

REPORT OF THE AUDITOR-GENERAL ON SUNSET HOTEL LTD FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Sunset Hotel Limited set out on pages 1 to 50 which comprise the statement of financial position as at 30 June 2018, and the statement of 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 Sunset Hotel 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 Companies Act, Cap 486 of Kenya.

Basis for Qualified Opinion

1.0. Inaccurate Share Holding - Discrepancy in Share Certificate and Undisclosed Share Certificates

Sunset Hotel was incorporated under the Kenya Companies Act (Cap 486) in 1976. The shareholders are Tourism Finance Corporation- TFC (formerly Kenya Tourist Development Corporation- KTDC) with 95.4% shareholding and Kisumu County Executive (formerly defunct Municipal Council of Kisumu) with 4.6% shareholding. The shares held by the defunct Municipal Council (MCK) and KTDC have not yet been transferred to the newly created entities as required by law. However, two (2) share certificates provided for audit indicated that entity shares were valued at Kshs.17,000,000 while the financial statements reflect shares worth Kshs.12,000,000 resulting in unexplained difference of Kshs.5,000,000. Also, KTDC shareholding stands at 67.3% as per the share certificates while MCK shares certificates were not availed for audit. Consequently, the correct ownership could not be verified.

2.0 Property, Plant and Equipment

2.1 Fully Depreciated Assets

The statement of financial position reflects property, plant and equipment balance of Kshs.92,680,945 as at 30 June 2018. However, the Hotel had not depreciated electric transformer, volund washing machines 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, although the Hotel maintains a fixed assets register, the assets cards are not properly numbered and are not labeled in the hotels name. Physical verification revealed that all the fixed assets were not coded or assigned distinct identification tags as required. Consequently, the validity and correctness of the fixed assets register could not be confirmed.

2.2 Revaluation Reserve

As reported in previous years, revaluation 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 the 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 fifteen (15) years ago.

Consequently, the accuracy of property, plant and equipment balance of Kshs.92,680,945 as at 30 June 2018 cannot be confirmed.

3.0 Material Uncertainty Related to Going Concern

During the year under review, the Hotel realized a loss of Kshs.21,901,756 against a loss of Kshs.27,700,389 reported in the year ended 30 June 2017. This raised the cumulative loss to Kshs.139,368,338 (2017: Kshs.117,466,482) as at 30 June 2018. The statement of financial position also reflects a negative working capital of Kshs.101,553,014.

In view of the foregoing, the hotel is technically insolvent and its continued existence as a going concern is dependent upon financial support from National Government and its creditors.

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

Non Remittance of Tax Arrears

Included in the statement of financial position is trade and other receivables under Note 21 of Kshs.59,596,097 is Paye As You Earn, Value Added Tax and Withholding Tax of Kshs.9,795,197, Kshs.9,191,315 and Kshs.1,456,346 respectively which have accrued from the year 2012 to 2018 and have not been remitted to Kenya Revenue Authority as per the requirements. Consequently, the continued operation of the Company is uncertain beside the risk of penalties and voidable interest charges.

2. Delayed Remittance of Statutory Deductions

Included in the statement of financial position is trade and other payables of Kshs.59,596,097 is National Social Security Fund (NSSF), National Health Insurance Fund (NHIF), Union dues, Sunset Sacco and staff insurance deductions of Kshs.2,373,198, Kshs.97,080, Kshs.344,370, Kshs.3,212,115 and Kshs.223,609 respectively. These payables have been outstanding since the year 2012. Consequently, the continued operation of the Company is uncertain and the company risks payment of voidable penalties and interest charges.

3. Audit Fee

Included in the statement of financial position trade and other payables of Kshs.59,596,097 is audit fee brought forward of Kshs.4,040,000 and charge for the year Kshs.600,000 totaling to Kshs.4,640,000 which has accrued for the last 14 years and have not been paid as at 30th June, 2018 as per the Public Audit Act 2015.

As a result, the hotel is breach of the law.

Budget as a Control Tool

Budget Performance

Comparison of budget and actual figures revealed variances as per the table below:

Audit Components	Budget Kshs.	Actual Kshs.	Variance Kshs.	% Absorption
Sales	104,636,670	34,089,815	70,546,855	33%
Cost of sales	22,444,886	8,460,510	13,984,376	38%
Administration costs	72,406,561	38,325,651	34,080,910	53%
Selling and distribution costs	1,778,500	608,983	1,169,517	34%
Depreciation costs	3,675,000	3,560,816	114,184	97%
Finance costs	3,730,350	5,035,611	-1,305,261	135%

Analysis of Sunset Hotel limited of budget against actual performance reveals that, the entity overspent on finance cost with Kshs.1,305,261. Further, the entity made low income from sales than they budgeted for by Kshs.70,546,855.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, are of most significance in the audit of the financial statements of the current year. These matters were addressed in the context of the audit of the financial statements as a whole, and in forming my opinion thereon, and I do not provide a separate opinion on these matters. For each matter below, a description of how the audit addressed the matter is provided in that context.

I have fulfilled the responsibilities described in the Auditor's Responsibilities for the Audit section of the report, including in relation to these matters. Accordingly, the audit included the performance of procedures designed to respond to the assessment of the risks of material misstatement of the financial statements. The results of the audit procedures, including the procedures performed to address the matters below, provide the basis for my audit opinion on the accompanying financial statements.

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 COMPLIANCE WITH LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, because of the significance of the matters discussed in the Basis for [Conclusion on Lawfulness and Effectiveness in Use of Public Resources/Qualified Opinion] section of my report, based on the audit procedures performed, I confirm that public resources have not been applied lawfully and in an effective way.

Basis for Conclusion

Staff Costs

Cash Payment of Permanent Employees Salaries

It has been observed that in some occasions the permanent employees of Sunset Hotel are being paid cash instead of their salaries being channeled in their respective bank accounts. A sample of payment vouchers paying salaries was done and a total of Kshs.3,112,793 was realized to have been paid to several employees as salaries in cash during the period under review.

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 matter(s) described in the Basis for [Conclusion on Effectiveness of Internal Controls, Risk Management and Governance/Qualified Opinion] 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. Understanding the Entity

Non Establishment of an Audit Committee

Sunset Hotel Ltd apart from not having an Internal Audit Department had not established an audit committee as required by the regulations. Consequently, the management is in breach of the regulation.

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, cap 486, the Laws of Kenya, 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 Sunset Hotel Ltd, so far as appears from the examination of those records; and,

The Sunset Hotel Ltd 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.

In preparing the financial statements, management is responsible for assessing the Sunset Hotel Ltd 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 Sunset Hotel Ltd 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 Sunset Hotel Ltd 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 Sunset Hotel Ltd 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 Sunset Hotel Ltd 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 Sunset Hotel Ltd 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 Sunset Hotel Ltd 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

24 January 2019