

REPORT OF THE AUDITOR-GENERAL ON MUNICIPAL COUNCIL OF MACHAKOS WATER AND SEWERAGE COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of Municipal Council of Machakos Water and Sewerage Company Limited set out on pages 14 to 42, which comprise the statement of financial position as at 30 June 2017, and the statement of profit and loss and other comprehensive income, statement of changes in equity, statement of cash flows 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 Municipal Council of Machakos Water and Sewerage Company Limited as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and do not comply with the County Government Act, 2012 and the Public Finance Management Act, 2012.

In addition, as required by Article 229(6) of the Constitution, based on the audit procedures performed, I confirm that public money has not been applied lawfully and in an effective way.

Basis for Adverse Opinion

1. Presentation and Disclosures in the Financial Statements

A review of the financial statements of Municipal Council of Machakos Water and Sewerage Company for the year ended 30 June 2017 has revealed the following unsatisfactory matters relating to presentation classification and disclosure:

- (i) The key entity information provided on page 2 of the financial statements refers to the name of the reporting entity as Machakos Water and Sewerage Company Limited while the financial statements are presented in the name of the Municipal Council of Machakos Water and Sewerage Company Limited rendering the two sets of information inconsistent. Further, the chairman's statement presented on page 6 of the financial statements in reference to the reporting entity uses the abbreviations of MAWASCO whose meaning is not explained.

- (ii) There is no explicit and unreserved statement of compliance with International Financial Reporting Standards in the notes to the financial statements as required by paragraph 16 of the International Accounting Standard 1 on presentation of financial statements.
- (iii) The statement of cash flows presented on page 17 and the statement of comparison of budget and actual amounts at page 18 do not explicitly disclose the name of the reporting entity.
- (iv) The financial statements do not contain details of inter party transfers and transfers from other Government entities as required by the guidelines issued by the Public Sector Accounting Standards Board.
- (v) The financial statements neither recognize nor discloses the year-end inventory rendering them incomplete and not fairly stated. Inventory which is part of day to day operations including water chemicals, pipes used to do minor repairs, plumbing accessories and office accessories should have been valued and included as inventory in the statement of financial position but the same were expensed in the statement of profit and loss and other comprehensive income.
- (vi) The table of contents at page 1 contain the following inconsistencies;

Item	Page No. shown in the Table of Content	Actual page No. in Financial Statements
Statement of changes in equity	15	16
Statement of cash flows	16	17
Statement of comparison of budget and actual amounts	17	18
Notes to the financial statements	18	19
Progress on follow-up of audit recommendations	19	43
Projects implemented by the entity	20	44

Consequently, the financial statements have not been prepared and presented in accordance with the requirements of International Financial Reporting Standards and guidelines issued by the Public Sector Accounting Standards Board.

2. Inaccuracies in the Financial Statements

2.1 Comparative Balances

The following differences have been noted between comparative figures (2015/2016) reflected in the financial statements for the year ended 30 June 2017 and the balances shown in the audited financial statements for 2015/2016:

Item	2015/2016 Comparative Figures Kshs	2015/2016 Audited Balance Kshs	Variance Kshs
Customer deposits	7,365,550	7,635,550	(270,000)
Note 6-Sales	85,424,664	85,460,664	(36,000)
Note 9(a) Administration costs	64,981,914	64,936,914	45,000

2.2 Statement of Cash Flows

The following anomalies have been noted in the statement of cash flows;

Item	Figure Reflected in the Statement Kshs	Supported/ Computed Balance Kshs	Variance Kshs
Increase in trade and other receivables	774,312	771,139	3,173
decrease in current liabilities	728,985	729,185	(200)
Net cash from investing activities	2,728,124	2,725,154	2,970
Increase in cash and cash equivalents	1,406,828	1,403,858	2,970
Cash at beginning of period	10,819,344	17,574,139	(6,754,795)
Note 14-Property, Plant and Equipment	37,109,894	37,131,813	(21,919)

2.3 Administration Costs

Notes 9(a) to the financial statements reflects administration costs of Kshs.69,834,117. However, the following differences have been noted between the amounts in the financial statements and the supporting schedules/ledger;

Administration Costs	Amount in the Financial Statements Kshs	Amount as per Supporting Schedules/Ledger Kshs	Difference Kshs
Wages of temporary employees (note 9(b))	3,181,450	3,232,877	(51,427)
Directors expenses- Training	345,000	845,000	(500,000)

Administration Costs	Amount in the Financial Statements Kshs	Amount as per Supporting Schedules/Ledger Kshs	Difference Kshs
Audit Supervision-Kenao	18,000	-	18,000
Billing Expenses	151,000	161,000	(10,000)
Telephone, Postal & Internet	746,190	750,690	(4,500)
Printing & Publishing	42,485	42,495	(10)
Computer repair & Maintenance	143,857	143,851	6
Total	4,627,982	5,175,913	(547,931)

Consequently, the completeness and accuracy of the administration costs totalling Kshs.69,834,117 for the year ended 30 June 2017 cannot be confirmed.

