

REPORT OF THE AUDITOR-GENERAL ON MWEA RICE MILLS LIMITED FOR THE YEAR ENDED 30 JUNE, 2019

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of Mwea Rice Mills Limited set out on pages 1 to 23, which comprise of the statement of financial position as at 30 June, 2019, 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, because of the significance of the matters discussed in the Basis for Adverse Opinion section of my report, the financial statements do not present fairly, the financial position of the Mwea Rice Mills Limited as at 30 June, 2019 and its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and do not comply with the Companies Act, 2015 and the Public Finance Management Act, 2012.

Basis for Adverse Opinion

1. Inaccuracies in Cost of Sales - Unexplained Cost of Paddy

As disclosed in Note 16 to the financial statements, the statement of profit and loss and other comprehensive income reflects cost of sales amounting to Kshs.91,996,451 which includes paddy to mills totalling to Kshs.54,669,580. Examination of Local Purchase Orders (LPOs), stock cards and delivery notes revealed the following unsatisfactory matters:

- (i) The Management purchased paddy twice totalling to Kshs.569,625 as per Goods Received Notes (96166 & 96167) and bin cards provided. However, transactions recorded in the ledger indicate that the Management purchased paddy totalling to Kshs.4,493,940 and thus, resulting in an unexplained variance of Kshs.3,924,315.
- (ii) Review of records, however, revealed cost of sales amounting to Kshs.11,300,625 was in respect of paddy to mills, which differs with the reported balance of Kshs.54,669,580 and thus, resulting in an unexplained variance of Kshs.43,368,955.
- (iii) Included in the cost of sales balance of Kshs.91,996,451 was an unexplained journal balance of Kshs.50,175,640, adjusting paddy to mills.

- (iv) The calculated cost of sales for basmati white rice totalled to Kshs.9,427,540 which varied from the reported amount of Kshs.6,773,700, resulting in unexplained variance of Kshs.2,653,840.
- (v) The cost of paddy to mills balance increased from Kshs.2,524,903 in the previous year to Kshs.54,669,580 resulting to an unreconciled increase of Kshs.52,134,677.
- (vi) Whereas the Company policy is to retain the following by products on milling namely; bran meal, chicken feeds and course bran, during the year under review, the company milled an estimated total of 7,046,925 kilograms of paddy which constituted 6,903,076 kilograms and 143,849 kilograms of paddy rice both for Millers and the Company respectively.
- (vii) However, calculation using the recovery rate on paddy milled was as follows; chicken feeds 123,803.84 Kgs while bran meal was 386,761 Kgs. It was observed that the Company did not maintain any records for these by-products.
- (viii) It was not possible to ascertain how many kilograms of the products were produced, sold and even retained at the end of the year.
- (ix) The Management reflected a Nil balance for all the by-products at the end of the year.

In the circumstances, the accuracy and completeness of the cost of sales amounting to Kshs.91,996,451 reflected in the statements of profit and loss and other comprehensive income for the year ended 30 June, 2019 could not be confirmed.

2. Inaccuracies in Turnover - Unaccounted for Turnover

As disclosed in Note 15 to the financial statements, the statement of profit and loss and other comprehensive income reflects turnover totalling Kshs.33,574,632. Examination of records, however, revealed the following unsatisfactory matters:

- (i) The turnover recorded in the daily revenue book amounting to Kshs.55,727,323 differs significantly with the balance of Kshs.33,574,632 reflected in the financial statements, resulting in understatement of turnover by Kshs.22,152,691.
- (ii) The daily revenue book reflected an amount of Kshs.25,100,455 while the revenue schedule indicated sales amounting to Kshs.33,574,632 resulting to an unexplained variance of Kshs.8,474,177.
- (iii) A visit to the stores reflected the existence of 187 bags of 50kgs in respect of discarded broken rice, an equivalent of 9,350 Kgs worth Kshs.1,870,000. It was explained that the consignment was returned from Uchumi Supermarket during the year under review. However, there was no documentation to show how the returned goods were taken on charge during the year under review.

- (iv) The balance includes basmati rice packet sales totalling to Kshs.8,794,530. However, examination of the inventory movement revealed an opening stock balance of Kshs.10,037,300 and closing stock of Kshs.454,560, resulting a turnover of Kshs.9,582,740 and which translates to unaccounted for sales amounting to Kshs.788,210, exclusive of the milled paddy during the year.
- (v) Paddy stock movement reflects an opening stock balance of Kshs.52,057,800 and closing stock of Kshs.4,536,000, resulting in paddy worth Kshs.47,521,800 being put in production. However, sales made during the year did not match with the movement of stock and paddy milled.

