

# REPORT OF THE AUDITOR-GENERAL ON HOMA BAY COUNTY WATER AND SANITATION COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE 2017

---

## REPORT ON THE FINANCIAL STATEMENTS

### Adverse Opinion

I have audited the accompanying financial statements of Homa Bay County Water & Sanitation Company Limited set out on pages 10 to 22, which comprise the statement of financial position as at 30 June 2017 and the statement of 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 explanation which, to the best of my knowledge and believe were necessary for the purpose of my audit.

In my opinion, because of the significance of the matters discussed in the Basis for Adverse Opinion paragraph section of my report, the financial statements do not present fairly, the financial position of Homa Bay County Water & Sanitation Company Limited as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance International Financial Reporting Standards and do not comply with the Kenyan Companies Act, 2015.

In addition, as required by Article 229(6) of the Constitution, based on the procedures performed, I confirm that public money has not been applied lawfully and in an effective way.

### Basis of Adverse of Opinion

#### 1. Inaccuracies in the Financial Statements

- i. The following difference were noted between some of the balance in the financial statements under comparison budget against actual in the respective notes to the financial statements

Items	Comparison Actual Kshs.	Accounts Notes Figure Kshs.	Variance Kshs.
Other Income note 1	1,651,178	1,631,336	19,786
Administrative Cost note 4	12,703,133	10,263,392	2,439,741
Operation & Maintenance Costs note 7	6,950,716	9,122,184	(2,171,468)
Tanker &Exhauster Running Cost note 7	3,539,000	2,287,801	1,251,199
Statutory Fees & Levies	5,384,574	5,099,580	284,994
Surplus/Deficit	7,679,835	7,435,224	244,611

- ii. The following differences were also noted between the approved budget and the summary statement of budget versus actual figures presented in the financial statements:

Item	Budget Approved Kshs	Budget Vs Actual Kshs	Difference Kshs.
Personnel Cost	22,353,723	25,509,143	(3,155,420)
Board Expenses	2,040,000	2,804,000	(764,000)
Tanker & Exhauster Running Cost	3,624,000	3,539,000	85,000
Operation & Maintenance Costs	16,180,000	5,098,400	11,081,600
Chemical	6,570,000	7,290,000	(720,000)
Statutory Fees & Levies	8,437,788	6,937,181	1,500,607

These budget Vs actual figures are not supported by approved budget which is the principal reporting document of the Company. In addition, the statement of comprehensive income reflects total revenue of Kshs.67,960,923 while the corresponding figures in budget statement is Kshs.67,980,765.

Consequently, it has not been possible to confirm the completeness, accuracy and completeness of the financial statements.

### iii. Trial Balance

During the year under review, it was noted that the balances reflected in the financial statements materially varied with those reflected in the trial balance.

Consequently, the accuracy of the balances posted in the financial statements could not be ascertained

## 2. Grants from the County Government

The statement of comprehensive income reflects a revenue figure of Kshs.67,960,923 which includes an amount of Kshs.17,190,436 being grants from County Government. However, no evidence was availed to support the grant and its purpose. Consequently, the validity and accuracy of the grants from County Government could not be confirmed.

## 3. Non-Revenue Water

During the year under review, the Company produced 1,189,386 cubic meter (M<sup>3</sup>) of water and out of this volume only 554,766 cubic meters (M<sup>3</sup>) was billed to consumers. The balance of 634,620 (M<sup>3</sup>) or approximately 53% of the total volume represents non-revenue water (NRW) which is 28% over and above the allowable loss of 25% in accordance with the Water Services Regulatory Board (WASREB) guidelines. The non-revenue water of 28% representing 335,271 (M<sup>3</sup>) may have resulted to loss of sales estimated at Kshs.12,941,460. as per WASREB guidelines of Kshs.38.60 per cubic meter. The significant level of NRW may negatively impact on the Company's profit and its long term sustainability.

#### **4. Intangible Assets**

Included in the financial assets under note 8 is intangible assets cost figure of Kshs.2,132,014 which includes additions of Kshs.1,940,314. However, no evidence has been availed for audit verification and it is not clear what kind of intangible assets it is.

