REPORT OF THE AUDITOR-GENERAL ON KENYA SAFARI LODGES AND HOTELS LIMITED FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Kenya Safari Lodges and Hotels Limited set out on pages 1 to 25 which comprise the statement of financial position as at 30 June 2018, and the statement of profit and loss and other comprehensive income, statement of changes in equity, statement of cash flows and statement of comparison of budget and actual amounts 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 effects 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 Kenya Safari Lodges and Hotels Limited as at 30 June 2018, 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 Kenyan Companies Act, 2015.

Basis for Qualified Opinion

1. Going Concern

The statement of financial position as at 30 June 2018 reflects current liabilities balance of Kshs.652,383,000 which exceeded current assets balance of Kshs.175,481,000 by Kshs.476,902,000. Further, the Company realized a loss of Kshs.35,781,000, resulting to accumulated deficit of Kshs.453,493,000 as reflected in the statement of financial position as at 30 June 2018.

In addition, the statement of profit and loss and other comprehensive income for the year ended 30 June 2018 shows turnover of Kshs.283,331,000, other income of Kshs.4,976,000 and finance income of Kshs.12,644,000, all totaling to Kshs.300,950,982,000 against a budget of Kshs.441,000,000, representing a performance level of 66% or under collection of Kshs.140,049,018 or 31%. The management has not provided satisfactory reasons as to why the revenue targets could not be met. Further, as previously reported, the Company converted the Tourism Finance Corporation, formerly Kenya Tourist Development Corporation (KTDC) loan of Kshs.75,554,000 into equity in the year 2013/2014 and waived the interest accrued thereon. However, despite the conversion of the debt to equity, the working capital position and financial performance has not improved.

Consequently, the Company may not be in a position to meet its financial obligations as and when they may fall due and its continued existence as a going concern depends on continued support from the Government, bankers and creditors.

2. Property, Plant and Equipment

2.1 Fully Depreciated Assets

The statement of financial position as at 30 June 2018 reflects a balance of Kshs.676,419,000 and a nil balance in respect to property, plant and equipment and intangible assets respectively which include fully depreciated assets with a total cost of Kshs.173,554,000 and Kshs.3,845,000 as disclosed in Notes 13 and 13A to the financial statements. Although some of the assets are in use, the economic value of these assets has not been accounted for in these financial statements as they are carried at nil balance, contrary to International Reporting Standard No.16 which states that "revaluations should be carried out regularly, so that the carrying amount of an asset does not differ materially from its fair value at the balance sheet date".

Consequently, financial statements for the year ended 30 June 2018 do not comply with International Financial Reporting Standard No. 16 as prescribed by the Public Sector Accounting Standards Board.

2.2 Non-Compliance with Terms of Leasehold Agreement

Note 13 to the financial statements for the year ended 30 June 2018 reflects land and buildings balance of kshs.661,567,000, out of which Kshs.40,000,000 is in respect of leasehold land for Voi and Ngulia Safari Lodges. However, lease agreements availed for audit review indicated that the two leases will expire in November 2018 and March 2019 respectively and may not be renewed by one of the shareholders, Kenya Wild Life Services, which owns 0.02% of the Company's shares. The lessor cited breach of lease terms and non-payment of lease rentals for the period between year 2012 and 2018. The management applied for renewal of the leases but documentary evidence that the request has been accepted by Kenya Wildlife Service was not been availed for audit verification.

The possible loss of the two lodges may adversely impact on the Company's future revenue generating capacity.

2.3 Freehold Land

Note 13 to the financial statements for the year ended 30 June 2018 reflects land and buildings balance of Kshs.661,567,000 which includes freehold land balance of Kshs.360,000,000 for Mombasa Beach Hotel whose support lease title was not availed for audit verification nor beacons demarcating the land boundary shown. In addition, various handing over reports between successive General Managers availed for audit review, do not include the freehold land which is charged as follows:

Charge No.	Date	Presentation No.	Charged by	Value	Comments
10	04.05.1992	005 of 23.04.1992	Anurali Jafferali M.	Unquantified	Sub-lease interest
15	25.02.2005	Not clear from copy but dated 21.03.2005	Kenya Tourism Development Corporation Ltd	Kshs.40,000,000	Details not availed

Consequently, the ownership of freehold land and accuracy of the balance of Kshs.360,000,000 for the year ended 30 June 2018 could not be ascertained.

