

# **REPORT OF THE AUDITOR-GENERAL ON KENYA NATIONAL SHIPPING LINE LIMITED FOR THE YEAR ENDED 30 JUNE, 2023**

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## **PREAMBLE**

I draw your attention to the contents of my report which is in three parts:

- A. Report on the Financial Statements that considers whether the financial statements are fairly presented in accordance with the applicable financial reporting framework, accounting standards and the relevant laws and regulations that have a direct effect on the financial statements.
- B. Report on Lawfulness and Effectiveness in Use of Public Resources which considers compliance with applicable laws, regulations, policies, gazette notices, circulars, guidelines and manuals and whether public resources are applied in a prudent, efficient, economic, transparent and accountable manner to ensure Government achieves value for money and that such funds are applied for the intended purpose.
- C. Report on the Effectiveness of Internal Controls, Risk Management and Governance which considers how the entity has instituted checks and balances to guide internal operations. This responds to the effectiveness of the governance structure, risk management environment and internal controls, developed and implemented by those charged with governance for orderly, efficient and effective operations of the entity.

An unmodified opinion does not necessarily mean that an entity has complied with all relevant laws and regulations and that its internal controls, risk management and governance systems are properly designed and were working effectively in the financial year under review.

The three parts of the report are aimed at addressing the statutory roles and responsibilities of the Auditor-General as provided by Article 229 of the Constitution, the Public Finance Management Act, 2012 and the Public Audit Act, 2015. The three parts of the report when read together constitute the report of the Auditor-General.

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Qualified Opinion**

I have audited the accompanying financial statements of Kenya National Shipping Line Limited set out on pages 1 to 38, which comprise the statement of financial position as at 30 June, 2023, and the statement of profit or 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 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 the Kenya National Shipping Line Limited as at 30 June, 2023, 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 and the Public Finance Management Act, 2012.

## **Basis for Qualified Opinion**

### **1. Inaccuracies in the Financial Statements**

Review of financial statements of the Company revealed inaccuracies and anomalies as follows;

- i. The statement of profit or loss and other comprehensive income reflects administrative costs amounting to Kshs.118,703,543. As disclosed in Note 12 to the financial statements, the amount includes provision for bad and doubtful debts of Kshs.1,010,915. However, Note 19 (a)(b) to the financial statements reflect an increase Kshs.2,140,048 and Kshs.866,809 in respect of trade receivables and other receivables respectively, all totalling to Kshs.3,006,857. The variance of Kshs.1,995,942 was not explained or reconciled.
- ii. The statement of profit or loss and other comprehensive income reflects prior year loss of Kshs.73,729,387. However, the operating profit or loss disclosures in Note 13 to the financial statements reflects provision for bad and doubtful debts indicated as Kshs.492,638 instead of Kshs.36,898,137 reported in the prior year audited financial statements.
- iii. The statement of profit or loss and other comprehensive income reflect profits before taxation of Kshs.309,708,160. As disclosed in Note 14 to the financial statements, the applicable tax on the profit is Kshs.92,912,448 at the rate of 30%. The Note further reflects further reflects a net tax credit of Kshs.34,149,573 for the year under review. However, the tax amount has not been disclosed as a receivable in the statement of financial position. In addition, the tax computation in Note 14 includes adjustments of Kshs.17,156,030 and negative Kshs.144,218,051 in respect of tax effects on expenses not deductible for tax purposes and tax effects on income not taxable respectively. However, the composition and details of the expenses and incomes referred to were not provided for audit review.
- iv. The statement of comparison of budget and actual amounts reflects actual income of Kshs.540,591,598. However, the amount varies with Kshs.475,591,598 total revenue reflected in the statement of profit or loss and other comprehensive income. The resultant variance of Kshs.65,000,000 was not explained or reconciled.

In the circumstances, the accuracy of the financial statements could not be ascertained.

### **2. Unsupported Professional and Legal Fees**

The statement of profit or loss and other comprehensive income reflect other income amounting to Kshs.476,684,229. As disclosed in Note 9 to the financial statements, the amount include court compensation of Kshs.475,260,543 which according to Management, was awarded in favor of the Company by the High court of Tanzania sitting in Dar es Salaam. However, receipts, bank statements and journals provided for review

reflected Kshs.421,097,189 resulting in unsupported and unreconciled variance of Kshs.54,163,354. Management explained that the variance was as a result of professional and legal fees amounting to Kshs.44,088,684 and provisions of Kshs.10,074,670 to cater for related court contingencies. However, no fee note was provided in support of the payments.

