

# **REPORT OF THE AUDITOR-GENERAL ON KILIFI MARIAKANI WATER AND SEWERAGE COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE, 2023**

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## **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 the 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 Kilifi Mariakani Water and Sewerage Company Limited set out on pages 1 to 50, which comprise the statement of financial position as at 30 June, 2023 and the statement of profit or 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 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 Kilifi Mariakani Water and Sewerage Company Limited as at 30 June, 2023 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 of, 2015, the Public Finance Management Act, 2012 and the Water Act, 2016.

## **Basis for Qualified Opinion**

### **1. Inaccurate Expenditure on General and Operational Expenses**

The statement of profit or loss and other comprehensive income and Note 12 to the financial statements reflects expenditure in respect of general and operational expenses totalling Kshs.459,224,127. Included in the expenditure is Kshs.208,093,920 in respect of bulk water costs. However, during the year under review, a total of Kshs.456,154,265 was incurred on bulk water, mainly on payment of electricity bills on behalf of Coast Water Works Development Agency (CWWDA), resulting to un reconciled variance of Kshs.248,060,345.

In the circumstances, the accuracy and completeness of the expenditure on general and operational expenses totalling Kshs.459,224,127 could not be confirmed.

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

The statement of financial position and Note 20 to the financial statements reflects a balance of Kshs.425,356,133 in respect to property, plant and equipment which includes additions of Kshs.153,098,066. However, a fixed asset register where the different classes of assets are recorded and maintained and the ownership documents for the land, buildings, and motor vehicles were not provided for review.

In the circumstances, the accuracy, ownership and completeness of the property, plant and equipment balance of Kshs.425,356,133 could not be confirmed.

### **3. Unsupported and Long Outstanding Trade and Other Receivables Balance**

The statement of financial position and Note 24 to the financial statements reflects trade and other receivables balance of Kshs.443,248,588 which includes a balance of Kshs.427,250,807 in respect of trade receivables whose details were not provided for review while trade receivables balance of Kshs.338,804,384 have remained uncollected for over ninety-one (91) days. In addition, the trade and other receivables balance include other receivables balance of Kshs.15,237,455 relating to previous years which is under investigations. However, the progress of these investigations has not been provided. Further, the aging analysis in respect of advances balance of Kshs.549,337 on staff receivables on outstanding loans and advances, has not been provided.

In the circumstances, the accuracy, recoverability and completeness of trade and other receivables balance of Kshs.443,248,588 could not be confirmed.

#### **4. Inaccuracy of Total Liabilities Balance**

The statement of financial position reflects a balance of Kshs.1,749,850,938 as total liabilities which includes a balance of Kshs.341,281,262 in respect of bulk water owed to CWWDA. However, the corresponding trade and other receivables balance in the books of CWWDA reflect a balance of Kshs.947,973,999 resulting to unreconciled variance of Kshs.606,692,737. In addition, the liabilities include trade and other payables balance of Kshs.376,526,319 whose details have not been provided.

In the circumstances, the accuracy and completeness of total liabilities balance of Kshs.1,749,850,938 could not be confirmed.

#### **5. Unsupported Capital Reserves Fund Balance**

The statement of financial position reflects capital reserves fund balance of Kshs.50,094,019 which includes land, buildings, motor vehicles, various expenditures and adjustment for cost of bills recognized at the inception of the company. These balances were however not supported with any documentation.

In the circumstances, the accuracy and completeness of the capital reserve fund balance of Kshs.50,094,019 could not be confirmed.

#### **6. Unsupported Coast Water Works Development Agency Liability**

The statement of financial position and Note 28 to the financial statements reflects a balance of Kshs.292,548,843 in respect of CWWDA liability which is part of capital and reserves. As previously reported, Management has not provided details to support the liability disclosed and the balance has remained unexplained despite the continuous increase of the balance.

In the circumstances, the accuracy of CWWDA liability of Kshs.292,548,843 could not be confirmed.

#### **7. Unaccounted for Long-Term Customer Deposits Balance**

The statement of financial position and Note 33 to the financial statements reflects trade and other payables balance of Kshs.376,526,319 which includes a balance of Kshs.92,772,272 in respect of long-term customer deposit. However, a local Commercial Bank deposit bank account reflects a balance of Kshs.69,296 resulting to unexplained variance of Kshs.92,702,976.

In the circumstances, the accuracy and completeness of long-term customer deposit balance of Kshs.92,772,272 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Kilifi Mariakani Water and Sewerage Company 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 qualified opinion.

## **Emphasis of Matter**

### **1. Budgetary Control and Performance**

The statement of comparison of budget and actual amounts reflects final revenue budget and actual on comparable basis of Kshs.824,502,253 and Kshs.697,320,045 respectively resulting to a revenue shortfall of Kshs.127,182,208 or 15% of the budget. Similarly, Management expended Kshs.795,962,751 against an approved budget of Kshs.710,056,522 resulting to an over-expenditure of Kshs.85,906,299 or 12% of the budget.

The underfunding and over expenditure affected the planned activities and may have impacted negatively on service delivery to the public.

### **2. Contingent Liabilities**

Note 40 to the financial statement on financial risk management section discloses that the Company did not have any known contingent liabilities in the period under consideration. Review of records revealed that Company incurred a total cost of Kshs.473,900 on legal expenses and had eleven (11) active court cases in which they were the defendants. However, the Company has not made a provision for the contingent liabilities likely to occur in the event of losing any of the cases. In addition, the contingent liabilities have not been disclosed by way of footnotes to the financial statements.

My opinion is not modified in respect of these matters.

