

REPORT OF THE AUDITOR-GENERAL ON GULF WATER SERVICES 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

Disclaimer of Opinion

I have audited the accompanying financial statements of Gulf Water Services Company Limited set out on pages 1 to 38, 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 do not express an opinion on the accompanying financial statements. Because of the significance of the matters discussed in the Basis for Disclaimer of Opinion section of my

report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for Disclaimer of Opinion

1. Non-Submission of Financial Statements

According to the information provided in the audited financial statements for the year ended 30 June, 2010 the Company was incorporated in the year 2007. However, the Company did not prepare and submit financial statements for twelve (12) financial years ended 30 June, 2011 to 30 June, 2022. This was contrary to Section 149 (2) of the Public Finance Management Act, 2012 which provides that an Accounting Officer shall, in respect of the entity concerned not later than three (3) months after the end of each financial year, prepare annual financial statements for that financial year and submit them to the Auditor-General for audit, with a copy to the County Treasury. Further, it was not possible to confirm the opening balances given that the comparative figures brought forward from the financial year 2011 to financial year were not audited.

In the circumstances, the accuracy and completeness of the financial statements could not be confirmed.

2. Presentation of the Financial Statements

Review of the financial statements presented for audit revealed that disclosures in the non-financial information section of the financial statements were not included in the financial statements. In addition, the financial statements were not signed by the Chief Executive Officer, Head of Finance and the Chairman of the Board. Further, mandatory disclosures including intangible assets, inventories, related party disclosures, analysis of County Government contribution, analysis of customer deposits and projects implemented by the Company were not included in the financial statements.

In the circumstances, the financial statements were not in compliance with the format prescribed by the Public Sector Accounting Standards Board.

3. Inaccuracies in Cash and Bank Balances

The statement of financial position and as disclosed in Note 30 to the financial statements reflects bank and cash balances of Kshs.793,614, comprising of cash at bank of Kshs.673,932 and cash in hand of Kshs.119,682. However, the board of survey reports to support the balances were not provided for audit.

In the circumstances, the accuracy of the cash and bank balance of Kshs.793,614 could not be confirmed.

4. Unsupported Revenue

The statement of profit or loss and other comprehensive income reflects total revenue amount of Kshs.77,526,185 which includes operating revenue amount of

Kshs.19,977,017. However, supporting schedules and primary revenue records including daily/weekly revenue summaries indicating actual transactions details such as revenue source, dates and amount for the operating income amount of Kshs.32,883,428 were not provided for audit. Further, electricity expenses amounting to Kshs.12,022,106 paid by the County Government of Kisumu on behalf of the Company were not disclosed in the financial statements as income-in kind.

In the circumstances, the accuracy and completeness of the total revenue of Kshs.77,526,185 could not be confirmed.

5. Unsupported Trade and Other Receivables

The statement of financial position reflects trade and other receivables balance of Kshs.14,237,848 as disclosed in Note 28 of the financial statements. However, the Company did not maintain an updated debtors' ledger to support the balance. In addition, the Company did not have a Debt Management Policy and policy on provision for bad and doubtful debts. The debtors were not circularized for independent confirmation.

In the circumstances, the accuracy and completeness of trade and other receivables balance of Kshs.14,237,848 could not be confirmed.

6. Long Outstanding Trade and Other Payables

The statement of financial position reflects trade and other payables balance of Kshs.7,785,065 as disclosed in Note 40 to the financial statements. Included in the balance is an amount of Kshs.5,523,186 which was outstanding for more than one year. Management did not provide measures put in place to settle the outstanding amounts.

Failure to settle debts in time may lead the Company into litigations resulting in fines and penalties.

7. Failure to Maintain Fixed Asset Register

The statement of financial position reflects property, plant and equipment net book value of Kshs.20,136,378 as reflected in Note 20 to the financial statements. However, the Management did not provide a fixed asset register to support the assets constituting the balance.