Consequently, the validity and accuracy of intangible assets cost figure of Kshs.2,132,145 could not be confirmed.

#### **5. The Company's Secretary Cost**

Included in the statements of comprehensive income and as disclosed under Note 4 to the financial statements is an administrative cost of Kshs.36,882,618, which includes consultancy fees of Kshs.1,082,270. These further includes the company secretary cost of Kshs.355,400 that has not been supported with appropriate documentation. In addition, no contract agreement or procurement documents were availed for the sourcing of the services. Consequently, the propriety of the expenditure of Kshs.355,400 could not be confirmed.

#### **6. Unsupported Operation and Distribution Cost**

Included in the notes to the statement of comprehensive income and as disclosed in the financial statements under Note 5, is operation and distribution costs of Kshs.36,192,471. However, the ledger amounts and schedules provided indicated Kshs.33,130,858 resulting to a variance of Kshs.3,061,613.00 which could not be confirmed.

Consequently, the validity and accuracy of the operation and distribution cost of Kshs.36,192,471 could not be confirmed.

#### **7. Understatement of Work in Progress**

The statement of financial position reflects an amount of Kshs.29,649,316 under non-current assets which includes work in progress (water kiosks) balance of Kshs.11,568,541. It was noted that the supporting schedules reflected a balance of Kshs.25,141,259 resulting into a difference of Kshs.13,572,718.

Consequently, the accuracy and the completeness of the expenditure of Kshs.13,572,718 could not be confirmed.

#### **8. Unaccounted for Chemical Inventories**

During the year under review, the Company purchased chemicals stocks for chlorine and aluminum costing Kshs.5,312,502 while stocks issued totaled Kshs.5,024,955 thus resulting in a stock balance in store of Kshs.287,547. However, included in the notes to the financial statements under note 9 is inventory figure of Kshs.179,912 resulting to a variance of inventory stock difference of Kshs.107,635 not accounted for in the stores.

Further, reflected in the statement of comprehensive income under Note 5 to the financial statements is operation and distribution costs of Kshs.36,192,471 which includes chemical usage of Kshs.5,080,316 while total chemical stock issued is Kshs.5,024,955.

Consequently, the accuracy of the inventories figure of Kshs.179,912 could not be confirmed.

## **9.0 Trade and Other Receivables**

### **9.1 Understatement of Gross Trade and Other Receivables**

The statement of financial position and as disclosed under Note 10(b) is trade receivables figure of Kshs.17,255,653 which includes gross trade and other receivables of Kshs.20,068,539 before provision for bad and doubtful receivables of Kshs.2,812,886. However, the schedules in support of the gross trade and other receivables reflect an amount of Kshs.23,825,724 resulting to unreconciled difference of Kshs.3,757,185.

Consequently, the validity and accuracy of gross trade and receivables of Kshs.20,068,539 could not be confirmed.

### **9.2 Provision for Bad and Doubtful Receivables**

Included in the Notes 10(B) to the financial statements under trade and other receivables figure of Kshs.17,255,653 is provision for bad and doubtful receivables figure Kshs.2,812,886 which has been constant for many years while the trade and other receivables figure keep on increasing and recoverability cannot be ascertained. The Company did not provide evidence of the existence of bad and doubtful debts policy to verify why the provision has remained constant for a period of over two years.

Consequently, the validity and accuracy of the trade and other receivables figure of Kshs.17,255,653 could not be confirmed

## **10.0 Deferred Income**

### **10.1 Amortization of deferred income**

Included in the financial statements under Note 14 is deferred income amortization and net book value of Kshs.948,278 and Kshs.26,245,361 respectively which is under non-current liabilities but no policy on deferred income was disclosed in the summary of significant accounting policies contrary to the provisions of International Accounting Standards 20, that the grant is recognized as income over the period necessary to match them with the related costs, for which they are intended to compensate on a systematic basis.