3. Inventories

The statement of financial position as at 30 June 2018 reflects a balance of Kshs.6,043,000 in respect to inventories as disclosed in Note 14 to the financial statements. However, included in the balance is Kshs.261,777, relating to obsolete stocks, contrary to International Accounting Standard No.1 which states that "financial statements must present fairly the financial position, financial performance and cash flows of an entity".

In the circumstances, the accuracy, validity and completeness of inventories balance of Kshs.6,043,000 as at 30 June 2018 could not be confirmed.

4. Trade and Other Receivables

4.1 Long Outstanding Trade Debtors

The statement of financial position as at 30 June 2018 reflects trade and other receivables balance of Kshs.144,850,000. Included in this balance is Kshs.129,474,000 in respect of trade debtors, out of which Kshs.87,643,652 had been outstanding for more than one(1) year. Further, the debtors balance is net of bad debts written off amounting to Kshs.38,636,527 and whose supporting Board resolution was not availed for audit review.

In the circumstances, the legality of bad debts written off of Kshs.38,636,527 and the recoverability of trade and other receivables balance of Kshs.87,643,652 as at 30 June 2018 could not be confirmed.

4.2 Other Debtors and Prepayments

Note 15 to the financial statements the year ended 30 June 2018 reflects other debtors and prepayments balance of Kshs.20,635,000. However, the balance has been arrived at after a setoff with credit balances amounting to Kshs.108,339,403. This is contrary to International Accounting Standard No.1 Section 32 which states that "assets and liabilities and income and expenses, shall not be offset unless required or permitted by International Financial Reporting Standard'. Further, debtors totaling Kshs.568,500 have been outstanding since year the 2014.

Consequently, the accuracy, and recoverability of other debtors and prepayments balance of Kshs.20,635,000 as at 30 June 2018 could not be confirmed.

5. Trade and Other Payables

As reported previously, trade and other payables balance of Kshs.642,458,000 shown in the statement of financial position as at 30 June 2018 includes long outstanding amounts payable to various statutory bodies in respect of payroll deductions, value added tax and other levies amounting to Kshs.435,911,000. Further, no provision for penalties arising out of non-remittance of these statutory deductions have been provided for in these financial statements.

Consequently, it was not possible to ascertain the accuracy, completeness and validity of the trade and other payables balance of Kshs.642,458,000 as at 30 June 2018.

6. Share Capital

As reported in the previous year, the share capital of the Company was increased from Kshs.9,319,000 to Kshs.100,954,000 through creation of 4,581,785 share of Kshs.20. The additional shares were issued through rights issue to existing shareholders in October 2013 at a price of Kshs.20 per share based on par value. However, the net assets of the Company as at 30 June 2013 amounted to Kshs.667,399,000, resulting to an approximate value of Kshs.1,432 per share, clearly showing that the rights issue price of Kshs.20 per share was way below their value.

Further, a search from the Registrar of Companies indicated that Kenya Safari Lodges and Hotels Limited was incorporated under the Company's Act Cap 486 under certificate of incorporation No.6909 of 12 October,1966 and whose shareholding is as summarized below:

Share holder	Shares Held	Proportion holding	Investors/ Ownership
Tourism Finance Corporation	4,161,855	82.45	State Corporation
Mountain Lodges limited	884,853	17.53	Private Company
Kenya Wild Life Service (Kenya National Parks)	1,016	0.02	State Corporation

However, the Company's Articles of Association do not allow issuance of the Company's shares to private investors which in this case is Mountain Lodges Limited. It is therefore not clear how and why private enterprise acquired shares in a state corporation. Further, no disclosure of this information has been made in the financial statements.

Consequently, the accuracy, validity and legality of the share capital value of Kshs.100,954,000 as at 30 June 2018 could not be ascertained.

7. Staff Costs

Note 6 to the financial statements for the year ended 30 June 2018 reflects staff salaries and wages of Kshs.107,395,000, out of which Ksh.7,200,000 was paid to the General Manager, who was hired for a period of thirty(30) months from December 2016. In the year 2016/2017, Kshs.3,300,000 was also paid for the same to the General Manager. This is contrary to Office of the President Circular OP/CAB.9/21/2A/LII/43 of 23 November 2004, under PC 7(Commercial) General Manager which set entry basic salary as Kshs.180,000, house allowance of Kshs.60,000 and other remunerative allowances of Kshs.30,000 all totalling Kshs.270,000 per month. The officer was thus overpaid by Kshs.5,370,000 as detailed below:

