

REPORT OF THE AUDITOR-GENERAL ON LAKE VICTORIA NORTH WATER SERVICES BOARD FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of Lake Victoria North Water Services Board set out on pages 1 to 30, which comprise the statement of financial position as at 30 June 2018, and the statement of financial performance, statement of changes in net assets, 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, 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, the financial position of Lake Victoria North Water Services Board as at 30 June 2018 and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards (Accrual Basis) and do not comply with the State Corporations Act, Cap 446.

Basis for Adverse Opinion

1. Presentation, Disclosure and Accuracy of the Financial Statements

The financial statements submitted for audit do not conform to International Public Sector Accounting Standards (Accrual Basis) as prescribed by the Public Sector Accounting Standards Board due to the following:

1.1 Presentation of Board Information

The Board Chairman has not signed the financial statements presented for audit and no explanation has been provided for the failure by the Board to adopt the financial statements.

In addition, the report of the Chief Executive Officer includes a disclosure of grant from Korea International Cooperation Agency (KOICA) of Kshs.500,000,000 for Chwele Water Project in Bungoma County which has not been disclosed in the financial statements.

Further, the financial statements do not include management discussion and analysis and the Corporate social responsibility statement as required.

1.2 Statement of Financial Performance

The transfers from other governments- gifts and services in kinds figure of Kshs.572,132,005 includes development grants of Kshs.510,232,005 as disclosed under note 5 to the financial statements which however differs with Kshs.578,108,750

as per the records availed for audit and disclosed in Appendix 1, resulting to an unreconciled variance of Kshs.67,876,745.

Management has explained that the development grants figure reported in the statement of financial performance and Note 5 is based on the expenditure of Kshs.590,932,012 incurred from deferred income in Note 25. However, the note shows additional grants received of Kshs.330,701,250 as opposed to the figure of Kshs.578,108,750 reported in appendix 1. No explanation has been provided for the arising variance of Kshs.247,407,500.

1.3 Statement of Financial Position

1.3.1 Property, Plant and Equipment

The property, plant and equipment balance of Kshs.6,009,935,929 excludes the value of land and buildings where the Board offices are housed at KEFINCO estates and no explanation is provided for such omission.

1.3.2 Borrowings

The borrowings balance reflects Kshs.11,415,311,249 as per supporting note 28 to the financial statements. However, the details about the terms of the loans, nature, rates of interest, repayment status and applied securities have not been provided for audit review.

1.3.3 Capital Works in Progress

The capital works in progress balance reflects Kshs.7,160,640,226 as at 30 June 2018 as disclosed under note 22 which in turn includes additional loan of Kshs.729,128,503 to Water Services and Sanitation Improvement Program (WASSIP) project as disclosed in note 22 to the financial statements which however differs with the total expenditure figure of Kshs.586,400,441 together with the pending bills of Kshs.2,018,750 reported in the project financial statements for the year ended 30 June 2018 leading to an unreconciled and unexplained variance of Kshs.140,709,312 arising between the two sets of records.

1.4 The Statement of Cash Flows

The statement of cash flows reflects a non-cash adjustment figure of Kshs.1,799,330. However, the reconciliation explaining how this figure was derived has not been provided for audit review. A similar figure is indicated in the statement of changes in net assets as transfers to/from accumulated surplus but also without a corresponding explanation as to what the transfer relates to and how the figure has affected the two statements. In addition, the statement reflects purchase of property, plant, equipment and intangible assets of Kshs.1,436,127,528; proceeds from borrowing of Kshs.124,390,557 and increase in deposits figure of Kshs.1,361,145,402, which have however not been indicated on how they have been derived as cash flow items.

1.5 The Statement of Comparison of Budget and Actual Amounts

The statement shows total budgeted revenue of Kshs.814,741,005 while the approved budget shows an amount of Kshs.14,528,609,000 to result to variance of Kshs.13,713,867,995. The statement also shows budgeted expenditure of Kshs.1,043,327,201 as compared to the approved budget figure of Kshs.14,827,012,000 to result to a variance of Kshs.13,778,684,799 which has not been explained or reconciled as below:

Description	Approved Budget (Kshs)	Financial Statements (Kshs)	Variance (Kshs)
Total budgeted recurrent revenue	322,609,000	814,741,005	(492,132,005)
Total budgeted development revenue	14,206,000,000	0	14,206,000,000
Total	14,528,609,000	814,741,005	13,713,867,995
Total budgeted recurrent expenditure	621,012,000	1,048,327,201	(427,315,201)
Total budgeted development expenditure	14,206,000,000	0	14,206,000,000
Total	14,827,012,000	1,048,327,201	13,778,684,799

In addition, Korea International Cooperation Agency (KOICA) had a budgetary provision of Kshs.59 million but no expenditure was incurred for this item. No works were also reported on the ADB loan funding notwithstanding the available budget provision of Kshs.10.85 billion for the year under review.

