

REPORT OF THE AUDITOR-GENERAL ON KYENI WATER AND SEWERAGE COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of Kyeni Water and Sewerage Company Ltd set out on pages 14 to 36 which comprise the statement of financial position as at 30 June 2018, 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, because of the significance of the matters discussed in the Basis for Adverse Opinion section of my report, the financial statements do not present fairly, the financial position of Kyeni Water and Sewerage Company Ltd 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 do not comply with the Water Act, 2016 and the Companies Act, 2015.

Basis for Adverse Opinion

1.0 Presentation of the Financial Statements.

The Public Sector Accounting Standards Board (PSASB) stipulates that all financial statements prepared under accrual basis (IFRS) should include the Board of Directors, statement of comparison of budget and actual amounts, progress on follow-up of auditor's recommendations, project implemented by the entity, inter- entity transfers and recording of transfer from other government entities. However, the Company's financial statements for the year ended 30 June 2018 did not include these statements and information. In addition, the report of Directors was signed by a Director instead of the Company Secretary. Further, PSASB stipulates that the statement of financial position of the Company should reflect the name of the chief executive and the head of finance who should also indicate his/her Institute of Certified Public Accountant (ICPAK) membership number. However, the two officers did not indicate their names while the head of finance did not indicate his ICPAK membership number in the financial statements for the year ended 30 June, 2018.

In the circumstances, the presentation of the financial statements was therefore not in accordance with the recommended PSASB format. In addition, it has not been possible to analyze the budgetary control and performance for the year under review.

2.0 Accuracy of Bank and Cash balances.

Note 11 to the financial statements reflects Kshs.5,346,069 in respect to bank and cash balances which includes a bank balances of Kshs.137, 537 in a bank and whose cashbook did not show any balance as at 30 June 2018.

In the circumstances, the accuracy of the Kshs.5,346,069 in respect to bank and cash balances as at 30 June 2018 cannot be ascertained.

3.0 Trade and Other Receivables

Note 10(b) to the financial statements reflects Kshs.24,825,181 in respect to trade receivables which includes Kshs.9,003,270 in respect to trade receivables for the year under review and whose supporting documents including debtors ledger and schedules were not availed for audit review. Further, the Kshs.24,825,181 trade receivables includes Kshs.2,758,353 in respect to provision for doubtful receivables which is 10% of the gross trade receivables of Kshs.27,583,534. However, the Company did not have bad debts policy contrary to Section 6.1.2 of the Water Company's finance manual which stipulates that the Commercial Manager shall review all outstanding debts, which are under dispute, on a monthly basis, before any bad debt provisions are made at the following rates:

Period Outstanding	Percentage Provision
241-360 days (8-12 months)	25%
Over 1 year	50%
Over 2 years	100%

In addition, the 10% rate of bad debts provision is not in line with the above cited Section 6.1.2 of the water Company's finance manual. Further, no risk management and assessment on the debts was undertaken in the year under review.

In the circumstance, the accuracy, validity and recoverability of Kshs.24,825,181 in respect to trade and other receivables as at 30 June 2018 cannot be ascertained.

4.0 Internal Borrowing from Customers Deposits

Note 16 (b) to the financial statements reflect Kshs.2,264,750 in respect to borrowings as at 30 June 2018. Information availed indicate that the Water Company withdrew the amount of money in the month of April 2016 from customer deposits balance of Kshs.7,294,395. However, no repayment agreement was availed for audit review and the management contravened the procedures where by customers' deposit amount should only be utilized for refund to customers who opt out of the water agreement with the company.

Consequently, the management is in breach of the law by utilizing clients' funds without proper procedures.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Kyeni Water and Sewerage Company Ltd 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 adverse 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 matter(s) described in the Basis for Adverse Opinion section, I have determined that there are no other key audit matters to communicate in my report.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, because of the significance of the matters discussed in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section of my report, based on the audit procedures performed, I confirm that public resources have not been applied lawfully and in an effective way.

Basis for conclusion

1.0 Audit Fees

Note 13 to the financial statements reflects Kshs.5,781,915 in respect to trade and other payables which includes Kshs.526,465 in respect to accumulated audit fees since 2010 comprising of Kshs.126,500 in respect to accrued expenses and Kshs.399,965 included in other payables which is payable to the Office of Auditor- General in accordance to Section 41(1)(c) of the Public Audit Act, 2015 which states that the funds of the Office of the Auditor-General shall consist of audit fees charged at the rates prescribed by the Auditor-General.

