

# **REPORT OF THE AUDITOR-GENERAL ON KENYA NATIONAL SHIPPING LINE LIMITED FOR THE YEAR ENDED 30 JUNE 2018**

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## **REPORT ON THE FINANCIAL STATEMENTS**

### **Qualified Opinion**

I have audited the accompanying financial statements of Kenya National Shipping Line Limited as set out on pages 19 to 43 which comprise the statement of financial position as at 30 June 2018, 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 Kenya National Shipping Line Limited 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(IFRS) and comply with the Companies Act, Cap 486 of the Laws of Kenya.

### **Basis for Qualified Opinion**

#### **1.0 Administration costs**

#### **1.1 Entertainment Expenditure**

Note 9 to the financial statements for the year ended 30 June 2018 reflects entertainment expenses of Kshs.1,044,342, being allowances paid to directors and staff while on official duties outside duty station while also in receipt of the full subsistence allowances which was to cater for all their expenses.

Consequently, entertainment expenditure of Kshs.1,044,342 incurred during the year ended 30 June 2018 is irregular.

#### **1.2 Transport, Travelling and Accommodation Expenditure**

Note 9 to the financial statements for the year ended 30 June 2018 reflects Kshs.7,656,254 in respect of transport, travelling and accommodation allowances advanced to staff on duty outside duty station. However, the advances were expensed on issue without surrender, contrary to the regulation 93(5) Public Finance Management (National Government)

Regulations, 2015 which states that 'A holder of a temporary imprest shall account or surrender the imprest within Seven (7) working days after returning to duty station'.

Consequently, the propriety and validity of transport, travelling and accommodation expenditure of Kshs.7,656,254 for the year ended 30 June 2018 could not be confirmed.

## **2.0 Trade and Other receivables**

### **2.1 Trade Receivables**

The statement of financial position as at 30 June 2018 reflects trade and other receivables balance of Kshs.17,601,704 after provision for bad and doubtful debtors of Kshs.51,427,696 as detailed under note 18 (a) to the financial statements. However, included in this amount is trade receivables balance of Kshs.38,205,968 which is not supported by invoices nor third party confirmations.

The trade receivables balance further includes Kshs.9,696,589 in respect of VAT recoverable, out of which Kshs.8,918,587 has been outstanding for over twelve(12) months. Consequently, the accuracy, validity and recoverability of trade and other receivables balance of Kshs.17,601,704 as at 30 June 2018 could not be confirmed. Further, the validity of the provision for bad and doubtful trade receivables of Kshs.51,427,696 could not be ascertained as at the same date.

### **2.2 Deposits and Prepayments**

Note 18(a) to the financial statements for the year ended 30 June 2018 reflects deposits and prepayments balance of Kshs.4,062,436, out of which Kshs.100,000 is rent deposit for the house occupied by the former Managing Director who left office in the year 2012, which has not been recovered after the house was vacated and surrendered to the landlord.

Consequently, the recoverability of rent deposit of Kshs.100,000 as at 30 June 2018 could not be confirmed.

## **3.0 Bank and Cash Balances**

As previously reported, note 19 to the financial statements for the year ended 30 June 2018 reflects bank and cash balance of Kshs.14,684,073. Included in this balance is Kshs.68,278 in respect of bank balance held at Barclays Bank of London (US\$ Account). However, the supporting bank statement and certificate of bank balance were not availed for audit verification.

Consequently, the existence of Barclays Bank of London account balance of Kshs.68,278 and the accuracy of cash and bank balance of Kshs.14,684,073 as at 30 June 2018 could not be confirmed.

## **4.0 Trade and Other Payables**

The statement of financial position reflects trade and other payables balance of Kshs.42,744,970 as at 30 June 2018. Included in this balance is Kshs.5,133,442 in respect of Pay as You Earn and Kshs.144,967 in respect of tax withheld from merchants, all totaling to Kshs.5,278,409, which had not been remitted to Kenya Revenue Authority as at 30 June 2018. No explanation was provided for non-remittance of these statutory deductions nor provision made in these financial statements for penalties and interest which may result.

Further, included in the trade and other payables balance is an amount of Kshs.5,429,040 which is due to container leasing companies. These companies have since stopped sending monthly statements in respect of the amount due. The amount disclosed in the financial statements is based on negotiated arrangement with major container leasing companies as per note 21 to the financial statements, hence not supported.

