

REPORT OF THE AUDITOR-GENERAL ON KITUI WATER AND SANITATION COMPANY FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Kitui Water and Sanitation Company set out on pages 19 to 54, which comprise the statement of financial position as at 30 June 2017, and the statement of comprehensive income, statement of changes equity, statement of cash flows 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 Kitui Water and Sanitation Company 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 the Water Act, 2016 and the Public Finance Management Act, 2012.

In addition, and as required by Article 229(6) of the Constitution, except for the matters described in the Basis for Qualified Opinion and Other Matter sections of my report, based on the procedures performed, 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 Accuracy of Financial Statements

1.1 Accuracy of the Financial Statements

The statement of financial position for the year under review reflects cash and cash equivalents of Kshs.21,188,152 as at 30 June 2017. However, note 13 of the notes to the financial statements indicates Kshs.22,288,152 resulting in an unexplained and unreconciled variance of Kshs.1,100,000.

In addition, the statement of cash flow as at 30 June 2017 shows operating surplus before working capital changes of negative Kshs.410,196. However, a recasting of the respective figures showed that the Kshs.410,196 ought to have been positive-Kshs.410,196.

1.2 Undisclosed Deffered Tax

Note 17 of the notes to the financial statements reflected a deferred tax of Kshs.21,745,433. However, the deferred tax was not recognized as a liability in the statement of financial position as required by International Accounting Standard (IAS) number 12.

In addition, the statement of changes in equity reflected balances in respect to capital fund and surplus reserved as at 30 June 2016. However, the balances that were required for this audit ought to have been as at 30 June 2017

Consequently, the accuracy and completeness of the financial statements as at 30 June 2017 could not be confirmed.

2.0 Doubtful Rate on the Provision of Bad and Doubtful Debts

Section 4 (1) of the summary of accounting policies at page 32 of the financial statements for the year under review sets a rate of 15% provision for bad and doubtful debts. However, the rate was not supported by Board resolution as required by the Code of Governance for State Corporations, Chapter 1 Section 1.2 (i) (c) issued by the Public Service Commission and State Corporation Advisory Committee in January 2015.

In the circumstance, the authenticity of the rate used for the provision of bad and doubtful debts could not be established as at 30 June 2017

3.0 Non-Revenue Water

During the year under review, the Company produced a total of 2,985,445 cubic metres (m³) of water. However, records made available for audit verification indicated that only 1,147,436 m³ was distributed and charged to the consumers. The balance of 1,838,009 cubic meters or approximately 62% of the total volume produced was not charged. However, the Water Service Regulatory Board (WASREB) guidelines allows a maximum loss of 25% for every cubic meter (m³) of water produced and hence only 746,361 m³ loss was allowed for the 2,985,445 cubic meters (m³) produced by the Company. The loss of 1,091,648 m³ (37%) of water produced at an estimate cost of Kshs.91,807,597 (Kshs.84.1 per cubic meter m²) during the year under review was therefore non-allowable loss.

The significant level of unaccounted for water may negatively impact on the Company's profitability and its long term sustainability.

4.0 Procurement of Chemical

Note 6 of the notes to the financial statements reflected a balance of Kshs. 97,628,671 in respect of operating expenses which included Kshs. 4,363,559 spent on procurement of chemicals as at 30 June 2017. However, the supporting schedules availed for audit verification reflected an expenditure of Kshs.3,765,824 on chemicals resulting to unexplained variance of Kshs.597,735.

Further, the procurement documents including procurement plan, tender documents and contracts in relation to the procurement of the chemicals stated at Kshs.4,363,559 as at 30 June 2017 were not made available for audit review.

Consequently, the accuracy, propriety and value for money of the Kshs.4,363,559 expenditure as at 30 June 2017 could not be ascertained.

5.0 Prior Year Adjustment

The statement of Changes in Equity reflected prior year adjustments totaling Kshs.11,596,539. However, no supporting documents were made available for audit verification. Further, the statement of cash flow reflected prior year adjustment of Kshs.11,600,592 leading to unexplained and unreconciled difference of Kshs. Kshs.4,053.

In the circumstances, the accuracy of the statement of changes in equity and by extension the statement of financial position as at 30 June 2017 could not be confirmed.

6.0 Payables and accruals

Note 15 of the notes to the financial statements showed that the payables and accruals increased by Kshs.25,935,193 from Kshs.69,813,250 as at 30 June 2016 to Kshs.95,748,443 as at 30 June 2017. Included in the Kshs.95,748,443 was Kshs.18,196,193 in respect to Kenya Revenue Authority (KRA) taxes which increased by Kshs. 10,265,401 from Kshs. 7,930,792 reported in 2015/2016 financial year. This huge increase of unpaid KRA taxes may attract interest and penalties which are avoidable should the company comply with the KRA rules and regulations.

In the circumstances, it was not possible to ascertain that the management had instituted proper financial management systems to enable settling of debts as they fall due.

