

REPORT OF THE AUDITOR-GENERAL ON SUNSET HOTEL LIMITED FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Sunset Hotel Limited set out on pages 17 to 42 which comprise the statement of financial position as at 30 June 2017, and the statement of comprehensive income, statement of changes in equity, statement of comparison of budget and actual performance and statement of cash flows 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 discussed in the Basis for Qualified Opinion section of my report, the financial statements present fairly, in all material respects, the financial position of Sunset Hotel Limited as at 30 June 2017, and of its financial performance and its cash flows for the period then ended, in accordance with International Reporting Standards and comply with the Kenya Company's Act 2015.

Further, as required by Article 229(6) of the Constitution, except for the matters described in the basis for qualified opinion section of my report, based on the procedures performed, I confirm that nothing has come to my attention to cause me to believe that public money has not been applied lawfully and in an effective way.

Basis for Qualified Opinion

1.0 Doubtful Going Concern Status

The Hotel realized loss of Kshs.27,700,389 against loss of Kshs.12,025,168 in the year ended 30 June 2016. This raised the cumulative losses as at 30 June 2017 to Kshs.117,466,482 from Kshs.89,766,093 as at 30 June 2016. The statement of financial position also reflects a negative working capital of Kshs.82,811,374 (2015/2016 Kshs.55,754,528). In view of the foregoing, the hotel is technically insolvent and its continued existence as a going concern is dependent upon financial support from the National Government and creditors.

2.0 Outstanding Audit Fees

As in the previous year, the trade and other payables balance of Kshs.45,403,773 as at 30 June 2017 includes audit fees amounting to Kshs.4,040,000 that have been outstanding for the last 13 years. The Hotel is therefore in breach of Section 41(1) of

the Public Audit Act, 2015 which requires a state corporation whose accounts are examined and audited by the Auditor-General to pay for the costs of the services.

3.0 Bad Practice in Valuing and Accounting for Property, Plant and Equipment

i) Fully Depreciated Assets

The statement of financial position reflects property, plant and equipment balance of Kshs.96,231,262. However, as at 30 June 2017, the Hotel had depreciated Electric Transformer, Volume Washing Machine and Motor Vehicles whose original cost amounted to Kshs.8,814,614 to nil value. These assets were still in use but had not been revalued to reflect current market value and further, no funds had been set aside to replace the fully depreciated assets. Further, the Hotel maintains a fixed assets register, the assets cards are not properly numbered and are not labeled in the Hotel's name. Physical verification revealed that all the assets were not coded or assigned distinct identification tags as required.

ii) Revaluation Reserve

As reported in previous years, revenue reserve balance of Kshs.79,262,476 has remained constant since the assets were last valued in 2004. The anomaly contravenes International Accounting Standard No.16 which requires that transfers be made to the revenue reserves on an annual basis as the assets are depreciated. Further, although the Standard requires that fixed assets be revalued periodically, the last revaluation of the Hotel's assets was done fourteen (14) years ago.

Consequently, the accuracy of Property, Plant and Equipment balance of Kshs.96,231,262 as at 30 June 2017 cannot be confirmed.

4.0 Long Standing Tax Arrears

As reported in previous years, the statement of financial position reflects Trade and Other Payables balance of Kshs.45,403,773 which in turn includes Value Added Tax (VAT), Pay as You Earn (PAYE) and Withholding Taxes balances of Kshs.11,489,577, Kshs.5,446,486 and Kshs.1,456,356 respectively, being arrears due to Kenya Revenue Authority (KRA). The arrears and penalties continue to attract additional charges as per the Value-Added-Tax Act and Income Tax Act Cap 470 which have not been incorporated in these financial statements.

5.0 Delayed Remittance of Statutory Deductions

The statement of financial position reflects trade and other payables balance of Kshs.45,403,773 which in turn includes deductions relating to National Social Security Fund (NSSF) amounting to Kshs.1,005,160, National Hospital Insurance Fund (NHIF) amounting to Kshs.102,530, Central Organization of Trade Unions (COTU) of Kshs.114,630, other payroll deductions Kshs.15,001, staff insurance deductions amounting to Kshs.44,880, and Sunset Sacco deductions amounting to Kshs.3,212,115. The payables have been outstanding for a considerable long period

of time and therefore their settlement is in doubt. Therefore, the Hotel has not complied with various aspects of the Retirement Benefits Act, Labour and Employment Act, and Co-operative Societies Act.