Consequently, the accuracy, validity and completeness of trade and other payables balance of Kshs.42,744,970 as at 30 June 2018 could not be confirmed.

## **5.0 Funds Awaiting Allotment**

As previously reported in the financial year 2016/2017, the statement of financial position as at 30 June 2018 reflects funds awaiting allotment balance of Kshs.73,681,500. However, note 20(b) indicates that the amount continues to be carried as funds awaiting allotment of shares while looking for an alternative way of reorganizing share capital between the existing shareholders which has not been completed.

Under the circumstances, the status of the shareholding and ownership of the Company as at 30 June 2018 could not be confirmed.

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

## **Emphasis of Matter**

### **1.0 Material Uncertainty Related to Going Concern**

As previously reported, the statement of comprehensive income for the year ended 30 June 2018 reflects a loss of Kshs.42,829,527(2017- Loss Kshs.46,157,888), resulting to an accumulated deficit of Kshs.418,646,792(2017 – Accumulated deficit Kshs.375,817,266). Further, the current liabilities balance of Kshs.69,409,865 exceeded the current assets of

Kshs.32,766,748 as at 30 June 2018, resulting in a negative working capital of Kshs.36,643,117.

In addition, the Directors have stated that the Company's going concern depends on implementation of various strategies, whose success is yet to be realized.

Under the circumstances, the financial statements have been prepared on a going concern basis on the assumption that the entity will continue to get financial support from the National Government and creditors and realization of various strategies put in place by the management.

## **2.0 Long Outstanding Shareholding Reorganization**

As previously reported, note 20 (a) to the financial statements for the year ended 30 June 2018 reports uncertainty surrounding the shareholding of the Company and an ongoing reorganization. The reorganization intended to reduce the par value of the shares from Kshs.1,000 to Kshs.500 per share, increase the authorized share capital from Kshs.100,000,000 (200,000 shares of Kshs.500 each) to Kshs.300,000,000 (600,000 shares of Kshs.500 each) and issue additional 147,363 shares. The additional shares were to be shared between Kenya Ports Authority (38,670 shares) and a new shareholder, Heywood Shipping Company Limited (108,693 shares). To effect the reorganization, the Company sought a Court order on 10 May 2003 to dispense with the requirement to serve notice to all the creditors of the Company, which the Court declined to grant. The management did not avail any evidence to confirm that the new shareholder was still willing to take up shares in the Company.

Under the circumstances, there is uncertainty about how long the shareholding reorganization process by the company as disclosed under note 20 (a) to the financial statements for the year ended 30 June 2018 would take to be concluded.

### **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 section, I have determined that there are no other Key Audit Matters to communicate in my report.

### **Other Matter**

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

##### **1.1 Revenue Budget**

The statement of comparison of budget and actual amounts for the year ended 30 June 2018 reflects an approved income budget of Kshs.240,168,000. However, the Company's

actual revenue for the year amounted to Kshs.58,480,295, resulting to net under-collection of Kshs.181,687,705 or 75.6% as detailed below;

Revenue Item	Final Budget (Kshs)	Actual Revenue (Kshs)	Under Collection (Kshs)	Over Collection (Kshs)	% Under/Over Collection
Service Income	184,428,000	1,713,114	182,714,886		99
Government Grants	55,350,000	55,350,000			
Finance Income	210,000	1,417,181		1,207,181	575
Other Income	180,000		180,000		100
<b>Total</b>	<b>240,168,000</b>	<b>58,480,295</b>	<b>182,894,886</b>	<b>1,207,181</b>	<b>75.6</b>

The huge under-collection may be attributed to possible unrealistic budget for the year under review and which may further hinder the Company's achievement of set objectives and planned activities thereby threatening its solvency. Therefore, there is need for the management to review its budgeting mechanism with a view to coming up with a realistic budget.

