REPORT OF THE AUDITOR-GENERAL ON WATER SERVICES REGULATORY BOARD FOR THE YEAR ENDED 30 JUNE, 2021

PREAMBLE

I draw your attention to the contents of my report which is in three parts:

A. Report on the Financial Statements that considers whether the financial statements are fairly presented in accordance with the applicable financial reporting framework, accounting standards and the relevant laws and regulations that have a direct effect on the financial statements.

B. Report on Lawfulness and Effectiveness in Use of Public Resources which considers compliance with applicable laws, regulations, policies, gazette notices, circulars, guidelines and manuals and whether public resources are applied in a prudent, efficient, economic, transparent and accountable manner to ensure Government achieves value for money and that such funds are applied for intended purpose.

C. Report on Effectiveness of Internal Controls, Risk Management and Governance which considers how the entity has instituted checks and balances to guide internal operations. This responds to the effectiveness of the governance structure, the risk management environment, and the internal controls developed and implemented by those charged with governance for orderly, efficient and effective operations of the entity.

An unmodified opinion does not necessarily mean that an entity has complied with all relevant laws and regulations, and that its internal controls, risk management and governance systems are properly designed and were working effectively in the financial year under review.

The three parts of the report are aimed at addressing the statutory roles and responsibilities of the Auditor-General as provided by Article 229 of the Constitution, the Public Finance Management Act, 2012 and the Public Audit Act, 2015. The three parts of the report, when read together constitute the report of the Auditor-General.

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Water Services Regulatory Board set out on pages 1 to 29, which comprise the statement of financial position as at 30 June, 2021, statement of financial performance, statement of changes in net assets, 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 Water Services Regulatory Board as at 30 June, 2021, and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards (Accrual Basis) and comply with the Water Act, 2016 and State Corporation Act, Cap 446 of the laws of Kenya and the Public Finance Management Act, 2012.

Basis for Qualified Opinion

1. Incomplete Property, Plant and Equipment

The statement of financial position reflects property, plant and equipment balance of Kshs.10,751,169 as disclosed in Note 20 to the financial statements. Review of the records relating to the Board's assets revealed that Management had acquired and implemented five (5) software applications for various aspects of the Board operations. However, fair values of the software applications had not been recognized as intangible assets in line with Paragraphs 43 and 74 of International Public Sector Accounting Standards Board (IPSAS) 31 – Intangible Assets. Further, software applications with a cost of Kshs.4,272,260 were categorized under computers and equipment asset class and not as an intangible assets.

In the circumstances, the accuracy and completeness of property, plant and equipment valued at Kshs.10,751,169 as at 30 June, 2021 could not be confirmed.

2. Inconsistencies in Recognition of Receivables from Non-Exchange Transactions

The Management adopted revenue recognition criteria where revenue from levies, penalties and fees are recognized when received as disclosed in Note 4(a) of the summary of significant accounting policies. However, the adoption of the criteria, contradicts clause 11(2) of the licensing guidelines for Water Service Providers (WSPs) which provides that license fees comprise a one-off fee of 0.1% based on last audited turnover payable upon issuance of the license and license operation fee of 4% payable by the 15th day of each month. Therefore, this makes revenue recognized by the Board inconsistent with the asset recognition criteria issued under IPSAS 23 - Revenue from Non-Exchange Transactions. The inconsistency resulted to non-recognition of significant debt obligations owed to the Board by various WSPs.

In the circumstances, the accuracy and completeness of receivables from non-exchange transaction of Kshs.42,155,677 could not be confirmed.

3. Unsupported Board Expenses

The statement of financial performance reflects Board expenses amounting to Kshs.17,752,058 as further disclosed in Note 13 to the financial statements. However, relevant supporting documents for the expenditure such as evidence of travel, mileage claims, attendance registers and journal adjusting vouchers for expenditure amounting to

Kshs.12,104,936 were not provided for audit. The Management also did not provide a notice of meeting and an attendance register for a virtual full Board meeting held on the 10 July, 2020 and for which, allowances amounting to Kshs.236,574 were paid contrary to Regulation 104 of the Public Finance Management (National Government) Regulations, 2015.

Therefore, the accuracy and completeness of the expenditure of Kshs.12,104,936 could not be confirmed.

4. Unsupported Motor Vehicles Maintenance, Fuel and Oil Expenses

The statement of financial performance reflects expenditure on use of goods and services amounting to Kshs.57,781,922. The expenditure, as disclosed in Note 14 to the financial statements, includes repairs and maintenance of motor vehicles expenses amounting to Kshs.3,062,198, out of which, payments totalling Kshs.995,913 were not adequately supported by invoices and inspection reports for repair services and spare parts supplied. Further, the Management operated without an approved Transport Policy and its motor vehicles lacked repairs and service logbooks (GP.55) contrary to its Human Resource Policies and Procedures Manual 2020.

