

Metro Colombo Urban Development Project - 2018

The audit of financial statements of the Metro Colombo Urban Development Project for the year ended 31 December 2018 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 schedule 2 of the Loan Agreement No.8145 – LK dated 18 May 2012 entered into between the Democratic Socialist Republic of Sri Lanka and the International Bank for Reconstruction and Development. My comment and observation which consider should be reported to the 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 Megapolis and Western Development is the Executing Agency and the Urban Development Authority, Sri Lanka Land Reclamation and Development Corporation and Colombo Municipal Council are the Implementing Agencies of the Project. The objectives of the Project are to reduce flooding in the catchment of the Colombo water basin, strengthen the capacity of Local Authorities in the Colombo Metropolitan Area, improve and maintain local infrastructure and services through selected demonstration investments. As per the Loan Agreement, the estimated total cost of the Project amounted to US\$ 321 million equivalent to Rs.42,031.74 million and out of that US\$ 213 million equivalent to Rs. 27,890.22 million was agreed to be financed by the International Bank for Reconstruction and Development. The balance amount of Rs.14, 141.52 million is expected to be financed by the Government of Sri Lanka. The Project had commenced its activities on 10 July 2012 and scheduled to be completed by 30 June 2017. However, the date of completion of the activities of the Project had been extended up to 30 June 2020.

1.3 Opinion

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2018, financial performance and cash flows for the year then ended in accordance with the Generally Accepted Accounting Principles.

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 Generally Accepted Accounting Principles, 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:

- (a) 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 over ride of internal control.
- (b) 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.
- (c) Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- (d) 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 Non-compliance with Laws, Rules and Regulations

The following observations are made.

	Reference to the Laws, Rules and Regulations	Audit Issue	Impact	Response of the Management	Auditor's Recommendations
(a)	Paragraph 9.3 of the Circular No.01/2016 of 24 March 2016 of the Department of Management Services.	Only 02 meetings of the Project Steering Committee had been held during the year under review.	Weaken monitoring mechanism on physical performance of the Project.	Due to unavoidable reasons only 02 meetings were held during the year under review.	Need to adopt with the requirements of the Circular.
(b)	Section III – B of the Project's Appraisal Document.	PAYE and Withholding Taxes amounting to Rs. 7.32 million had been paid by the Project, contrary to said regulation.	Misapplication of the proceeds of the Loan.	These taxes related to the direct payments made to the Consultant and cannot be settled from the local funds.	Need to discuss with the Lending Agency and the Department of External Resources.

3. Physical Performance

3.1 Physical and Financial Progress of the activities of the Project

The activities of the Project were scheduled to be implemented under 56 construction contracts of 02 components of Flood and Drainage Management and Supporting the Local Authorities in the Metro Colombo Region. Out of that only the works under 38 construction contracts had been completed at a cost of Rs. 10,335 million with delays ranging from 01 months to 10 months as at 31 December 2018. The following observations are also made in this regard.

Activity	Physical Performance as at 31 December 2018		Impact	Response of the Management	Auditors' Recommendation
	Expected %	Achieved %			
Improvements to Madiwela East Diversion Scheme – III	100	52	Expected benefits will not be reached to the stakeholders during the periods specified.	Not commented.	Early action need to be taken to catch up the delays enable to receive the benefits for the stakeholder.
Design and construction of St. Sebastian North Lock Gates and Pumping Station	63	43			
Design and construction of New Mutwal and Torrington Tunnels	13.5	11			
Construction of Linear Park Along Western Bank of West Beira Lake – Stage III	62	37			
Design and construction of Ambatale Strom Water Pumping Station	Not specified	Not commenced			
Improvements to Norris Canal	10	06			
Kollonnawa Canal Diversion Scheme Stage – II	85	37			
Kollonnawa Canal Diversion Scheme Stage – III	Not specified	Not commenced			
Development of bio – diversity park at Kotte Rampart	Not specified	Not commenced			

3.2 Contract Administration

The following observations are made.

