

# **REPORT OF THE AUDITOR-GENERAL ON MIGORI WATER AND SANITATION COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE 2018**

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## **REPORT ON THE FINANCIAL STATEMENTS**

### **Qualified Opinion**

I have audited the accompanying financial statements of Migori Water and Sanitation Company Limited set out on pages 20 to 51, which comprise the statement of financial position as at 30 June 2018, and the statement comprehensive income, statement of changes in equity, statement of cash flows and statement of comparison of budget and actual amounts for the year then ended, and a summary of significant accounting policies and other explanatory information in accordance with the provisions of Article 229 of the Constitution of Kenya and Section 35 of the Public Audit Act, 2015. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit

In my opinion, except for the effects 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 Migori Water and sanitation Company Limited as at 30 June 2018, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Kenyan Companies Act, 2015.

### **Basis for Qualified Opinion**

#### **1. Cash and Bank Balances**

The cash and bank balances of Kshs.5,543,183 as at 30 June 2018 comprises the balances held in seven bank accounts and one M-pesa account as disclosed in Note 17 to the financial statements. The management presented in the financial statements the balances indicated in the bank statements instead of the reconciled cash book balances totalling Kshs.5,349,171. As result the cash and bank balances shown in the financial statements have been overstated by Kshs.194,012. In addition, the revenue A/c No. 1106248791 was overdrawn by Kshs.78,417. Consequently, the accuracy and completeness of the cash and cash bank balances could not be confirmed.

#### **2. Trade and Other Receivables**

Included in the trade and other receivables balance of Kshs.26,808,222 are debts totalling Kshs.23,987,929 which have been outstanding for a long period as analyzed below:

<b>Debtor</b>	<b>Description</b>	<b>Amount Kshs</b>	<b>Period Outstanding</b>
Water Sales Revenue	Water Sales	22,994,929	No ageing report
Allaxis Hotel	Exhauster	30,000	10 months
Akidiva Memorial Hospital	Exhauster	72,000	12 months

Sulwe Hotel	Exhauster	35,000	19 months
Rongo University	Exhauster	270,000	1 month
Allaxis Hotel	Water Tanker	30,000	9 months
Sulwe Hotel	Water Tanker	6,000	30 months
Rapogi Boys Secondary School	Water Tanker	24,000	4 months
Migori County Government	Water Tanker	465,000	18 months
Ministry Of Environment	Excavator	61,000	30 months
<b>Total</b>		<b>23,987,929</b>	

The following anomalies were noted:

- i. No ledger account was provided to support the outstanding water sales receivables.
- ii. No ageing analysis and detailed status report of the water sales debtors. No documentary evidence of efforts made to follow up the long outstanding debts, for instance demand notices served to the debtors. in a bid to recover the outstanding debt.

In the circumstances, the completeness, accuracy and recoverability of the trade receivables balance as at 30 June 2018 could not be confirmed.

### 3. Property, Plant and Equipment

Note 24 to the financial statements on property, plant and equipment indicates that the net fixed assets balance increased by Kshs.28,638,269 from Kshs.35,326,442 as at 30 June 2017 to Kshs.63,964,711 as at 30 June 2018. However, the following anomalies were noted:

- i. The Company had not updated its fixed assets register.
- ii. Additions to the fixed assets during the year under review included a total of Kshs.910,300 paid in cash to various members of staff as facilitation to undertake various activities relating to implementation of Uriri Bware water and sanitation project, Kegonga water and sanitation project and Rongo Roisiri water and sanitation project. Further, payment schedules duly signed by the beneficiaries acknowledging receipt of cash, cash sale receipt and/ or documentary evidence in support of the expenditure were not provided for audit review. In addition, this expenditure was of revenue in nature and therefore should not have been capitalized.
- iii. The additions to the fixed assets amounting to Kshs.6,833,651 were not adequately supported with relevant documents such as the minutes of tender evaluation committees, report of inspection and acceptance committees, assets/stores register as evidence that the payments were made for goods received, works done or services rendered.

Consequently, the accuracy and completeness of the fixed assets balance of Kshs.63,964,711 as at 30 June 2018 could not be confirmed.

#### **4. Trade and Other Payables**

The statement of financial position as at 30 June 2018 reflects trade and other payables balance of Kshs.26,147,320 while the schedules provided for audit shows an amount of Kshs.26,666,420, leading to unexplained variance of Kshs.519,100.

