

# **REPORT OF THE AUDITOR-GENERAL ON KENYA FERRY SERVICES LIMITED FOR THE YEAR ENDED 30 JUNE 2017**

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## **REPORT ON THE FINANCIAL STATEMENTS**

### **Qualified Opinion**

I have audited the accompanying financial statements of Kenya Ferry Services Limited set out on pages 28 to 62, 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 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 Ferry Services Limited as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with Kenya Ferry Services Limited Act, 2006.

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

### **Basis for Qualified Opinion**

#### **1.0 Property, Plant and Equipment**

##### **1.1 Fully Depreciated Assets**

The statement of financial position as at 30 June 2017 reflects a balance of Kshs.2,181,924,000 in respect of property, plant and equipment which includes fully depreciated assets with a total cost of Kshs.473,885,000 (2015/2016 - Kshs.69,784,000) as per disclosure under note 16 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 zero value contrary to International Accounting 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.

As a result, it has not been possible to ascertain that the property, plant and equipment balance of Kshs.2,181,924,000 as at 30 June 2017 is fairly stated.

## **1.2 Idle Assets**

As reported in the year 2015/2016 audit report, the management procured and installed weigh bridges on both sides of the Likoni channel at a cost of Kshs.26,779,893 as indicated in the assets register. Although the weigh bridges were integrated with the revenue system, they are practically idle assets since Kenya Ferry Services Limited does not use them to charge for use of its ferries by motor vehicles. Further, management indicated that the bridges were a control measure to enhance safety by estimating the weight of motor vehicles boarding ferries at the Channel. However, there was no evidence showing that the weights of motor vehicles measured through the weigh bridges are used to control the number of motor vehicles that board the ferries.

Consequently, it has not been possible to confirm the propriety and value for money from expenditure totaling Kshs.26,779,893 as at 30 June 2017 incurred on the installation of weigh-bridges at Likoni Ferry.

## **1.3 Irregular Award of Tender for Two New Ferries**

As reported in the year 2015/2016 audit report, Kenya Ferry Services Limited awarded a contract for supply and delivery of two new passenger ferries at a cost of Kshs.1,863,000,000 (US \$18,630,000). Audit verification of the bid evaluation process revealed that the contract was awarded to a bidder who was ranked no. 4 at the technical evaluation stage. The technical evaluation report indicated that the type of ferry to be supplied by the winning bidder was Roll on / Roll off and that dead weight at designed draft was 490 tons. However, review of the winning bidder's tender document revealed that the bidder did not provide this information.

In addition, the Company made a down payment of Kshs.598,023,000 (US \$ 5,920,726.7) to the local appointed agent in August 2015. Section 17.1 of the contract document required that such payment be made upon production of an unconditional bank guarantee issued by an established and reputable bank located in Kenya. The winning tenderer submitted a performance bank guarantee of Kshs.93,150,000 (USD 931,500) issued by a foreign Bank, located in Istanbul, Turkey. However, there was no evidence showing that due diligence was carried out to establish the validity of the guarantee. It was further noted that the performance bond dated 13 July 2015 was submitted sixteen days after signing the contract contrary to Paragraph 10 of General Conditions of the contract which required the contractor to furnish the employer with the performance security before signing of the contract.

Further, the Company made an advance payment of Kshs.598,023,000 (US \$ 5,920,726.7) to the Kenyan company but failed to withhold 6% of VAT totaling Kshs.35,881,380 and withholding tax at 20% for non-resident company totaling

Kshs.119,604,600 despite professional advice from Kenya Revenue Authority to subject payments to both taxes.

Furthermore, according to the contract signed on 27 June 2015, the new ferries were to be delivered after seventeen (17) months, by November 2016. However, the first ferry (MV Jambo) was delivered in July 2017 being nine months after the set timeline. In addition, as the time of this audit in October 2017, the second ferry had not been delivered and information available indicates that delivery of the vessel was suspended by a court order.

In light of the foregoing, it has not been possible to confirm the validity and accuracy of the building and supply of two new ferries at cost of Kshs.1,863,000,000 (USD18,630,000) and propriety of expenditure totaling Kshs.1,519,379,614 paid to the contractor as at 30 June 2017.

## **2.0 Income from Operations**

The statement of comprehensive income for the year ended 30 June 2017 reflects an amount of Kshs.417,908,000 as income from operations. Included in income from operations figure of Kshs.417,908,000 as reflected in note 2 to the financial statements is revenue from toll collections of Kshs.401,275,000. Information available indicates that toll collections are fees paid by motorists ferried across the channel. However, audit inspection of the receipting area revealed that there was no independent record on the number of vehicles ferried by vessels across the channel. In addition, the weighbridges that were installed on both sides of the channel are not functional and therefore no record of vehicles that pass at the toll stations is maintained.

It was therefore not possible to reconcile the number of vehicles ferried against revenue recorded.

Further, Kenya Ferry Services Limited does not have any equipment or means of measuring the motor vehicles length to establish the appropriate charges. This contravenes part 2 of The Ferries (Vehicle Toll Charges) (Amendment) Rules, 2013 which provides that the Company should charge vehicles based on the length of the vehicles using Ferries for crossing the Likoni channel.

In the light of the foregoing circumstances, it has not been possible to confirm that the income from operations amounting to Kshs.401,275,000 for the year ending 30 June 2017 is fairly stated.