As a result, the Hotel risks penalties and interest on the outstanding remittances owed to statutory bodies for several years.

6.0 Unexplained Provisioning Method for Bad and Doubtful Debts.

During the year under review, the management of the Hotel made provisions for bad and doubtful debts amounting to Kshs.1,703,677 against trade debtors of Kshs.15,190,609. In the previous year, the provisions for trade debtors amounted to Kshs. 957,132 against total debtors balance of Kshs.19,411,219 as at 30 June 2016. Apparently, the rate for provision for bad and doubtful debts prescribed in the Hotel's accounting manual was set before the average probable failure rate or actual defaults experienced over time were determined. In the absence of sufficient information showing how the provisioning rate was arrived at, it is not possible to confirm the validity and accuracy of the provision of Kshs.1,703,677 made by management in regard to debts owed to the Hotel.

7.0 Unexplained Reduction in Trade and Other Receivables

Included in the statement of financial position is a balance of Kshs.14,077,591 relating to trade and other receivables. However, during the year under review, trade receivables decreased by Kshs.5,598,879 from Kshs.19,676,470 as at 30 June 2016 to Kshs.14,077,591 as at 30th June 2017. The decrease cannot be attributed to debt collection as no schedule showing payment of debts has been provided for audit verification.

Consequently, the accuracy and completeness of the trade and other receivables amount of Kshs.14,077,591 as at 30 June 2017 cannot be confirmed.

8.0 Discrepancy in Share Capital Balance and Undisclosed Share Certificate

Sunset Hotel was incorporated in 1976 under the Kenya Companies Act. The shareholders are Tourism Finance Corporation with 95.4% shareholding and the defunct Municipal Council of Kisumu with 4.6% shareholding. The shares held by the defunct municipal council have not yet been transferred to the County Government of Kisumu as required by law.

Further, while the share certificate provided for audit reflected shares valued at Kshs.17,000,000, the financial statements reflect shares worth Kshs.12,000,000. Management has not explained the difference of Kshs. 5,000,000 between the share capital balances reflected in the two records. Further, the certificate confirming ownership of a portion of the share capital (4.6%) by the defunct Municipal Council of Kisumu was not made available for audit review and therefore has not been confirmed as valid.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Sunset Hotel 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 matters described in the Basis for Qualified Opinion section, I have determined that there are no key audit matters to communicate in my report.

Other Matter

Analysis of Budget Performance

Comparison of budgeted and actual income and expenditure balances revealed variances as detailed below:

Items	Budget Kshs.	Actual Kshs.	Variance Kshs.	Performance (%)
Sales	101,265,939	42,242,826	59,023,113	41.7
Staff Expenses	11,780,375	9,341,581	2,438,794	79.2
Terminal Dues	1,725,000	1,191,439	533,561	69.0
Staff Travel	1,843,554	1,626,598	216,956	88.2
Administrative Expenses	1,132,290	2,630,687	(1,498,397)	232.3

Analysis of the balances revealed that the management Hotel overspent on administrative expenses without approval by the Board. Management have not provided a plausible explanation for this irregularity.

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 Hotel's ability to sustain services, disclosing, as applicable, matters related to sustainability of services and using the going concern accounting assumption unless

the management is aware of the intention to liquidate the Hotel or cease its operations. Those charged with governance are responsible for overseeing the Hotel's financial reporting process.

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 and responsible for overseeing the 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 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 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 misstatements 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, but not for the purpose of expressing an opinion on the effectiveness of the Hotel'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 Sunset Hotel Limited's ability to continue offering 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 Sunset Hotel Limited to cease to continue offering 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 of the entities or business activities to express an opinion on the financial statements.

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.

From the matters communicated with management, I determine those matters that were of most significance in the audit of consolidated financial statements of the current period and are therefore the key audit matters. These matters are described in my auditor's report unless law or regulation precludes public disclosure about the matters or when, in extremely rare circumstances, I determine that a matter should not be communicated in my report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Companies Act, 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 Hotel, so far as appears from my examination of those books:
- iii. The Company's statement of financial position and statement of comprehensive income are in agreement with the accounting records; and

- iv. In my opinion, the information given in the report of the directors is consistent with the financial statements.



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

Nairobi

10 August 2018