Development Project, the Ministry of Higher Education and Highways is the Executing Agency and Road Development Authority is the Implementing Agency of the Project. The objective of the Project is to assist to enhance the economic condition of the Southern Province by encouraging industries, tourism, fisheries and agriculture sectors. The output of the Project was the first access controlled highway of Sri Lanka of the length of 126 kilometres, connecting Kottawa in the Western Province to Matara in the Southern Province with an access road to connect the City of Galle. As per the Loan Agreements, the estimated total cost of the Project amounted to US\$ 661.14 million. Details of the overall sources of funds for the construction of the Southern Expressway are shown below.

<u>Lending Agency</u>	<u>Amount Agreed</u> <u>US\$ million</u>	<u>Percentage</u> <u>%</u>
Asian Development Bank	186.00	28.13
Japan Bank for International Corporation	103.00	15.58
Nordic Development Fund	5.40	0.82
Swedish International Development Association	0.80	0.12
Export and Import Bank of China	138.21	20.90
GOSL	227.73	34.45
<b>Total</b>	<b><u>661.14</u></b>	<b><u>100.00</u></b>

The section of the Southern Expressway of 95.05 kilometres from Kottawa in the Western Province to Pinnaduwa in the Southern Province had been opened for the use of general public on 27 November 2011 and other section of the Expressway from Pinnaduwa to Godagama in the Southern Province of 30 kilometres was opened for the use of general public on 16 March 2014. Upon completion of the construction works, the Road Development Authority had decided to utilize the savings of the Loans amounting to Rs.4.40 billion for rehabilitation works of 14 national and provincial roads which have direct or indirect connectivity to the Southern Expressway and reconstruction works of 02 bridges in the Southern Province. The activities of the Project are expected to be completed as at 31 December 2016.

### 1.3 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Public Sector Accounting Standards. This

responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error, selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

#### **1.4 Auditor's Responsibility**

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Project's preparation and fair presentation of the financial statements 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 Project's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management as well as evaluating the overall presentation of the financial statements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion. The examination also included such tests as deemed necessary to assess the following;

- a) Whether the systems and controls were adequate from the point of view of internal control so as to ensure a satisfactory control over the Project management and the reliability of books, records, etc. relating to the operations of the Project,
- b) Whether the expenditure shown in the financial statements of the Project had been satisfactorily reconciled with the enhanced financial reports and progress reports maintained by the Project,
- c) Whether adequate accounting records were maintained on a continuing basis to show the expenditure of the Project from the funds of the Government of Sri Lanka and the Lending Agencies the progress of the Project in financial and physical terms, the assets and liabilities arising from the operations of the Project, the identification of the purchases made out of the Loans etc,
- d) Whether the funds, materials and equipment supplied under the Loans had been utilized for the purposes of the Project,
- e) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project,
- f) Whether the financial statements had been prepared on the basis of Sri Lanka Public Sector Accounting Standards,

- g) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- h) Whether the financial covenants laid down in the Loan Agreements had been complied with.

### **1.5 Basis for Qualified Audit Opinion**

My opinion is qualified based on the matters described in paragraph 2.2.1 of this report.

## **2. Financial Statements**

### **2.1 Opinion**

So far as appears from my examination and to the best of information and according to the explanations given to me, except for the effects of the adjustments arising from the matters referred to in paragraphs 2.2.1 of this report, I am of the opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2016 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2016 in accordance with Sri Lanka Public Sector Accounting Standards.
- (b) the funds provided had been utilized for the purposes for which they were provided and
- (c) the financial covenants laid down in the Loan Agreements had been complied with.

### **2.2 Comments on Financial Statements**

#### **2.2.1 Preparation of the Financial Statements**

The financial statements of the Project for the year under review had been presented with amalgamation of the financial statements prepared upto 31 December 2015 separately under the Loan Agreements entered into with 03 Lending Agencies, without considering the matters such as closure of the periods of respective Loans and the completion of the construction works of the Expressway on 16 March 2014. Further, actions had not been taken to wind up the accounts, eventhough the process of handing over of properties, equipments and motor vehicles etc procured by the Project to the Implementing Agency had been completed as at 31 December 2016.

#### **2.2.2 Non - Compliance with Laws, Rules and Regulations**

An Engineer of the Road Development Authority had been appointed as a Consultant of the Project for rectification of the civil works at Kokmaduwa intersection , instead of being appointed an independent Consultant as required by the Clauses of 3.1 and 3.2 of the Contract Agreement .

## **3. Financial and Physical Performance**

### **3.1 Utilization of Funds**

Certain significant statistics relating to the financing of funds, budgetary provision in respect of Southern Transport Development Project for the year under review and utilization of funds during the year under review and up to 31 December 2016 are shown below.

