

REPORT OF THE AUDITOR-GENERAL ON NEW KENYA CO-OPERATIVE CREAMERIES LIMITED FOR THE YEAR ENDED 30 JUNE, 2019

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of New Kenya Co-operative Creameries Limited set out on pages 1 to 53, which comprise the statement of financial position as at 30 June, 2019, statement of profit and loss and other comprehensive income, statement of changes in equity, statement of cash flows and the 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 the New Kenya Co-operative Creameries Limited as at 30 June, 2019, 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 Kenya Companies Act, 2015 and the Public Finance Management Act, 2012.

Basis for Qualified Opinion

1. Unconfirmed Land Ownership and Valuation

The statement of financial position as at 30 June, 2019 reflects land owned by the Company valued at Kshs.3,945,073,828 comprised of leasehold land and freehold land of Kshs.3,637,573,828 and Kshs.307,500,000 as disclosed in Note 14 and Note 15 to the financial statements respectively.

However, title deeds for twenty-two (22) properties with a value of Kshs.853,900,000 were not availed for audit verification. In addition, the value of four (4) parcels of land is not disclosed. Similarly not disclosed in the financial statements is the value of two (2) disputed properties; LR No.37/371 and LR No.37/22 situated in Upper Hill, Nairobi and transferred to third parties. The legal status of the properties has not been determined yet.

In addition, available records indicated that twenty-three (23) disputed and unvalued properties were registered in the names of third parties. Further, five (5) acres out 32.94 acres of parcel LR.NO.MN/VI/2860 on which Miritini Milk Processing Factory is located have been encroached by informal settlers, some of whom have already built residential and other structures on the land.

Although the Company has initiated legal proceedings with a view to recover the disputed properties, and has also engaged the National Land Commission and the Ministry of Lands on the matter, no tangible change in the status of the lands has been attained so far.

In the circumstances, ownership of the occupied lands by the Company as well as those registered in the names of third parties is at risk.

In view of the foregoing, it was not possible to confirm the valuation and ownership of land valued at Kshs.3,945,073,828 in the Company's Statement of Financial Position as at 30 June, 2019.

2. Unsupported Trade and Other Receivables

The Statement of Financial Position at 30 June, 2019 reflects trade and other receivables amounting to Kshs.2,308,191,509, as disclosed under Note 18(a) to the financial statements. The balance includes Kshs.77,619,144 owed by Uchumi Supermarkets Limited and Kshs.290,690,273 by Nakumatt Holdings Limited. Available information indicates that the former is facing receivership proceedings and the latter is in liquidation. In addition, the Trade and Other Receivables balance includes unpaid cheques totalling Ksh.17,747,784, rent arrears of Kshs.31,977,504 which in turn include Kshs.16,798,890 from tenants who have already vacated the Company's premises, and staff debtors amounting to Kshs.15,330,504. The staff debtors' balance includes amounts owed by former staff of the Company, some of whom are now deceased.

In view of these anomalies, recoverability of the trade and other receivables balance totalling Kshs.2,308,191,509 reflected in the Statement of Financial Position as at 30 June, 2019 has not been confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of New Kenya Co-operative Creameries Limited Management in accordance with ISSAI 130 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.

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 Qualified Opinion section, I have determined that there are no other key audit matters to communicate in my report.

Other Matter

1. Prior Year Matters- Outstanding Trade and Other Payables

The report for 2017/2018 highlighted trade and other payables balance totalling Kshs.1,790,214,805 as at 30 June, 2018 which included the sum of Kshs.25,680,870 that had been outstanding for more than three years. Further, Kshs.7,302,499 due to contracted farmers had been outstanding for three years, since 2015.

No information has been provided to show how these debts were paid during the year under review.

2. Budget Control and Performance – Unrealized Revenue Target

During the year under review, the Company set a revenue budget of Kshs.13,257,990,204 but realized Kshs.9,623,007,943 thus incurring a revenue shortfall of Kshs.3,544,093,162 or 26.7% of the budget.

No plausible explanation has been provided for the underperformance.

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 Qualification, 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

Unsupported Write-Offs of Finished Goods

The Company's accounting records indicated that Management wrote-off Kshs.59,104,947 worth of finished goods during the year under review. However, the Company's policy on write-off of stock and reports, if any, to the National Treasury and the Auditor-General on the write-offs have not been presented for audit review. In the absence of relevant information, it is not possible to confirm that provisions of Section 148(5) of the Public Finance Management (National Government) Regulations, 2015 were observed in relation to the write-offs. Further, I am unable to confirm that the losses of public funds so incurred were regularized.

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 in Basis for Qualified Opinion, Basis for and Conclusion on Lawfulness and Effectiveness in Use of Public Resources

and the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance, 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. Delay in Clearing Trade and Other Payables

The Statement of Financial Position as at 30 June, 2019 reflects trade payables totalling Kshs.2,003,908,361, as further disclosed in Note 28 to the financial statements. The balance includes debts totaling Kshs.18,967,368, which had been outstanding for more than one (1) year, owed to trade suppliers and Kshs.24,056,791 owed to farmers by the defunct Kenya Cooperative Creameries. Although Management has indicated that the debts have remained unpaid because the creditor farmers have not presented themselves for vetting, information on the actions taken to identify the farmers has not been presented for audit review.

In the circumstance, the Company's internal control, risk management and governance on trade payables is not effective.

2 Ineffective Control on Rental Properties

As mentioned in the Basis for Qualification section of this report, as at 30 June, 2019, rental income arrears totalling Kshs.31,977,504 include Kshs.16,798,890 owed by tenants who had vacated the Company's premises without making payment. In addition, the Company's own staff owed Kshs.15,330,504 as at that date.

Further, Management have not presented the Company's rental properties management policy and tenancy agreements for audit review.

In view of these omissions, internal control on rental properties owned by the Company and collection of rental income is weak.

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. 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 overall 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 Company, so far as appears from the examination of those records; and,
- iii. the Company's financial statements are in agreement with the accounting records and returns.

Responsibilities of Management and Board of Directors

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards (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 overall governance.

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 going concern basis of accounting unless the Management is aware of the intention to liquidate the Company or have its operations cease.

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.

The Board of Directors is responsible for overseeing the financial reporting process, reviewing the effectiveness of how the Company 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 overall 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 overall 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 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 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 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 communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.



Nancy Gathungu
AUDITOR-GENERAL

Nairobi

09 October, 2020