REPORT OF THE AUDITOR-GENERAL ON GARISSA 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, 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 Company 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 Company.

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

Adverse Opinion

I have audited the accompanying financial statements of Garissa Water and Sewerage Company Limited set out on pages 1 to 45, 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 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 Garissa 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) and do not comply with the Water Act, 2016 and the Public Finance Management Act, 2012.

Basis for Adverse Opinion

1.0 Revenue

1.1 Failure to Bill all Customers

The statement of profit or loss and other comprehensive income reflects operating revenue amount of Kshs.301,060,526 in respect of water sales and as disclosed in Note 6 to the financial statements . However, review of the income records revealed that the number of customers served by the Company were 18,126, out of which only 7,927 or 44% are metered. Water billing was done to only 2,420 metered customers leaving 5,507 metered customers not billed, hence loss of revenue. In addition, the Company has been using expired water tariffs approved on 14 May, 2010 and expected to have been reviewed on June, 2012 for further adjustment as per Gazette Notice No.5321, Vol. CXII – No.49, page 1724.

In the circumstances, the accuracy and completeness of operating revenue balance of Kshs.301,060,526 could not be confirmed.

2.0 Unsupported Trade Receivables

The statement of financial position reflects trade and other receivables balance of Kshs.868,725,168 as disclosed in Note 17 to the financial statements. However, the Management did not maintain an updated receivables' ledger that would show balance brought forward, amount accrued during the year, payments received and balance carried forward. In addition, a breakdown illustrating gross trade receivables, provision for doubtful receivables and net trade receivables were also not provided for audit.

In the circumstances, the accuracy and completeness of trade and other receivables balance of Kshs.868,725,168 could not be confirmed.

3.0 Variances in Cash and Cash Equivalents

The statement of financial position reflects bank and cash balances of Kshs.16,537,977 and as disclosed under Note 18 to the financial statements. However, three (3) bank reconciliation statements for revenue accounts at First Community Bank, development account at Kenya Commercial Bank and reserve account at First Community Bank reflects cash book opening balance of Kshs.755,049 and two (2) Nil balances while the audited cash book closing balance reflects an amount of Kshs.430,473, Kshs.438,664 and an overdrawn amount of Kshs.27,908,052 respectively, resulting in unexplained variance of Kshs.27,756,300.

In the circumstances, the accuracy and completeness of the cash and cash equivalents balance of Kshs.16,537,977 could not be confirmed.

4.0 Unrecorded Meter Deposits

The statement of financial position reflects trade and other payables balance of Kshs.224,620,998 and as disclosed in Note 23 to the financial statements. Included in the schedule supporting the amount is Nil balance for meter deposits. However, review of income ledgers revealed that customers paid unknown amount of meter deposits during water connections but the Management did not maintain a separate bank account for customer deposits and relevant register. Further, the Management did not account for the customer deposits as payables but income contrary to best accounting practices.

In the circumstances, the disclosure, accuracy and completeness of trade and other payables balance of Kshs.224,620,998 could not be confirmed.

5.0 Lack of Updated Fixed Asset Register

The statement of financial position reflects property, plant and equipment (PPE) net book value of Kshs.205,137,781 and as disclosed in Note 16 to the financial statements. However, the Management failed to prepare a fixed asset register in the prescribed format, lacking essential details such as identification or serial numbers, tag numbers, make/model, delivery/installation dates, depreciation rates, annual depreciation, accumulated depreciation, net book value, disposal dates, disposal values, responsible officer details, dates of revaluation, revaluation amounts and asset conditions.

In addition, ownership documents, such as the letter of allotment or title deeds for parcels of land with a net book value of Kshs.668,095, was not provided for audit . Further, five (5) motor vehicle logbooks used by the Company as collateral for a loan of Kshs.25,000,000, were not provided for audit despite the loan having matured on 26 February, 2023 and the related amount being settled.

In the circumstances, the accuracy and completeness of the property, plant and equipment balance of Kshs.205,137,781 could not be confirmed.