In the circumstances, the accuracy, completeness and authenticity of court compensation amounting to Kshs.475,260,543 could not be confirmed.

### **3. Changes in Ordinary Share Capital**

The statement of changes in equity for the year ended 30 June, 2023 reflects ordinary share capital of Kshs.168,600,000 (comprising 168,600 ordinary shares of Kshs.1,000 each), an increase of Kshs.75,077,000 from Kshs.93,523,000 as at 30 June, 2021. As reported in the previous year, the increase was as a result of reorganization of share capital by allocation of 19,335 ordinary shares of Kshs.1,000 each to the Kenya Ports Authority, increasing the Authority's shareholding from 70,023 to 89,358 shares. An additional 55,742 ordinary shares of Kshs.1,000 each was allocated to M/S SAS Shipping Agencies Services SARL in respect of Kshs.54,346,500 paid to the Kenya National Shipping Line Limited (KNSL) by M/S Heywood Shipping Company Limited and Kshs.1,395,500 in new capital call paid by M/S SAS Shipping Agencies Services SARL, all totalling to Kshs.55,742,000.

Further, the reorganization of share capital entailed transfer of 11,750 ordinary shares of Kshs.1,000 each by M/S Unimar and a similar number of shares by M/S DEG to M/S SAS Shipping Agencies Services SARL.

The changes in shareholding structure reduced the Kenya Ports Authority equity ownership in the Company by 22% from 75% to 53%, while reducing M/S Unimar and M/S DEG's equity from 13% each to nil and increasing M/S SAS Shipping Agencies Services SARL shareholding from zero to 47%. Information provided indicates that this was done in compliance and fulfilment of a Memorandum of Understanding between the Cabinet Secretary for Infrastructure, Housing and Urban Development and Mediterranean Shipping Company (MSC) of August, 2018. The Memorandum of Understanding required KNSL to give M/S Heywood the opportunity to convert its economic interest in KNSL shareholding and to complete the allocation of necessary shares to increase M/S Heywood's shareholding to not less than 47%.

The Memorandum of Understanding further required that the restructured KNSL be given a place at the port of Mombasa to operate from. Consequently, a Terminal Operation Agreement transferring the operation and management of Container Terminal 2 (CT2) at the port of Mombasa to KNSL, was signed between the Kenya Ports Authority and the Kenya National Shipping Line Limited on 24 January, 2022. However, available information indicates that there is a court case seeking stoppage of transfer of the operation and management of CT2 to KNSL. The case has not been determined and the information is not disclosed in the financial statements.

In addition, due diligence on MSC and its affiliates was to be concluded and The National Treasury provided an undertaking that all the necessary steps would be followed in order to adhere to the laws, regulations and procedures for achieving better value for the

Kenyan public. However, documentary evidence detailing how M/S SAS Shipping Agencies Services SARL was selected as an equity holder in KNSL and whether due diligence on MSC and its affiliates was concluded were not provided for audit review.

In the circumstances, the regularity of the selection of the Company as an equity holder in KNSL could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Kenya National Shipping Line Limited Management in accordance with ISSAI 130 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.

### **Emphasis of Matter**

#### **Budgetary Control and Performance**

The statement of comparison of budget and actual reflect income budget and actual amounts on comparable basis of Kshs.276,486,199 and Kshs.540,591,598 respectively resulting to a revenue underbudgeting of Kshs.264,622,699 or 95.5%. Similarly, the Company expended Kshs.165,883,438 against an approved budget of Kshs.156,907,570 resulting to over expenditure of Kshs.8,975,868 or 5.7% of the budget. The over-expenditure was not supported by requisite approvals as provided for by the Public Finance Management Act, 2012. In addition, Management prudence in the budgeting process was not confirmed as evidenced by significant variances between the budgeted and actual amounts.

My opinion is not modified in respect of this matter.

### **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. There were no key audit matters to report in the year under review.

