

REPORT OF THE AUDITOR-GENERAL ON NAKURU WATER AND SANITATION SERVICES COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Nakuru Water and Sanitation Services Company Limited set out on pages 1 to 44, which comprise the statement of financial position as at 30 June 2018, 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, except for the effects of the matter described in the Basis for Qualified Opinion section of my report, the financial statements present fairly, in all material respects, the financial position of Nakuru Water and Sanitation Services Company Limited as at 30 June, 2018, and its financial performance and cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Companies Act, 2015.

Basis for Qualified Opinion

1. Non-Disclosure of ADB Loan

Note 8(d) on operating and maintenance expense reflects total expenditure of Kshs.319,924,551, which includes Kshs.39,468,545 ADB Loan repayment. The Company is servicing a loan of Kshs.994,706,658 due to the African Development Bank (ADB) through the Rift Valley Water Services Board (RVWSB) at the rate of Kshs.39,468,544.80 p.a. It was however noted that the loan was not disclosed as a long term liability in the statement of financial position although loan repayment of Kshs.39,468,544.80 has been reflected under note 8 (d).

In the circumstances, it has not been possible to confirm total loan repaid and the amount outstanding as at 30 June 2018.

2. Doubtful Reserve-Assets Transferred

The statement of financial position reflects reserve- assets transferred of Kshs.262,893,991 as at 30 June 2018. However, note 18 (c) indicates operational assets transferred to the Company by the Ministry of Water Resources Development in the year 2004, included customers accounts of Kshs.443,091,806. Further, no details of the customers account balance transferred were provided for audit verifications, and hence it was not possible to confirm the existence of the assets.

In the circumstances, the reported balance of Kshs.262,893,991 in respect of reserve-asset transferred in the statement of financial position could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Nakuru Water and Sanitation Services 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 opinion.

Key Audit Matters

Key audit matters are those matters that, in my professional judgment, are of most significance in the audit of the financial statements. Except for the matter(s) described in the Basis for Qualified Opinion section, I have determined that there are no other key audit matters to communicate in my report.

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 in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section 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. Long Outstanding Trade and Other Payables

Note 17 to the financial statements reflects trade payables, accrued expenses and other payables of Kshs.621,740,721 out of which Kshs.359,455,261.40 was outstanding Rift Valley Water Service Board (RVWSB) administrative fees which has accumulated over time since year 2013. The accumulation of the administrative fees resulted from “not to pay” instructions issued by the County Government of Nakuru. It is however not clear why the board has failed to resolve this matter.

In the circumstances, the unpaid balance may not be cleared.

2. Trade and Other Receivables

Examination of records provided for audit in respect of trade and other receivables as at 30 June 2018 disclosed the following unsatisfactory matters: -

2.1 Lack of Debtor Aging Analysis Report

During the year under review, the company had debtors totaling Kshs.710,483,930 as disclosed under note 15 to the financial statements .However, the company failed to prepare debtors aging analysis report contrary to provisions of Section 5.2 of its finance manual which requires for the preparation of monthly debtors aging analysis report . Lack of aging analysis may result into insufficient provision for bad and doubtful debts and may also affect debt collection strategies.

No satisfactory explanation has been given for failure to prepare debtors aging analysis report and therefore the accuracy of the debtors balance as at 30 June, 2018 could not be confirmed.

2.2 Long Outstanding Debts

- i. Reported among the debtors is long outstanding debts owed by the County Government of Nakuru amounting Kshs.60,000,000 in respect of water supplied .It is not clear why the County Government of Nakuru, a major shareholder of the Company with shareholding of 99.92% has been unable to settle water bills. Further, it was noted that no efforts appear to have been made to collect the outstanding amount as no evidence of disconnection orders issued were provided for audit verifications.
- ii. Also reported under debtors is an amount of Kshs.215,000,000 owed by the defunct Municipal Council of Nakuru. It is however, not clear why this debt has not been transferred to the County Government of Nakuru since all assets and liabilities of defunct Local Authorities were inherited by County Governments.
- iii. It was further noted that trade and other receivables increased by Kshs.55,806,288 from Kshs.654,677,642 reported in the previous year to Kshs.710,483,930 during the period under review. This increase has not been explained.

In the circumstances, the accuracy of the debtors balance as at 30 June, 2018 could not be confirmed.

My responsibility is to express a conclusion based on the review. The review was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the review so as to obtain limited assurance as to 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.

A review is limited primarily to analytical procedures and to inquiries, and therefore provides less assurance than an audit. I have not performed an audit, and, accordingly, express my conclusion in the form of limited assurance, which is consistent with the more limited work I have performed under this compliance review.

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, GOVERNANCE AND RISK MANAGEMENT SYSTEMS

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 else has come to my attention to cause me to believe that internal controls, risk management and overall governance were not effective.

Basis for conclusion

1. Revenue

1.1. Non- Revenue Water (NRW)

During the year under review, the Company produced 12,409,678 cubic meters of water. However, out of this volume, only 8,026,147 cubic meters of water was billed to customers with total revenue amounting to Kshs.860, 874,266. The balance of 4, 383,531 cubic meters of water or approximately 35% of the total revenue represented Non-revenue Water (NRW). According to the Water Services Regulatory Board (WASREB) guidelines, this quantity is 10% above the allowable loss of 25%. The abnormal loss of 10% of the water produced may have resulted in a loss of approximately Kshs.3,886,633. No proper explanation has been given for the persistent water loss. The significant level of unaccounted for water (UFW) may negatively impact on the company's profitability and long term sustainability.

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 Companies Act, 2015 I report based on my audit, that:

- i. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit;
- ii. In my opinion, adequate accounting records have been kept by the , so far as appears from the examination of those records; and,
- iii. The financial statements are in agreement with the accounting records and returns.

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 Financial Reporting 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.

In preparing the financial statements, management is responsible for assessing the Nakuru Water and Sanitation Services Company Limited 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 Nakuru Water and Sanitation Services 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.

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 Nakuru Water and Sanitation Services Company Limited 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 Nakuru Water and Sanitation Services Co. policies and procedures may deteriorate.

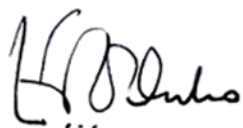
As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- 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 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 Nakuru Water and Sanitation Services Company Limited 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 Nakuru Water and Sanitation Services Company Limited 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 Nakuru Water and Sanitation Services 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.



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

Nairobi

16 April 2019