

# **REPORT OF THE AUDITOR-GENERAL ON NYANDARUA 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 Nyandarua Water and Sanitation Company Limited set out on pages 19 to 50, 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 Nyandarua 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 and comply with the Water Act 2016 and the Companies Act 2015.

### **Basis for Qualified Opinion**

#### **1. Personnel Cost**

The statement of profit and loss and other comprehensive income reported personnel cost at Kshs.10,294,675 compared to Kshs.8,671,881 in 2016/2017 representing an increase of Kshs.1,622,794 or 18.7%. Included under personnel cost is Kshs.4,523,935 in respect to contracted staff salaries. Summation of the contracted staff supporting schedules revealed expenditure of Kshs.3,597,981, hence unexplained variance of Kshs.925,954. In addition, the contracted staff expenditure included Kshs.2,389,292 which was not supported by approved attendance timesheets reflecting time worked, time off and overtime. In addition, it was noted that the respective officers' payroll numbers, national Identity numbers, KRA Personal Identification Numbers, NSSF numbers and NHIF numbers were not indicated in the presented schedules. It was therefore not clear whether proper remittance of deductions was made to the respective bodies or authorities. In the circumstances, the personnel costs of Kshs.10,294,675 and the corresponding statutory deductions could not be confirmed.

#### **2. Property, Plant and Equipment**

The statement of financial position reported non-current assets at Kshs.21,262,497 compared to Kshs.108,801 as at 30 June 2017 an increase by Kshs.21,153,696. The assets schedule and note 10 to financial statements included additions of land and water tank at Kshs.1,000,000 and Kshs.4,000,000 respectively that were explained to be inherited from the Rift Valley Water Services Board. However, the handover and takeover minutes and valuation reports showing these transactions were not presented for audit. Further, it was

noted that the Company is not in possession of land ownership documents for the water treatment land at Olkangui and for the pump station parcels of land located at Gatimu and Kibathi. Similarly, the Company does not have ownership documents for the eight (8) water tank parcels of land, 1 parcel at Olkangui, 2 parcels at Gatimu, 3 parcels at Shamata and 2 parcels at Kibathi. These parcels of land were not disclosed in the financial statements and the Company is at risk of losing them.

Under the circumstances, the accuracy, completeness, presentation and disclosure of non-current assets at Kshs.21,262,497 could not be confirmed.

### **3. Long outstanding Trade Receivables**

The statement of financial position as at 30 June 2018 reflects trade receivables balance of Kshs.12,176,323 compared to Kshs.5,792,501 as at 30 June 2017, an increase by Kshs.6,383,822 or 110%. This balance however, includes Kshs.4,795,982 which has been outstanding for more than three (3) years and whose recoverability remain doubtful. Analysis of the Company's aging analysis report as at 30 June 2018 revealed that Kshs.4,063,963, approximately 33% of trade receivables was outstanding for more than three (3) months. This contravenes WASREB regulations on receivables which state that account receivables shall not be more than two months of monthly billing and also points out to inadequate and ineffective debt collection measures. In addition, it was noted that provision for bad debts was estimated at a rate of 3% of gross trade receivables, translating to Kshs.375,621 and not Kshs.344,363 in note 14. The resulting increase in provision for bad debts of Kshs.217,201 was not captured as an expense in the statement of profit and loss and other comprehensive income for the year ended 30 June 2018.

Failure to collect revenue owed by water consumers affects the Company's liquidity and eventual sustainability of services. In the circumstances, the accuracy of the balance of Trade Receivables could not be confirmed.

### **4. Unreconciled Trade and Other Payables**

The statement of financial position reported trade and other payables at Kshs.18,649,693 compared to Kshs.12,867,536 as at 30 June 2017 an increase by Kshs.5,782,157 or 45%. However, the Company did not provide third party confirmations or creditor statements for confirmation and reconciliation purposes. Further, trade payables of Kshs.14,631,884 have been outstanding for more than one year and no reasons have been given for their non-settlement. Except for the tax arrears, the Company has not put in place mechanisms in form of budgetary provisions or commitments to have the obligations settled as they fall due. In the circumstance, the reported trade payables balance of Kshs.18,649,693 as at 30 June 2018 could not be confirmed as fairly stated.

### **5. Overstatement of Customer Deposits**

The statement of financial position reported customer deposits at Kshs.2,480,000 compared to Kshs.2,661,500 as at 30 June 2017 a decrease by Kshs.181,500. The Company did not maintain separate customer deposit bank account or cashbook, although the total reported cash and cash equivalent balance was Kshs.1,135,363, resulting to unexplained difference of Kshs.1,344,637. It is therefore not clear where these funds have been deposited or held.

In the circumstances, the accuracy and completeness of customer deposits of Kshs.2,480,000 as at 30 June 2018 could not be confirmed.