Year	Period	No. of Months	Monthly Salary (Kshs.)	Total (Kshs.)
2016/2017	December 2016 to February 2017	3	300,000	900,000
2016/2017	March 2017 to June 2017	4	600,000	2,400,000
2017/2018	July 2017 to June 2018	12	600,000	7,200,000
	Total Paid	**19**		**10,500,000**
	Approved Salary	19	270,000	5,130,000
	Overpayment			**5,370,000**

Consequently, salary amounting to Kshs.5,370,000 paid to the General Manager is irregular.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Kenya Safari Lodges and Hotels 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 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 issues described in the basis for qualified opinion section of my report, there were no Key Audit Matters to report in the year under review.

Other Matter

1. Budgetary Control and Performance

During the year under review, the Company had an approved budget of Kshs.353,896,000 for recurrent expenditure against actual expenditure of Kshs.263,428,000, resulting in under absorption of Kshs.90,468,000 or 25% as detailed below:

Expenditure Item	Final Budget (Kshs. '000)	Actual expenditure (Kshs. '000)	Over Absorption (Kshs.'000)	Under Absorption (Kshs.'000)	% Under / Over Absorption
Salaries & Wages	116,658	107,395		9,263	8
Staff Expenses	53,077	42,274		10,803	20
Staff Travel	9,442	10,097	655		6
Property Upkeep &Expenses	11,004	6,919		4,085	37
Repairs & Renewals	19,244	9,957		9,287	48
Operating Costs	84,360	53,294		31,066	36
Office Expenses	8,454	6,203		2,251	27
Administration Expenses	3,578	559		3,019	84
Directors Fees/Expenses	1,933	2,225	292		15
Advertising & Promotion	7,561	1,337		6,224	82
General Charges	13,665	8,820		4,845	35
Depreciation & Amortization	21,686	11,813		9,873	45
Interest & Other Charges	3,234	2,535		699	22
Total Operating Expenses	**353,896**	**263,428**	**947**	**91,415**	**25**

The management did not avail the Board's approval of the over expenditure of Kshs.947,000. Further, the under absorption may be as a result of poor revenue collection and unrealistic budget hence, the need for the management to review the budget preparation process with a view to making it more effective.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, based on the audit procedures performed, except for the matters described in the Basis for Qualified Opinion/Report on Lawfulness and Effectiveness in Use of Public Resources sections of my report, I confirm that, nothing else has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

Basis for conclusion

1. Failure to Establish a Sinking fund

During the year ended 30 June 2018, the Board approved the Company's a budget without provision for the renewal of depreciating assets, contrary to Section 16 (1) of the State Corporations Act, Cap 446 which provides that "every state corporation shall make provision for the renewal of depreciating assets by the establishment of sinking funds and for contributions to such reserve and stabilization funds as may be required".

Consequently, Company is in breach of the Law.

2. Operations of the Trust Deed and Staff Retirement Benefits Scheme

Records availed for audit review indicated that during the year under review, the Company did not remit insurance premiums for staff death benefits, contrary to Rule 2(d) and Rule 4 of the scheme trust deed and rules which require the Company to pay a special contribution as premiums for death benefits for its staff. Further, no budgetary provision has been made in these financial statements for the scheme.

Consequently, the Company is in breach of its own trust deed and the intended family beneficiaries may not benefit in case of death of an employee.

3. Uncollected Service Charge

During the year ended 30 June 2018, the Company paid service charge amounting to Kshs.16,311,824.21 to its employees through the payroll. The service charge is levied in compliance with Clause 21 (i) of Collective Bargaining Agreement of 2016 which provides that 'the employer will operate a service charge on accommodation sales arising from apartments and cottages serviced by the organization's employees and on food sales covering all food outlets whether by cash or credit and distribute 10% to the Company and 90% to employees'. However, the expenditure was not provided for in the budget contrary to Section 12 of the State Corporation Act Cap 446 which provides that no state corporation shall without the prior approval in writing from the Minister and the Treasury, incur any expenditure for which provision has not been made in an annual estimate prepared and approved in accordance with provisions of the Act'. Further, the service charge paid was levied on credit sales which form part of debtors balance of Kshs.144,850,000 as at 30 June 2018, hence how the expenditure was financed could not been explained. In addition, collectability of all these debtors is uncertain given that management has made a provision for bad debts of Kshs.5,259,439.85.