The following additional observations were made:

- i. An amount of Kshs.20,412,416 had been outstanding for more than 90 days.
- ii. An amount of Kshs.14,328,625 was not supported with creditors ledgers, unpaid invoices, LPO/LSO and store ledger/register indicating that the items supplied were received or the services were rendered.

Consequently, the accuracy and completeness of trade and other payables balance of Kshs.26,147,320 could not be confirmed.

#### **5. Capital Reserves**

The capital reserves balance of Kshs.77,354,669 reflected in the financial statements was not supported with ledgers showing the movements over the years. As a result, the accuracy, validity and completeness of the capital reserves balance of Kshs.77,354,669 as at 30 June 2018 could not be confirmed.

#### **6. Production Costs**

##### **6.1. Motor Vehicles Repairs**

Included in the production costs of Kshs.17,138,395 shown in the statement of comprehensive income for the year ended 30 June 2018 is an amount of Kshs.899,750 which was paid in respect of motor vehicles repairs. The amount in turn includes an expenditure of Kshs.565,700 that was not supported with pre and post inspection reports by mechanical engineer and records of defects in the vehicles log books. Consequently, the propriety, validity and accuracy of the expenditure totalling Kshs.565,700 on repairs of motor vehicles could not be confirmed.

##### **6.2. Repairs of Water Supplies**

Included also in the production costs figure of Kshs.17,138,395 is an amount of Kshs.755,037 which was paid in respect of repairs of water supplies. The amount in turn includes an expenditure of Kshs.567,602 which was not supported with stores ledger/register, quotations, LPO/LSO and inspection reports. Consequently, the validity, propriety and accuracy of the expenditure totalling Kshs.567,602 on repairs of water supplies could not be confirmed.

##### **6.3. Expenditure on Casual Wages**

Included in the production expenses figure of Kshs.17,138,395 is an expenditure of Kshs.215,100 in respect of casual wages. The latter includes an amount of Kshs.164,500 which was not supported with muster roll indicating the location and nature of work done by the casual workers. Further, it was not clear if pay as you earn taxes was deducted and remitted to the Kenya Revenue Authority as required by the Income Tax Act. Consequently, the accuracy and validity of the expenditure totalling Kshs.164,500 which was spent on the casual wages could not be confirmed.

## **7. Board Emoluments**

Included in the directors' emoluments of Kshs.893,760 reflected in the financial statements are payments totalling Kshs.273,950 which were made on diverse dates but were not adequately supported with board minutes, attendance sheets and other requisite documents. Consequently, the accuracy and validity of the expenditure of Kshs.273,950 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Migori 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.

## **Material Uncertainty in Relation to Going Concern**

As disclosed on page 39 to the financial statements, during the year under review the Company made a loss of Kshs.11,247,880 compared to a loss of Kshs.3,891,668 in the previous year, an indication that the Company performance declined in 2017/2018 financial year. The operating loss also depleted further the revenue reserves from negative Kshs.9,205,997 as at 30 June 2017 to negative Kshs.20,453,877 as at 30 June 2018. The Company's total current liabilities balance of Kshs.39,419,474 also exceeded its total current assets balance of Kshs.32,401,955 resulting in a negative working capital of Kshs.7,017,519 as at 30 June 2018.

The precarious financial situation described above is an indication of the existence of a material uncertainty which may cast a significant doubt on the Company's ability to continue as a going concern and to meet its obligations as and when they fall due. The financial statements have been prepared on a going concern basis as disclosed by the directors on page 39 of the financial statements on the assumption that the Company will continue to receive financial support from the Migori County Government.

## **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 under material uncertainty in relation to going concern and in the Basis for Qualified Opinion, and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources sections, I have determined that there are no other key audit matters to communicate in my report.

### **Other Information**

The directors are responsible for the other information. The other information comprises the report of directors as required by the Companies Act, 2015, and the statement of the directors' responsibilities which are obtained prior to the date of this report, and the annual report which is expected to be made available after that date.

My opinion on the financial statements does not cover the other information and I do not express an audit opinion or any form of assurance thereon.