Consequently, the completeness and accuracy of turnover during the year of Kshs.33,574,632 could not be confirmed.

3. Lack of Valuation of Plant, Property and Equipment

As previously reported the statement of financial position reflects property, plant and equipment balance of Kshs.28,781,786 as at 30 June, 2019 which includes , a balance of Kshs.9,156,781 relating to buildings which were fully depreciated but had not been revalued. Further, the balance includes a piece of land which was acquired in 1992 at a cost of Kshs.280,000. The land has not been revalued contrary to International Accounting Standard No.16 which requires sufficient regularity in revaluation of property, plant and equipment to ensure the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period.

In the circumstances, it was not possible to confirm that the property, plant and equipment balance of Kshs.28,781,786 is fairly stated.

4. Unsupported Investment Properties

As disclosed in Note 3 to the financial statements and as previously reported, the statement of financial position reflects investment property with a net book value of Kshs.574,231,139. the balance includes houses located in Kilimani, Nairobi and a residential building located in Mwea. However, ownership documents provided were in the name of TAWS LTD while the title deed of land on which the building in Mwea is located was not provided for audit review.

Consequently, the ownership of the investment properties amounting to Kshs.574,231,139 could not be confirmed.

5. Unsupported Inventories

As disclosed under Note 4 to the financial statements, the statement of financial position reflects inventories balance of Kshs.23,563,868 which includes rice paddy at cost of Kshs.4,536,000 while the balance in the stock-take sheet summary reflects Kshs.46,017,280, resulting to an unreconciled variance of Kshs.41,481,280. Management did not support the balances with costing schedules.

Further, the balance constitutes a balance of Kshs.454,560 in respect of milled rice while the stocktaking sheet summary reflected an amount of Kshs.3,263,600 resulting in an unreconciled variance of Kshs.2,809,040.

In addition, the value of inventory includes spare-parts valued at Kshs.15,309,840, which were obsolete as at 30 June, 2019 as per their respective stock sheets and stock cards which reflected nil balances. The inventories balance of Kshs.23,563,868 has therefore, been overstated by inventories amount of Kshs.15,309,840.

In the circumstances, the accuracy and completeness of inventories balance of Kshs.23,563,868 as at 30 June, 2019 could not be confirmed.

6. Trade and Other Payables

As disclosed in Note 14 to the financial statements, the statement of financial position reflects trade and other payables balance of Kshs.51,325,607. Examination of records revealed the following unsatisfactory matters:

6.1 Unreconciled Intercompany Transactions

The balance includes an amount of Kshs.44,115,151 in respect of the holding company, National Irrigation Board being intercompany transactions. However, the National Irrigation Board financial statements reflect a receivables balance of Kshs.69,064,828 from Mwea Rice Mills resulting to an unreconciled variance of Kshs.24,949,677.

6.2 Non-remittance of Outstanding Tax

Further, the balance includes an amount of tax provision of Kshs.2,069,563 which was brought forward from the previous and has remained unpaid. Penalties and interests in respect of the unpaid taxes have not been provided for in the financial statements. No measures have been taken by the Company to pay the tax due and recognize the penalties and interests. In addition, an analysis for the balance has not been provided.

Consequently, the completeness and accuracy of the trade and other payables balance of Kshs.51,325,607 could not be confirmed.

7. Long Term Liabilities

As disclosed in Note 12 to the financial statements, the statement of financial position reflects long term liabilities balance of Kshs.74,647,904. The balance constitutes a balance of Kshs.52,610,534 relating to capital fund for Mill rehabilitation. Available information indicated that the Company had entered into an arrangement where it would process rice for the National Irrigation Board at a levy which was charged based on kilograms milled for the purposes of rehabilitating the Mills. The levy was later stopped when the Board opted to shed off none core business such as processing

and marketing of rice. The amount of levy charged had accumulated to Kshs.52,610,534 at the time of the cessation.

Further, the long term liabilities constitute Government proposed levy balance of Kshs.22,037,370 that has remained unsettled for more than thirty one years. However, no documentary evidence has been provided to support this liability.

Consequently, the accuracy, validity and completeness of the long-term liabilities amounting to Kshs.52,610,534 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Mwea Rice Mills 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 adverse 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. There were no key audit matters to report in the year under review.

Other Information

The Directors are responsible for the other information. The other information comprises the report of Directors as required by the Companies Act, 2015, and the statement of the Directors' responsibilities which are obtained prior to the date of this report, and the annual report which is expected to be made available after that date.

My opinion on the financial statements does not cover the other information and I do not express an audit opinion or any form of assurance thereon.

