

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

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Ngagaka Water and Sanitation Company Limited set out on pages 15 to 37 which comprise the statement of financial position as at 30 June 2018, and the statement of profit or loss and other comprehensive incomes, 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 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 Ngagaka 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 (Accrual Basis) and comply with the Water Act, 2016 and the Companies Act, 2015.

Basis for Qualified Opinion

1.0 Irregular Water Maintenance and Rehabilitation Expenditure

Note 5 to the financial statements reflects Kshs.4,293,163 in respect to production costs which includes Kshs.4,007,433 in respect to water maintenance and rehabilitation which further includes Kshs.1,255,000 in respect to payments to casual laborers which did not have supporting documents including nature of activities that were undertaken, daily register of the casual laborers engaged, applicable payment rates and a report of work done.

In the circumstances, the propriety of Kshs.1,255,000 expenditure reflected in the financial statements for the year ended 30 June 2018 cannot be confirmed.

2.0 Interest on Fixed Deposit

Note 7 to the financial s statements reflected Kshs.166,992 in respect to finance income which comprised of interest from four (4) fixed deposit investments totaling to Kshs.13,125,000 in a commercial bank as shown below:

Investment Date	Maturity Date	Investment Period	Principal Amount (Kshs.)	Interest Amount (Kshs.)
26-05-17	19-08-17	3 moths	2,925,000	57,014
20-08-17	29-12-17	4 months	3,400,000	60,096
30-12-17	10-05-18	4.5 months	3,400,000	49,882
15-05-18	16-08-18	3 months	3,400,000	0
Totals			13,125,000	166,992

However, although the investment period cut across three financial years of 2016/2017, 2017/2018 and 2018/2019, the entire Kshs.166,992 was charged to 2017/2018 financial year which may have overstated the finance income.

In addition, the Company did not provide the rationale for the choice of the investment decision, negotiation of the investment rate, the choice of the service provider and approval by the board of directors contrary to Article 227 (1) of the Constitution of Kenya which provides that when a state organ or any public entity contracts for goods and services, it shall do so in accordance with a system that is fair, transparent, competitive and cost effective.

In the circumstances, the accuracy of Kshs.166,992 in respect to finance income for the year ended 30 June 2018 could not be confirmed. In addition, the management is in breach of the law.

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

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

1.0 Budget Control and Performance

1.1 Revenue Analysis

The statement of comparison of budget and actual amounts for the year ended 30 June, 2018 reflects budgeted revenue of Kshs.32,575,200 and actual revenue of Kshs.32,652,937. The Company over- realized the budget by Kshs.98,137 on two items and under- realized the budget by Kshs.20,400 on two other items as shown below:

Item	Budget (Kshs)	Actual (Kshs)	Over (Kshs)	Under (Kshs)	%
Water sales	31,800,000	31,830,755	30,755		0.10%
Capital Grant	228,000	295,382	67,382		29.55%
Other income	19,200	9,800		(9,400)	-48.96%
Application fee	528,000	517,000		(11,000)	-2.08%
TOTAL	32,575,200	32,652,937	98,137	(20,400)	

The excess collection of Kshs.98,137 (0.3%) over the revenue may be a pointer to very low set targets hence there is need for the management to review its budgeting mechanism with a view to coming up with a more realistic revenue budgets to achieve higher revenue growth.

1.2 Expenditure Analysis

The statement of comparison of budget and actual amounts for the year ended 30 June, 2018 reflects a budgeted expenditure of Kshs.32,557,400 and actual expenditure of Kshs.29,891,473 resulting to an under expenditure of Kshs.2,744,066 on sixteen (16) items and over expenditure of Kshs.78,139 on four (4) other items as shown below:

Items	Budget (Kshs)	Actual (Kshs)	Under (Kshs)	Over (Kshs)	%
Staff Costs	14,960,000	14,609,476	(350,524)		-2.3%
Directors emoluments	540,000	354,000	(186,000)		-34.4%
Electricity and water	84,000	89,019		5,019	6.0%
Tel. emails, postage & comp.	600,000	651,758		51,758	8.6%
Transportation, travelling & sub.	1,128,000	1,121,050	(6,950)		-0.6%
Advertising, printing & N/papers	208,800	218,274		9,474	4.5%
Rent expenses	60,000	47,000	(13,000)		-21.7%
Staff training & seminars	1,080,000	1,065,300	(14,700)		-1.4%
Staff uniforms & welfare	448,000	422,097	(25,903)		-5.8%
Insurance costs	30,000	27,164	(2,836)		-9.5%
bank charges	60,000	54,005	(5,995)		-10.0%

