

Southern Expressway Project - Section 2 - 2018

The audit of financial statements of the Extension of Southern Expressway Project – Section 2 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. My comments and observations which I 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, then 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 main objective of the Project is to provide a link between the proposed Hambantota International Development Hub project, commercial capital, Hambantota International Harbor and International Airport (Mattala) by extending the already functioning Southern Expressway (Colombo to Matara) from Matara to Hambantota. As per the Loan Agreement, the estimated cost of the extension of 26 km of Southern Expressway from Beliatte to Wetiya under Section - 02 of the Project amounted to Rs.60,601.60 million and out of that 85 per cent of the cost of US\$ 360.29 million equivalent to Rs. 46,920 million was agreed to be provided by the Export Import Bank of China for the civil and consultancy works. The balance 15 per cent of US\$63.58 million was agreed to be financed by Hatton National Bank of Sri Lanka. The activities under the Section - 02 of the Project had been commenced on 28 October 2016 and scheduled to be completed by 27 October 2019.

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 2018 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 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	Impact	Responses of the Management	Auditor's Recommendation
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Provision for the interest to be paid for delay in payment of compensation on land acquisition had not been made in terms of Sri Lanka Public Sector Accounting Standards 08.	Understatement of assets and liabilities.	It will be provided in terms of SLPSAS - 08 in the current year financial statements.	Provisions should be made in line with the Sri Lanka Public Sector Accounting Standard No.08.

2.2 Non- compliance with Rules and Regulations

No	Reference to the Rules and Regulations	Non- Compliances	Responses of the Management	Auditor's Recommendations
(a)	Tri-party Memorandum of Understanding dated 27 June 2017	As the physical inspection conducted on 23 December 2019 revealed that the construction activities of three roads under the Tripartite Memorandum of Understanding (MoU) are not being carried out in such a manner as to obstruct the general public.	Three roads out of six roads coming under the purview of the Tripartite Agreement signed by the PRDA, RDA, and the Contractor have been handed over to the PRDA. Remaining three roads will be handed over after the completion of ongoing rehabilitation works.	Action should be taken to comply with the agreed terms to avoid disturbances for the public.
(b)	Sub Clause 4.2 of the General Condition of the Contract	Although the Performance Securities should be provided by the contactors at their own cost, a sum of Rs.307 million had been paid to the contractors to reimburse the cost of Performance Securities as at 31 December 2019.	The Condition of Contract states that the Performance Security shall be provided at his own cost means that the submission of Performance security is a prerequisite to enter into a Contract between the parties after which the Contractor is subsequently entitled to receive the cost of Performance Security under PS item 107(2) of the Contract BOQ.	The review of Bill of Quantities needed to be done by the Procurement Specialist and the Technical Evaluation Committee, before issuing the bidding documents.

3. Physical Performance

3.1 Physical Progress of the Activities of the Project

No	Component	Audit Issues	Impacts	Responses of the Management	Auditor's Recommendations
(a)	Resettlement of affected people	The project had purchased a land with extent of 2.0526 Hectares (5A.OR.11.43P) for Rs. 18 million to distribute among the people who lost their lands due to construction of highway. However, 9 perch extent of one lot of land had been remained as at 31 December 2018.	The affected people will be further aggrieved and cause ambiguous situation.	The unutilized 9 perch land lot has been kept under the project until the problem is resolved. If the land is not requested by any affected family it will be handed over to the relevant Pradeshiya Saba for community use.	Action should be taken to speed up the resettlement process.
(b)	Planning of the civil construction works	Although the sections 03 and 4 of the expressway were opened to the public on 7 November 2019, due to the poor progress of the construction work on this section, the general public had lost the benefit of using the entire expressway.	Poor planning at the initial stage of the project resulted to wait approximately another 6 months for the General Public to fully utilize the expressway	Delay of signing the loan agreement between the Sri Lankan Government and China EXIM bank has led to delay in the commencement of ESEP section 02.	Action should be taken to provide the best outcome to the public by considering all aspects in future planning.
(c)	Actual progress against the targets	The Project had been commenced four months delay and expected physical progress and financial progress of the Project as at 30 November 2019 was 88.24 per cent and 66.21 per cent respectively and the actual progress of the Project was 86.75 per cent and 60.84 per cent respectively. Therefore, the Project was marginally behind the expected targets.	Possibility to delay the overall completion and increase the cost of the project.	Extension of time has been granted up 11 April 2020. According to the programme contractor's actual progress slightly behind planned works.	Action should be taken to speed up the balance works.