## **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**

### **1. Failure to Offer Sewerage Services**

The Memorandum of Association and as prescribed in the Water Act, 2016 the Company is mandated to offer sewerage services within the towns of Kilifi, Kaloleni, Malindi, Magarini, Rabai and its environs. Review of the Company's financial records revealed that the Company has not offered these services in the past and did not do so in the year under review. There was however no explanation why the company has failed to offer this service as mandated.

### **2. Unresolved Prior Year Matters**

Various prior year audit issues remained unresolved as at 30 June, 2023. Even though Management indicates progress has been made in resolving the issues, evidence has not been provided and the issues remain unresolved. This is contrary to Section 68, 2 (l) of the Public Finance Management Act, 2012 which states that the accounting officer shall take appropriate measures to resolve any issues arising from audit which may remain outstanding. Management has not provided satisfactory explanation for the delay in resolving the issues.

## 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 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**

#### **1. Excessive Non-Revenue Water**

The statement of profit or loss and other comprehensive income and Note 6 to the financial statements reflects operating revenue of Kshs.548,894,965. Review of records revealed that the Company produced a total of 10,334,725 cubic meters (M<sup>3</sup>) of water. However, only 5,674,186 cubic meters (M<sup>3</sup>) of water was billed to customers. The balance of 4,660,539 cubic meters (M<sup>3</sup>) or 45% of the total volume of water produced was not billed accounting for 20 percentage points over and above the allowable limit of 25% by Water Service Regulatory Board Guidelines. Management attributed the loss to old and dilapidated water supply network, illegal water connections and old inaccurate and stalled customer meters that don't give correct customer consumptions. The 4,660,539 cubic meters Non-Revenue Water may have resulted into a loss estimated at Kshs.450,839,361.

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

#### **2. Failure to Observe Third Net Pay Rule**

A review of the payroll revealed that a number of employees as detailed below had deductions that were more than two thirds of their basic pay, contrary to provision of Section 19(3) of the Employment Act which states that the total amount of all deductions which under the provisions of subsection (1), may be made by an employer from the wages of his employee at any one time shall not exceed two thirds of such wages or such additional or other amount as may be prescribed by the Minister either generally or in relation to a specified employer or employee or class of employers or employees or any trade or industry.

<b>Month</b>	<b>Basic Pay Kshs.</b>	<b>Net Pay Below 1/3 of Basic Kshs.</b>
July, 2022	44,543	14,141
July, 2022	60,000	19,044
August, 2022	172,000	49,958
August, 2022	72,000	20,107
October, 2022	24,000	7,714
October, 2022	134,200	34,334
November, 2022	38,289	12,522
December, 2022	42,316	12,304
March, 2023	35,634	11,849
March, 2023	39,359	12,731
March, 2023	59,561	19,678
March, 2023	35,700	11,722
May, 2023	60,000	18,317
May, 2023	35,700	19,763
June, 2023	34,000	11,134
June, 2023	24,000	7,879

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

### **3. Failure to Adhere to National Cohesion and Integration Act**

Examination of the personnel records indicated that the total number of employees of the Company were two hundred and sixty-six (266), out of which two hundred forty-six (246) or 92.4% were from the dominant local ethnic community contrary to Section 65 (e) of the County Government Act, 2012 and the National Cohesion and integration Act which states that no public establishment shall have more than one third of its staff from the same ethnic community.

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

### **4. Lack of Gender Balance**

Review of documents provided indicates that two hundred and sixteen (216) members of staff of the water Company, representing eighty one percent (81%) of all staff under permanent and contract terms were male contrary to Section B. 22 (2) of the Human Resource Policies and Procedures Manual for the Public Service, 2016 on non-discrimination in employment which provides that the Government will endeavour to have a gender balanced Civil Service by ensuring that not more than two thirds of positions in its establishment are filled by either gender.

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

### **5. Accrued Tax Liability**

Included in the statement of financial position as disclosed in Note 33 to the financial statement is an amount of Kshs.376,526,319 being trade and other payables balance

which includes an outstanding tax liability balance of Kshs.18,300,794 with no movement from the previous year. Management did not explain the outstanding tax liability and did not give a payment plan on settling the liability. This is contrary to the provisions of the Income Tax Act, Cap 470 Section 92 (a) which requires that all taxes due shall be paid on or before 30 September of the following year.

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

## **6. Use of Expired Water Sales Tariff**

The statement of profit or loss and other comprehensive income and Note 6 to the financial statements reflects operating revenue totalling Kshs.548,894,965. Review of records revealed that the water tariff used in billing was approved through Gazette Notice No.7535 dated 4 August, 2017 for the period 2017/2018 to 2019/2020 financial years and was not renewed by WASREB as required.

In the circumstances, Management was 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**

#### **Lack of an Efficient Inventory Control System**

The statement of financial position revealed inventories balance of Kshs.19,338,241. During a physical verification of the inventory receipt and issue system in the stores department, it was observed that the store records are maintained in manual form through the use of stock cards. However, the system in place did not provide details about who requested the inventory issue, the location of the issue, and the customer (in the case of meters) to enable tracing of the issued inventory. In addition, the system does not provide ways of determining utilizations, reorder levels, and obsolete inventory held in the store.

Further, it was observed that the water inventory was not recorded despite the Company purchasing bulk water total volume of 10,880,179 cubic meters (M<sup>3</sup>) worth Kshs.233,699,960, which generated an operating revenue of Kshs.548,894,965.

As a result, the effectiveness of internal controls, risk management and governance of the inventory system 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 the Board of Directors**

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 overall governance.

In preparing the financial statements, Management is responsible for assessing the Company's ability 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, 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 Company's financial reporting process, reviewing the effectiveness of how 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 controls 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 controls would not necessarily disclose all matters in the internal controls 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 controls 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 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 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 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 Nancy Gathungu, CBS**  
**AUDITOR-GENERAL**

**Nairobi**

**29 April, 2024**