1.6 Other Notes to the Financial Statements

The statement of compliance and basis of preparation is not in line with the financial report. In addition, it does not conform to the revised format recommended by the Public Sector Accounting Standard Board. There is no note on adoption of new and revised standards and disclosure on subsequent events.

The disclosures on credit risk and liquidity risk are incomplete and do not reflect the information in the financial statements. Further, note 30 to the financial statements discloses contingent liability of Kshs.15,000,000. However, the details of the liability have not been provided or disclosed in the financial statements as required. In addition, there is no disclosure on capital commitments, ultimate and holding entity information, and progress on follow-up of auditor recommendations is incomplete. Further, there is no report on projects implemented by the Board during the year under review.

1.7 Accounts of Water Services and Sanitation Improvement Project

The audit of the financial statements of the Water Services and Sanitation Improvement Project indicated that the Project received a total of Kshs.577,421,000 from IDA as disbursements towards implementation of the Project while the special

account statement showed that there was no withdrawal from the account for the year under review and no reconciliation was provided to explain the variation in the two sets of records.

In view of the non-conformance to the prescribed format, the variances observed and non-disclosures of material items/activities, the accuracy and completeness of the financial statements for the year ended 30 June 2018 cannot be confirmed.

2. Long Term Borrowings - Non-Servicing of Loans

The statement of financial position reflects borrowings figure of Kshs.11,415,311,249 under non-current liabilities being principal loan balances of Kshs.4,854,726,700 from German Financial Cooperation (KfW), Kshs.5,910,862,190 from International Development Association (IDA) and Kshs.603,105,047 from the Belgian Government as disclosed in note 26 to the financial statements.

The loan agreements for KfW showed that three (3) loans signed on 23 September 2004, 27 November 2006 and 04 June 2009 of EURO9,500,000, EURO9,500,000 and SDR96,600,000 respectively have never been serviced and repayment instalments are in arrears as detailed below:

No.	Date of Signing Agreement	Lending Agency	Amount Borrowed EUR/SDR	Date of 1 st Instalment	Total Principal Instalments Due in EUR/SDR	Total Principal Instalments in (Kshs)
1	23 Sept 2004	KfW	EUR 9,500,000	Dec. 2014	1,422,000	163,819,567
2	27 Nov 2006	KfW	EUR 9,500,000	Dec.2016	775,000	91,876,452
3	4 June 2008	KfW	SDR 96,600,000	Dec. 2018	466,000	652,400
Total						256,348,419

The principal amounts due had accumulated to Kshs.256,348419 by 31 December 2018 but have not been recognised under current liabilities. In addition, the accrued interest and penalties have not been calculated and accounted for in the financial statements as required.

In addition, the loans are denominated in foreign currency (EUR, SDR and USD) but the management has not disclosed the exchange rate used in the conversion in the financial statements.

Further, the Belgian Government loan agreement was not availed for audit verification hence the terms and conditions of the loan could not be ascertained.

Consequently, the expenditure for the year under review has been understated by the accrued interest and penalties. Further, the current liabilities have been understated by the same amount of accrued interest and penalties.

3. Classification and Disclosure of Capital Works in Progress

The statement of financial position reflects non-current assets balance of Kshs.13,170,576,155 as at 30 June 2018 which includes capital works in progress amount of Kshs.7,160,640,225 as analysed under note 22 and shown below:

	2016/17	2017/18	Total
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Category	(Kshs)	(Kshs)	(Kshs)
Water and Sanitation Services Improvement Project (WASSIP)	5,515,799,571	729,128,503	6,244,928,074
Kenya Italy Debt Development Programme (KIDDP)	223,398,762	(223,398,762)	0
Pans and Dams	444,949,947	(133,112,543)	311,837,404
Chebara Institutions	0	330,800	330,800
Vihiga Cluster	0	603,543,947	603,543,947
Total	6,184,148,280	976,491,945	7,160,640,225

However, apart from the Chebara institutions and Vihiga cluster projects, the detailed schedules for the specific projects which are said to be on-going under Water and Sanitation Services Improvement Project (WASSIP) and Kenya Italy Debt Development Programme (KIDDP) were not availed for audit review.

In the circumstances the capital works in progress figure of Kshs.7,160,640,225 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 Lake Victoria North Water Services Board 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 matters described in the Basis for Adverse Opinion section, I have determined that there are no other key audit matters to communicate in my report.

Other Matter

Water Services and Sanitation Improvement Project - Implementation Status

As at 30 June 2018, the Water Services and Sanitation Improvement Project had received USD31,746,678 (Kshs.3,130,426,998) which is 86% of the envisioned funding of USD35,912,500 (Kshs.3,630,832,758). However, the management did not provide project implementation status to confirm the implementation level.