### **Other Matter**

#### **Unresolved Prior Year Audit Matters**

In the audit of the previous year, several matters were raised under Report on the Financial Statements, Report on Lawfulness and Effectiveness in Use of Public Resources and Report on Effectiveness of Internal Controls, Risk Management and Governance. However, the matters remained unresolved as at 30 June, 2023. Although, Management has indicated under the progress on follow up of auditor's recommendations section of the financial statements that some of the issues have been resolved, no evidence was provided to indicate that the matters were deliberated on by relevant oversight bodies and the resolutions therefrom.

## **Other Information**

The Directors are responsible for the other information, which comprises the Chairman's statement, report of the managing director, corporate governance statement, management discussions and analysis, environmental and sustainability reporting, corporate social responsibility statement, report of the directors and the statement of directors' responsibilities. The other information does not include the financial statements and my auditor's report thereon.

My opinion on the financial statements does not cover the other information and I do not express any form of assurance or conclusion thereon.

## **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 Conclusion on Lawfulness and Effectiveness in Use of Public Resources section 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. Irregular Allowances**

The statement of profit or loss reflects administration expenditure of Kshs.118,703,545 as disclosed in Note 12 to the financial statements. The amount includes Kshs.1,079,529 and Kshs.841,376 in respect of hospitality and entertainment, and telecommunications. Review of payments in respect of the expenditure revealed the following anomalies: -

- i. Telecommunications expenditure included Kshs.480,000 paid to the acting Managing Director at monthly rate of Kshs.40,000. The allowances was approved by the Board of Directors in a meeting held on 20 March, 2015. However, no evidence was provided to indicate that allowance was approved by Salaries and Remuneration Commission (SRC), contrary to Section 11 of the Salaries and Remuneration Commission Act, 2011.
- ii. Review of expenditure incurred on hospitality and entertainment revealed an amount of Kshs.109,219 paid to the Controller and Administration Manager as monthly entertainment allowance at a rate of Kshs.9,102. However, the allowance was not supported by an approval by the Salaries and Remuneration Commission.

In the circumstances, the accuracy and propriety of the expenses under telephone, entertainment could not be confirmed.

#### **2. Rent Payment for Unoccupied Offices**

The statement of profit or loss and other comprehensive income and Note 12 to the financial statements reflects administration costs of Kshs.118,703,545. The amount include rental payments of Kshs.18,646,692, representing an increase of Kshs.15,306,712 or 458% of Kshs.3,339,980 incurred in the previous. The substantial

increase was due to the Company relocating from a government owned premises to a privately-owned one during the year, which attracted higher rental charge. No justification was provided for relocation as the rental payments increased the operational costs without corresponding revenue. In addition, Management in Section A of paragraph 9 of the reports and financial statements indicated that the Company has been relying on subventions from the National Government for its operations and that the Directors and Management were pursuing a number of strategies to ensure the company returns to profitable trading, which further negates the decision to relocate.

Further, the lease commenced on 1 August, 2022 and was set to run for a term of six (6) years, with occupancy of 12,693 square feet at an initial cost of Kshs.100 per square feet per month. At the time of the audit in December, 2023, the rented space on the first floor of the building had not been occupied, seventeen (17) months since the lease agreement was signed and rental payments commenced.

In the circumstances, the value for money of the rental expenses could not be confirmed.

The audit was conducted in accordance with the International Standards for Supreme Audit Institutions (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 comply, in all material respects, with the authorities that govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

## REPORT ON THE EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

### **Conclusion**

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, I confirm that, nothing has come to my attention to cause me to believe that internal controls, risk management and governance were not effective.

### **Basis for Conclusion**

The audit was conducted in accordance with the International Standards for Supreme Audit Institutions (ISSAIs) 2315 and 2330. The Standards require that I plan and perform the audit to obtain assurance about whether effective processes and systems of internal controls, risk management and overall 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 Kenyan 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 my audit.
- (ii) In my opinion, adequate accounting records have been kept by the Company, so far as appears from the examination of those records;

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

### **Responsibilities of Management and Board of Directors**

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 controls, risk management and overall governance.

In preparing the financial statements, Management is responsible for assessing the Company's ability to continue as a going concern disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management is aware of the intention to liquidate the Company or to cease operations.

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.

The Board of Directors is responsible for overseeing the Company's financial reporting process, reviewing the effectiveness of how Management 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 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 overall 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 Company's 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 Management.
- Conclude on the appropriateness of 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. 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.



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



**FCPA Nancy Gathungu, CBS**  
**AUDITOR-GENERAL**

**Nairobi**

**12 March, 2024**