Consequently, the validity and accuracy of the deferred income balance for the year ended 30 June 2017 could not be confirmed.

### **10.2 Construction of Decentralized Treatment Facility**

Included in the statements of financial position is non-current liabilities under Note 14 is deferred income of Kshs.26,245,361 which includes contract for construction of decentralized treatment facility and associated works in Mbita Sub-County which was awarded to a local construction company who was the lowest evaluated bidder. The contract sum was Kshs.7,352,915. In addition, certificate of substantial completion was issued on 19

May 2017 and the contractor had been paid the total contract sum at the end of the year under review.

Physical verification conducted on 20 February, 2018 revealed that the works were substantially complete except for electrical installation estimated to cost Kshs.20,000 and construction of earth channels to direct water and tank overflows estimated at Kshs.150,000 which had not been done and the contractor was not on site.

Further, it was observed that the treatment facility is operating far below capacity and is therefore not meeting the economic objective.

Consequently, the residents did not get value for money and the propriety of expenditure of Kshs.170,000 could not be confirmed.

## **11.0 Trade and Other Payables**

### **11.1 Understated Corporate Levy –**

Included in the notes to the financial statements under Note 15 is trade and other payables which includes the Lake Victoria South Water Service Board (LVWSB) corporate levy of Kshs.15,979,987 while LVWSB financial statements for 2016/2017 reflected that debt owed by the Company is Kshs.17,288,623 resulting to unreconciled difference of Kshs.1,308,636.

Consequently, the validity and accuracy of the corporate levy of Kshs.15,979,987 as at 30 June 2017 could not be confirmed.

### **11.2 WARMA Levies and Other Accruals**

Included in the trade and other payables figure is WARMA levies figure of Kshs.18,675,716 and other accruals figure of Kshs.2,029,792. However, no documentary evidence was availed to show the makeup of these figures.

Consequently, the validity and accuracy of total balance of Kshs.20,705,508 could not be confirmed.

## **12.0 Unsupported Customer Deposits**

Included in the financial statements under note 16 is customer deposits account of Kshs.5,345,214.00. However, the bank statement balance as at 30 June 2017 availed reflect an amount of Kshs.7,773 resulting to a difference of Kshs.5,337,441.00 which was not reconciled nor supported.

Consequently, the accuracy of the customer deposits of Kshs.5,337,441 could not be confirmed.

## **13. Cash Flow Statement**

Statement of cash flows present information about historical changes in an entity's cash and cash equivalents that classifies cash flow during the period according to operating, investing and financing activities and also being part of a complete set of financial statements. However, the Company failed to prepare a statement of cash flow.

Consequently, the accounting principle have not been abided by and how the Company manage its finances is doubtful.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Homa Bay Water and Sanitation 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 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, were of most significance in the audit of the financial statements of the current year. Except for the matters described in the in the Basis for Adverse Opinion and Other Matter sections of my report, I have determined that there are no other Key Audit Matters to communicate in my report.

### Other Matter

#### 1. Budget Analysis

During the year under review, the Company Board approved the revenue budget of Kshs.91,981,563 while the approved budget breakdown reflects Kshs.93,593,511 while budget vs actual expenditure budget reflects Kshs.86,578,724. Therefore, the revenue target was lower thus denying the Company an opportunity to provide adequate water services to the citizens of Homa Bay County.

The comparison of budget against actual expenditure as shown below;

Item	Budget Kshs	Actual Kshs	Over Expenditure Kshs	Under Expenditure Kshs	Absorption %
Personnel Cost	22,353,723	23,192,739	839,016		104
Administrative Costs	8,838,000	10,263,392	1,425,392		116
Chemical	6,570,000	5,080,316		1,489,684	77
Electricity	25,550,000	15,383,635		10,166,365	60
Operation & Maintenance Costs	16,180,000	9,122,184		7,057,816	56
Tanker & Exhauster Running Costs	3,624,000	2,287,801		1,336,199	63
Board Expenses	2,040,000	3,426,487	1,386,487		168
Statutory Fees & Levies	8,437,788	5,099,580		3,338,208	60

<b>Total</b>	<b>93,593,511</b>	<b>77,282,621</b>	<b>3,650,895</b>	<b>23,388,272</b>	<b>83</b>
--------------	-------------------	-------------------	------------------	-------------------	-----------

An Analysis of the budget against actual expenditure revealed that the Company overspent on three budget items namely; personnel cost by 4%, administrative costs by 16%, board expenses by 68% without any approval. No plausible explanation has been provided by management for the failure to seek approval for over spending.