Consequently, it has not been possible to confirm that the project is on course.

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 matters discussed in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section of my report, based on the audit procedures performed, I confirm that public resources have not been applied lawfully and in an effective way.

Basis for Conclusion

1. Avoidable Expenditure

The Board appointed an officer on 22 August 2012 to the position of Water Services Provision Manager through a competitive recruitment process and was engaged on probationary terms for a period of six (6) months after which the Board was expected to communicate to the officer its decision on his suitability for the job. However, no communication was made until 19 May 2014, about twenty (20) months later, when he was informed vide letter reference LVNWSB, that his engagement had been terminated on suspicion that he did not disclose all material facts about himself and was likely to continue drawing two salaries if confirmed which was contrary to Employment Act, Cap 226 section 42 (2 & 3) and section B.16 (4&5) of the Public Service Commission Human Resource Policy.

The officer consequently filed a case against the Board on 09 June 2014 at the Employment & Labour Relations Court in Kisumu contesting the termination of employment. On 2 March 2016, the Court ruled in favour of the officer and ordered his reinstatement and compensation for the period he should have been in employment. The Board filed an appeal in the Court of Appeal but later withdrew the case opting for an out of court settlement.

The Board Management therefore committed and paid an amount of Kshs.2,170,842 being salary and allowances for the affected officer for the period he was out of office of Kshs.1,271,242, his legal fees of Kshs.200,000 and the board's legal fees of Kshs.699,600. The expenditure of Kshs.2,170,842 was avoidable and amounts to nugatory payment.

2. Irregular Payment for Consultancy Services

The statement of financial performance reflects an expenditure of Kshs.18,551,809 under repairs and maintenance which includes Kshs.1,785,000 incurred on consultancy services to assess the current position of the Board Club House at Kefinco Estate in Kakamega, prepare bid documents and supervise the rehabilitation works of the Club House. The consultancy was awarded vide contract reference No. LVNWSB/ICS/KEFINCO/2016/01 at a contract price of Kshs.3,570,000. The contract was signed on 8 January 2016 and was to take a total of nine (9) months or two hundred and seventy (270) days with a completion date of October 2016. However, by the time of audit in January 2019, the consultancy report had not been submitted, including the inception report which was expected to have been submitted by 16 May 2016. According to the consultancy agreement, the consultant was to be paid ten percent (10%) of contract sum on submission of inception report; twenty percent (20%) on each of four (4) phases, namely presentation of report on the status of

ownership/title of the Club House; completion of report on the condition of the facility and reinstatement/rehabilitation needs assessment; submission of report on approved design of the proposed facility, bid document for rehabilitation works and a confidential engineer's estimate and submission of a supervision report on the rehabilitation works; further ten percent (10%) on submission of as-built drawings and works completing report.

During the year, the Board received and processed claims from the consultant amounting to Kshs.2,499,000 which is 75% of the contract sum; out of which Kshs.1,785,000 was paid and Kshs.714,000 accrued worth. However, no reason has been provided for processing the claims without evidence of delivery of the consultancy service in line with the contract agreement. In addition, no reason has been provided for the delay in delivering of the consultancy by 27 months or 300% of the contract period.

Further, it was noted that this Club House as an asset of the Board had not been recorded in the assets register nor included in the property, plant and equipment figure of Kshs.5,617,314,642 reflected in the statement of financial position as at 30 June 2018.

In addition, the management did not explain nor provide evidence of ownership of the Club House that was previously the property of Kenya Finland Cooperation (KEFINCO).

Consequently, the propriety of the repairs and maintenance expenditure of Kshs.2,499,000 incurred on consultancy for the Club House could not be ascertained.

3. Rural Water Supply Development - Project Implementation Status

The statement of financial performance reflects expenditure on rural water supply development of Kshs.480,015,632 during the year under review. However, a sample verification of these projects revealed that they were not being implemented as per the terms of the contracts in regard to designs, contract periods, costs and good workmanship.

Procurement of contractors for the projects was not competitively done. The works were not monitored, leading to delays in project implementation and wastage through poor workmanship. The communities intended to benefit from the projects had also not been adequately sensitized and guided appropriately, hence many projects had operational challenges. A summary of the sampled projects is provided:

Project Name and Value (Kshs.)	Expenditure in 2017/2018 (Kshs.)	Observations
Sirare Mayu Community Water Project - Kshs.14,397,571	11,328,212	The project was not operational due to low levels of water in the borehole that was commissioned in March 2018. when the yielded was indicated to be 7.2m ³ /hr at test pumping although no report has been provided to confirm the current water levels.