	Audit Issue	Impact	Response of the Management	Auditor's Recommendations
(a)	<u>Construction of Liner Park along Beira Lake – Stage II</u>			
	It was observed that the contract had been awarded at a cost of Rs. 294.15 million instead the Engineer's Estimate thereon amounted to Rs. 343.45 million. However, the respective works had been completed at a cost of Rs. 157.72 million. Further, the works estimated at a cost of Rs. 9.75 million had been subsequently cancelled, due to changes made in the scope of works. However, the mobilization advances amounting to Rs. 47.9 million had been released to the contractor based on the initial Engineer's Estimate.	Allowed opportunities to obtain financial gains through releasing of the mobilization advances additionally.	Some of the proposed construction works in the preliminary Engineering Estimate had to be altered, due to other projects implemented by the National Water Supply and Drainage Board. Further, the works estimated at a cost of Rs. 70 million had been withdrawn, as the works of floating wetland, Geo Cell Malt etc were not carried out. However, the contractor does not have the contractual obligation to request loss of profit in accordance with the sub clause 126 of the General Condition.	Action need to be taken to maintain cordial relationships with other institutions in order to decide the scope of works and prepare estimates in accurate manner.
(b)	<u>Design and Building of Torrington Tunnel and New Mutwal Tunnel Project</u>			
(i)	The contract on designing and construction of Mutwal and Torrington Tunnels had been awarded at a cost of US\$ 32.09 million and Rs. 246.06 million on 30 May 2018 and scheduled to be	Possible delays in completion of the contract.	The contractor had revised the construction schedule for design and construction of new Mutwal and Torrington Tunnels Project, without affecting the Project completion date.	The catch-up programme need to be prepared to cover up the delays.

completed within 02 years period. However, it was observed that necessary equipment had not been mobilized even as at 31 December 2018.

Further, the works under geotechnical investigation was time consuming and major prerequisite of the design process which was completed at present with the confirmation of the Survey Department.

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| (ii) | It was expected to achieve the physical target of 13.5 per cent on construction of Tunnels of Torrington and Mutwal as at 31 December 2018. However, only 11 per cent of progress had been achieved as at that date. The Project Management Unit had not been taken action to obtain the revised work programme from the contractor as per the Clause 8.4 of the Conditions of Contract. | Delays in completion of the activities of the Project and possible extension of the period of the contract. | Not properly commented. | Need to call the revised work programme from the contractor with immediate effect. |
| (iii) | Contrary to the Clause No. 06 of Terms of Reference of Contract Agreement, the monthly progress reports had not been prepared and submitted by the Consultant to the Project Management Unit in an agreed format. As a result, the progress report had not been presented on a quantitative basis and could not be compared with the work programme. | Project monitoring activities would not be done in effective manner. | Not properly commented. | Progress reports should be prepared in an agreed format and need to be communicated to take decisions timely. |
| (iv) | According to the monthly progress report of the Consultant as at 31 December 2018, only 03 design status reports, out of 102 such reports had been completed | Payments made without considering the physical progress. | Producing of an engineering design drawing is only the outcome of a design exercise and it is a very time consuming process need to be logically | Need to coordinate the design works carefully and evaluate the progress thereon. |

as at that date. However, US\$ 333,564 had been paid to a foreign firm of Consultants without considering their obligations to submit the periodic reports.

developed, according to the required technical order.

(c) **Construction of Liner Park along Beira Lake – Stage I**

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| (i) | The contract had been awarded at a cost of Rs. 184.26 million and completed the works at a cost of Rs 142.72 million. The scope work had been reduced, as many of works programme under the Project were scheduled to be carried out under other mega projects implemented within the City of Colombo. | (a) Possible wastage of time and cost on designing and works carried out.
(b) Allowed opportunities to the contractors to obtain financial gains on releasing of mobilization advances. | Several structural changes had to be made, due to other mega projects implemented within the City of Colombo. | Need to maintain good relationships with the other Project Implementing Agencies to understand the nature of works carried out by the respective projects. |
| (ii) | The Landscaping Maintenance Manual required to be submitted by the contractor, as per the Contract Specification No. 14.3.7 had not been prepared and submitted. | The maintenance of the landscaping works carried out at a cost of Rs.21.58 million remained at risk. | Necessary instruction had been issued to the contractor to comply with the obligations laid out in the contract documents. | Prompt action need to be taken to influence the contractor to meet with the obligations. |

3.4 Observations made on site visits

The following observations are made.

