

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

REPORT ON THE FINANCIAL STATEMENTS

Disclaimer of Opinion

I have audited the accompanying financial statements of Kapenguria Water and Sewerage Services Company Limited set out on pages 12 to 24, which comprise the statement of financial position as at 30 June 2018, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory information in accordance with the provisions of Article 229 of the Constitution of Kenya and Section 35 of the Public Audit Act, 2015.

I do not express an opinion on the accompanying financial statements. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for Disclaimer of Opinion

1.0 Inaccuracies in the Financial Statements

The financial statements provided for audit for the year ended 30 June 2018 reflects variances between the financial statements and supporting schedules which have not been reconciled or explained as summarized below:

Item	Amount as Per Schedule (Kshs)	Amount stated in the Financial Statement (Kshs)	Variance (Kshs)
Statement of Financial Position			
Receivables	12,046,291	12,905,141	(858,850)
Payables	18,352,141	18,553,141	(201,000)
Total	30,398,432	31,458,282	(1,059,850)
Statement of Comprehensive Income			
Cost of sales	7,590,784	8,709,286	(1,118,502)
Total	7,590,784	8,709,286	(1,118,502)

Consequently, the accuracy, validity and completeness of the Company's financial statements for the year ended 30 June 2018 could not be confirmed.

2.0 Unaccounted for Revenue

The statement of comprehensive income for the year ended 30 June 2018 reflects income of Kshs.9,441,631 in respect of water sales, Meter rent, ledger fee and exhauster services

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income. However, records made available for audit verification revealed that during eight (8) months period ending June 2018, the Company collected revenue totalling Kshs.3,974,114 while bank statements indicate that only Kshs.2,811,969 was banked during the same period resulting in an unaccounted for revenue amounting to Kshs.1,162,145 as summarized below:

Month	Revenue Collected (Kshs)	Revenue Banked (Kshs)	Under Banking (Kshs)
July 2017	570,950.00	540,480.00	30,470.00
August 2017	461,265.00	125,865.00	335,400.00
September 2017	573,550.00	375,585.00	197,965.00
October 2017	288,795.00	91,715.00	197,080.00
November 2017	537,270.00	420,980.00	116,290.00
January 2018	618,230.00	531,810.00	86,420.00
May 2018	434,810.00	282,990.00	151,820.00
June 2018	489,244.00	442,544.00	46,700.00
Total	3,974,114.00	2,811,969.00	1,162,145.00

No reason or justification was provided for failure to bank all revenue intact as required by the government financial regulations and procedures.

Under the circumstances, the completeness and accuracy of revenue collection of Kshs.9,441,631 for year the ended 30 June 2018 could not be ascertained.

3.0 Property, Plant and Equipment

The statement of financial position reflects a nil balance in respect of property, plant and equipment as at 30 June 2018. Note 6(i) to the financial statements indicates that all the company assets are leased from Rift Valley Water Services Board. However, and as previously reported, the lease agreement for these leased assets was not made available for audit verification. Further, the nature of the lease was not confirmed and also the leases were not accounted for in line with International Accounting Standards (IAS) 17 which stipulates that at the commencement of the lease term, leases shall recognize finance leases as assets and liabilities in the balance sheet.

Consequently, the accuracy, validity and completeness of the property, plant and equipment nil balance in the financial statements as at 30 June 2018 could not be confirmed.

4.0 Receivables

4.1 Debtors Inherited from the Ministry of Water

As reported in the previous year, included in the receivables' balance of Kshs.12,905,141 as at 30 June 2018 are debtors amounting to Kshs.2,496,486 inherited by the Company

from the Ministry of Water in the year 2007 and whose supporting documents were not availed for audit verification. Further, no documentary evidence was availed for audit review to indicate measures or efforts being made by the management to recover these long outstanding debts. In addition, the management has also not made any provision for bad debts in the financial statements arising from the inherited debtors that have been outstanding for over eleven years and whose recoverability is in doubt.