In connection with the audit of the financial statements, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or the knowledge obtained in the audit, or otherwise appears to be materially misstated. Based on the work I have performed on the other information obtained prior to the date of this auditor's report, if I conclude that there is material misstatement of this other information, I am required to report that fact. I wish to report in this regard that contrary to the Directors' opinion in the statement of Directors' responsibilities, the financial statements do not present fairly, the financial position of the Mwea Rice Mills 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 do not comply with the Kenyan Companies Act, 2015.

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 described in the 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 Changes in Share Capital

As disclosed in Note 8 to the financial statements, the statement of financial position reflects share capital balance of Kshs.5,000,000 comprising of 250,000 ordinary shares of Kshs.20 each. According to the Article of Association, National Irrigation Board and Mwea Farmers Co-operative Society each owns 50% of the shares. However, in the current ownership structure, National Irrigation Board holds majority shares at 55% while Mwea Farmers Co-operative Society holds the balance 45% of the shares. No evidence has been provided to support the changes in the ownership of the company.

In the circumstances, Management is in breach of the law.

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 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. Weakness in Controls in Revenue Management

As disclosed in Note 17 to the financial statements, the statement of profit and loss and other comprehensive income reflects other income balance of Kshs.3,354,383 which includes an amount of Kshs.1,964,611 in respect of rental income. However, examination of records indicates that during the year, the Ministry of Lands had submitted a valuation report on market rental rate for the Company's house - Leaders House on Moi Avenue and a mansionettes situated at the off Lenana Road and Woodlands Road Junction in Hurlingham, Nairobi. The minimum yearly expected rental income as per the valuation report for the year ended 30 June, 2019 was Kshs.16,548,000 against realized rental income of Kshs.7,665,646, resulting to an unrealized revenue amounting to Kshs.8,882,354.

Further, one of the tenants with a monthly rental of Kshs.192,250 or an income of Kshs.2,307,000 for twelve months had only paid Kshs.976,250 resulting to under collection of Kshs.1,330,750. The above is premised on the fact that the company had a final revenue budget totalling Kshs.108,000,000 but actual collection amounted to Kshs.44,594,661 only, resulting in an under-collection of revenue of Kshs.63,405,339 or 59% of the budgeted amount. The under-collection of revenue is an indication of lack of efficiency and effectiveness in operations and management of public resources. The budget and budgetary controls were not adhered to and service delivery to the citizens may have been affected.

In the circumstances, it has not been possible to ascertain whether all the rental revenues have been recorded and why the Company has not implemented the valuation report as well as instituting effective debt collection measures to realise all the rental dues.

2. Long Outstanding Receivables

As disclosed in Note 5 to the financial statements, the statement of financial position reflects the trade and other receivables balance of Kshs.28,702,923 which constitutes an amount of Kshs.20,421,874 comprising of a fixed deposit and an interest of Kshs.16,815,053 and Kshs.3,606,821 respectively, being receivables from Continental Credit Finance Ltd which went under receivership in 1986.

Although the Management has made a full provision for bad and doubtful debt for the recoverability of the principal and interest as at 30 June, 2019, the Official Receiver in respect of a winding up Case No.29 of 1986 between Mwea Rice Mills and Continental Credit Finance has contended that their records recognizes only the principal amount and not interest. The report on the outcome of the case or the current status of the case has not been provided for audit review.

Further, as disclosed in Note 7 to the financial statements, the statement of financial position reflects under current assets a balance of Kshs.1,952,021 owed by the Kenya Revenue Authority as at 30 June, 2019 which has been outstanding since 2016/2017

financial year. No measures have been taken by the company to recover the balance or have it offset against the outstanding tax due to the Authority.

In the circumstances, it was not possible to ascertain the fair value and recoverability of trade and other receivables balance of Kshs.28,702,923 as at 30 June, 2019.

3. Lack of Policy Documents and Guidelines

The Company did not have in place policy documents and guidelines establishing the procedures on operations internally. As a result, there was lack of standardization, effective control and accountability in the operations of the entity.

Consequently, test of policies and procedures could not be undertaken during the audit and there was deliberately no effective internal controls in operations.

4. Internal Audit

The company did not have an internal audit section and was neither subjected to any internal audit during the year under review to assess the efficiency and effectiveness of its operational and risk management processes.

In the circumstances, effectiveness of internal controls could not be confirmed.

Basis for Conclusion

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 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 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 my audit;
- (ii) In my opinion, accounting records have not been kept by the Company, so far as appears from the examination of those records; and
- (iii) The company's financial statements are not in agreement with books of account;

Responsibilities of Management and Board of Directors

The 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 the 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, the Management is responsible for assessing the ability of the Company's to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management is aware of the intention to liquidate the Company or to cease operations.

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, the 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 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 the 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.



CPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

30 December, 2021