## **3.0 Long Outstanding Debts**

As previously reported, Note 22 to the financial statements reflects trade and other receivables balance of Kshs.716,622,000 which includes two debtors: one of Kshs.12,300,496 and the other Kshs.50,652,633 which have been outstanding since the year 2008/2009. Although the management has indicated that the debts are

subject to court cases, no documentary evidence has been provided to confirm the management's assertion.

Further, included in trade and other receivables balance of Kshs.716,622,000 as at 30 June 2017 are staff receivables of Kshs.10,157,000. Audit verifications revealed that staff advances amounting to Kshs.4,178,131 was owing from former staff. The management has not clearly explained how the staff were cleared before settling the debts.

Consequently, it has not been possible to confirm the validity and recoverability of trade and other receivables balance of Kshs.716,622,000 as at 30 June 2017.

#### **4.0 Trade and Other Payables**

As previously reported, included in trade and other payable balance of Kshs.245,631,000 as shown in note 29 to the financial statements are trade creditors amounting to Kshs.202,614,000 out of which Kshs.84,438,282 are long outstanding creditors, an indication that the Company could be having difficulties in meeting its credit obligations when they fall due which may lead to legal cases being instituted against the Company. Although the management indicates that the liabilities shall be settled, there is no documentary evidence of how the Company plans to pay while the amount has increased by Kshs.5,533,000 compared to figure of Kshs.197,081,000 reported in 2015/2016 financial year.

Under the circumstance, it has not been possible to confirm the validity and accuracy of trade and other payable balance of Kshs.245,631,000 as at 30 June 2017.

#### **5.0 Administration Expenses**

The statement of comprehensive income for the year ended 30 June 2017 reflects Kshs.111,392,000 in respect of administration costs. Included in administration costs figure of Kshs.111,392,000 is Kshs.8,572,000 in respect of legal dues. Records availed for audit indicate that Kshs.6,020,000 was paid to a law firm as a deposit based on a proposal presented by the firm to finalize outstanding cases arising from Mtongwe ferry disaster of 1994. However, as at the time of audit, there was no documentary evidence of any progress made towards achieving objectives of the proposal including court applications and settlement of claims by affected persons. It was therefore not clear which service was rendered by the law firm. The public have not realized value for money.

Consequently, the propriety and validity of expenditure amounting to Kshs.8,572,000 incurred on the administrative expenses for the year ended could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Kenya Ferry Services 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 qualified 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 matters described in the Basis for Qualified Opinion and other matter sections, I have determined that there are no Key Audit Matters to communicate in my report.

### Other Matter

#### 1.0. Budgetary Controls and Performance

According to the statement of comparison of budget actual amounts, the Company had a total budget of Kshs.987,257,000 compared to a budget of Kshs.905,526,000 for financial year 2015/2016 representing an increase of Kshs.81,731,000 or 9 %.

Audit analysis of the budget performance revealed significant over-expenditure on the following budget lines:

COMPONENT	Budget	Actual	Over-Expenditure	% Variance
Printing advertising and information services	2,264,000	5,103,000	(2,839,000)	125%
Sports Creation	5,475,000	7,492,000	(2,017,000)	37%
Training Expenses	11,800,000	15,542,000	(3,742,000)	32%
IT Implementation	2,344,000	6,197,000	(3,853,000)	164%
Legal dues/fees arbitration and compensation	11,500,000	8,572,000	2,928,000	25%
Contracted Professional Services	3,500,000	10,753,000	(7,253,000)	207%
Fuel and Lubricants Ferry Vessels	62,024,000	71,379,000	(9,355,000)	15%
Board Expenses	14,500,000	22,521,000	(8,021,000)	55%
Dry Docking	13,500,000	63,041,000	(49,541,000)	367%
Safety Equipment Repairs	5,000,000	8,676,000	(3,676,000)	74%
<b>Totals</b>	<b>131,907,000</b>	<b>219,276,000</b>	<b>(87,369,000)</b>	

However, there was no evidence of authority to reallocate funds from the voted lines. This is an indication of irregular reallocation funded from voted lines. In addition, the

management did not avail evidence of approval from the line ministry in line with Section 12 of the Corporations Act, 1986. The management was therefore in breach of law.

## **2.0. Safety of Ferries**

- 2.1. Information available indicates that MV Likoni and MV Kwale ferries were due for dry-docking in February 2017 and March 2017 respectively. However, as at the time of audit, October, 2017 the same had not been dry-docked although the ferries were still operating. Management has attributed the delay to lack of funds. This endangers the safety of ferry users.
- 2.2. According to International Safety Management (ISM), vessel engine is supposed to be overhauled after every 8500 hours of operation. However, it was noted that MV Kwale engine had operated for more than 30,000 hours without undergoing engine overhaul. The safety of the vessel is not guaranteed.
- 2.3. It was also observed that most of the pulleys on most ferries are defective thus causing the plows to be submerged in water when the ferries are moving. This endangers both pedestrians and motorists.
- 2.4. The Company has not insured all ferries for third party liability and therefore it would be difficult for the Company to settle liabilities in case of an accident which requires compensation.

## **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 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, disclosing, as applicable, matters related to sustainability of services and using the going concern basis of accounting unless the Government either intends to liquidate the Kenya Ferry Services 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.

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 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.
- 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 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.

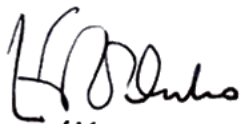
I communicate with the management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

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 OTHER LEGAL AND REGULARITY REQUIREMENTS

As required by the Companies Act, 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 the Company, so far as appears from my examination of those records; and,
- iii) The Company's statement of financial position and statement of comprehensive income are in agreement with the accounting records.



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

**Nairobi**

**12 April 2018**