

# **REPORT OF THE AUDITOR-GENERAL ON KWALE WATER & SEWERAGE COMPANY 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 Kwale Water & Sewerage Company Limited set out on pages 14 to 30, which comprise statement of financial position as at 30 June 2017, and the statement of profit and loss and other 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 believe, 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 Kwale Water & Sewerage Company 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 the Kenyan Companies Act, 2015.

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 Presentation of Financial Statements**

As reported in the previous year, note 7 to the financial statements on administration expenses includes bank charges and commissions amounting to Kshs.1,366,464 in the comparative figure for the year ended 30 June 2016. However, the International Accounting Standards No. 1 on presentation of financial statements requires finance costs to be presented separately.

In the circumstances, the financial statements do not comply with the requirements of the International Accounting Standards No. 1 on presentation.

#### **2.0 Inaccuracies in the Financial Statements**

As previously reported, the financial statements availed for audit reflected the following inaccuracies in the comparative figures for the year ended 30 June 2016;

2.1. The cash flow statement includes an amount of Kshs.10,294,916 as cash outflow for purchase of property plant and equipment, out of which Kshs.3,960,000 was not an actual cash flow as indicated in note 8 to the financial statements on additions to motor vehicles.

2.2. Note 3 to the financial statements for the year ended 30 June 2016 reflects revenue of Kshs.124,544,115. However, the casted figure is Kshs.124,547,115 resulting to unexplained nor reconciled variance of Kshs.3,000.

As a result, the accuracy and completeness of the comparative figures for the financial statements for the year ended 30 June 2017 could not be confirmed.

### **3.0 Going Concern**

The Company recorded a profit of Kshs.3,688,040 for the year ended 30 June 2017. However, the total current liabilities of Kshs.188,728,624 exceeded the total current assets of Kshs.173,364,817 resulting to a negative working capital of Kshs.15,363,807. Further, the accumulated revenue reserve as at 30 June 2017 was a deficit of Kshs.43,799,411. This is an indication that the Kwale Water & Sewerage Company Limited may not be able to settle its obligation as and when they fall due. Therefore, the Kwale Water & Sewerage Company Limited's going concern assumption is threatened and its continued existence depends on continued financial support by its creditors and bankers.

### **4.0 Non-Current Assets**

#### **4.1 Assets Register**

As reported in the previous year, included in the property, plant and equipment balance of Kshs.26,816,663 is Kshs.16,316,440 worth of assets acquired during the year. The asset register availed for audit had neither values nor date which the assets were acquired.

In the absence of up to date fixed assets register, the accuracy of the non-current assets totaling to Kshs.26,816,663 as at 30 June 2017 could not be confirmed.

#### **4.2 Purchase of Motor Vehicle**

As reported in the previous year, included in the property, plant and equipment of Kshs.26,816,663 as at 30 June 2017 is Kshs.2,475,000 net book value and a cost price of Kshs.4,950,000 relating to a motor vehicle (Ford Ranger XLT) acquired by

the Kwale Water & Sewerage Company Limited through asset financing from a bank at a cost of Kshs.3,960,000 and the balance of Kshs.990,000 paid by the Kwale Water & Sewerage Company Limited. A motor vehicle company was awarded a contract to supply the vehicle which was delivered on 31 January 2016. However, the asset financing arrangement with the Bank did not materialize resulting to the vehicle being repossessed by the supplier for non-payment of Kshs.3,960,000 despite the fact that Kwale Water & Sewerage Company Limited had paid a down payment of Kshs.1,490,000 (Kshs.990,000 in the year 2015/2016 and Kshs.500,000 in the year 2016/2017). The unpaid amount stood at Kshs.3,460,000 as at 30 June 2017.

Under the circumstance, it was not possible to confirm the accuracy and existence of the property, plant and equipment of Kshs.26,816,663 as at 30 June 2017.

#### **4.3 Water Meters**

As reported in the previous year, the Company received water meters worth Kshs.1,455,000 from the County of Kwale. However, it is not clear how the meters were accounted for in these financial statements.

Consequently, the accuracy and completeness of the property, plant and equipment balance of Kshs.26,816,663 as at 30 June 2017 could not be confirmed.