In the circumstances, the accuracy and completeness of the expenditure on repairs and maintenance of motor vehicles amounting to Kshs.995,913 could not be confirmed.

5. Unsupported Journal Entries

Review of accounting records and books presented for audit revealed that journal entries made in the system with a net effect of Kshs.16,678,823 and credit memos amounting to Kshs.4,246,163 were processed during the year under review in various accounts. However, journal adjusting vouchers supporting the entries were not provided for audit. This is contrary to the provisions of Regulation 103(1) of the Public Finance Management (National Government) Regulations, 2015, which states that Journal entries prepared for all adjustments shall be authorized by the Accounting Officer or an officer designated by him or her before posting them in a financial record.

In the circumstances, the accuracy and completeness of revenue of Kshs.230,981,599 and expenses of Kshs.220,348,511 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Water Services Regulatory Board 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 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. There were no key audit matters to report in the year under review.

Other Matter

Unresolved Prior Year Issues

In the audit report of the previous year, several issues were raised under the Report on Lawfulness and Effectiveness in Use of Public Resources, and Report on Effectiveness of Internal Controls, Risk Management and Governance. However, these issues remain unresolved contrary to Section 149(2)(l) of the Public Finance Management Act, 2012 which require the Accounting Officers to resolve any issues resulting from an audit that remain outstanding.

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 Conclusion on Lawfulness and Effectiveness in Use of Public Resources, 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. Exclusion of Notes to the Financial Statements

The Management did not make key disclosures on credit risk, capital commitments and surplus remission in the Notes to financial statements as required by the Annual Financial Reporting Template of 30 June, 2021.

Therefore, the Management was in breach of the financial reporting guidelines issued by the Public Sector Accounting Standards Board.

2. Budget Over-Expenditure

The statement of comparison of budget and actual amounts reflects final receipts budget and actual on comparable basis of Kshs.230,436,678 and Kshs.243,337,477 respectively resulting to an over-funding of Kshs.12,900,799 of the budget. Similarly, the Management spent a total of Kshs.220,348,511 against an approved budget of Kshs.210,000,000 resulting to an over-expenditure of Kshs.10,348,511 or 5% of the budget. This was contrary to the provisions of Regulation 43(b) of the Public Finance Management (National Government) Regulations, 2015.

3. Enforcement of Collection of Regulatory Levy

Review of records relating to licenses revenue revealed that only two (2) out of forty-seven (47) Water Service Providers were compliant with the requirement of remitting a license operation fee of 4% of turnover the 15th day of each month to the regulator. This meant that the Board lost realizable revenue from regulatory levies due to non-compliance of Water Service Providers to the licensing conditions and prevailing service level agreements.

Further, Management did not demonstrate efforts made to enforce the licensing conditions, thus not complying with its statutory obligation as provided under Section 72(1)(d) of Water Act, 2016.

4. Outstanding Imprest

Review of the system generated data on imprests revealed that a balance of Kshs.25,427,998.80 was outstanding in the imprest and advance control account beyond the stipulated period, contrary to Regulation 93(5) of the Public Finance Management (National Government) Regulations, 2015 that states a holder of a temporary imprest should account or surrender the imprest within seven (7) days after returning to duty station.

Management was therefore 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 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. Lack of Receipt Vouchers

The Management made postings of revenue receipts into the general ledger without preparation of pre-numbered receipt vouchers in the year under review and no such voucher(s) in whatever form were provided for audit. By not conforming to requirements of preparation of receipt vouchers. Therefore, the Management was in contravention of Regulation 104 of the Public Finance Management (National Government) Regulations of 2015 104(1) which states that all receipts and payments vouchers of public moneys shall be properly supported by pre-numbered receipt and payment vouchers and shall be supported by the appropriate authority and documentation.

In the circumstances, the mitigation of risks associated with collection and banking of all revenue could not be confirmed.

2. Incomplete Fixed Assets Register

During the year under review, there was no register of fixed assets maintained in the form prescribed in Appendix 6 of the Guidelines on Asset and Liability Management in the Public Sector of July, 2020 which requires maintenance of a separate folio for each class of assets. The Management also did not capture details of the financier or source of funds, serial number, tag numbers, make and model of motor vehicles, date of delivery or installation, payment voucher number, original location, current location, replacement date (if applicable), date of disposal, disposal value, responsible officer, asset condition, and any other relevant information in a fixed asset register.

In the circumstances, the Management ability to effectively manage and safeguard its assets could not be confirmed.

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 effective processes and systems of internal control, risk management and overall 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.

Responsibilities of Management and Board of Directors

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Public Sector Accounting 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 overall governance.

In preparing the financial statements, Management is responsible for assessing the Board's ability to continue to sustain its services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless Management is aware of the intention to terminate the Board 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, 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 Board's financial reporting process, reviewing the effectiveness of how the Management 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 Board 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 applicable 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 Board's ability to continue 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 Board to cease to continue 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 Board 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.

CPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

31 August, 2022