6.0 Unsupported WASREB and WARMA Fees

The statement of profit or loss and other comprehensive income reflects operating expenditure of Kshs.101,132,508 and as disclosed in Note 11 to the financial statements. The balance includes an amount of Kshs.2,121,858 and Kshs.1,800,000 for WASREB Levies and WARMA water use charges respectively. However, Management did not provide invoices and permit from the regulatory body.

In the circumstances, the accuracy and completeness of the combined operating expenditure of Kshs.3,921,858 could not be confirmed.

7.0 Unsupported Project Cost

The statement of profit or loss and other comprehensive Income reflects project cost of Kshs.457,070,285 and as disclosed in Note 15 to the financial statements. The amount includes Kshs.4,119,956 and Kshs.6,683,849 in respect of domestic travel and repair and maintenance of motor vehicles respectively. However, included in the domestic travel is an amount of Kshs.1,436,500 that was not supported with imprest warrants, approval of activities, work plans, signed payment schedules and motor vehicle work tickets. In addition, repair and maintenance of motor vehicles of Kshs.6,683,849 was not supported with user requisitions, pre and post inspection reports in support of the repairs and maintenance services.

In the circumstances, the accuracy and regularity of the expenditure of Kshs.1,436,500 and Kshs.6,683,849 for domestic travel and repair and maintenance of motor vehicles could not be confirmed.

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

1.0 Unresolved Prior Year Matters

Prior year audit issues remained unresolved as at 30 June, 2023. Management has not provided reasons for the delay in resolving the prior year audit issues.

2.0 Stalled Projects

Review of the project’s implementation status report as at 30 June, 2023 revealed that six (6) projects with contract sums totalling to Kshs.137,006,335 had stalled. However, the Management did not provide any reason for the stalling of these projects.
In the circumstances, the stalled projects will affect delivery of service to the public and could also lead to increased project costs, time overruns, and a negative impact on the overall efficiency of resource utilization.

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.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

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

Basis for Conclusion

1.0 Non-Revenue Water

Water abstraction records revealed that the quantity of water produced during the financial year under review was 4,400,699M^3 and the quantity of water billed for consumption was 3,035,887M^3, resulting to water sales valued at Kshs.301,060,526 as reported in Note 6 to the financial statements. The difference of water quantity amounting to 1,364,812M^3, which translates to approximately 44% of water produced was neither billed nor accounted for. The 44% is above the recommended rate of 25% by 19% whose estimated abnormal loss of water sales is Kshs.73,699,848

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

2.0 Irregularities in Procurement of Genset Fuel

The statement of profit or loss and other Comprehensive Income reflects project cost of Kshs.457,070,285 and as reflected under Note 15 to the financial statements. The balance includes an amount of Kshs.20,528,897 in respect of other expenses relating to water and sanitation development project funded by the World bank. Review of fuel records revealed that the Company used direct procurement to acquire genset fuel amounting to Kshs.15,400,000. In addition, detail orders, fuel register, supplier statements or generator worksheets showing the number of hours the generators were running and amount of fuel consumed were not provided for audit.
Further, the Management did not fairly and equitably distribute the procurement of chemicals to all the pre-qualified suppliers as one supplier was awarded and paid 85% of total expenditure on chemicals during the year under review.

In the circumstances, the regularity and value for money of the procurement of chemicals could not be confirmed**.**

3.0 Non-Remittance of Statutory Deductions

3.1 Non-Remittance of Pay As You Earn (PAYE) Deductions

The statement of financial position reflects trade and other payables balance of Kshs.224,620,998 as disclosed in Note 23 to the financial statements. Included in the amount is Kshs.24,815,265 for Pay As You Earn (PAYE). However, review of payroll and ledgers revealed deductions amounting to Kshs.9,039,725 during the year under review, resulting to a cumulative amount of Kshs.24,815,265 not remitted to the Kenya Revenue Authority contrary to Income Tax Act, Cap 470.

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

3.2 Non-Remittance of National Social Security Fund and National Hospital Insurance Fund Dues

The statement of financial position reflects trade and other payables balance of Kshs.224,620,998 as disclosed in Note 23 to the financial statements. The amount includes Kshs.2,553,737 and Kshs.558,650 due to the National Social Security Fund and National Hospital Insurance Fund respectively. However, these amounts were not remitted to National Social Security Fund and National Hospital Insurance Fund contrary to Section 20 (6) of the National Social Security Fund Regulations of 2014 and Section 18(2) of the National Hospital Insurance Act, 2008.

