

REPORT OF THE AUDITOR-GENERAL ON ISILO WATER AND SEWERAGE COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Isiolo Water and Sewerage Company Limited set out on pages 9 to 25, which comprise the statement of financial position as at 30 June 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information in accordance with the provisions of Article 229 of the Constitution of Kenya and Section 35 of the Public Audit Act, 2015. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit.

In my opinion, except for the effect of the matters described in the Basis for Qualified Opinion section of my report, the financial statements present fairly, in all material respects, the financial position of Isiolo Water and Sewerage Company Limited as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Companies Act 2015.

In addition, as required by Article 229(6) of the Constitution, except for the matters described in the Basis for Qualified Opinion and Other Matter sections of my report, based on the procedures performed, I confirm that, nothing has come to my attention to cause me to believe that public money has not been applied lawfully and in an effective way.

Basis for Qualified Opinion

1.0 Disclosure and Presentation of the Financial Statements

The International Financial Accounting Standards (IFRS) reporting template prescribed by the Public Sector Accounting Standards Board requires that a report on the follow up of previous year's audit recommendations be included as part of the annexures to the financial statements. However, although the Company had a qualified audit opinion in the previous year, the report on follow-up on previous year's audit recommendations had not been included as an annexure to the financial statements as at 30 June 2017.

Further, a review of the financial statements revealed non conformity with standard financial reporting template issued by Public Sector Accounting Standards Board since important information were not included in the financial statements as follows;

- i). Management team and Board members names, passport photo qualifications and area of responsibility including management discussion and analysis.
- ii). Statement of comparison of budget and actual amounts and explanation on variations between actual and budget.

- iii). New standards and amendments to published standards effective as at the end of the reporting period, new and revised standards issued but not yet effective in the period ended, their impact and interpretations on the financial statement for the year ended and future annual periods.
- iv). Items in the statement of changes in equity were not cross referenced to the related information in the notes.
- v). Appendix on projects implemented by the entity and status of projects was not provided as required

In view of the foregoing, the disclosure and presentation of the financial statements for the year under review did not conform with the Accrual Basis of Accounting Method under the International Financial Reporting Standards.

2.0 Accuracy and Completeness of the Financial Statements

The cash flow statement reflected a decrease in creditors and accruals of Kshs.203,637 for the year under review. However, the statement of financial position reflected a decrease of Kshs.7 in creditors and accruals from Kshs.93,736 as at 30 June 2016 to Kshs.93,729 as at 30 June 2017 resulting in an unexplained and unreconciled difference of Kshs.109,908.

In the circumstances, the accuracy and completeness of the financial statements for year under review could not be ascertained.

3.0 Non-Revenue Water (NRW)

During the year under review, the Company produced a total of 1,437,030 cubic meters (m³) of water at a production cost of Kshs.5.77 per cubic meter. However, out of this volume, only 870,274M³ was distributed and billed to customers. The balance of 566,756 or approximately 39% of the total volume produced was not billed. However, the Water Services Regulatory Board (WASREB) guidelines allows a maximum loss of 25% for every cubic meter (M³) of water produced and hence only 359,258 M³ loss was allowed out of 1,437,030 cubic meters (m³) produced by the Company. The loss of 359,258 (M³) (14%) of water produced at a cost of Kshs.2,072,919 was therefore non-allowable loss. In the circumstance, the significant level of unaccounted for water negatively impacts on the Company's profitability and its long term sustainability.

4.0 Property, Plant and Equipment's

The financial statements for the year under review reflected property plant and equipment balance of Kshs.14,335,159 which included Kshs.2,305,356 relating to sewer and water extension. However, as per the vesting agreement, the ownership of water distribution infrastructure vests in Northern Water Services Board and any capital expenditure relating to distribution need prior approval by the Water Services Board. No documents were made available to show that the prior approval was sought and granted.

In addition, the Company owned two (2) motor vehicle registration numbers KAW 970G and KBY 744Q and although the Company, is a public Company the vehicles had private number plates instead of blue number plates reserved for public companies in Kenya.

In the circumstances, the security, existence and accuracy of plant, property and equipment balance of Kshs.4,335,159 as at 30 June 2017 could not be ascertained.

5.0 Irregular Recruitment of Employees

Note 9 of the notes to the financial statements reflected a balance of Kshs.26,903,788 in respect to salaries, wages and allowances. The payroll indicated that the Company recruited 12 new staff during the year under review. However, review of the documents provided on the recruitment process showed that the vacancies were not advertised and the entire process of recruitment was not followed as required by the Company's Human Resource Policy. Therefore, the salary paid to the 12 new staff amounting to Kshs.1,698,000 during the year was made irregularly.

In the circumstance, it was not possible to determine whether the new staff were competitively recruited and whether they were required by the Company.

