

REPORT OF THE AUDITOR-GENERAL ON MT ELGON LODGE LIMITED FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Mt Elgon Lodge Limited set out on pages 1 to 35, which comprise the statement of financial position as at 30 June 2018, and the statement of comprehensive income, statement of changes in equity, statement of cash flows and comparison of budget and actual amount 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 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 Mt Elgon Lodge Limited as at 30 June 2018, and of its performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Kenya Companies Act, 2015.

Basis for Qualified Opinion

1. Property, Plant and Equipment

The property, plant and equipment reflects total cost/valuation figure of net book value of Kshs.47,977,062 of which could not be confirmed since the asset register and asset valuation certificate were not availed for audit verification.

In the circumstances, it was possible to confirm accuracy of the value of property, plant and equipment as at 30 June 2018.

2. Cash and Cash Equivalents

2.1 Inconsistency in Reported Cash and Bank Balance

The financial statement for the year under review indicates that the Lodge had a balance of Kshs.417,563. However, the following anomalies were noted:

- (i) There was no bank reconciliation statement for account No.1105159779 of KCB Bank, Kitale branch availed for audit review. No satisfactory explanation was given as to why the Lodge did not prepare the reconciliation statements.
- (ii) Further, it was noted that there was rampant alterations of the cash book entries, which may be a clear indication that cash book was being tampered with to read certain figures.
- (iii) The cashbook was not being checked and signed by senior officers.

- (iv) In some cases, the accountant did not capture the particulars of transactions in cashbook.

2.2 Suspense Account

Included in trial balance is Kshs.177,887 posted to suspense account. However, there was no suspense account records and breakdown of the transactions relating to suspense amount reported of which was not availed for audit verification.

Consequently, the validity, accuracy and completeness of the financial statements for the year ended 30 June 2018 could not be confirmed.

2.3 Statement of Cashflows

The cash and cash equivalents balance is reflected as an overdraft of Kshs.187,367 in the statement of cashflows while it is recorded as Kshs.417,563 in the statement of financial position and hence leading to an unexplained and unreconciled difference of Kshs.604,930.

In the circumstances, it has not been possible to confirm that the cash and cash equivalents balance of Kshs.417,563 as at 30 June 2018 is fairly stated.

3. Trade and Other Receivables

The policy for provision of bad debts has not been disclosed in the financial statements. This is contrary to section 21 of the International Public Sector Accounting Standards (IPSAS) 19 which requires that the basis for provision of bad debts should be disclosed. Further, the debtors' ledger in support of the debtors' balance of Kshs.2,294,536 was not availed for audit verification. The balance of Kshs.2,294,536 had an increase of Kshs.468,717 from previous year Kshs.1,825,819 relating to staff receivables on loans advanced to staff which is not recoverable from staff salaries. Further, staff loans and advances registers were not availed for audit verification and the management did not explain the measures taken to recover the long outstanding debts of over 120 days.

In the circumstances, it was not possible to ascertain the accuracy of the staff debtor balance of Kshs.468,717 as at 30 June 2018.

4. Trade and Other Payables

4.1 Unsupported Trade and Other Payables

The trade and other payables balance of Kshs.25,459,332 as at 30 June 2018 is not supported by details of invoices, demand notices, suppliers' statement, fee notes and delivery notes for confirmation of the authenticity of the payables. In addition, statutory deduction figure of Kshs.10,931,370 as analyzed below remained outstanding;

Creditor	Amount (Kshs.)
VAT	4,983,866
CLT	824,841
NSSF	202,000
NHIF	413,600
PAYE	1,502,444

UNION	268,133
NSSF Penalty	2,267,717
Tourism Levy	468,769
Total	10,931,370

4.2 Unsupported Advance

The trade and other payables balance of Kshs.25,459,332 is Kshs.9,466,377 relating to advances from Tourism Finance Corporation. However, there was no supporting document to ascertain authenticity, terms and conditions of the advanced amount.

4.3 Outstanding Audit Fees

Included in the current liabilities balance of Kshs.25,459,332 is Kshs.6,624,362 for other payables which in turn includes Kshs.1,729,891 outstanding audit fees payable to Office of the Auditor General relating to a number of years. However, the management has not indicated how it plans to clear the outstanding audit fee that is long overdue. Failure to pay audit fees contravenes Section 41 of the Public Audit Act, 2015.

4.4 Unremitted of Statutory Deductions

During financial year 2017/2018, the management deducted a total of Kshs.469,866 with respect to VAT, catering levy and service charge as analyzed below:

Month	Sales (Kshs.)		Deductions (Kshs.)		
	Gross Amount	Net Amount	Vat 16%	Levy 2%	Service Charge 7%
July	47,010	37,608	6,017	752.16	2,633
August	70,610	56,488	9,038	1,129.76	3,954
September	90,800	72,640	11,622	1,452.80	5,085
October	22,440	17,952	2,872	359.04	1,257
November	48,910	39,128	6,261	782.56	2,739
December	199,310	162,680	26,029	3,253.60	11,388
January	91,310	73,048	11,688	1,460.96	5,113
February	189,260	151,408	24,225	3,028.16	10,599
March	1,155,960	924,768	147,963	18,495.36	64,734
April	88,200	70,560	11,290	1,411.20	4,939
May	280,890	224,712	35,954	4,494.24	15,730
June	60,590	48,472	7,756	969.44	3,393
Total	2,345,290	1,879,464	300,714	37,589.28	131,562
		Grand Total			469,866

However, as at 30 June 2018, the management had not remitted the statutory deductions to the relevant authorities as required.