Project Name and Value (Kshs.)	Expenditure in 2017/2018 (Kshs.)	Observations
Tachasis-Cheplaskei Community Water Project - Kshs.25,572,376	0	<p>The contract was awarded on 23 September 2016. As at the time of audit in Jan 2019, the project was still not operational having delayed for more than one year six months.</p> <p>The bills of quantities provided for fencing of the three spring areas using precast concrete poles, but this was done using wooden poles.</p> <p>It was also noted that one of the masonry tanks had cracks and leakages which is a sign of poor workmanship. Further the innovative low cost tank is not being supplied with water since it is located at a higher altitude from the intake thus it needs pumping in order to supply water to the tank for distribution. This appears to be as a result of lack of provision of a pump to lift the water from the spring to the tank.</p> <p>One tank completed by the contractor was condemned but no information to confirm how much had been incurred on the tank. A solar panel for the project had also been vandalised, before the project is operationalized.</p>
Leseru Community Water project - Kshs.56,351,411 (KIDDIP)	34,296,478	<p>The project was awarded on 20 June 2016 and was to be completed on 20 June 2017. As at the time of audit in January 2019, the project was still not operational having delayed for more than one and half years.</p> <p>Management reported that the project also had a condemned tank, now being constructed by the Board.</p> <p>It was also noted that the spillway has not been done as provided for in the bills of quantities and also no fencing of the intake and water treatment plant had been done.</p>
Lumakanda - Kipkaren community water supply - Kshs.34,728,435	13,229,710	<p>A contract for rehabilitation and extension of this water project was awarded to local contractor on 11 October 2017 for a contract period of eight months and be completed on 11 June 2018.</p> <p>At the time of audit in January 2019, the works were ongoing. However, there were major cracks and leakages in the two composite filtration units (CFU) serving the water supply system.</p> <p>The leakages is a sign of poor workmanship.</p>

Project Name and Value (Kshs.)	Expenditure in 2017/2018 (Kshs.)	Observations
Masaba-Wabukhonyi Community Water supply Kshs.17,758,293	0	The contract was awarded on 18 April 2016. Most of the works such as spring protection, construction of masonry tank, construction of elevated steel tank, pipping work and installation of pump and electrification of the system had been done. However, the water distribution lines from the distribution tank had not been done thus rendering the project none operational since October 2016 which was the expected completion date. Even though the Board has indicated that a new contractor has been engaged to complete the works at a cost of Kshs.1,997,814, there is no evidence of how much of the previous works had been certified and paid for. Further, there is no evidence of termination of the previous contractor.
Lunakwe Community Water Supply - Kshs. 23,608,121	9,781,070	The contract for construction was awarded on 15 Sep 2017 with the expected completion date being 15 March 2018. A physical verification of the project revealed the following; <ul style="list-style-type: none"> • Elevated steel tank was still under construction • 3no. water kiosks were partially complete with painting work yet to be done • Pipe laying was not yet complete • Installation of submersible pump not yet done • Solar panels fitted but other accessories were yet to be installed. Notice to terminate the contract had subsequently been issued.
Shianda - Community Water project - Kshs.7,616,290	3,939,574	The contract was awarded for construction of the project on 8 Nov 2017 with expected completion date being 8 May 2018. A physical verification of the project revealed the following; <ul style="list-style-type: none"> • 50m³ steel tank not yet done • 1no. water kiosk partially complete with painting work yet to be done • Pipe laying complete • New contractor hired to move on site. The contract has subsequently been terminated and two new contracts awarded for the remaining works. One of the new contracts for construction of 50m ³ elevated steel tank at a cost of