#### **5.0 Trade and Other Receivables**

As reported in the previous year, the statement of financial position reflects a balance of Kshs.165,428,518 in respect of trade and other receivables as at 30 June 2017. Included in the trade and other receivables balance is Kshs.354,948 staff imprests and Kshs.545,703 staff debtors. These amounts have been outstanding for a very long time and there was no evidence that the management has made efforts to recover the same.

Consequently, the recoverability of trade and other receivable balance of Kshs.165,428,518 as at 30 June 2017 could not be confirmed.

#### **Non-Current Liabilities**

As reported in the previous year, the statement of financial position reflects an amount of Kshs.10,711,101 in respect of customer deposit as at 30 June 2017. This is an increase by Kshs.1,873,700 compared with a balance of Kshs.8,837,401 as at 30 June 2016. However, records availed for audit review reflects a customer deposit balance of Kshs.1,259,772 resulting to unexplained variance of Kshs.9,451,329.

Consequently, it was no possible to ascertain the accuracy and completeness of the customer deposits balance of Kshs.10,711,101 as at 30 June 2017.

## **6.0 Current Liabilities**

### **6.1 Trade Creditors**

As reported in the previous year, included in the current liabilities of Kshs.188,728,624 is trade creditors of Kshs.135,737,913 as detailed in note 16 to the financial statements. The trade creditors increased from Kshs.114,971,311 as at 30 June 2016 to Kshs.135,737,913. This is an increase by Kshs.21,766,602 representing 18%. Included in the trade creditors is an amount of Kshs.5,000,000 which is an advance from County Government of Kwale. The agreement availed for audit verification indicated that the Kwale Water & Sewerage Company Limited was to settle the debt before the end of financial year 2014/2015. However, as at 30 June 2017 the Kwale Water & Sewerage Company Limited had not settled the advance.

Further, the agency current account in respect of Cost Water Services Board as maintained by the Kwale Water & Sewerage Company Limited has a balance of Kshs.71,876,648 as at 30 June 2017. However, records maintained by the Coast Services Board reflects a figure of Kshs.98,797,985 resulting to unreconciled variance of Kshs.26,921,337.

In addition, the management failed to produce documentary evidence such as invoices to support creditors of Kshs.2,899,907 and Kshs.4,090,210 from two (2) suppliers which have been outstanding since 2014-2015.

Consequently, the accuracy and completeness of trade and other payables balance of Kshs.188,728,624 as at 30 June 2017 could not be confirmed.

### **6.2 Unremitted Statutory Deductions**

As reported in the previous year, the trade and other payables balance of Kshs.188,728,624 as at 30 June 2017, include Kshs.38,765,456 in respect of unremitted NHIF, NSSF and Pay As You Earn as detailed in Note 16 to the financial statements. Non remittance of statutory deduction may lead penalties and litigation which have not been factored in these financial statements.

Consequently, the accuracy and completeness of trade and other payables balance of Kshs 188,728,624 as at 30 June 2017 could not be confirmed.

## **7.0 Non-Revenue Water**

Records availed for audit revealed that during the year under review, Kwale Water & Sewerage Company Limited produced 4,328,623 cubic meters of water for the year ended 30 June 2017. Out of which, only 1,765,090 cubic meters were billed to customers at Kshs.133,020,690. The balance of 2,563,533 cubic meters or

approximately 59% of the total volume represented Unaccounted for Water (UFW). Given the normal allowable loss of 25% of water produced, approximately 1,481,377 cubic meters of the UFW may have resulted to loss of sales estimated at Kshs.111,639,514 as at 30 June 2017.

The significant level of UFW may negatively impact on the Company's profitability and its long term sustainability. Further there is no evidence that the management has put strategies to reverse this trend.

## **8.0 Provision for Doubtful Debts**

The statements of profit and loss and other comprehensive income reflects an amount of Kshs.44,939,582 in respect of administrative costs, out of which Kshs.3,224,116 relates to provision for doubtful debts as detailed in note 7 to the financial statements. Included in the provision for doubtful debts is an amount of Kshs.2,529,709 which relates to amounts that were purported to have been stolen by staff. There is neither evidence that the theft was reported to the police nor any evidence indicating the effort the management is making to fully recover the stolen money.