In the circumstances, the accuracy and completeness of property, plant and equipment balance of Kshs.20,136,378 could not be confirmed.

8. Unsupported Water Network Maintenance Expenses

The statement of profit or loss and other compressive income reflects maintenance expenses of Kshs.11,070,412 as disclosed in Note 13 to the financial statements. However, payment vouchers, procurement files, requisition letters from the user department, Local Purchase Orders and Local Service Orders to support the goods procured and services rendered were not provided for audit.

In the circumstances, the accuracy and completeness of the maintenance expenses amount of Kshs.11,070,412 could not be confirmed.

9. Unaccounted for Customer Deposits

The statement of financial position reflects customer water deposits balance of Kshs.2,570,350 and as disclosed in Note 39 to the financial statements. However, the Company maintained one bank account for its operations where customer water deposits were also deposited.

In the circumstances, the accuracy, completeness and existence of customer water deposits balance of Kshs.2,570,350 could not be confirmed.

10. Non-Revenue Water

During the year under review, the Company produced a total of 1,048,226 cubic meters (M³) of water. However, 338,230 M³ were billed to customers, resulting to Non-Revenue Water (NRW) of 709,996 M³ or 63% which was over and above the NRW level of 25% recommended by the Water Service Regulatory Board (WASREB). This may have resulted to loss of water sales revenue estimated at Kshs.92,299,480 at a rate of Kshs.130 per cubic meter. Further, the Company operated without Non-Revenue Water function as required by the Water Services Regulatory Board. It was therefore not possible to confirm whether Management was committed to reducing the high levels of Non-Revenue Water.

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

11. Non-Establishment of Non-Revenue Water Function

During the year under review, the Company operated without Non-Revenue Water function as required by the Water Services Regulatory Board. It was therefore not possible to confirm whether Management was committed to reducing the high levels of Non-Revenue Water.

Without the Non-Revenue Water function, the Company may not be able to reduce Non-Revenue Water to recommended levels.

12. Operation Without a Board of Directors

During the year under review, the Company did not have a Board of Directors in place. This was contrary to Section 79(1) of the Water Act, 2016 which provides that water services provider shall have a Board of Directors and in the case of a Company the members of its Board of Directors shall be constituted in accordance with the Companies Act, 2015 and the directors shall be nominated to serve on the Board in accordance with the company's Memorandum and Articles of Association.

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

13. Lack of Substantive Accounting Officer

Information provided during the audit and records examined revealed that the operations and management of the Company were undertaken by a team from the Kisumu Water and Sewerage Company Ltd. As a result, the Company operated without a substantive Managing Director and a management team.

In the absence a substantive accounting officer and management team, it was not possible to confirm the effectiveness of governance processes in the Company.

14. Lack of Company's Incorporation Documents

Management did not provide Memorandum of Association, Articles of Association and CR12 indicating names of Company Directors for audit review.

In the circumstances, the registration and shareholding status of the Company could not be confirmed.

15. Lack of a License from the Water Services Regulatory Board

The Company operated without a license from the Water Services Regulatory Board. This was contrary to Section 85(1) of the Water Act, 2016 which provides 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 circumstances, Management was in breach of the law.

16. Non-Remittance of Regulatory Fees

The statement of financial position reflects trade and other payables under current liabilities balance of Kshs.7,592,936 as disclosed in Note 40 to the financial statements. Included in this amount is a long outstanding payables to the Water Services Regulatory Board of Kshs.374,634. No explanation was provided for the failure to settle the outstanding amount.

Failure to settle long outstanding debts may result in losses in case of fines and penalties.

17. Lack of an Approved Procurement Plan

The Company did not have an approved procurement plan as required by Section 53(2) and (5) of the Public Procurement and Asset Disposal Act, 2015 which requires entities to have in place procurement and asset disposal plans that are based on indicative or approved budgets which shall be integrated with the applicable budget process.