Project Name and Value (Kshs.)	Expenditure in 2017/2018 (Kshs.)	Observations
		Kshs.2,895,000 while the other contract has not been disclosed.
Sokyot Community Water Project, Turbo Sub County, Uasin Gishu County – Kshs.15,480,256	10,303,593	The project was expected to be completed by 28 February 2018. Verification revealed that the 100 cubic meters elevated steel tank was leaking; fencing not fully done; connection to the distribution line not done; no pump manual; client equipment purchased not seen. The community, (about 118,000 people) have not been supplied with water.
Sambut Community Water Project, Turbo Sub County, Uasin Gishu County – Kshs.8,911,815	3,993,975	100 cubic meters elevated steel tank supplied but raising main not connected to the tank; fencing only concrete posts done; distribution line not done and therefore the community has no water. Expected completion date was 10 October 2018
Samoei Community Water Project, Turbo Sub County, Uasin Gishu County – Kshs.7,528,994	103,800	100 cubic meters elevated steel tank supplied but panels are not properly locked; chambers not complete, have no gate valves; All pipes laying done but not connected to the tank; Community has no water. Expected completion date was 10 October 2018
Illula Community Water Project, Ainabkoi Sub County, Uasin Gishu County – Kshs.13,464,000	3,402,000	Community committee had not been formed by the time the project started; pump house constructed; solar powered pump installed; upraising connected; piping laid for 4.3 km out of 5 km; water noted to be muddy and brown and may not be suitable for human consumption. The project was to be complete by 10 March 2018
Kipture Community Water Project, Mosop Sub County, Nandi County	6,836,135	Spring protected; polythene cover allows silting; no community water drawing point on site; pump manual not availed to the community; 1 out of 4 kiosks not working due to failure of gravity to deliver water upstream; no sanitation facilities at the site; return valve not installed in the uptake line; main tank 100 cubic meters masonry has minor leakages.
Chemaluk Community Water Project, Moiben Sub County, Uasin Gishu County – Kshs.8,385,828	5,600,200	Community has piped water from ELDOWAS; Solar powered project pumping to a 100 cubic meter tank; Water said to be salty and therefore not confirmed for human consumption; Kiosks are not popular; only 5 connections. Project completion date was 5 September 2018
Tebeswet Community Water	1,586,600	Tank 24 cubic meters elevated steel tank delivered; Solar powered pump installed; kiosk not

Project Name and Value (Kshs.)	Expenditure in 2017/2018 (Kshs.)	Observations
Project – Kshs.9,868,320		operational; training not done; low water levels; Water slightly saline. Completion date was 28 September 2018
Cheburbur Community Water Project – Kshs.8,987,000	5,504,225	Pump house constructed; solar powered pump installed; upraising connected; Piping laid for 3 km; Water noted to be brown hence not suitable for consumption. Completion expected to have been 16 October 2018
Kapseret Community Water Project	1,040,600	Borehole sank in 2017 still capped; foundation for steel tank elevation started and abandoned; Variations proposed to drop the kiosk.
Jabali Community Water Supply Project	5,784,748	Poor workmanship
Total	116,730,920	

Non-completion of the community water projects is an indication that the Board failed to develop, maintain and manage water and sanitation infrastructure for increased provision of adequate, safe and affordable water services to the affected communities as stated in its mission statement. The beneficiary communities did therefore not obtain value for Kshs.116,730,920 incurred on the above water projects for the year ended 30 June 2018.

4. Procurement of Enterprise Resource Planner (ERP) System

The Board entered into a contract on 1 July 2015 with a business systems supplier for supply, delivery, installation, configuration and commissioning of an Enterprise Resource Planner (ERP) system (both software and professional charges) at a contract sum of Kshs.6,900,000. The supplier offered Sage 300 software which, according to the technical specifications included capability for HR administration, general ledger, report writing and system audit management. The system implementation should have been completed and handed over to the management by 30 June 2016. However, a review of the ERP System in December 2018 revealed the following:

- (i) The system was formally taken over by the Board in June 2017 about 52 weeks after the expiry of the contract period.
- (ii) The contractor had not fully delivered on contract obligations as components of the system on workflow and integration of payroll to the financial module had not been implemented.
- (iii) The system could not generate backdated payroll data, consolidated general ledger or other analytical data summaries.

- (iv) The contract included support to four (4) service providers Nzoia Water Services Company (NZOWASCO), Kakamega Water Services Company (KACWASCO), Kapsabet-Nandi Water Services Company (KANAWASCO) and Amatsi Water Services Company (AWASCO) whose project implementation status reports were not provided for audit verification.
- (v) The professional fee charged in the contract of Kshs.3,200,000 could not be ascertained as there were no details of the methodology used to determine the cost or how performance of the service would be evaluated/regulated before payment.
- (vi) The contract did not specify any required periodic health checks or audit reports to be generated under the audit management module.
- (vii) The Board maintained three (3) standalone systems as listed below:

Application Name	Description and Purpose of the Application	Modules/subsystems of Application Used
Docuware	For digitalization of documents	For documenting all the whole organization documents
Fleet Management system	To manage the board fleet-fuel consumption and tracking of motor vehicles and analysis of trips	Fleet Management
Leave management system	For managing staff leave	Staff leave

The use of these standalone systems is due to the Sage 300 ERP System not having been fully integrated and suffers from operational and design deficiencies contrary to what was envisioned at procurement. It was anticipated that the ERP was to improve management and administration by phasing out these standalone systems by housing all the system activities in the new ERP.

- (viii) Further, it was also noted that the performance bond issued by Chase Bank (Kenya) Limited expired in December 2015, six (6) months into the contract period thereby leaving the Board exposed to risks of non-performance without recourse.

In the circumstances, the propriety of the expenditure of Kshs.5,327,920 or approximately 77% out of the contract price incurred on the acquisition of the ERP system for the year ended 30 June 2018 cannot be confirmed. Further, the acquired ERP was not suitable for all the needs of the Board and therefore the Board did not get value for money spent on it.