5. Unsupported Loan Account

The non-current Liabilities balance reflects borrowing from Tourism Finance Corporation (TFC) amounting to Kshs.3,527,222. However, no details were provided in regards to terms and conditions of the loan and further, the loan confirmation certificate was not availed for audit verification.

In the circumstances, it was not possible to ascertain the validity, accuracy, existence and authenticity of the borrowings amounting to Kshs.3,527,222 as at 30 June 2018.

6. Inaccuracies in the Expenditure Items

The financial statements figures differed with support schedules and ledger amounts leading to an unexplained negative variance of Kshs.6,499,158 as detailed below;

No	Description	Financial Statements	Schedules/Ledger amounts	Variances
		Amount Kshs.	Kshs.	Kshs.
	Salaries and allowances of permanent employees	2,113,328	4,939,318	(2,825,990)
	Wages of temporary employees	109,720	11,150	98,570
	Statutory deductions (NHIF, NSSF & PAYEE)	396,351	1,382,376	(986,025)
	Staff welfare and expenses	45,684	93,582	(47,898)
	Communication services and supplies	25,175	10,020	15,155
	Office and General Supplies and Services	45,119	37,436	7,683
	Repairs and maintenance	46,380	58,750	(12,370)
	Other operating expenses	306,419	240,168	66,251
	Trade and payables	22,412,144	19,597,610	(2,814,534)
	Total			(6,499,158)

In addition, note 2 to the financial statements reflects Ksh.535,775 relating to cost of sales. However, there was no breakdown of how the figure reported was computed. In the absence of the computations, it has not been possible to confirm as to how the amount was arrived at.

Consequently, the validity, accuracy and completeness of the financial statements as at 30 June 2018 could not be confirmed.

7. Staff Costs

Included in the administration cost of Kshs.1,323,969 is Kshs.502,996 incurred on staff costs during the year ended 30 June 2018. However, the analysis of payroll and staff documentations revealed that the staff have never received salaries for the whole financial period under review and there were no records like master roll availed to enable verification of the staff who were paid as casuals and further, the statutory deductions were not paid for the same period.

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

Emphasis of Matter

Going Concern

The Lodge registered a loss of Kshs.661,061 for the year under review compared to Kshs.2,983,236 posted in the year 2016/2017, resulting in accumulated losses of Kshs.33,150,106. In addition, the current liabilities balance of Kshs.25,459,332 exceeded the current assets balance of Kshs.2,775,871 resulting in a negative working capital of Kshs.22,683,436 as at 30 June 2018. The Lodge is therefore technically insolvent and the financial statements have been prepared on a going concern basis on assumption that it will continue to receive financial support from Government and Tourist Finance Corporation (TFC). However, TFC, withdrew the monthly financial support towards staff salaries and creditors with effect from May 2016.

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 Emphasis of Matter sections, I have determined that there are no key audit matters to communicate in my report.

REPORT ON LAWFULNESS AND EFFECTIVE IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, based on the procedures performed, except for the matter described in the Report on Lawfulness and Effective in Use of Public Resources section of my report, I confirm that, nothing 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. Failure to Adhere to Budget

1.1 Failure to Avail Approved Budget for Financial Year 2017/2018

During financial year 2017/2018, the management of the Lodge incurred expenditure totaling to Kshs.2,000,650 as disclosed in statement of comprehensive income. However, the management only availed proposed budget for the year under review and not an approved budget.

1.2 Budget Performance

Comparative analysis of Lodge's budget revealed that the budgeted revenue collection was Kshs.8,614,551. However, the Lodge realized revenue collection of Kshs.1,875,364 resulting to under collection of Kshs.6,739,187 or approximately 78% of the budgeted revenue for the year.

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 procedures performed, except for the matter described in the Conclusion on Effectiveness of Internal Controls section of my report, I confirm that, nothing has come to my attention to cause me to believe that internal controls, risk management and overall governance were not effective.

Information Communication Technology (ICT)

During audit verification and assessment of the Information Technology position of the Lodge, the following anomalies was noted:

- (i) There is no IT department and systems in place to manage the overall entity documentations and improve performance.
- (ii) No disaster recovery plan to enable recovery of information in case of any disaster.
- (iii) No back up and retention strategy to enable the Lodge continue with its services in case of any eventualities.
- (iv) No formally documented approved user management standards and procedures to minimize errors.

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

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

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

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 such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Hotel's ability to continue as a going concern and using the applicable basis of accounting unless the management either intends to liquidate the Lodge 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 money is applied in an effective manner.

Those charged with governance are responsible for overseeing the Lodge'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 with limited assurance as to 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 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. The nature, timing and extent of the compliance work is limited compared to that designed to express an opinion with reasonable assurance on the financial statements.

Further, in planning and performing the audit of the financial statements and review 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.
- 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 Lodge'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 Lodge'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 Lodge to cease 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 Lodge 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

07 March 2019