Items	Budget (Kshs)	Actual (Kshs)	Under (Kshs)	Over (Kshs)	%
Fees, levies, Comm. & honoraria	4,062,000	2,451,455	(1,610,545)		-39.6%
Provision for Audit	290,000	290,000	0	0	0.0%
M/vehicle, fuel, oil & maintenance	996,000	1,007,888		11,888	1.2%
Consultancy/subscription	119,000	55,000	(64,000)		-53.8%
Staff end year party/cleaning	381,600	354,079	(27,521)		-7.2%
Water maint. & rehabilitation	4,200,000	4,007,433	(192,567)		-4.6%
Water chemicals	300,000	285,730	(14,270)		-4.8%
Interest on loan	60,000	44,307	(15,693)		-26.2%
Procurement of water meters	2,700,000	2,505,438	(194,562)		-7.2%
Computer & office Equipment	250,000	231,000	(19,000)		-7.6%
TOTAL	32,557,400	29,891,473	(2,744,066)	78,139	

The under-spending of the budget by Kshs.2,744,066 reflected equivalent services denied to the customers by the Water Company. There is need therefore for the management to relook at its budgeting mechanism with a view to focusing on areas which will improve service delivery to the citizens of Runyenjes Constituency. Further, no approval was availed for audit review for the Kshs.78,139 over-expenditure.

Consequently, the company is in breach of the law.

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 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

1.0 Ethnic Distribution

The Company staff establishment at the time of the audit revealed a total of 31 staff, out of which 28 (90%) were from one ethnic community contrary to Section 65 (1) (e) of the

County Government Act, 2012 which requires that at least 30% of vacant post at entry level to be filled by candidates who are not from the dominant community.

In the circumstances, the management was in breach of law.

2.0 Presentation of the Financial Statements

The Public Sector Accounting Standards Board (PSASB) stipulates that the statement of financial position of the Company should reflect the name of the Chief Executive and the name and Institute of Certified Public Accountant (ICPAK) membership number of the Head of Finance. However, the two officers did not indicate their names while the head finance officer did not also indicate his ICPAK membership number in the statement of financial position for the year ended 30 June, 2018.

In the circumstances, the presentation of the financial statements for the year under review were not in accordance with the recommended format.

3.0 Internal Borrowing from Customers Deposits

Note 16 to the financial statements reflect borrowings of Kshs.1,070,000. Information available indicate that the water company did withdraw the amount of money in the month of February 2014 from customers' deposits under trade and other payables balance of Kshs.4,599,173. However, no agreement was availed for audit review and the management contravened the procedures where by customers' deposit amount should only be utilized for refund to customers who opt out of the water agreement with the company.

Consequently, the management is in breach of the law by utilizing clients' funds without proper procedures.

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 INTERNAL CONTROLS EFFECTIVENESS, GOVERNANCE AND RISK MANAGEMENT SYSTEMS

Conclusion

As required by Section 7 (1) (a) of the Public Audit Act, 2015, based on the audit procedures performed, except for the matter(s) described in the Basis for Conclusion

on Effectiveness of Internal Controls, Risk Management and Governance 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.

Basis for Conclusion

1.0 Non-Revenue Water

Note 1 to the financial statements reflects Kshs.31,830,755 in respect to sale of water for the year ended 30 June, 2018. It is noted that the Company produced a total of 1,378,508 cubic meters (m³) of water during the year under review. However, only 622,340 cubic meters is billed to customers. The balance of 756,168 cubic meters (approximately 55%) of the total water produced, with a sale price of Kshs.38,835,276 represents Non-Revenue Water(NRW) which is over and above the allowable loss of 25% as provided by schedule E of the Water Service Regulatory Board (WASREB) guidelines.

In the circumstances, the Company significantly exceeded the allowable NRW loss of 25% by 30% or approximately Kshs.21,135,936 which if not addressed will negatively impact on the Company's profitability and its long- term sustainability.

2.0 Lack of Internal Audit Unit

The Company did not have an internal audit section to carry out internal audit functions contrary to Section 1551(1) (a) of the PFM Act 2012 states that a County Government entity shall ensure that appropriate arrangements for conducting internal audit according to the guidelines issued by the Accounting Standards Board.

In the circumstances, the Company breached the law

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 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 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 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, risk management and 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 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.

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.

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 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 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 Company's 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 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 Company 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 Ngagaka 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 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

25 February 2019