Sources	Amount agreed for financing in the Loan Agreement		Budgetary provision for the year 2016	Funds utilized during the year 2016	Funds utilized up to 31 December 2016
	US\$. million	Rs. million	Rs. million	Rs. million	Rs. million
Asian Development Bank	186.00	21,392	-	-	20,581
Japan Bank for International Corporation	329.00	43,766	-	-	43,635
Nordic Development Fund	5.40	621	-	-	583
Swedish International Development Association	0.80	92	-	-	75
China EXIM Bank	138.21	15,895	2,041	2,040	16,965
GOSL	227.73	26,107	352	336	37,952
<b>Total</b>	<b><u>887.14</u></b>	<b><u>107,873</u></b>	<b><u>2,393</u></b>	<b><u>2,376</u></b>	<b><u>119,791</u></b>

As mentioned in the above, the activities of the Project had been continued upto 31 December 2016, even after completion of the construction works of the Expressway in order to utilize the savings of the allocations made under the Loans amounting to Rs 4.40 billion. Further, out of that a sum of Rs 1,570 million had remained unspent at the date of closing of the Loan Agreement of 30 June 2016 entered into with Export and Import Bank of China, and it was transferred to the Bank Account of the contractor who engaged in Expressway construction works carried out from Pinnaduwa to Godagama. It was observed that there was no proper action plan to utilize the balance amount of the Loan, at the time of transferring of the proceeds of the Loan to the Bank Account.

### 3.2 Physical Performance

The following observations are made.

- (a) As mentioned in the above, the Road Development Authority had decided to rehabilitate 46.70 kilometers of 06 national roads and 56.50 kilometers of 14 provincial roads and widening of reconstruction of 02 bridges of in the Southern Province and rectification works for slope failure at Kokmaduwa in the southern section of the Expressway to utilize the unspent balances aggregating Rs.4.40 billion. A Memorandum of Understanding thereon had been signed on 28 January 2014 with the contractor who engaged for the construction of the section of the Expressway from Pinnduwa to Godagama. According to the progress reports, the rehabilitation works of 23.20 kilometres of 07 national and or provincial roads had been completed as at 31 December 2016. However, the rectification works of slope failure at Kokmaduwa had remained in progress as at 31 December 2016.
- (b) It was revealed at the physical investigation made on 11 October 2017, the rehabilitation works of a road of 220 metres in Matara Town directed to private residences which was not included in the scope of the works had been completed at a cost of Rs.01 million. Further, it was observed at the physical inspection that severe cracks of the rehabilitated road of Abegunawardhana Mawatha in Matara and the required rectification works had not been completed even as at 31 December 2016. Further, the drainage system along the Godagama – Thelijjavila Road with a length

of 11 kilometre required to be made at an estimated cost of Rs.294 million had not been completed.

### **3.3 Contract Administration**

The following observations are made.

- (a) It was observed that the variation orders at a cost of Rs. 5,324 million related to construction of Expressway from Pinnaduwa to Godagama had been approved and paid during the year under review even after lapse of defect liability period on 14 March 2015, contrary to the provisions made under the Section 13.1 of Condition of Contract. As a result, the initial estimated cost of the contract amounting of Rs. 5,017 million for the construction of respective section of the Expressway had been exceeded by 106 per cent.
- (b) It was observed that the contract awarded at a cost of Rs. 260 million on protection and rectification works of landslide at Kokmaduduwa in the southern section of the Expressway had been carried out through a subcontractor without being obtained the consent of the Road Development Authority. Further, the works scheduled to be completed by 30 September 2016 had not been completed even as at 31 December 2017, eventhough additional payments of Rs. 19 million had been made on extra works done thereon.

### **3.4 Uneconomic Transactions**

According to the sub clause 4.2 of the general condition of the contract documents, the performance bonds are required to be obtained at his own costs. However, a sum of Rs.19.20 million spent by the contractor relating to the performance bonds had been reimbursed by the Project.

### **3.5 Transactions in Contentions Nature**

The following observations are made.

- (a) It was observed that 04 motor vehicles had been procured during the year under review at a cost of Rs.31.20 million for the use of the Expressway Management Unit, out of the proceeds of the Loan transferred to the contractor exceeding the estimated cost of Rs.20 million thereon. However, the required approvals of the authorized parties had not made available for audit.
- (b) It was observed that the Project Monitoring Unit had been functioned even as at 31 December 2016, after the closure of the activities of the Project without being transferred the supervision and monitoring activities to the Road Development Authority. As a result, a sum of Rs.35 million had been spent by the Project during the year under review to meet the costs related to the Project Management Unit .

### **3.6 Fruitless Transaction**

It was observed that interest aggregating Rs.384.80 million had been incurred by the Project as at 31 December 2017, due to delays in settling of the compensation payments on lands acquired by the Project. Further, the details relating to the lands acquired had not been furnished for audit.