In connection with the audit of the financial statements, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or the knowledge obtained in the audit, or otherwise appears to be materially misstated. Based on the work I have performed on the other information obtained prior to the date of this auditor's report, if I conclude that there is material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

## **REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES**

### **Conclusion**

As required by Article 229(6) of the Constitution, based on the audit procedures performed, except for the matters described under material uncertainty in relation to going concern and in the Basis for Qualified Opinion and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources sections of my report. I confirm that nothing else has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

### **Basis for Conclusion**

#### **1. Employee costs and Casuals**

Included in personnel and establishments costs under Note 8 to the financial statements are gross salary and wages totalling Kshs.8,492,000 out of which an amount of Kshs.4,935,000 had not been paid to the staff as of 30 June 2018 contrary to the provisions of the Company's Human Resources Policies and Procedures

Manual. No satisfactory explanation was provided for failure by the Company to honour its contractual obligations.

## **2. Agency Account**

Included in the agency account balance of Kshs.8,421,223 shown in the statement of financial position are amounts of Kshs.6,611,683 and Kshs.1,809,539 which were due to Lake Victoria South Water Service and Water Service Regulation Board (WASREB), respectively as of 30 June 2018. No satisfactory reasons were given for failure by the Company to meet the cost of all the levies within the stipulated timeline to avoid accruing penalties.

## **3. Issued Share Capital**

According to the available information the share capital of the Company is Kshs.100,000 which is divided into 5,000 shares of Kshs.20 each. These shares were previously issued to the defunct local authorities but later taken over by the Migori County Government. However, these shares had not been paid for as at 30 June 2018. Further, the share capital still remains in the defunct local authorities' names since they have not been officially transferred to the Migori County Government.

## **4. Un-Accounted for Water**

During the year under review the Company produced 444,032 cubic meters of water out of which 273,542 cubic meters only were billed to customers. The balance of 170,490 cubic meters or approximately 38% of the volume represents Non-Revenue Water (NRW) which is 13% over and above the allowable loss of 25% in accordance with the Water Services Regulatory Board guidelines.

It was also noted that a number of water production projects remained non-operational due to the failure by the Company to pay accumulated electricity bills. The failure of the key functions to remain operational led to declining revenue in the year under review.

## **5. Budgetary Control and Performance**

During the year under review, the Company had an operating expenditure budget of Kshs.74,436,746 but the actual expenditure was Kshs.20,481,520, resulting in an under-expenditure of Kshs.53,955,330. Further, the Company collected revenue amounting to Kshs.21,658,057 against the budget estimate of Kshs.80,889,400 from its six revenue streams leading to an under-collection of Kshs.59,231,343.

The huge variances observed between the budget and actual amounts is an indication that the Company was unable to fund its planned programs and meet its set objectives during the year under review leading to huge losses.

In the circumstances, the Company was inefficient and ineffective in delivery of the services to its stakeholders.

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion

## REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

### **Conclusion**

As required by Section 7 (1) (a) of the Public Audit Act, 2015, based on the audit procedures performed, except for the matters described under material uncertainty in relation to going concern and in the Basis for Qualified Opinion and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources sections of my report, I confirm that, nothing else has come to my attention to cause me to believe that internal controls, risk management and governance were not effective way.

### **Basis for Conclusion**

The audit was conducted in accordance with ISSAI 1315 and ISSAI 1330. The standard requires that I plan and perform the audit to obtain assurance about whether processes and systems of internal control, risk management and governance were operating effectively, in all material respects. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

## REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Kenyan Companies Act, 2015 I report based on the 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 my audit;
- (ii) In my opinion, proper books of account have been kept by the Company, so far as appears from the examination of those books;
- (iii) The Company's statement of financial position and statement of comprehensive income are in agreement with books of account; and
- (iv) In my opinion the information given in the report of the directors on page 18, is consistent with the financial statements.

### **Responsibilities of Directors and Those Charged with Governance**

Directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the requirements of the Kenyan Companies Act, 2015 and, for maintaining effective internal control as the directors 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, directors are responsible for assessing the ability of Migori Water and Sanitation Company Limited to continue as a going concern, disclosing, as applicable, matters related to going concern and using the applicable basis of accounting unless the directors either intends to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Directors are 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, the directors are also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them, and that public resources are applied in an effective way.

Those charged with governance are responsible for overseeing the Company's financial reporting process, reviewing the effectiveness of how the entity monitors compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

### **Auditor-General's Responsibilities for the Audit**

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.



In addition to the audit of the financial statements, a compliance review 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.

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 policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' 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 ability of the to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are

inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Migori Water and Sanitation 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 directors 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 the directors 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**

**03 June 2019**