5. Work in Progress

5.1 Vihiga Cluster Water Project

The Government of the Republic of Kenya and a Belgian company negotiated for a mixed credit facility from the Government of the Kingdom of Belgium amounting to EURO.15,500,000 which was to be utilized for the purpose of financing Vihiga Cluster Water Supply Project. The contract for the construction was signed on 09 February 2016 and was to take 30 months from the effective date of commencement. The project was to be implemented on the “design, fund and build model” and consisted of three main parts namely Maseno Water Supply System, Kaimosi Water Supply System and Mbale Water Supply System. A review of the project implementation status as at the time of audit revealed the following:

- (i) The capital works in progress figure of Kshs.7,160,640,226 includes additions during 2017/2018 amount of Kshs.603,543,947 as disclosed in note 22 to the financial statements paid to the contractor during the year. However, there was no evidence/documentation of the direct payment of Kshs.603,543,947, an indication that the payment was processed outside the payment processing system stipulated by the National Treasury and communicated to the Board vide Circular Ref No. MOF/ERD/11/149/78/01(36) of 07 June 2017.
- (ii) Part of the expenditure journalized in Kshs.603,543,947 of Kshs.107,370,113 (Euro 853,647) described as project management and logistics was not supported with any documentary evidence and therefore not verified.
- (iii) Further examination of the records including the initial project design and contract agreement indicates that the project was conceived sometimes during the 2012/2013 financial year but did not materialize until 2015/2016 when the funding was secured and the contractor identified and eventually a contract agreement signed on 09 February 2016 at a contract sum of Euro 15.5 million or Kshs.1,755,619,900 at the ruling then exchange rate of Kshs.113.27 to the Euro. This project was two-fold according to the procurement manual for works, as it was a lump-sum contract with bills of quantities as described under Chapter 6.1 (Lump Sum or Fixed Sum Contracts) and 6.2 (Bill of Quantities Contracts).
- (iv) As required under the Kenya law, the contractor was to provide a performance bond but it was noted that the performance warranty provided from the Commerzbank Brussels for Euro 775,000 was to be governed by laws of Belgium although Article 14 of the contract states that the law governing the contract shall be the laws of Kenya.
- (v) The project entailed construction of water treatment plants in Maseno and Mbale with a daily treatment capacity of 5,000 cubic meters; and another one of half capacity at Kaimosi. However, during the course of the implementation, the project was significantly changed but the Board did not avail the revised bills of quantities for each of these works together with the relevant approvals. The basis of evaluation of performance for the project could not therefore be

ascertained. Although the Board explained that under the 'design build contract' the client only provides the requirements of the works in summarised form and then the contractor designs the works with detailed bills of quantities, the client should retain the right of final approval of the designs before the works are implemented.

- (vi) Based on the bills of quantities contained in the original project design document, the contractor was to supply 2,659 water meters valued at Kshs.23,290,000. It was however noted that the contractor was allowed to provide non-branded water meters without boxes, which would be difficult to verify the supplies. Although the Board has averred that the meters are yet to be approved and supplied, no reason has been provided for the decision to procure non-branded meters.
- (vii) Included in the approved master list ref. DFN 415/232/011 of 17 January 2018, were 2No. 4 WD station wagon vehicles valued at Euro 300,000 or Kshs.37,733,430 which were not in the original project design. According to the contract agreement, only three (3) project vehicles were provided for i.e. 2No. 4WD double cabins and 1No. 10-ton truck at a total cost of Euros 220,000 or Kshs.27,671,182. However, management did not provided justification for the additional two vehicles after considering that Treasury had already approved their importation duty free. Although the three vehicles ought to have been delivered at the commencement of the contract, only one double cabin pick-up 4WD had been delivered but registered in the name of the site manager- an employee of the contractor and not the Board.
- (viii) The project allowed for a provision in the contract at Kshs.30,631,188.12 for land wayleaves for pipeline routes including cadastral surveys and title deeds. No details were however provided in respect to the Resettlement Action Plan (RAP) or the associated expenditure disclosed anywhere in the financial records. It was also noted that no RAP Policy had been developed to guide the process. The Board indicated that they were in the process of developing a RAP policy, but this is unlikely to benefit the implementation of the project that ought to have been completed had it been run as per the project schedule.
- (ix) Verification of the project implementation revealed that a number of changes qualifying as variations were made but no detailed recording of these variations were made or any orders prepared for the omissions or additions and their associated costs so that evaluation can be objectively undertaken and the financial implications on the project clearly identified. Some of the changes included;
 - Omission of two Hydro Electric Power Stations of 1.0 megawatts each initially valued at Kshs.520,000,000 at Maseno and Kaimosi plants,
 - New lay out of the water treatment plants; Maseno treatment plant lagoons were reduced in size,