6.0 Payables and Accruals

The financial statements reflected payables and accruals balance of Kshs.(93,736) as at 30th June 2017. The figure includes a negative balance of Kshs.101,819 (Note 18) attributed to VAT Control. However, no supporting documents such as creditors ledger or a schedule of payees particulars were made available for Audit verification.

In the circumstances, the accuracy of the payables and Accruals balance of Kshs.(93,736) as at 30 June 2017 could not be ascertained.

7.0 Over Expenditure

During the year under review, six (6) expenditure items whose budgetary allocation was Kshs.22,735,308 had an expenditure of Kshs.31,682,218 resulting to an over-expenditure of Kshs.8,946,910 as follows;

No	Item	Budget (Kshs.)	Actual (Kshs.)	Variance (Kshs.)	% Variance
1	Professional Fees	350,000	495,400	(145,400)	-41.5%
2	Salaries, wages and Allowances	19,500,580	26,903,788	(7,403,208)	-38.0%
3	Staff Welfare	800,000	1,300,990	(500,990)	-62.6%
4	Casual Wages	1,450,200	2,233,184	782,984	-54.0%
5	Water abstraction Levy	480,500	568,197	(87,697)	-18.3%
6	Telephone and Email	154,028	180,659	(26,63)	-17.3%
	Total	22,735,308	31,682,218	(8,946,910)	-39.4%

However, the respective approval for the Kshs.8,946,910 over-expenditure was not made available for audit review.

In the circumstance the Kshs.8,946,910 expenditure as at 30 June 2017 was irregular.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Isiolo Water and Sewerage Company Limited in accordance with ISSAI 30 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAI and in accordance with other ethical requirements applicable to performing audits of financial statements in Kenya. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Key Audit Matters

Key audit matters are those matters that, in my professional judgment, are of most significance in the audit of the financial statements. Except for the matters described in the Basis for Qualified Opinion section and Other Matter, I have determined that there are no Key Audit Matters to communicate in my report.

Other Matter

Budget and Budgetary Control

The Company's budget for the year 2016/2017 was approved on 9 June, 2016 vide Board minutes MIN/7/5/2015. However, the budget was not forwarded to the County Executive Committee Member (Finance) as stipulated in Part IV, Section 30 (6) & (7) of the PFM Act 2012 (County Government) Regulations and the National treasury circular number 19/15 on budget preparation.

Further, the Company had an approved budget of Kshs.75,780,989 comprising of Kshs.72,780,989 (96%) for recurrent expenditure and Kshs.3,000,000 (4%) for development expenditure. The annual revenue for the Company was budgeted at Kshs.66,782,710 with all of it being internally generated resulting in a budget deficit of Kshs.8,998,280. No explanation was provided on how the Company intended to finance the deficit.

In addition the Company collected Kshs.69,927,827 (105%) of the budgeted revenue and spent Kshs.73,474,715 during the year under review resulting into an over-expenditure of Kshs.3,546,889 as follows;

Items	Budget	Actual	Variance	Performance
Water and Sewerage	63,371,710	65,570,224	-2,198,514	103%
Other Revenue	3,411,000	4,145,102	-734,102	122%
Gain in Investments	-	212,500	-212,500	0%
Total Income	66,782,710	69,927,826	-3,145,116	105%
Recurrent				
Personnel	33,623,766	37,034,659	6,719,978	110%
Operations	35,237,388	19,349,082	15,888,306	55%
Maintenance	3,919,836	27,221,845	-23,302,009	694%
Total Recurrent	72,780,990	73,474,715	-693,725	101%
Development	3,000,000	-	3,000,000	0%
Total expenditure	75,780,990	73,474,715	2,306,275	97%
Surplus/ (Deficit)	(8,998,280)	(3,546,889)		

No documents were made available to show how the Kshs.3,546,889 over expenditure was financed. In addition, the development budget of Kshs.3,000,000 has been recurring since 2015/2016 financial year, an indication of lack of funding or financing for development projects. Thus denying the Company the ability to grow and increase service delivery to the residents of Isiolo County.

In the circumstances, the Company's budget preparation mechanism appeared not capable to produce a realistic budget.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue to sustain its services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless the management either intends to liquidate the Company's or to cease operations, or have no realistic alternative but to do so.

Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 47 of the Public Audit Act, 2015.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

The audit objectives are 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 in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness 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 conducted in accordance with ISSAIs, I exercise professional judgement 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 and for the purpose of giving an assurance on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue to sustain its services. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the Company to cease to continue to sustain its services.
- 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.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Company to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

I communicate with the management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

I also provide management with a statement that I have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.

REPORT ON OTHER LEGAL AND REGULARITY REQUIREMENTS

As required by the Companies Act 2015, I report based on my audit, that:

- i. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit;
- ii. In my opinion, adequate accounting records have been kept by the Company, so far as appears from the examination of those records; and,

- iii. The Company's financial statements are in agreement with the accounting records and returns.



FCPA Edward R. O. Ouko, CBS
AUDITOR-GENERAL

Nairobi

28 June 2018