3. Trade and Other Receivables

The statement of financial position reflects trade and other receivables balance of Kshs.71,239,178 as at 30 June 2017. However, and as shown at Note 15(b), out of the reported gross trade receivables balance of Kshs.87,122,951 only receivables amounting to Kshs.47,163,519 or 54% were active leaving a balance of Kshs.39,959,432 or 46% inactive. However, contrary to the prudence concept, the management provided only an amount of Kshs.15,983,773 or 40% of the inactive receivables as doubtful debts leaving the balance of inactive debts amounting to Kshs.23,975,659 exposed. In the circumstances, the full recoverability of trade and other receivables balance of Kshs.71,239,178 as at 30 June 2017 cannot be confirmed.

4. Cash and Bank Balances

The statement of financial position reflects cash and bank balance of Kshs.12,226,221 as at 30 June 2017 and as detailed at Note 16 to the financial statements. However, it was observed that despite the Company maintaining monthly bank reconciliation statements as required by law, bank charges attachments did not have dates of the transaction. Further, it was noted that the Company used bank certificate balances instead of cashbook balances in the determination of cash and bank balance figure, an indication that the accounting principles of double entry were not adhered to. The following differences were noted between balance reflected in the note and cash book balances.

Bank Account	Balance as per the Note to the financial statements (Kshs)	Cashbook Balance (Kshs)	Difference (Kshs)
Coop bank collection account No.01120033182901	3,103	147,246	(144,143)

Bank Account	Balance as per the Note to the financial statements (Kshs)	Cashbook Balance (Kshs)	Difference (Kshs)
Family bank collection account No.07300014638	16,750	692,562	(675,812)
WSTF account No.073000028996	8,186,291	7,383,360	802,931
Family salary account No.073000030542	817,920	4,153,411	(3,335,491)

In addition, confirmation certificates for the following accounts were not provided for audit verification;

Account	Balance (Kshs)
Family bank account No.073000030291	24,385
M-Pesa 823222	35,960
Family bank account No.07300014638	16,750
WSTF (UBSUP) account No.073000028996	8,186,291
Family salary account No.073000030542	817,920
Family salary account No.073000030552	6,945

Consequently, the completeness and accuracy of cash and bank balance of Kshs.12,226,221 as at 30 June 2017 cannot be confirmed.

5. Trade and Other Payables

The statement of financial position reflects trade and other payables balance of Kshs.62,662,536 as at 30 June 2017 which includes an amount of Kshs.7,506,480 in respect of sundry trade payables supported by unpaid suppliers' invoices. However, no creditors' ledgers were maintained in support of the reported balances.

Note 18 to the financial statements on trade and other payables reflects statutory deductions totalling Kshs.5,784,150 that have remained outstanding over the years which include among others PAYE tax and pension deductions. Further, the statutory deductions owing were not supported by documentation including demand notes and statements of account from the creditors.

Consequently, the completeness and accuracy of trade and other payables balance of Kshs.62,662,536 as at 30 June 2017 cannot be confirmed.

6. Customers' Deposits

The statement of financial position reflects customer deposits balance of Kshs.8,361,850 as at 30 June 2017 and as disclosed at Note 19 to the financial statements. However, the corresponding deposits bank account reflects a balance of Kshs.2,527,033 resulting in unexplained difference of Kshs.5,834,817, an indication that the deposit money was used for operations purposes. In addition, records detailing

amounts deposited by each customer were not maintained. Instead, monthly block figures obtained from the bank statements were maintained. Consequently, the completeness and accuracy of customers' deposit balance of Kshs.8,361,850 cannot be confirmed.

7. Non-Revenue Water/Unaccounted for Water

During the year under review, Machakos Municipal Water and Sewerage Company Limited produced a total of 1,025,482 cubic metres of water out of which only 584,016 cubic metres were billed to customers. The balance of 441,466 cubic metres or approximately 43% of the total volume of water produced was not billed to customers thus resulting in estimated loss through unaccounted for water amounting to Kshs.46,958,829. After providing for the maximum industrial allowable loss of 25%, the company thus incurred abnormal water loss of Kshs.20,870,591 equivalent to 18%. The significant level of unaccounted for water (UFW) may negatively impact on the Company's profitability and its long-term sustainability.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Municipal Council of Machakos Water and Sewerage Company Limited in accordance with ISSAI 30 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAI and in accordance with other ethical 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 and Other Matter sections, I have determined that there are no key audit matters to communicate in my report.

Other Matter

1. Budget Performance

During the year under review, the Company's budgeted revenue from water sales amounted to Kshs131,160,384 but managed to collect Kshs.97,671,846 resulting in an unexplained under collection of Kshs.33,488,538 or 25%. The collection for the year, however, represented a 14% increase from the previous year's collection of Kshs.85,460,664. The Company's budgeted expenditure amounted to Kshs.163,445,236 against actual expenditure Kshs.106,272,801 resulting in an under expenditure of Kshs.57,172,435. The under expenditure of Kshs.57,172,435 is an indication that some approved programs were not undertaken during the year thus affecting delivery of services to customers.

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 to me after that date.

My opinion on the financial statements does not cover 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.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the applicable basis of accounting unless the management either intends to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 47 of the Public Audit Act, 2015.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances and for the purpose of giving an assurance on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. 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's 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 Company to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

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

I also provide management with a statement that I have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the 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 not 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 profit and loss and other comprehensive income are not in agreement with books of account; and
- iv. In my opinion the information given in the report of the directors on pages 11 and 12, is consistent with the financial statements.



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

Nairobi

25 February 2019