Under the circumstance, it's not possible to confirm the recoverability of the amount stolen by staff of Ksh.2, 529,709.

## **9.0 Audit Fees**

As reported in the previous year, included in the trade and other payables under note 16 are trade creditors figure of Kshs.135,737,913 out of which Kshs.2,360,000 is an audit fees owed to the Office of the Auditor-General. Further the Company failed to disclose the audit fees balance separately. This is contrary to Section 41 of the Public Audit Act, 2015. As a result, the Company breached the Law.

The audit was conducted in accordance with international Standards of supreme Audit Institutions (ISSAIs). I am independent of Kwale Water and Sewerage 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 requirement applicable to performing audits of financial statements in Kenya. 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 and Other Matter sections of my report, I have determined that there are no key audit matters to communicate in my report.

## Other Matter

### 1.0 Budget Analysis and Performance

#### 1.1 Expenditure

During the year under review the Kwale Water & Sewerage Company Limited had a total expenditure budget of Kshs.164,556,775.00 as summarized below;

Item	Budgeted Amount (Kshs.)	Actual Expenditure (Kshs.)	Under Absorption (Kshs.)	Over Absorption (Kshs.)	Under Absorption (%)	Over Absorption (%)
Staff Costs	43,506,498	50,797,523	-	7,291,025		14.4%
Professional Fees	6,004,500	1,037,875	4,966,625	-	82.7%	
Finance Costs	20,278,817	11,217,537	9,061,280	-	44.7%	
Board Emoluments	5,590,000	2,895,550	2,694,450	-	48.2%	
Operations and Maintenance	59,650,493	60,500,257	-	849,764		1.4%
Administration Costs	20,270,847	21,486,752	-	1,215,905		5.7%
Transport cost	9,255,620	8,301,868	953,752	-	10.3%	
<b>TOTAL</b>	<b>164,556,775</b>	<b>156,237,362</b>	<b>17,676,107</b>	<b>9,356,694</b>	<b>11.3%</b>	<b>5.7%</b>

From the above analysis the Kwale Water & Sewerage Company Limited overspent in three (3) items, however, the management failed to explain the main reason for over absorption. In addition the Kwale Water & Sewerage Company Limited underspent in four items this is an indication that the management may not have delivered the services as expected.

#### 1.2 Income Analysis

The Kwale Water & Sewerage Company Limited had a projected income of Kshs.167,569,485. However, during the year management realized Kshs.133,020,690 as analyzed below;

Item	Budgeted Amount (Kshs.)	Actual Income (Kshs.)	Over (Kshs.)	under (Kshs.)	Over (%)	Under (%)
Income (water sale)	161,030,085	133,020,690		28,009,395		17.4%

Other Incomes	6,539,400	28,485,302	21,945,902		77.0%	
<b>Gross Income</b>	<b>167,569,485</b>	<b>161,505,992</b>	<b>21,945,902</b>	<b>28,009,395</b>	<b>77.0%</b>	<b>17.4%</b>

From the above analysis the Kwale Water & Sewerage Company Limited failed to meet the expected /projected sale of water by Kshs.28,009,375 (17.4%) However, the management has not come up with a strategy for meeting the sales target.

### **Responsibilities of Management’s 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 the International Financial Reporting (IFRS) and for such internal control as management determines is necessary to enable 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 Kwale Water & Sewerage Company Limited’s ability to continue as a going concern disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the management either intends to liquidate the corporation or to cease operations, or have no realistic alternative but to do so.

The 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 Kwale Water & Sewerage Company Limited’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 Kwale Water & Sewerage Company Limited'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 Kwale Water & Sewerage Company Limited'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 Kwale Water & Sewerage Company Limited 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 of the entities or business activities of the Kwale Water & Sewerage Company 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.

## REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Kenya 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; and,
- ii. In my opinion, adequate accounting records have been kept by the Kwale Water & Sewerage Company Limited so far as appears from the examination of those records; and
- iii. The Kwale Water & Sewerage Company Limited's financial statements are in agreement with the accounting records and returns.



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

**Nairobi**

**03 July 2018**