## 1.2 Expenditure Budget

The statement of comparison of budget and actual amounts for the year ended 30 June 2018 reflects an approved total expenditure of Kshs.211,751,000 against actual expenditure of Kshs.45,959,822, resulting to net under absorption of Kshs.165,791,178 or 78% as detailed below;

Expenditure	Final Budget (Kshs)	Actual Expenditure (Kshs)	Under Utilization (Kshs)	Over Utilization (Kshs)	% Budget Utilization
Compensation of Employees	37,452,000	25,822,126	11,629,874		31
Administration Costs	39,201,000	19,139,303	20,061,697		51
Service Costs	132,605,000	207,161	132,397,839		99.8
Finance Cost	360,000	617,742		257,742	71.6
Depreciation	2,133,000	173,490	1,959,510		92
<b>Total</b>	<b>211,751,000</b>	<b>45,959,822</b>	<b>166,048,920</b>	<b>257,742</b>	<b>78</b>

The huge net under absorption is a pointer to possible unrealistic budget and the management should review the budget making process with a view to coming up with realistic budgets for service delivery to citizens of Kenya.

## 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 and Qualified Opinion sections 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**

### **1.0 Employment costs**

#### **1.1 Acting Allowances**

Note 8 to the financial statements for the year ended 30 June 2018 reflects salaries and wages of Kshs.17,626,919, out of which Kshs.460,347 relates to allowances paid to the Managing Director who has been serving in an acting capacity for five(5) years, contrary to the policy C.14 (1) of the Public Service Commission Human Resources Policies of May 2016 which states that, 'when an officer is eligible for appointment to a higher post and is called upon to act in that post pending advertisement of the post, he/she is eligible for payment of acting allowance at the rate of twenty percent (20%) of his substantive basic salary and that acting allowance will not be payable to an officer for more than six (6) months'.

Consequently, acting allowances amounting to Kshs.2,071,561 paid to the officer for four(4) years and six(6) months between January 2014 and June 2018 is in breach of the Law and Company policy.

#### **1.2 Pension Fund Contributions**

Note 8 to the financial statements for the year ended 30 June 2018 reflects pension fund contributions by the employer of Kshs.2,953,858. However, records availed for audit review indicated that employees contributed 10% while the employer contributed 20% of the basic salary plus house allowance. This is contrary to the Treasury Circular No. 18/2010 of 24 November 2010 which states that, 'personal emoluments must be defined as basic salary excluding housing, transport and any other allowances or fluctuating emoluments'. Therefore, due to the inclusion of house allowances in pension calculation, the Company made illegal employer contribution amounting to Kshs.500,187 for the year under review.

### **2.0 Trade and Other Payables**

The statement of financial position as at 30 June 2018 reflects trade and other payables of Kshs.42,744,970 as disclosed in Note 21 to the financial statements. Included in this balance is other payables of Kshs.19,715,573, is provision for audit fees of Kshs.1,350,000 comprising current year provision of Kshs.450,000 and outstanding audit fees amounting to Kshs.900,000 for financial years 2015/2016 and 2016/2017. The failure to settle the long

outstanding audit fees contravenes Section 41(1) of the Public Audit Act, 2015 which states that, 'The funds of the Office of the Auditor-General shall consist of audit fees charges at the rates prescribe by the Auditor General'.

Consequently, the Company is in breach of the Law.

The audit was conducted in accordance with 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 are in compliance, 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 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, 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 internal controls, risk management and overall governance were not effective.

## REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Companies Act No. 17 of 2015, 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 Kenya National Shipping Line Limited , so far as appears from the examination of those records; and,
- iii. The financial statements are in agreement with the accounting records and returns.

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.

### **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 (IFRS) 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.

In preparing the financial statements, management is responsible for assessing Kenya National Shipping Line Limited's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the applicable basis of accounting unless the management either intends to liquidate Kenya National Shipping Line 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.

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 money is applied in an effective manner in line with Article 229(6) of the Constitution of Kenya, 2010.

Those charged with governance are responsible for overseeing Kenya National Shipping Line Limited'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 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 review is planned and performed to express a conclusion with limited assurance as to 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 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. The nature, timing and extent of the compliance work is limited compared to that designed to express an opinion with reasonable assurance on the financial statements.



Further, in planning and performing the audit of the financial statements and review of compliance, I consider internal controls 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 the 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 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 Kenya National Shipping Line Limited'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 Kenya National Shipping Line Limited 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 Kenya National Shipping Line Limited 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**

**21 March 2019**