

REPORT OF THE AUDITOR-GENERAL ON MANDERA 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 the Government achieves value for money and that such funds are applied for the intended purpose.
- C. Report on the 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, risk management environment and 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 Mandera Water and Sewerage Company Limited set out on pages 1 to 25, which comprise of the statement of financial position as at 30 June, 2023 and the statement of profit or loss and other comprehensive income, the 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 Mandera 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 Water Act, 2016, the Companies Act, 2015 and the Public Finance Management Act, 2012.

Basis for Qualified Opinion

1. Uncertainty on Going Concern

The statement of profit or loss and other comprehensive income reflects loss of Kshs.17,413,551 (2022: Kshs.20,009,010 and 2021: Kshs.20,430,878), decreasing the revenue reserves by Kshs.57,853,439 to negative Kshs.104,800,188 as at 30 June, 2023. This condition indicates existence of a material uncertainty, which may cast significant doubt on the Company's ability to continue as going concern. In addition, out of the total revenue of Kshs.185,089,731 for the year, the Company generated only Kshs.18,689,150 representing 10% of the total revenue. The material uncertainty relating to going concern and measures put in place to improve the Company's financial performance was not disclosed in the financial statements.

In the circumstances, the Company is technically insolvent and its continued operations is dependent on the continued support from the creditors and County Government of Mandera.

2. Unsupported Equity Balance

As was reported in the previous year, the statements financial position reflects members' equity balance of Kshs.61,982,062 consisting of ordinary share capital of Kshs.100,000 and Government investments of Kshs.61,882,062 as disclosed in Note 20 to the financial statements. Documents to support the two balances were not provided for audit review. In addition, the details of the Government investments of Kshs.61,882,062 were not provided given that the Company is wholly owned by the County Government of Mandera through shares.

In the circumstances, the accuracy of the members' equity balance of Kshs.61,982,062 could not be confirmed.

3. Property Plant and Equipment Balance

The statement of financial position reflects property, plant and equipment balance of Kshs.335,245,149 comprising of balances for various classes of fixed assets as disclosed under Note 15 to the financial statements. However, Note 15 reflects negative values of Kshs.5,226,378 for computer and related equipment and Kshs.734,932 for furniture and fittings reducing the net book value of property plant and equipment by the same amount.

Further, seven (7) motor vehicles of undetermined value were not registered in the name of the Company.

In the circumstances, ownership status of the Company's motor vehicles and the accuracy of property, plant and equipment balance of Kshs.335,245,149 could not be confirmed.

4. Unsupported Trade and other Receivables

As was reported in the previous year, the statement of financial position reflects trade and other receivables balance of Kshs.55,422,844 and as disclosed in Note 18 to the financial statements. However, an updated debtors' ledger was not maintained to keep track of changes during the year and the closing balances. In addition, schedules to support the balance were not provided and aging analysis for the receivables was not included in the financial statements.

Further, Management did not demonstrate strategies put in place to recover the customer debts for water sales. Demand notes were not issued to customers with outstanding water bills.

In the circumstances, the accuracy and recoverability of trade and other receivables balance of Kshs.55,422,844 could not be confirmed.

The audit was conducted in accordance with the International Standards for Supreme Audit Institutions (ISSAIs). I am independent of the Mandera Water and Sewerage Company Limited Management in accordance with ISSAI 130 on the 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 budget documents provided reflected an annual income and expenditure budget of Kshs.462,981,233. However, the statement of comparison of budget and actual amount reflected a total budget of Kshs.421,664,170, resulting to a variance of Kshs.41,317,063. Further, the Company expended Kshs.271,074,433 against an actual budget of Kshs.462,981,233 resulting to an under-expenditure of Kshs.191,906,800 or 41.4% of the budget. In addition, the Management did not provide evidence for approval of the budget by the Board of Directors and the County Assembly. Budget under absorption may have resulted to non-implementation of planned programmes negatively impacting on service delivery by the Company.

My opinion is however, 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

In the audit of the previous year, several issues were raised under report on Financial Statements and report on Lawfulness and Effectiveness in Use of Public Resources. However, the Management did not resolve the issues as at 30 June, 2023.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution and based on the audit procedures performed, except for the matters described in the Basis for Conclusion on Lawfulness and Effectiveness in the 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. Engagement of Casual Workers for a Prolonged Duration

Included in the staff costs of Kshs.33,771,005 as disclosed under Note 8 to the financial statements is an expenditure of Kshs.15,697,781 relating to compensation of casual employees. Records provided for audit revealed that the Company engaged sixty (60) casual workers continuously for more than three (3) months, with some who had served continuously for four (4) years. This was contrary to Section 37(1)(a) and (b) of the Employment Act, 2007 which provides that where a casual employee works for a period or a number of continuous working days which amount in the aggregate to the equivalent of not less than one month or performs work which cannot reasonably be expected to be completed within a period or a number of working days amounting in the aggregate to the equivalent of three months or more, the contract of service of the casual employee shall be deemed to be one where wages are paid monthly. The contracts of the casuals were renewed after every three (3) months.

Further, Management did not provide Board's approval for engagement of the casuals while master rolls for the casuals were not maintained to support the wages paid.