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

18. Lack of Risk Management Policy and Disaster Recovery Plan

The Company did not put in place risk management policies, strategies, disaster recovery plan and risk register to mitigate risk. This was in contravention of Regulation 158(1) of the Public Finance Management (County Governments) Regulations, 2015 which

provides that the Accounting Officer shall ensure that; (a) the County Government entity develops risk management strategies, which include fraud prevention mechanisms; and (b) The County Government entity develops a system of risk management and internal control that build robust business operations.

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

19. Non-Compliance with Law on Ethnic Composition

The Company had a total of twenty-four (24) employees out of whom 87% of the employees were from the same ethnic community. This was contrary to Section 7(1) and (2) of the National Cohesion and Integration Act, 2008 which provides that all public establishments shall seek to represent the diversity of the people of Kenya in the employment of staff and 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.

20. Lack of a Strategic Plan

The Company operated without a strategic plan. It was therefore not possible to confirm whether the Company's budget was aligned to the strategic objectives of the Company. This was contrary to Section 149(2)(g) of the Public Finance Management Act, 2012 which provides that an accounting officer shall, in respect of the entity concerned prepare a strategic plan for the entity in conformity with the medium-term fiscal framework and financial objectives of the county government.

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

21. Lack of Policy Documents

The Company did not have an approved Information Technology Security Policy, IT Strategic Plan and IT Continuity Plan. In addition, the Company did not have IT strategic or steering committees. Further, there were no fire suppression systems to mitigate loss in case of a fire outbreak.

In the circumstances, the existence of effective risk management in the Company could not be confirmed.

22. Weaknesses in the Billing System

Review of the billing system in place revealed that the billing module which was used for generating bills, viewing bills and updating balances was not able to extract the balances for customers. Further, the customer data module which was used to capture all the customer's data could not track active and dormant customers.

In the circumstances, the credibility, integrity and reliability of the input, storage, processing and output of the Company's data and information could not be confirmed.

23. Weaknesses in Human Resource Management

Review of the Company's payroll revealed that the Company had twenty-four (24) employees out of which two (2) employees were seconded from Kisumu Water and Sewerage Company Limited. However, review of payroll and personal files for twenty-two (22) employees directly engaged by the Company revealed that the payrolls were not verified on a monthly basis and authorized by a senior official.

In addition, key information such as job groups were missing in the payrolls. Further, the Company operated without a human resource policy manual, staff establishment and scheme of service.

In the circumstances, it was not possible to confirm the existence of effective internal controls on staff recruitment, promotions and management in the Company.

24. Failure to Establish an Internal Audit Function and Audit Committee

The Company did not have an internal audit function and Audit Committee as required by Regulation 167(1) of the Public Finance Management (County Governments) Regulations, 2015 which provides that subject to paragraph (2) of this regulation, each county government entity shall establish an audit committee.

In the circumstances, the existence of effective risk management and governance processes in the Company could not be confirmed.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

I do not express a conclusion on the lawfulness and effectiveness in the use of public resources as required by Article 229(6) of the Constitution. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit conclusion.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

I do not express a conclusion on the lawfulness and effectiveness in the use of public resources as required by Article 229(6) of the Constitution. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit conclusion.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Companies Act, 2015, Because of the significance of the matters under the Basis for Disclaimer of Opinion section of my report, 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 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

My responsibility is to conduct an audit of the Company's financial statements in accordance with International Standards of Supreme Audit Institutions (ISSAIs) 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. However, because of the matters described in the Basis

for Disclaimer of Opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

In addition, my responsibility is 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. I also consider internal controls, risk management and governance processes and systems in order to give an assurance on the effectiveness of internal controls, risk management and governance 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. However, because of the matters discussed in the Basis for Disclaimer of Opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit conclusion on lawfulness and effectiveness in use of public resources, and on effectiveness of internal controls, risk management and governance.

I am independent of the Gulf Water Services 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.



FCPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

26 March, 2024