

REPORT OF THE AUDITOR-GENERAL ON MALINDI WATER AND SEWERAGE COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE, 2023

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 Malindi Water and Sewerage Company Limited set out on pages 1 to 53, which comprise of 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 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 the Malindi Water and Sewerage Company Limited as at 30 June, 2023 and its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRS) Accrual Basis and comply with the Public Finance Management Act, 2012, Companies Act, 2015 and the Water Act, 2016.

Basis for Qualified Opinion

1. Omitted Expenditure on Electricity Bills

The statement of profit or loss and other comprehensive income reflects total operating expenses of Kshs.612,053,159. Available information indicates that during the year under review, payments in respect of electricity bills amounting to Kshs.136,855,149 was made to Kenya Power and Lighting Company (KPLC) on behalf of Coast Water Works Development Agency (CWWDA). However, this expenditure has not been disclosed in the statement of profit or loss and other comprehensive income.

In the circumstances, the accuracy and completeness of the total operating expenses of Kshs.612,053,159 could not be confirmed.

2. Unexplained Variance in Trade and Other Payables Balance

The statement of financial position and as disclosed in Note 34 to the financial statements reflects trade and other payables balance of Kshs.901,675,036 which includes Kshs.510,377,647 owed to Coast Water Works Development Agency (CWWDA). However, review of records maintained by the Agency indicates that the amount owed by the Company to the Agency is Kshs.506,375,138 resulting in unexplained variance of Kshs.4,002,509.

In the circumstances, the accuracy and completeness of trade and other payables balance of Kshs.901,675,036 could not be confirmed.

3. Understatement of Inventories Balance

The statement of financial position and Note 23 to the financial statements reflects inventories balance of Kshs.54,250,974. However, inventory of water and chlorine have not been disclosed.

In the circumstances, the accuracy and completeness of inventories balance of Kshs.54,250,974 could not be confirmed.

4. Long Outstanding Trade and Other Receivables Balance

The statement of financial position and Note 24 to the financial statements reflects a balance of Kshs.380,317,011 in respect of trade and other receivables. Included in this balance is Kshs.217,121,994 in respect of debts which had been outstanding for more than six (6) months. In addition, these customers' accounts did not reflect current bills, an

indication that they may have been disconnected or suspended and no evidence of debt recovery measures in place was provided for audit review.

In the circumstances, the accuracy and recoverability of trade and other receivables balance of Kshs.380,317,011 could not be confirmed.

5. Long Outstanding Customer Deposit Receivable

The statement of financial position and Note 26 to the financial statements reflects customer deposit receivable balance of Kshs.8,443,600 which were long outstanding. Management indicated that the deposits were in respect of customer fixed deposits received before the inception of the Company in 2006 and was to be refunded by Coast Water Works Development Agency (CWWDA). However, no refund had been as at the time of audit in January, 2024.

In the circumstances, the accuracy and recoverability of the customer deposit receivable balance of Kshs.8,443,600 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Malindi 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

Budgetary Control and Performance

The statement of comparison of budget and actual amounts reflects final revenue budget and actual on comparable basis of Kshs.1,175,466,185 and Kshs.618,108,591 respectively, resulting in an under-funding of Kshs.557,357,593 or 47% of the budget. Similarly, the Company expended Kshs.1,161,249,742 against an approved budget of Kshs.1,175,466,184, resulting in an under-expenditure of Kshs.14,216,442 or 1% of the budget.

The underfunding of the approved budget affected the planned activities and may have impacted negatively on service delivery to the public.

My opinion is not modified in respect of this matter.

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 Matters

Various prior year audit issues remained unresolved as at 30 June, 2023. Although Management has indicated that the issues have either been resolved or partially resolved, no evidence or explanation was provided to support that assertion.

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

1. Non-Compliance with Law on Ethnic and Gender Composition

Review of payroll records revealed that the Company had a staff establishment of two hundred and thirteen (213) employees out of which one hundred and fifty-six (156) or 73% were from the dominant ethnic community in the County contrary to Section 7(2) of the National Cohesion and Integration Act, 2008 which states that no public establishment shall have more than one third of its staff from the same ethnic community. In addition, one hundred and seventy-six (176) or 83% employees were male while thirty-seven (37) or 17% were female. This was contrary to paragraph B.22 (2) of the Public Service Commission Human Resource Policies and Procedures Manual, 2015 which states that the Government will endeavor to have a gender balanced Civil Service by ensuring that not more than two-thirds (2/3) of positions in its establishment are filled by either gender.

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

2. Excessive Expenditure on Board Meetings

The statement of profit or loss and other comprehensive income and Note 13 to the financial statements reflects Board expenses amounting to Kshs.5,717,039. Review of records revealed that the Board held ten (10) full Board meetings during the year under review contrary to Office of the President Circular reference number OP/CAB.9/1A dated 11 March, 2020 paragraph A (2) which states that the Board meetings shall be restricted to a minimum of four(4) and capped at a maximum of six (6) for each financial year resulting to excess expenditure of Kshs.2,286,816.

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

3. Non-Remittance of Pension Deductions

The statement of financial position and Note 37 to the financial statements reflects a balance of Kshs.109,339,387 in respect of retirement benefit obligations. Review of records revealed that this balance is owed to LAPTRUST as pension scheme contribution that had not been remitted as at 30 June, 2023. In addition, Management has not disclosed the interest and penalties which the unremitted balance had attracted.

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

4. Long Outstanding Trade and Other Payables Balance

The statement of financial position and Note 34 to the financial statements reflects trade and other payables balance of Kshs.901,675,036 which includes a balance of trade payables that have been outstanding for over ninety (90) days of Kshs.861,528,814.

In the circumstances, the non-settlement of trade and other payables as they fall due may result in payment of fines and penalties.

5. 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.499,912,102 which includes revenues from water sales totalling Kshs.483,153,452. 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 year 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 matter 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

Officer Serving in Acting Capacity Beyond Stipulated Period

Records provided for audit review indicated that the Deputy Technical Manager was appointed as the Acting Manager Sanitation with effect from 1 June, 2021. It was stated in the letter that the acting appointment would be for six (6) months without allowances. However, at the time of audit in January, 2024, or nineteen (19) months after the appointment, the officer was still serving in the same capacity. No explanation was provided for the acting appointment beyond the stipulated period and for failure to confirm the officer or substantively fill the position.

In the circumstances, the existence of effective human resource policy guidelines to manage and deploy staff 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.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Kenyan Companies Act, 2015, 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 Company, so far as appears from the examination of those records; and,
- iii. The Company's financial statements are in agreement with the accounting records and returns.

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 (IFRS) and for maintaining effective internal controls 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 controls, 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 terminate 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 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 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 Management.
- Conclude on the appropriateness of 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 Management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal controls that are identified during the audit.

I also provide Management with a statement that I have complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on my independence and where applicable, related safeguards.



FCPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

29 April, 2024