3.2 Contract Administration

No	Audit Issues	Impacts	Responses of the Management	Auditor's Recommendations
(a)	Although the locations of Service Areas have been mentioned in Chapter 8.33 of the feasibility report, it had not mentioned in the BOQ and also, there is no any plan to construct Service Areas for the Extension of Southern Expressway. Further, after the 46km change of the Southern Expressway from Kottawa to Matara there were no any Service Areas is available for the users.	Providing services to passengers travelling 176 km from Welipenna to Hambantota was in a problematic situation.	There is no BOQ provision in ESEP contracts towards the construction of a service area and this has to be undertaken as a Contract Variation utilizing the Contract savings after obtaining concurrence from the Cabinet of Ministers and the China Exim Bank.	Required provisions should be get arranged for the construction of service areas for the Southern Expressway Extension Project.
(b)	According to the sub clause 4.2 of the General Condition of the contracts, the contractor shall ensure that the performance security is valid and enforceable until the contractor has executed and completed the works and remedied any defects. Based on the given extension of time, the defect liability period of the project will be ended on 11 April 2021. However, the available performance bond had been covered only the period up to the date of 26 June 2020.	Possibility to incur losses for any breach of contract terms by the Contractor during the defect liability period.	Instructions will be issued to extend the performance security up to the end of Defect Liability Period (Up to 2021.02.24) before its expiry date of 26 June 2020.	Action should be taken immediately to extend the period of performance security.
(c)	Rs.18.6 million had been paid as interest for delay payment up to Interim Payment Certificate No.37 as per the sub clause 14.7 (b) of General Condition of the Contract.	Increase in the total cost of the Project which could avoidable.	IPC 21, IPC 22, IPC 23 and IPC 24 payments were delayed due to the insufficiency of budgetary allocation for year 2018. Additional allocation was received after the due date of the above IPC payments.	Action should be taken to make the payments on time to avoid interest costs.

- (d) As per the Technical Specification, all equipments and consumables which are purchased under those two BOQ items, shall revert to the employer in good condition at the end of the contract. However a fixed asset register had not been maintained by the project to verify whether all purchased items been recorded in the assets register.
- Inability to ensure whether all the assets will transfer to the employer and lack of information regarding fixed assets may lead to misuse of assets.
- Fixed assets register was not properly updated at the time audit. Fixed asset register will be updated with requested information immediately.
- A fixed asset register should be maintained and updated properly.
- (e) Though the CL.207.12 Section 01 of Volume 03 of Technical Specification specifically mentioned that no charge is payable for the material obtained from the Right of way (ROW) had been paid Rs.10,million as royalty payments for rock excavated within ROW.
- Increase in the total cost of the Project due to payments made in contrary to the agreed terms.
- This implies that Road Development Authority will not charge for suitable material borrowed within ROW. Under the Mines and Minerals Act No 33 of 1992, the GSMB charges royalty payment to issue a mining license for the rock excavation within ROW.
- Payments should be made in line with the Conditions of the Contracts.
- (f) It was observed that Rs. 7,454 million paid exceeding approved BOQ only up to Interim Payment Certificate No.37 in August 2019. Out of those items, 32 items show variances more than 100 per cent. Further noted that, the project had not taken any action even to Revised the BOQ.
- Possibility to increase total cost of the Project and the possibility to misuse the funds.
- The Contract BOQ of the unsolicited proposal has been prepared from preliminary conceptual drawings to award the Contract to seek the Contractor funding. Detailed design stage, the Contractor had found deviation of BOQ quantities from the Contract scope.
- Action should be taken to revise the BOQ and estimates should be prepared accurately in future.
- (g) Though the project had completed 86.75 percent of physical work up to November 2019, the management had been called a detail design and cost estimation for a new interchange at Tangalle - Weeraketiya road and 8 extra connectivity or link to express
- Possibility to incur extra cost for the land acquisition and other preliminary works.
- New interchange for Tangalle-Weeraketiya road was not in the original scope of the Contract. The Government has decided to increase the connectivity to expressway to promote
- Scope of the works should be identified clearly at the initial stage of the projects.

way interchanges standard two-lane roads from the contractor on 17 and 20 December 2019. Changing the scope of the designed massive construction work at the time of nearly ending project is questionable to the audit.

tourism and the development of economy in Tangalle area. Badigama new IC will be constructed using the Contract savings for the benefit of populace in the area.

3.3 Observations made on site visits

Audit Issue		Impact	Response of the Management	Auditor's Recommendation
There were two Non-Conformance Report (NCR) had not been rectified until the audit inspection date of 23 December 2019. Details are as follows.		Delay in the rectification works may cause to further damage the road condition.	Contactor has not carried out the rectification works up to now. Accordingly, the payments have been withheld for the two NCRs. The Engineer is investigating the cause for failure and instructions will be issued for the rectification works.	Action should be taken to carry out the rectification works immediately.
Date of Issue	Description			
15 January 2018	Cracks on asphalt surface on internal road of Dahaamuna resettlement land.			
10 August 2019	Outer lane observed			