4.2 Unpaid Share Capital

The receivables' balance of Kshs.12,905,141 as at 30 June 2018 also includes unpaid share capital of Kshs.100,000 which was owned by the defunct Municipal Council of Kapenguria-Kshs.70,000 and Mnagei Mazingira Community based organization - Kshs.30,000 which have been outstanding since inception of the Company in 2006. As reported previously, there is no evidence that the management has made any efforts to have the amounts paid.

In the circumstances, the validity, accuracy and completeness of the receivables balance of Kshs.12,905,141 as at 30 June 2018 could not be confirmed.

5.0 Inventory

The statement of financial position reflects a nil balance in respect of inventory as at 30 June 2018. However, physical stock taking reports as at 30 June 2018 were not availed for audit review. Consequently, the accuracy and completeness of the nil stock balance as at 30 June 2018 could not be confirmed.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

I do not express a conclusion on the lawfulness and effectiveness in the use of public resources as required by Article 229(6) of the Constitution. Because of the significance of the matters described in the Basis for [Conclusion on Lawfulness and Effectiveness in Use of Public Resources/ Disclaimer of Opinion] section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit conclusion.

Basis for Conclusion

1.0 Failure to Install Water Meters

Included in the turnover figure of Kshs.9,441,631 reflected under note 2 of the financial statements is meter rent figure of Kshs.226,800. As previously reported, an audit of water production records and customer meter records revealed that out of five (5) production/intake points, only one (1) point (Makutano) is installed with bulk meters with the four (4) other points not fitted with bulk meters. Also a total of 666 customers were not fitted with meters as at 30 June 2018 in all the 5 zones and instead billed on flat rate instead of volume of water consumed.

Under the circumstances, the validity, accuracy and completeness of the turnover of Kshs.9,441,631 reflected in the statement of comprehensive income could not be confirmed.

2.0 Un-Accounted for Water (UFW)

Records availed for audit review indicate that 428,300 cubic meters (m³) of water was produced during the year under review out of which 196,210 cubic metres (m³) was billed to customers for Kshs.9,441,631 resulting in 232,090 cubic meters (m³) Unaccounted For Water (UFW) or approximately 54% of the produced water. This is 29% over and above the recommended maximum of 25% by the Water Services Regulatory Board (WASREB) guidelines. No verifiable explanation was provided for the high percentage of unaccounted for water. The significant level of Unaccounted for Water (UFW) of 232,090 m³ at a rate of Kshs.48.12 per cubic metre may have resulted in a loss of sales estimated at Kshs.11,168,178 which could have reversed the net loss to profit had it been billed. This may therefore, impact negatively on the Company's profitability and its long term sustainability.

3.0 Salary Advance

Included in the administrative expenses figure of Kshs.10,412,607 reflected under note 5(ii) of the financial statements is salaries figure of Kshs.7,182,295 out of which Kshs.816,500 salary advances were not supported by signed payment schedule. In addition, no evidence was provided to show if the granted salary advance was being recovered from the staff salary.

Consequently, the propriety of salaries figure of Kshs.7,182,295 under administrative expenses for the year ended 30 June 2018 could not be confirmed.

5.0 Payables

5.1 Staff Salary and Deduction Due

Included in the payables figure of Kshs.18,353,141 is staff salary and deduction due of Kshs.3,668,595 as disclosed under note 9 to the financial statements. However, the breakdown and aging analysis for this figure was not availed for audit review.

In the circumstances, the validity, accuracy and completeness of the payables balance of Kshs.18,353,141 as at 30 June 2018 could not be confirmed.

5.2 Customer Deposits

As reported in the previous year, included in the payables' balance of Kshs.18,353,141 is customer's deposits amount of Kshs.1,334,000 as disclosed in note 9 to the financial. However, the Company did not provide a cash book together with the bank statement in support of the customers deposits of Kshs.1,334,000 as at 30 June 2018 as required by Section 19 (c) of the Model Water Services Regulations 2007 and hence raising doubt on the existence of the cash paid by customers as deposits.

Consequently, the accuracy of the customer's deposits balance of Kshs.1,334,000 could not be confirmed and the Company management breached the law.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

I do not express a conclusion on the effectiveness of internal controls, risk management and governance as required by Section 7(1)3(a) of the Public Audit Act, 2015. Because of the significance of the matters described in the Basis for [Conclusion of Internal Controls, Risk Management and Governance /Disclaimer of Opinion] section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit conclusion.