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

4.0 Provision of Water Services Without a License

Review of the records reveals that the Company has been operating without a license from the Regulatory Board. This was contrary to Section 85(1) of Water Act, 2016 which states that, a person shall not provide water services except under a license issued by the Regulatory Board, upon submission of an application and such supporting documents as the Board may require.

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

5.0 Non-compliance with Budget Process Deadlines

During the year under review, the Board approved the Company's budget on 19 August, 2022, three (3) months after commencement of the financial year contrary to Section 128 (1) of the Water Act, 2016 that requires estimates of revenue and expenditure of the water company be prepared three (3) months before the commencement of the financial year.

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

6.0 Imprest Management

The statement of profit or loss and other Comprehensive Income reflects administrative expenses balance of Kshs.51,909,642 and as disclosed in Note 10 to the financial statements, which includes Kshs.1,045,000 in respect of travelling and accommodation. It was, however, noted that staff were issued with cash through signed petty cash forms instead of standard imprest warrant (GP26) contrary to Section 91(2) of Public Finance Management (County Government) Regulations, 2015, which requires that the officer authorized to hold and operate an imprest shall make formal application for the imprest through an imprest warrant.

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

7.0 Budget Over-Expenditure

The statement of comparison of budget and actual amounts reflects final income budget and actual on comparable basis of Kshs.326,932,369 and Kshs.799,236,210 respectively, resulting to an over-funding of Kshs.472,303,841 or 59% of the approved budget. Similarly, the statement reflects final expenditure budget and actual on comparable basis of Kshs.364,824,128 and Kshs.741,492,313 respectively, resulting to an over-expenditure of Kshs.376,668,185 or 52% of the approved budget. The over-funding and over-spending indicate a misalignment between the budgetary allocation and the actual financial requirements of the organization. The over spending was against Section 107.(1) of public Finance Management Act, 2021 that requires a County entity to manage its public finances in accordance with the principles of fiscal responsibility. This will impact negatively on the implementation of other programs of the Company.

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, because of the significance of the matters discussed in the Basis for Adverse Opinion and Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance section of my report, based on the audit procedures performed, I confirm that, internal controls, risk management and overall governance were not effective.

Basis for Conclusion

1.0 Non-Establishment of Internal Audit Committee

During the year under review, the Company operated without an Audit committee contrary to Section 155(5) of the Public Finance Management Act, 2012 which states that the entity shall establish an internal audit committee.

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

2.0 Weak Information Technology (IT) Internal Controls

The Company did not have reliable Information Communication Technology (ICT) controls and an IT department despite operating Information Technology (IT) enabled environment like billing software. The Company does not have approved policies on Information Technology security including disaster recovery plan and IT continuity plan, consequently the critical data/information may not be recovered in case a disaster occurs. In addition, the Company does not have IT strategic or steering committees which could result in non-implementation of IT governance, as part of enterprise governance. Further, there were no fire suppression systems therefore the information may be lost in case of a fire outbreak.

In the circumstances, effectiveness in internal controls in the management of the Company's IT environment could not be confirmed.

3.0 Lack of Approved Staff Establishment

Review of the human resource records indicated that the Company did not have an approved staff establishment structure. It was, therefore, not clear how staffing requirements were determined and whether the resources allocated to the function were used in an optimal way. This was contrary to paragraph B 6 (3) of the County Public Service Human Resource Manual, 2013 which provides that in the recruitment process, due consideration will be given to appropriate organizational structure in each department and optimal staffing levels.

In the circumstances, optimal distribution of human resources which may result in overlap in roles or shortages in critical areas, 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 Companies Act, 2015, I report based on my audit, that:

i. I have not 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 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 the accounting records and returns.

Responsibilities of Management and 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 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 governance.

In preparing the financial statements, Management is responsible for assessing the Company's going concern, disclosing, as applicable, matters related to the 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 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 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
<u>AUDITOR-GENERAL</u>

Nairobi

16 January, 2024