In the circumstances, the water Company is in breach of the law.

2.0 Lack of Internal Audit Unit

The Company did not have an internal audit section to carry out internal audit functions contrary to Section 1551(1) (a) of the Public Finance Management Act 2012 states that a County Government entity shall ensure that appropriate arrangements for conducting internal audit according to the guidelines issued by the Accounting Standards Board have

been established and (subsection 5) ensure that an internal audit committee has been established in accordance with prescribed regulations.

In the circumstances, the Company breached the law

3.0 Lack of Audit Committees

The Company did not have in place an audit committee contrary to Section 167 (1) (a) of the Public Finance Management (PFM) - County Government Regulations 2015 which states that each County Government entity shall establish an audit committee.

As a result, the Water Company is in contravention of the law

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

As required by Section 7 (1) (a) of the Public Audit Act, 2015, because of the significance of the matters discussed in the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance section of my report, based on the audit procedures performed, I confirm that internal controls, risk management and governance were not effective.

Basis for conclusion

1.0 Non-Revenue Water

Note 1 to the financial statements reflects Kshs.13,302,050 in respect to sale of water for the year ended 30 June 2018. Documents made available showed that the Company produced a total of 1,039,740 cubic meters (m³) of water in the year under review. However, only 493,522 cubic meters was billed to customers. The balance of 546,218 cubic meters (approximately 53%) of the total water produced, with a sale price of Kshs.14,722,381 represented Non-Revenue Water (NRW) which is over and above the allowable loss of 25% as provided by schedule E of the Water Service Regulatory Board (WASREB) guidelines.

In the circumstances, the Company significantly exceeded the allowable NRW loss of 25% by 28% or approximately Kshs.7,846,839 which if not addressed will negatively impact on the Company's profitability and its long- term sustainability.

2.0 Board of Directors

The Companies Act 2015, Section 128(2) and 132(1) stipulates that the Company should have at least two members as the Board of Directors appointed by a resolution at a general meeting of the Company. However, the terms of the previous Board expired on 4 April 2017 and there was no evidence to show that another Board of Director was

appointed in accordance with the law. Further, it was noted that the Company is directed by an eight – member interim committee appointed by the County Executive Committee Member (CECM) for Irrigation, Environment and Natural Resources. However, it is not clear which law the CECM invoked in appointing the interim committee. In addition, the Board corporate governance statement in the financial statements indicated that the board meets regularly and has various committees including audit, Finance, Human Resource and Technical committees. However, there was no evidence to show that the said Board and Board Committees existed or held any meetings during the year under review. Further, there was no evidence including Board minutes to show that the financial statements for the year ended 30 June 2018 were adopted by board of directors.

In the circumstances, the internal controls, risk management and governance of the Company cannot be confirmed.

3.0 Information Technology (IT) Internal Control Weakness and Lack of a strategic plan

The Company did not have an IT policy, Security policy, Environmental policy, IT Continuity Plan and Disaster Recovery Plan in the year under review. Further, there was no documentary evidence to confirm that the Company had a Strategic plan, and an Operational plan.

In the circumstances, the Company risk poor governance in its daily operations while its data security, integrity, confidentiality, recoverability and availability cannot be confirmed.

The audit was conducted in accordance with ISSAI 1315 and ISSAI 1330. The standard requires that I plan and perform the audit to obtain assurance about whether effective processes and systems of internal control, risk management and governance were operating effectively, in all material respects. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Companies Act 2015, I report based on the 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 not been kept by the company, so far as appears from my examination of those books; and
- iii. The company's financial statements are not in agreement with the accounting records and returns.

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 Public Sector Accounting Standards (Accrual Basis) 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, risk management and governance.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue to sustain 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 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 resources are applied in an effective way.

Those charged with governance are responsible for overseeing the Company'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 Company's 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 audit is planned and performed to express a conclusion about 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, and that public resources are applied in an effective way, 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.

Further, in planning and performing the audit of the financial statements and audit 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 Company's policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, 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.
- 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 as a going concern or 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 as a going concern or 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 Kyeni Water and Sewerage Company Ltd 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

8 April 2019