Basis for Conclusion

1.0 Budgetary Control and Performance

A review of sales revenue estimates for the financial year 2017/2018 indicated a sales budget of Kshs.26,200,000. However, the reported collections for the year amounted to Kshs.18,433,617 thereby resulting into a short fall of Kshs.7,766,383 or 30% of the estimated sales revenue as analyzed below:

	Budgeted Amount (Kshs)	Actual Amount as per Records (Kshs)	Variance (Kshs)
Revenue	13,000,000	9,441,631	3,558,369
GOK Grants	13,200,000	8,991,986	4,208,014
Total	26,200,000	18,433,617	7,766,383

The management did not explain the cause for under collection of revenue.

The Company risks not meeting its budgetary targets and finally not meeting service delivery plans or providing effective services to the consumers.

2.0 Going Concern

The statement of comprehensive income for the year ended 30 June 2018 indicates that the water company made a loss of Kshs.2,921,106 which when added to previous years' cumulative losses of Kshs.4,981,816 resulted to accumulated deficit of Kshs.7,902,922 as at 30 June 2018. In addition, the company's reported current liability of Kshs.18,353,141 exceeds the reported current assets of Kshs.13,046,705 resulting to a negative working capital of Kshs.5,306,436 an indication that the company is not able to settle its obligation as and when they fall due. Also noted was a negative turnover trend from Kshs.10,837,400 reported in 2016/2017 to Kshs.9,441,631 in the current year, a reduction by Kshs.1,395,769.

The Company's going concern is threatened and its continued existence depends on the continued support from the County Government, creditors and its bankers.

3.0 Lack of Substantive Board

During the year under review, the Company did not have a fully constituted Board. The management of the company affairs was being done by the Managing director with the assistance of West Pokot County Government ministry of water officials contrary to Section 79 (1) of the Water Act, 2016 which requires that a water services provider should have a board of directors and in the case of a company, the members of its board of directors shall be constituted in accordance with the Companies Act, 2015 or any other written law and that the directors be nominated to serve on the board in accordance with the company's memorandum and articles of association. Further, the company had not revised the memorandum and article of association in line with the revised Water Act, of 2016 and Water Regulation, 2016. In addition, a ten-year Service Provision Agreement signed between the Company and the Rift Valley Water Services Board effective from 29 June 2007 expired on 30 June 2017 and no renewal has been done.

In the absence of a substantive Board, the entity governance process, accountability process and control systems is weak.

4.0 Lack of Internal Audit Function

As previously reported, the Company did not have an internal audit function contrary to Section 155(1) of the Public Finance Management Act, 2012 which states that a county government entity shall ensure that it has appropriate arrangements for conducting internal audit according to the guidelines issued by the Public Sector Accounting Standards Board.

Consequently, the management is in breach of the law.

5.0 Failure to Establish an Audit Committee

As reported in the previous year, during the year under review the Company did not establish an audit committee. This is contrary to Regulation 167(1) of the Public Finance Management (County Government) Regulations, 2015 which require each County Government entity to establish an audit committee in accordance with prescribed regulations to monitor the entity governance process, accountability process and control systems of the entity, offer objective advice on issues concerning risk, control, regulatory requirement and governance of the Company. The management is therefore in breach of the law.

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, risk management and governance.

In preparing the financial statements, management is responsible for assessing the ability to continue as a going concern/ sustain services, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the

management either intends to liquidate the 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 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

My responsibility is to conduct an audit of the financial statements in accordance with International Standards of Supreme Audit Institutions (ISSAIs) 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. However, because of the matters described in the Basis for Disclaimer of Opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

In addition, my responsibility is 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. I also consider internal control, risk management and governance processes and systems in order to give an assurance on the effectiveness of internal controls, risk management and governance 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. However, because of the matters described in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources, and Internal Controls, Risk Management and Governance sections of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit conclusion.

I am independent of 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.



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

Nairobi

08 April 2019