	Audit Issue	Impact	Response of the Management	Auditor's Recommendations
(a)	<u>Construction of Liner Park along Beira Lake – Stage II</u>			
(i)	According to the recommendation of the Consultants, Kumbuk or Teak timber should be used for seats at the Park. However, the samples tested by the State Timber Cooperation had proved that other varieties of timber had been used to erect seats at a cost of Rs. 7.90 million.	The constructed seats were not comply with the specification and durability of the seats are remained in doubt.	According to the test reports, type of wood used for the sample was Suriyamara. Action will be taken to adjust the payments.	Need to comply with the specification and ensure the durability of the items.
(ii)	According to the reports of the National Building Research Organization, the paving blocks applied for 1,380 square metres at an estimated cost of Rs. 4.44 million was not complied with the required compressive strength indicated in the specification.	The objectives of the activities of the Project would not be achieved in sustainable manner.	Not properly commented.	Need to instruct the contractor to mitigate the defects and adjust the payments accordingly.
(iii)	The Heavy Duty GI pipes had not been used to construct the visual barriers and picnic tables, as required by the specifications and a sum of Rs. 8.99 million had been paid thereon.	-Do -	It was identified that heavy duty GI pipes were not used for this purpose, according to the contract specifications. Necessary action will be taken to rectify the matter.	Need to take action to strengthen the controls to ensure the quality of works done by the contractors.
(b)	<u>Construction of Liner Park along Beira Lake – Stage I</u>			
(i)	It was observed that a sum of Rs. 1.80 million had been paid for the wood works carried out without being obtained the tests reports to confirm the quality of timber used.	Durability of the wood works would not be ensured.	The wooden parts for the seats were fitted, according to the timber samples approved by the contractor.	Need to obtain the test report before settle the payments and ensure the internal controls thereon.

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| (ii) | It was observed that the approval of the Ministers of Cabinet had not been obtained for the works carried out under 04 sub projects implemented under the component of the Flood and Drainage Management at a cost of Rs. 4,822.50 million. | Unauthorized works attended by the Project. | Due to political instability in October 2018, the approval of the Cabinet of Ministers could not be available and action will be taken to obtain the relevant approval in 2019. | Need to take prompt action to comply with the regulations and obtain the approvals from the relevant authorities. |
| (iii) | The procurement process on 120 items of works and goods under various categories under the sub projects were implemented with delays over 10 months affecting directly to smooth operations of the activities of the Project. | The physical performance of the Project was adversely affected. | Due to the complexity of some of the contracts, the procurement process thereon had taken long time. | Proper action need to be taken to monitor and evaluate the progress of procurement activities to achieve the objectives of the Project. |
| (iv) | The works completed under 11 sub projects had been handed over the sites with delays ranging from 01 to 2 ½ year as at December 2018. | Expected benefits to the stakeholders will not be received in timely manner. | The Project will take action to recover the late fee on delays in handing over the works by the contractor. | Need to evaluate the progress of the works of the contractors in timely manner. |

3.5 Issues Related to Human Resources Management

It was observed that the posts of the key management positions of the Project Monitoring Unit such as Deputy/ Senior Project Directors, Specialists, Senior Engineers and Architects etc had remained vacant regularly, whilst recruiting officers for the lower grades exceeding the approved cadre positions of the Project. It affected to smooth operations of the Project to complete the assigned activities in timely manner in order to achieve the objectives of the Project.

3.6 System and Controls

Description	Impact	Response of the Management	Auditor's Recommendation
It was observed that a part of fixed assets of the Real-time Integrated Flood Management System valued at Rs.2,74 million had only been depreciated during the year under review, out of the total assets valued at Rs.29.71 million of the System.	Misapplication of accounting principles	The assets procured from the counterpart funds accounted in operational expenses has been recorded as Fixed Assets of the Project and depreciated.	The procedures laid down in the Accounting Standards need to be adopted.