## **6. Unreconciled Capital and Reserves**

The statement of financial position reported capital and reserves at Kshs.13,772,240 compared to Kshs.(8,426,246) as at 30 June 2017. The reported balance differed with Kshs.(5,440,613) in the statement of changes in equity. Included in capital and reserves is Kshs.5,304,334 capital which has remained constant over the years and was explained under note 20 to be opening balances from the Ministry of Water and Irrigation during the inception of the company. Examination of the Memorandum and Articles of Association revealed that the Company was incorporated on 1<sup>st</sup> July, 2009 as a public company limited by guarantee with Nyandarua County Council (now County Government of Nyandarua) and Rift Valley Water Services Board holding 51% and 49% of the shares respectively. However, there was no evidence that incorporation documents with the capital of Kshs.5,304,334 were registered with the Registrar of Companies as required by Sections 12 and 13 of the Companies Act, 2015.

In view of the observations made, the accuracy, ownership and completeness of capital reserve balances could not be confirmed.

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

## **Emphasis of Matter**

### **1. Going Concern**

The Company's current assets as at 30 June 2018 stood at Kshs.13,639,436 while current liabilities stood at Kshs.21,129,693, resulting to a negative working capital of Kshs.7,490,257. This translates to current ratio of 0.65 against a recommended current ratio of between 1.2 to 2.0. This indicates that the Company is undergoing liquidity problems which may affect provision of water services to the residents and the management has not put in place adequate and appropriate measures to address this situation. The Company's ability to meet its obligations as they fall due is in doubt while its ability to sustain services is threatened.

## **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. Budget and Budgetary Control

The statement of comparison of budget and actual amount for the year ended 30 June 2018 reflects approved budget amounts of Kshs.22,480,000 and Kshs.22,237,830 for revenue and expenditure respectively, representing a budget increase of 18% from 2016/17. Significant variances between the final approved budget and actual revenue/ expenditure were observed in respect of the following items:

Item	Original Budget Kshs.	Actual Comparable Basis Kshs.	Performance Difference Kshs.	% of Performance Difference
<b>Revenue</b>				
Other Income	2,500,000.00	5,622,750.00	(3,122,750.00)	-125%
Grant	-	5,115,140.00	(5,115,140.00)	100%
<b>Total Revenue</b>	<b>2,500,000.00</b>	<b>10,737,890.00</b>	<b>(8,237,890.00)</b>	
<b>Expenditure</b>				
Direct Costs	5,970,000.00	10,692,476.00	(4,722,476.00)	-79%
Administrative Expenses	6,325,872.00	5,187,042.00	1,138,830.00	18%
Operation and Maintenance	-	4,291,860.00	(4,291,860.00)	100%
Finance Costs	80,000.00	48,989.00	31,011.00	39%
<b>Total Expenditure</b>	<b>12,375,872.00</b>	<b>20,220,367.00</b>	<b>(7,844,495.00)</b>	

The over expenditure on some of the items is an indication that either the Company under-budgeted on these components or incurred an expenditure not factored in the approved budget. The management did not give explanations of the highlighted material differences between the budget and actual amounts. Further, during the year under review, the Company received revenue of Kshs.5,115,140 worth of grants from Nyandarua County government which was not included in the approved budget estimates contrary to the requirements of the budget process. This Company was therefore in breach of the Public Finance Management Act, 2012 by failing observe budget discipline.

### 2. Non-filing and Late Remittance of Taxes

The operations and maintenance expenses was reported at Kshs.4,291,860 from Kshs.503,820 in 2016/2017 an increase by Kshs.3,788,040. Included in this expense is tax arrears at Kshs.3,040,000 which is composed of fines and penalties for non-filing or late filing of Kshs.70,000 Value Added Tax (V.A.T), Kshs.980,000 corporate tax and Kshs.1,990,000 Pay As You Earn (P.A.Y.E). Failure to remit these taxes has resulted to freezing of two main bank accounts hence affecting the Company's cash flows.

## 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 matter(s) described in the Basis for Qualified Opinion 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.

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 described in the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance 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. Non - Revenue Water**

The Company produced 484,825 cubic meters of water estimated at Kshs.43,634,250 but only billed 252,919 cubic meters of water estimated at Kshs.22,762,785. This implies that 231,906 cubic meters of water produced was not billed, translating to a 48% water loss estimated at Kshs.20,871,465. Therefore, the company exceeded the 25% maximum water loss allowed by the Water Service Regulatory Board (WASREB) by 23%. This significant level of unaccounted for water negatively impacts on the Company's profitability and its long term sustainability of services to the residents.

#### **2. Weaknesses in Internal Controls**

The Company does not have strong controls on Information Technology and do not have approved policies on disaster recovery plan, IT continuity plan, IT security and also various IT committees are not in place. The Company has not established an ad hoc audit committee contrary to section 4.9 of the WASREB guidelines on corporate governance. In addition, the Company has not established internal audit and no internal audits were carried out in the year under review. Under the circumstances, the Company is at risk of losing essential data and information and is exposed to fraud and other losses.

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 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 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 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 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 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 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.

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 policies and procedures may deteriorate.

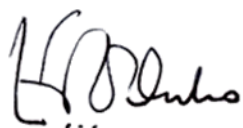
As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- 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 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**

**9 August 2019**