REPORT OF THE AUDITOR-GENERAL ON KENYA NATIONAL SHIPPING LINE LIMITED FOR THE YEAR ENDED 30 JUNE, 2019

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 21 to 47, which comprise the statement of financial position as at 30 June, 2019, 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 National Shipping Line Limited as at 30 June, 2019, 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, 2015.

Basis for Qualified Opinion

1. Going Concern

As previously reported, the statement of comprehensive income for the year ended 30 June, 2019 reflects a net loss from operations of Kshs.46,987,078 resulting in an accumulated deficit of Kshs.465,633,970. Further, the current liabilities balance of Kshs.72,165,410 exceeded the current assets of Kshs.23,343,780 resulting in a negative working capital of Kshs.48,821,630 as at 30 June, 2019. 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.

2. Bank and Cash Balances

Note 22 to the financial statements reflects bank and cash balances totalling Kshs.2,725,078 as at 30 June, 2019. Included in the balance is an amount of Kshs.67,351 in respect of a bank balance held at Barclays Bank of London (US Dollar Account). However, the supporting bank statement and certificate of bank balance were not availed for audit verification.

Consequently, the existence of the bank balance of Kshs.67,351 and the accuracy of cash and bank balances of Kshs.2,725,078 as at 30 June, 2019 could not be confirmed.

3. Unsupported Administration Expenses

Section 104(1) of the Public Finance Management (National Government) Regulations, 2015 requires that, all receipts and payment vouchers of public moneys shall be properly supported by pre-numbered receipt and payment vouchers and the appropriate authority and documentation. However, and as disclosed under note 12 to the financial statements, the statement of comprehensive income reflects administration costs of Kshs.20,995,845 which includes Kshs.2,124,711 not supported by appropriate documentation.

Under the circumstances, the accuracy and completeness of expenditure of Kshs.2,124,711 could not be confirmed.

4. Taxation

Note 13 (a) to the financial statements for the year ended 30 June, 2019 reflects nil balance in respect of tax charge since the Company recorded a loss of Kshs.46,987,078. However, the recorded loss of Kshs. 46,987,078 was not adjusted to determine the tax loss as required by International Accounting (IAS) Standard No. 12 paragraph 5 which states that, 'Taxable profit (tax loss) is the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable)'.

Consequently, the accuracy of the tax loss amounting to Kshs.46,987,078 for the year ended 30 June, 2019 could not be confirmed.

5. Trade and Other Receivables

5.1 Unsupported Trade Receivables

Note 21(a) to the financial statements for the year ended 30 June, 2019 reflects a trade receivables balance of Kshs.38,170,111. Included in the balance are trade receivables of Kshs.34,474,707 whose support schedule does not have invoice details to confirm when services were rendered. Further, customer statements of account to confirm when the services were rendered were also not availed for audit verification.

Consequently, the accuracy, validity and recoverability of trade receivables balance of Kshs.34,474,707 as at 30 June, 2019 could not be confirmed.

5.2 Provision for Bad and Doubtful Debts

Note 21(a) to the financial statements for the year ended 30 June, 2019 further reflects gross trade and other receivables balance of Kshs.71,534,998 and Kshs.51,431,999 in respect to provision for bad and doubtful trade receivables, resulting to net trade and other receivables balance of Kshs.20,102,999. However, Management did not provide a debtors age analysis for audit review to confirm that the provision was in line with the Company's bad and doubtful debts policy, contrary to Paragraph 8 of the Kenya National

Shipping Line Limited's Finance Policy, which states that 'unsettled debts for a period under two years shall attract 50% provision for bad and doubtful debts while those remaining outstanding for over two years shall attract 100% provision for bad and doubtful debts'.

Consequently, the accuracy, validity and recoverability of net trade and other receivables of Kshs.20,102,999 as at 30 June, 2019 could not be confirmed.

6. Trade and Other Payables

The statement of financial position reflects trade and other payables balance of Kshs.45,490,224 as at 30 June, 2019. Included in this balance is Kshs.4,360,119 in respect to Pay-As-You Earn (PAYE) due on or before March, 2017 which had not been remitted to the Kenya Revenue Authority as at 30 June, 2019. No explanation was provided for non-remittance of the statutory deductions neither was a provision made in the financial statements for the accruing penalties and interest.

Further, included in the trade and other payables balance is an amount of Kshs.5,496,106 due to two (2) container leasing companies. These companies are said to have stopped sending invoices for container leasing charges and monthly statements in respect of the amount due. The amount disclosed in the financial statements is therefore based on outstanding balances when statements were last received from the container leasing companies, hence not up to date nor supported.