Consequently, the Company is in breach of the Law and may be paying service charge expense from uncollectable credit sales thereby exposing the Company to liquidity problems.

4. Strategic Plan

The Company's strategic plan for the period 2012-2018 was to expire in November 2018 yet none has been prepared for the next period 2018-2022. This is contrary to the Public Finance Management Act, 2012 Section 68(2) (g) which requires an accounting officer of a National Government entity to prepare a strategic plan in conformity with the medium term fiscal framework and fiscal policy objectives.

Consequently, the management is in breach of the Law.

5. Legal Fees

Note 7 to the financial statements for the year ended 30 June 2018 reflects legal fees of Kshs.274,000. However, no approval of the Attorney-General as required by Circular No.AG/CONF/6/E/247/ VOLII which requires State Corporations to get approval and authority from Attorney-General before incurring expenditure on legal fees.

Consequently, the propriety and completeness of legal fees of Kshs.274,000 for the year ended 30 June 2018 could not be confirmed.

6. Audit Fees

As previously reported, included in the trade and other payables balance of Kshs.642,458,000 as at 30 June 2018 is Kshs.2,008,000 as disclosed in Note 19 to the financial statements in respect to audit fees balance which has been outstanding for more than two years, contrary to Section 41 of the Public Audit Act, 2015 which provides that 'funds for the Auditor-General shall consist of audit fees charged at rates prescribed by the Auditor-General. Further, note 7 to the financial statements indicates provision for audit fees of Kshs.450,000 for the current year, which is contrary to costs incurred by the Auditor-General to audit the financial statements of the Company and whereby an invoice of Kshs.1,500,000 has been raised for the year ended 30 June 2018. The fee charged by the Office of the Auditor-General in year 2016/2017 was also Kshs.1,500,000.

Consequently, the Company is in breach of the Law and the total expenses for the year are understated by the difference of Kshs.1,050,0000.

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that govern them. A review is limited primarily to analytical procedures and to inquiries, and therefore provides less assurance.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON INTERNAL CONTROLS EFFECTIVENESS, GOVERNANCE AND RISK MANAGEMENT SYSTEMS

Conclusion

As required by Section 7 (1) (a) of the Public Audit Act, 2015, based on the procedures performed, except for the matters noted in the Basis for Qualified Opinion and Other Matter sections of my report, I confirm that, nothing has come to my attention to cause me to believe that internal controls, risk management and overall governance were not effective.
REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Kenyan 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 Kenya Safari Lodges and Hotels Limited, so far as appears from the examination of those records; and,

iii. Kenya Safari Lodges and Hotels Limited financial statements are in agreement with the accounting records.

Responsibilities of Management and Those Charged with Governance

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and for maintaining effective 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 and for its assessment of the effectiveness of internal control.

In preparing the financial statements, management is responsible for assessing the Kenya Safari Lodges and Hotels Limited's ability to continue to sustain services, disclosing, as applicable, matters related to going concern and using the applicable basis of accounting unless the management either intends to liquidate the Kenya Safari Lodges and Hotels Limited 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.

In addition to the responsibility for the preparation and presentation of the financial statements described above, management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them, and that public money is applied in an effective manner.

Those charged with governance are responsible for overseeing the Kenya Safari Lodges and Hotels Limited's financial reporting process, reviewing the effectiveness of how the entity monitors compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

Auditor-General's Responsibilities for the Audit

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.

In addition to the audit of the financial statements, a compliance review is planned and performed to express a conclusion with limited assurance as to whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities that govern them in accordance with the provisions of Article 229(6) of the Constitution and submit the audit report in compliance with Article 229(7) of the Constitution. The nature, timing and extent of the compliance work is limited compared to that designed to express an opinion with reasonable assurance on the financial statements.

Further, in planning and performing the audit of the financial statements and review of compliance, I consider internal control in order to give an assurance on the effectiveness of internal controls, risk management and governance processes and systems in accordance with the provisions of Section 7 (1) (a) of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. My consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under the ISSAIs. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Because of its inherent limitations, internal control may not prevent or detect misstatements and instances of non compliance. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

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.

- 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 Kenya Safari Lodges and Hotels Limited's ability to continue as a going concern. 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 Kenya Safari Lodges and Hotels Limited to cease to continue as a going concern.

- 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 Kenya Safari Lodges and Hotels Limited 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.

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

Nairobi

07 January 2019