

REPORT OF THE AUDITOR-GENERAL ON KIAMBERE-MWINGI WATER AND SANITATION COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of Kiambere-Mwingi Water and Sanitation Company Limited set out on pages 22 to 58 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 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, because of the significance of the matters discussed in the Basis for Adverse Opinion section of my report, the financial statements do not present fairly, in all material respects, the financial position of Kiambere-Mwingi Water and Sanitation Company 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 (Accrual Basis) and do not comply with the Water Act, 2016 and the Companies Act, 2015.

Basis for Adverse Opinion

1.0 Presentation of the Financial Statements

The financial statements for the year under review did not include a statement of profit and loss and other comprehensive income and a statement of comparison of budget and actual amounts as prescribed by the International Public Sector Accounting Standards Board (PSASB). In the absence of the statement of comparison of budget and actual amounts, it has not been possible to analyze the Company's budgetary controls and performance for the year under review. Further, the Company's financial statements included a statement of comprehensive income instead of a statement of profit and loss and other comprehensive income as required by PSASB.

In addition, PSASB stipulates that the statement of financial position of the Company should reflect the name, signature and Institute of Certified Public Accountant of Kenya (ICPAK) membership number of head of finance. However, the head of finance did not indicate his ICPAK membership number in the statement of financial position for the year ended 30 June 2018.

In the circumstances, the presentation of the financial statements for the year under review was not in accordance with the prescribed accounting standards.

2.0 Financial Performance

The Company's statement of comprehensive income for year under review reflects Kshs.87,591,201 in respect to total income and Kshs.101,915,327 in respect to total expenditure resulting to a loss of Kshs14,324,126. This loss has consequently reduced the revenue reserves by Kshs.14,324,126 from negative Kshs.13,660,284 as at 30 June 2017 to negative Kshs.28,457,030 as at 30 June 2018.

In addition, the Company's financial position as at 30 June 2018 reflects Kshs.25,371,049 in respect to total current assets against Kshs.38,398,142 in respect to total current liabilities resulting to Kshs.13,027,093 in respect to excess current liabilities over current assets. The Company's liquidity position is therefore in doubt as it may not be able to meet its current liabilities as and when they fall due which could threaten its going concern. The Company may therefore have to rely on its creditors and governments grants to remain afloat.

In the circumstances, if proper strategies are not put in place to reverse the trend, the Company is likely to face financial challenges in future which could threaten its going concern.

3.0 Share Capital

As reported in the previous years, the Kiambere-Mwingi Water and Sanitation Company Limited was registered with a share capital of Kshs.100,000 divided into 5,000 shares of Kshs.20 each. The shares were distributed to eleven individuals who had not paid for the shares contrary to Section 360 (1) of the Company's Act, 2015 which states that a subscriber to the memorandum of a public Company who takes shares of the Company as a result of an undertaking given in the memorandum shall pay for the shares, and any premium on the shares, in cash. The Company has not provided explanation for this unsatisfactory state of affairs as at 30 June 2018.

In the circumstances, the Company was in breach of the law. In addition, the validity and accuracy of share capital of Kshs.100,000 reflected in the financial position as at 30 June 2018 could not be ascertained.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Kiambere-Mwingi 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 audit 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, are of most significance in the audit of the financial statements. Except for the matter described in the Basis for Adverse Opinion section, I have determined that there are no other key audit matters to communicate in my report.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, because of the significance of the matter discussed in the Lawfulness and Effectiveness in Use of Public Resources section of my report, I confirm that public resources have not been applied lawfully and in an effective way.

Audit Fees

Note 15 to the financial statements reflects Kshs.29,321,947 in respect to payables and accruals which includes Kshs.928,000 in respect to accumulated audit fees (since 2013/2014 financial year) which is payable to the Office of Auditor- General in accordance to Section 41 (1)(c) of the Public Audit Act, 2015 which states that the funds of the Office of the Auditor-General shall consist of audit fees charged at the rates prescribed by the Auditor-General.

In the circumstances, the water 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, because of the significance of the matter discussed in the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance section of my report, I confirm that, internal controls, risk management and governance were not effective.

Basis for Conclusion

Non-Revenue Water

Note 2(a) to the financial statements reflects Kshs.49,903,830 in respect to sale of water for the year ended 30 June 2018. Appendix 2 to the financial statements shows that the Company produced a total of 656,187 cubic meters (m³) of water during the year under review out of which only 398,364 cubic meters was billed to customers. The balance of 257,823 cubic meters (approximately 39%) of the total water produced, with total sales value of Kshs.22,843,118 at a rate of Kshs.88.6 per cubic meter represents Non-Revenue Water(NRW) which is over and above the allowable loss of 25% as provided by schedule E of the Water Service Regulatory Board (WASREB) guidelines.

In the circumstances, the Company significantly exceeded the allowable NRW loss of 25% by 14% or approximately Kshs.8,308,575 (93,776.25 per cubic meter at Kshs.88.6 per cubic meter) which if not addressed will negatively impact on the Company's profitability and its long- term sustainability.

The audit was conducted in accordance with ISSAI 1315 and ISSAI 1330. The standards require 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.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Companies Act, 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 not been kept by the Company , so far as appears from the examination of those records; and,
- iii. The Company's financial statements are not 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

(Accrual Basis) 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 Company'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 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.

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 Company'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 audit is planned and performed 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.

Further, in planning and performing the audit of the financial statements and audit of compliance, I consider internal control 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 Company's 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 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.



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

Nairobi

9 April 2019