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

Other Matter

1.0 Budget and Budgetary Controls

The total budgeted expenditure for the year under review was Kshs.180,400,000 while the actual expenditure was Kshs.151,954,211 resulting into an under-expenditure of Kshs.28,445,789. Further, an analysis of the budget revealed the following issues:

1.1 Over Expenditure

During the year under review, fifteen (15) expenditure items with a budgeted amount of Kshs.53,938,440 had an actual expenditure of Kshs. 73,858,027 thereby exceeding their budget by Kshs.19,919,587 as follows;

Audit Components	Budgeted Amount (Kshs.)	Actual expenditure (Kshs.)	Over Expenditure (Kshs.)	%
Salaries & Wages	31,400,000	31,976,550	576,550	2%
Leave/Transfer Allowance	502,500	670,034	167,534	33%
Staff Training	173,940	565,450	391,510	225%
Postage	50,600	97,829	47,229	93%
Stationery & Printing	595,000	873,130	278,130	47%
Gratuity/Pension	1,400,000	8,160,041	6,760,041	483%
Cleaning Materials	5,000	29,383	24,383	488%
Taxes	10,995,000	11,026,267	31,267	0%
Staff welfare	80,000	478,728	398,728	498%
Staff insurance	6,400	22,650	16,250	254%
Transport Hire	80,000	81,400	1,400	2%
Internet & E-Mail services	90,000	122,416	32,416	36%
Repair of water systems (Boreholes, pipes & fittings)	6,660,000	9,673,198	3,013,198	45%
9% remittance TAWSB and WASREB Arrears	1,700,000	9,301,693	7,601,693	447%
Bank charges	200,000	779,258	579,258	290%
Total	53,938,440	73,858,027	19,919,587	37%

However, no supplementary budget was made available for audit review to support the Kshs.19,919,587 over expenditure.

In the circumstance, the expenditure may have been incurred irregularly.

1.2 Under Expenditure

During the year under review, thirty (30) expenditure items with a total budget of Kshs.111,641,560 had an actual expenditure of Kshs.88,162,793 resulting to an under-expenditure of Kshs.23,478,767 with some items having had no expenditure at all as follows;

Components	Current year final budget (Kshs.)	Actual expenditure (Kshs.)	Over/Under (Kshs.)	%
Wages(CASUALS)-Unskilled labour	3,740,500	-	(3,740,500)	-100%
Staff uniforms	100,000	-	(100,000)	-100%
Medical Expense	2,500	-	(2,500)	-100%

WASPA	100,000	-	(100,000)	-100%
Performance Contracting	100,000	-	(100,000)	-100%
Advertisement	340,000	-	(340,000)	-100%
Office Mobile Phone	8,000	-	(8,000)	-100%
Staff welfare	50,000	-	(50,000)	-100%
Genset Hire	20,000	-	(20,000)	-100%
Annual General Meeting (AGM)	390,000	20,000	(370,000)	-95%
Insurances(Motor vehicles & Motorbikes)	500,000	139,872	(360,128)	-72%
Top up Allowance	1,500,000	574,228	(925,772)	-62%
Office expenses	170,400	70,449	(99,951)	-59%
Repair & maintenance of Computers (soft ware & hardware) And computer Consumables	450,000	205,451	(244,549)	-54%
Entertainment	1,000,000	541,831	(458,169)	-46%
Board Expenses	2,594,460	1,444,180	(1,150,280)	-44%
Networking/Internet/Internet connection	400,000	230,652	(169,348)	-42%
Licences/professional fees renewal	646,700	426,100	(220,600)	-34%
Social Responsibility	100,000	66,450	(33,550)	-34%
Telephone & Postage	874,000	614,707	(259,293)	-30%
Staff Travel & Subsistence	3,800,000	2,675,967	(1,124,033)	-30%
Newspaper & periodicals	180,000	129,700	(50,300)	-28%
Chemicals	5,400,000	4,363,559	(1,036,441)	-19%
Motor vehicle Running repairs and maintenance including GK A907	2,539,000	2,084,263	(454,737)	-18%
Rent	34,000	28,000	(6,000)	-18%
SPA and Related Issues	102,000	85,000	(17,000)	-17%
Electricity (Masinga and Others)	80,000,000	68,738,723	(11,261,277)	-14%
1% wasreb	1,100,000	965,486	(134,514)	-12%
Motor Vehicle Running Fuels	5,400,000	4,758,175	(641,825)	-12%
	111,641,560	88,162,793	(23,478,767)	-21%

It was not explained why the under expenditure of Kshs.23,478,767 (see table above) was not appropriated to other priority expenditure items through a supplementary budget to ensure maximum efficiency on the available resource.

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 Board's ability to continue to as a going concern/ sustain services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless the management either intends to liquidate the Board's 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 Board'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. 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.

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 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 the Company to cease as a going concern or to continue 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 the Company to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

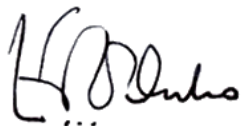
I communicate with the management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

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 REGULATORY REQUIREMENTS

As required by the Companies' Act, I report based on my audit, that:

- 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, adequate accounting records have been kept by the Company, so far as appears from the examination of those records; and,
- The Board's financial statements are in agreement with the accounting records.



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

Nairobi

09 July 2018