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

2. Late Remittance of Statutory Deductions

Review of the Company's statutory deductions revealed that National Social Security Fund (NSSF) deductions amounting to Kshs.214,971 in respect to four months namely, July, 2022, August, 2022, November, 2022 and April, 2022 were not remitted within the statutory timelines. This was contrary to Section 27(1) of the National Social Security Fund Act, 2013 which states that, If any contributions for which a contributing employer is required to pay to the Fund is not paid within one month after the end of the month in which the last day of the contribution period to which it falls, a sum equal to five per cent of the amount of that contribution shall be added to the contribution for each month or part of a month that the amount due remains unpaid.

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

3. Use of Unapproved Water Tariffs

According to the records provided for audit, the Company billed its customers based on a flat rate of Kshs.1,000 per customer which was not approved by the Water Services Regulatory Board (WASREB). Management did not seek approval from the Water Services Regulatory Board (WASREB) for the tariffs. This was contrary to Section 72(1)(b) of the Water Act, 2016 which states that the powers and functions of the Regulatory Board shall be to evaluate and recommend water and sewerage tariffs to the county water services providers and approve the imposition of such tariffs in line with consumer protection standards.

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

4. Operation Without Valid Service Provision Agreement, Memorandum and Articles of Association

Review of the Company statutory compliance and registration documents and discussion with Management revealed that the Company and Northern Water Service Board (now Northern Water Works Development Agency) signed a five-year service provision agreement in 2008 which has since expired. The Company did not renew the service provision agreement and was providing water services without authorization.

Further, Management did not provide for audit review the Company's Memorandum and Articles of Association in line with the revised Water Act, 2016 and Water Regulations, 2016.

In the circumstances, legality of the Company's operations could not be confirmed.

The audit was conducted in accordance with the International Standards for Supreme Audit Institutions (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 comply, 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 THE EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

As required by Section 7(1)(a) of the Public Audit Act, 2015 and 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 governance were not effective.

Basis for Conclusion

1. Lack of Debt Management and Bad Debt Policies

The statement of financial position and as disclosed in Note 12 to the financial statements reflects trade and other receivables balance of Kshs.55,221,769. It was, however, noted that the Company did not have a debt management policy and a policy on bad and doubtful debts. Further, aging analysis was not prepared to facilitate monitoring of receivables and cash flow forecasting.

In the circumstances, the recoverability of the full amount of receivables balance of Kshs.55,221,769 could not be confirmed.

2. Weak Internal Controls on Inventory Management

Note 17 to the financial statements reflects inventory balance of Kshs.57,307,727 as at 30 June, 2023 which includes balances in respect of water fittings, general stores, chemicals, water meters, fuel, stationery, uniform, and motor vehicle spare parts. However, the inventory did not include water stocks in the Company water reservoirs across the region and the value for the volume of water in the reservoirs was not disclosed in the financial statements.

Further, there was no evidence to confirm that the store items were issued on a first in, first out basis as required by Section 172(i) of the Public Procurement and Assets Disposal Regulations, 2020. In addition, Management did not provide a report on obsolete and unserviceable inventory including water meters as required by Section 172(c) of the Public Procurement and Assets Disposal Regulations, 2020.

In the circumstance, the effectiveness of internal controls on Inventory Management could not be confirmed.

3. Failure to Account for Non-Revenue Water (NRW)

During the year under review, the Company's estimated annual water production was 543,620 cubic metres of water. It was however noted that only two production sources had master meters while the other four production sources were based on estimates of pump discharge and monthly pumping hours. Further, data on volume of water consumed could not be confirmed since all the customers were not metered.

In the circumstances, the existence of an adequate mechanism to safeguard public resources could not be ascertained.

4. Failure to Establish an Internal Audit Unit and Audit Committee

The Company operated without an audit committee and an audit department as required by Regulation 167 of the Public Finance Management (County Governments) Regulations, 2015 which requires each county government entity to establish an audit committee which shall support the accounting officers with regard to their responsibilities for issues of risk, control and governance and associated assurance and also to follow up on the implementation of the recommendations of internal and external auditors.

In the circumstance, it was not possible to confirm existence of effective internal controls, risk management and Governance structures in the Company.

5. Lack of Information Technology Internal Controls

Review of the Company's Information Technology (IT) internal control and risk management processes revealed that the Company did not have an IT strategy committee and IT steering committee. In addition, policies in respect of physical access to IT environments were not place.

Further, the Company did not have disaster management and recovery policies in place including fire suppression systems. The Company did not have business continuity plan and IT continuity plan including an off-site back-up plan.

Lack of effective Information Technology internal controls may result to huge loses in case of occurrence of a disaster.

The audit was conducted in accordance with the International Standards for Supreme Audit Institutions (ISSAIs) 2315 and 2330. The Standards require that I plan and perform the audit to obtain assurance about whether effective processes and systems of internal controls, 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.

Responsibilities of the Management and the Board of Directors

The 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 controls as the 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 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 applicable basis of accounting unless Management is aware of the intention to liquidate the Company or cease operations.

The 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, the Management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements comply 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 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 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

09 January, 2024