- Land acquisition at Mbale treatment plant,
- National Construction Authority project fees estimated at 0.05% of the project cost,
- Omission of general clearance of 12,500 square meters to a depth of 4 meters at Kaimosi Dam initially estimated to cost Kshs.100,000,000,
- Contingencies were revised from Kshs.205,655,718 or 15% to Kshs.92,836,187 equivalent to 5% of the contract sum,
- Ground breaking ceremony expenses charged against contingencies,
- Allowance for project meetings charged at Kshs.210,000 monthly for 36 months,
- Increase in piping by 4 kilometers,
- Refurbishment of elevated steel tank at Mbale Hospital at Euro 41,071.03 or Kshs.4,585,327.

From the foregoing, it is evident that the feasibility and designs were not collaborated well with the mechanical, electrical and plumbing works. Further, the bulk of these changes were omissions and no particulars were provided on how the planned expenditure was utilized and no variation orders were availed for audit review.

- (x) The project site supervisor was noted to be an electro-mechanical engineer instead of qualified civil engineer thus without capacity to handle civil works and is therefore not clear who was technically supervising the engaged sub-contractor or why the client has not enforced the staffing requirement of having a civil engineer.
- (xi) The contractor's staff levels showed that there were only two members of staff, a manager based in Nairobi and a specialist electro-mechanical engineer who was also the site supervisor. With this type of arrangement and given the value of the contract, the contractor is more of a consultant supervising implementation of the works, having delegated all the works through sub-contracting, yet he was awarded due to the capacity which has not been matched on the ground. This is despite an indication that due diligence was undertaken to assess the capacity.

Under the circumstances, the objectives of the project may not be achieved and the propriety of Kshs.603,543,947 so far incurred on the project for the year under ended 30 June 2019 cannot be confirmed.

5.2 Chebara Institutions Project

Included under work in progress balance in respect to Kenya Italy Debt for Development Programme (KIDDP) is an expenditure of Kshs.330,800 during the year under review in preparation of bids for the completion of Chebara Institutions works that stalled. The stalled works were noted to have been outstanding and were a carry-over since 2012/2013 when the idea of the institutions was conceptualized. The projects had received funding totalling Kshs.631,513,966 from the National Government through various ministries and channelled directly to Chebara Boys High School. The contracts for the projects execution commenced from January 2012 and were expected to be completed in August 2013. However, the implementation of the projects was abandoned at different levels of completion due to lack of funding. The Board placed an advert inviting bids to tender for 3 main works in two local dailies on 05 June 2018 for;

- (i) Proposed completion of Chebara Boys' High School classrooms, administration block, laboratory, library, and the roofing of Chebara Chapel and associated works under tender No. LVNWSB/GoK/EMC/01/2017-18;
- (ii) Proposed completion of Chebara Girls' High School dormitory, ablution block, roofing of dining hall, Chebara Youth Polytechnic fence, gate house, and guard house and associated works under tender No. LVNWSB/GoK/EMC/02/2017-18;
- (iii) Construction of Chebara institutions water supply and associated works under tender No. LVNWSB/GoK/EMC/03/2017-18.

The tenders were opened and evaluated but were later cancelled on grounds of pending cases in court from former contractors. It was particularly noted that the status of these institutions projects were known and details were with the Board from whose records the bids were generated. It was not therefore clear why the Board advertised and later terminated the process. Information available indicates that the Board received funding of Kshs.77,500,000 from the Ministry of Water and Irrigation to complete the stalled Chebara Institutions projects during the 2015/2016 financial year. According to the correspondence between the Ministry and the Board Ref No.WD/3/3/1294/VOL.IV (18) dated 25 January 2017, the funds were to be retained in the bank account until some pending issues involving beneficiaries/stakeholders be resolved before implementation can continue.

However, the management went ahead with the procurement process to complete the projects without taking into consideration of the findings and recommendations of the Auditor-General on the status of the projects which was communicated vide letter reference No. LVNWSB/CORPS/INSP/1/ (53) dated 26 August 2016.

The expenditure of Kshs.330,800 incurred on advertising therefore was avoidable and amounts a nugatory payment. In addition, the cancellation of the procurement process, will result to delayed implementation of the projects thus denying the citizens

of Elgeyo Marakwet County benefits that would have accrued from the projects if completed and may also lead to projects' cost escalation.