Consequently, the management was in breach of the regulations.

## 2. Revenue Analysis

Analysis of budget against financial statements data revealed significant variances between budgeted and actual receipts as shown in the table below. Further, grants from County government and main source of revenue had under-collected by Kshs. 25,974,797.

<b>Item</b>	<b>Budget Kshs</b>	<b>Actual Kshs</b>	<b>Over Collection Kshs</b>	<b>Under Collection Kshs</b>	<b>Collection %</b>
Water Sales	52,195,000	36,199,772		15,995,228	69
Sewerage Income	9,786,563	8,166,557		1,620,005	83
Tanker/Exhauster Income	3,250,000	4,772,822	1,522,822		147
Other Incomes	1,200,000	1,631,336	451,178		136
Grants from Government	25,550,000	17,190,436		8,359,564	67
<b>Total</b>	<b>91,981,563</b>	<b>67,960,923</b>	<b>1,974,000</b>	<b>25,974,797</b>	<b>74</b>

The under collection has made the Company not provide enough water to the citizen of Homa Bay County. However, management has not provided explanations for this huge shortfall in revenue collection.

## 3. Submission Feedback on Quality Review of Annual Financial Statements for the Year 2016-2017 has not been responded to

It was observed that the Company has not acted on the recommendation of the National Treasury quality assurance review.

Consequently, the Company breached the regulations.

## 4. Failure to Prepare Procurement Plan

During the year under review, the Company did not prepare a procurement plan contrary to provisions of Section 115(2) of the Public Finance Management Regulations 2015. Consequently, the Company was in breach of the law.

## 5. Going Concern

The Company reported a loss of Kshs.7,435,224 for the year under review (2016- loss of Kshs.122,584) resulting in accumulated losses of Kshs.31,472,424 although the financial statements under note 13 reflects Kshs.23,914,616. In addition, the current liabilities balance of Kshs.52,359,509 also exceeded the current assets balance of Kshs.20,437,416

resulting in a negative working capital of Kshs.31,992,093 as at 30 June 2017. The Company is therefore technically insolvent and the financial statements have been prepared on a going concern basis on assumption that it will continue to receive financial support from Government, creditors and bankers.

## **6. Ownership**

As previously reported, the Company changed its name from South Nyanza Water Services Company Limited to Homa Bay County Water and Sanitation Company Limited in 2014, and the ownership from Kendu Bay Town Council, Homa Bay County Council and Suba County Council each with shares subscription of 497,482, and 480 respectively transferable to Homa Bay County Government. However, the Memorandum of Association still reflects the defunct local authorities as owners of the Company instead of County Government of Homa Bay suggesting that the changes have not yet been registered with the Registrar of Companies.

## **7. Previous Year Matters**

The Company did not indicate the status and follow up of audit issues reported in the previous year in the 2016/2017 financial statements as required by Public Sector Accounting Standards Board Reporting Template.

Consequently, the Company breached the regulation.

### **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 (IFRS) 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 as a going concern/ sustain services, disclosing, as applicable, matters related to going concern/ sustainability of services and using the going concern 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.

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 of Kenya. 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 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 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 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 consolidated/ 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 consolidated and separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities 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 LEGAL AND OTHER 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 been kept by the Company, so far as appears from the examination of those records;
- (iii) The Company's statement of financial position and statement of profit or loss and other comprehensive income are in agreement with the accounting records; and
- (iv) In my opinion, the information given in the report of the directors is consistent with the financial statements.



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

**Nairobi**

**09 August 2018**