Consequently, the accuracy, validity and completeness of trade and other payables balance of Kshs.45,490,224 as at 30 June, 2019 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

Share Capital - Long Outstanding Funds Awaiting Allotment

As previously reported, and as disclosed in Note 23 to the financial statements, the statement of financial position as at 30 June, 2019 reflects funds awaiting allotment of shares balance of Kshs.73,681,500 equivalent to 147,363 shares, being additional shares to be shared between the Kenya Ports Authority - 38,670 shares and a new shareholder, Mediterranean Shipping Company (MSC) under the name of Heywood Shipping Company Limited (formerly United Agencies Limited) -108,693 shares. Available information, revealed that at their 24th meeting held on 31 July, 1997, the Board of Directors through a special resolution by the three (3) initial shareholders namely: Kenya Ports Authority, Unimar and DEG introduced a strategic partner M/s. Mediterranean

Shipping Company. Although, the strategic partner paid a sum of Kshs.54,346,500, it is not clear how the strategic partner was identified and allotted 108,693 new shares.

If the above is effected, the allotment of the shares would result to dilution of investment of the Kenya Ports Authority by 21.8% from 74.8% to 53% of the ordinary shareholding in the Company. The National Treasury has, however, provided a roadmap that will ensure that all the necessary steps will be followed in order to adhere to the laws, regulations and procedures for ensuring that public interest is upheld. Further, The National Treasury has also given an undertaking on the Kenya National Shipping Line Limited shareholding, undertaking to conduct due diligence before finalization of the transaction, obtain clearance from the Attorney General and subsequent approval from the Cabinet.

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

Budgetary Performance

The statement of comparison of budget and actual amounts for the year ended 30 June, 2019 reflects actual receipts totalling Kshs.46,083,949 against an approved budget of Kshs.99,881,000 resulting in net under-collection of Kshs.53,797,051 or 54% of the total budget. Further, actual expenditure for the year amounted to Kshs.48,481,027 against a budget of Kshs.99,881,000 resulting in an under expenditure of Kshs.51,106,973 or 51% of the total budget.

The under-collection and under-expenditure, which occurred under all budget items, may hinder the Company's achievement of the set objectives. Management should therefore review the budget making process with a view to developing a more realistic budget.

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 Qualified Opinion and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources 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. Employment Costs

Note 11 to the financial statements reflects employment costs of Kshs.26,767,091 for the year ended 30 June, 2019. Included in this balance is Kshs.18,985,000 in respect of salaries and wages, out of which an amount of Kshs.316,796 is overpayment of salary to the Chief Accountant who was doubling as the Acting Managing Director. The overpayment is a result of 10% increment approved by the Board on 29 October, 2018 to a monthly basic salary of Kshs.290,397 against the maximum basic salary of Kshs.263,997 set by the Salaries and Remuneration Commission (SRC).

Further, the officer was paid a monthly telephone allowance of Kshs.40,000 totalling Kshs.480,000 during the year under review. Although the allowance was approved by the Board on 20 March, 2015, Ministerial and Salaries and Remuneration Commission's approval of the same was not availed for audit review. This is contrary to the State Corporations Act, Cap.446 Section 4(3) which states that, 'a state corporation may engage and employ such number of staff, including the Chief Executive, on such terms and conditions of service as the Minister may, in consultation with the Committee, approve'.

In addition, the salaries and wages includes Kshs.522,714, being allowances paid to the Managing Director who has been serving in an acting capacity for six (6) years, contrary to Section C.14 (1) of the Public Service Commission; Human Resources Policies Manual 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, the validity of Kshs.1,319,510 on employment costs for the year ended 30 June, 2019 could not be confirmed.

2. Pension Fund Contributions

Note 11 to the financial statements for the year ended 30 June, 2019 reflects pension fund contributions by the employer of Kshs.3,262,690. However, records availed for audit review indicated that the amount comprises employer contribution of 20% of the basic salary plus house allowance instead of Kshs.2,867,243 based on basic salary only, 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'. The contravention of the circular resulted in a higher contribution by the employer by Kshs.395,447.

Consequently, Management is in breach of the Law.

3. Internal Audit Function

The financial statement for the year ended 30 June, 2019 indicated under Corporate Governance Statement that the Board discharges its functions through committees which includes an Audit and Risk Board Committee. However, information provided and review of the organizational structure and establishment indicated that the Company does not have an internal audit function contrary to the Public Finance Management Act, 2012

Section 73(1)(a) which states that. 'Every national government entity shall ensure that it complies with this Act and has appropriate arrangements in place for conducting internal audit according to the guidelines of the Accounting Standards Board'.

Consequently, the Management is in breach of the Law.

4. Risk Management Policy

The financial statement for the year ended 30 June, 2019 indicated under Section D of Management Discussion and Analysis that the Company's major risks included operational, financial, foreign currency, credit and liquidity risks. However, information provided for audit and through discussions held with the management revealed that the Company has not developed risk management policy and fraud prevention strategy contrary to Section 165 of the Public Finance Management (National Government) Regulations, 2015 which states that 'the Accounting Officer shall ensure that the national government entity develops risk management strategies, which include fraud prevention mechanism and a system of risk management and internal control that builds robust business operations.

Consequently, the Management 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 Matters 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.

Basis for Conclusion

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance about whether effective proce,sses and systems of internal control, 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 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 the 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.

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, risk management and overall governance.

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 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 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 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 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.

Nancy Gathungu
AUDITOR-GENERAL

Nairobi

05 February, 2021