5.3 WASSIP Projects Report

5.3.1 Kishermuruak Water Project

Contrary to provisions of Section 5 of the Water Act, 2016, which requires that every resource be vested in and held by the National Government in trust for the people of Kenya, the Rift Valley Water Services Board and the project accounting officer are yet to secure the site of Kishermuruak water resource. Even though a consent (Deed of Gift) was signed between the land owner and the Kishermuruak Community, the Project Manager has not followed up and acquired ownership of the site on which the project is located. Further, It was also noted that item No.3.5.4 in the bills of quantities (supply and installation of reverse osmosis treatment plant) costing Kshs.4,000,000 has not been implemented to date, more than one and half years after the end of the expected completion date which is indicated in the project contract document as 24 March 2017 .

5.3.2 Kongelai and Kasepa Boreholes

Kongelai borehole was sunk to a depth of 140 meters deep and capped on 27 November 2014 with a tested yield of one (1) cubic meter per hour as indicated in the test pumping report. The borehole works were completed and handed over on 18 September 2017 or about 3 years after sinking. However, the borehole completion report indicated that the yield rate of 1 cubic meters per hour was not achieved and instead the borehole returned a lower rate of 0.4 cubic meters per hour. The Project Management have attributed the reduction in the rate to the long period taken before equipping the borehole thus casting doubt on the long-term viability of the borehole. In addition, Kasepa borehole that was sunk to a depth of 120 meters and capped on 12 December 2014 with a tested yield of 3 cubic meters per hour as indicated in the test pumping report was noted to be 98m instead of 120m as indicated in the borehole completion report resulting to a shortfall of 22 metres. Further the yield rate was found to be 0.29 cubic meters per hour which is too low to allow any motorized pumping. The variation between the test pumping reports and the boreholes completion reports means the projects did not achieve the intended objectives leading to loss of public funds.

5.3.3 Liter Water Project

Liter Water Supply Project was undertaken within the compound of Liter Girls High School in Elgeyo Marakwet County. The drilling of the borehole, equipping and civil works were done during the year under review and previous financial years. As at time of audit, all the structures as per the bills of quantities were complete. However, the water supply was not in use since the water was said to be too saline and unfit for human consumption as per the testimonies of the school administration who were the intended beneficiaries of the project. The school principal indicated that they would

have preferred the development at another source of water preferably a spring where they get their current supply of water, had their views been sought. The supervision and implementation of the project may have been poor as the salinity of the water should have been detected at the time of test pumping before the equipping of the borehole begun which could have seen the project save Kshs.7,961,200 which was applied towards equipping of the borehole whose water cannot be used.

5.3.4 Kapcherop Water Supply

Kapcherop Water Supply was undertaken at a contract price of Kshs.114,586,833 with Kshs.14,254,490 having been paid during the year under review and a final completion certificate issued on 6 June 2018. During an audit visit to the project site in October 2018, it was observed that the project was not operational for more than three months as a result of clogging of the intake caused by siltation. The siltation has been occasioned by soil erosion around the intake area, which would have been avoided had a proper feasibility study of the location of the intake been done and the project designs considered the risks of the topography of the site. This view is corroborated by a report of the project technical team which reviewed the status of substantial completion on 19 October 2017. The audit report noted that environmental and water quality issues were not taken into account during feasibility study, preliminary and detailed design and implementation process to ensure issues pertaining to water quality, health and safety are well captured and implemented. The report concluded that in its current state the water project cannot meet the intended purpose of provision of adequate, quality and affordable water as per the Board's mandate and community expectation.

The contractor was subsequently discharged from site by issue of a final completion certificate on 6 June 2018 without having further evaluation of the project to ensure that the issues raised in the report had been attended to.

In view of the unsatisfactory matters noted above, it has not been possible to confirm that the projects achieved the intended objectives of providing clean and affordable drinking water.

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 matters discussed in the Report on Effectiveness of Internal

Controls, Risk Management and Governance and Basis for Adverse Opinion section of my report, based on the audit procedures performed, I confirm that internal controls, risk management and governance were not effective.

Basis for Conclusion

Irregular Deployment on Acting Capacity

Audit review of the human resource records and Board minutes revealed that since 12 January 2017 when the Board of Directors suspended the then Chief Executive Officer, the Board has not filled the position but has successively appointed two serving officers in acting capacity to date. One officer served from the time of suspension of the CEO in January 2017 to April 2018 (approximately 14 months) while the second has served from April 2018 to the time of audit (May 2019) (approximately 13 months). This is contrary to Section 34 (3) of the Public Service Commission Act, 2017 which stipulates that an officer may be appointed in an acting capacity for a period of at least thirty days but not exceeding a period of six months. The appointment of the officers to such key position of the Board on acting terms for long periods of time has an effect of compromising the decision-making capacity of the officers and consequently the internal control environment in the Board.

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.

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 Public Sector Accounting 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 Board'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 Board 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 Board'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 Board's policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional scepticism 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 Board'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 Board 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 the Board 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

26 August 2019