

# **REPORT OF THE AUDITOR-GENERAL ON SOUTH NYANZA SUGAR COMPANY LIMITED FOR THE YEAR ENDED 30 JUNE, 2020**

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## **REPORT ON THE FINANCIAL STATEMENTS**

### **Qualified Opinion**

I have audited the accompanying financial statements of South Nyanza Sugar Company Limited set out on pages 26 to 71, which comprise the statement of financial position as at 30 June, 2020, and the statement of profit or loss and other comprehensive income, statement of changes in equity, statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information in accordance with the provisions of Article 229 of the Constitution of Kenya and Section 35 of the Public Audit Act, 2015. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit.

In my opinion, except for the effects of the matters described in the Basis for Qualified Opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the South Nyanza Sugar Company Limited as at 30 June, 2020, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with Kenya Companies Act, 2015.

### **Basis for Qualified Opinion**

#### **1. Unsupported Provisions**

As disclosed in Note 10 to the financial statements, the profit and loss and other comprehensive income reflects administrative expenses of Kshs.581,244,000 which includes provisions of Kshs.115,412,000 relating to tax penalties and legal cases. The Management has not provided the measurement basis for the provisions as required by the International Accounting Standards IAS 37 which requires that appropriate recognition criteria and measurement bases are applied to provisions and that sufficient information is disclosed in the notes to the financial statements to enable users to understand their nature, timing and amount.

Consequently, the accuracy and completeness of the provisions of Kshs.115,412,000 could not be confirmed.

#### **2. Understated Cash and Bank Balances**

As disclosed in Note 20 to the financial statements, the statement of financial position reflects cash and bank balances of Kshs.3,096,000. However, stale cheques amounting to Kshs.580,785 had not been reversed into the cashbook as at the time of the audit. The management had not provided an explanation why the same had not been written back to the cash book.

Consequently, the accuracy and the completeness of the cash and cash equivalent balance of Kshs.3,096,000 could not be confirmed.

### **3. Receivables from Out Growers**

As disclosed in Note 19 to the financial statements, statement of financial position reflects receivables from out growers balance of Kshs.107,099,000. The balance arises from the Company's provision of agricultural inputs and services to the out growers, and the related accrued interest recoverable. The gross receivables balance of Kshs.1,087,034,000 is an aggregation of out growers' balances from the main Agricultural Management Systems (AMS), out growers' ledger and old balances uploaded in a separate ledger in the AMS system.

Further, validation of the individual out growers' balances revealed several unsupported transactions in the out growers' ledger, inconsistent transactions between the underlying out growers files and ledger, and transactions in out growers files not recorded in the ledger.

In addition, a provision for impairment of receivables from out growers of Kshs.979,935,000 was provided at the end of the year, an indication that the Management was unable to recover the debts from the farmers.

Consequently, the accuracy and recoverability of provision for impairment losses of Kshs.979,935,000 could be not confirmed.

### **4. Deferred Income Tax**

As disclosed in Note 25 to the financial statements, statement of financial position reflects Kshs.26,944,000 in respect of deferred income tax. However, the Management did not provide an analysis on the computation and justification for reporting it as tax liability based on IAS 12 which provides that differences between the carrying amount and tax base of assets and liabilities, and carried forward tax losses and credits, are recognized, with limited exceptions, as deferred tax liabilities or deferred tax assets, with the latter also being subject to a 'probable profits' test.

Consequently, the accuracy and completeness of deferred income tax balance of Kshs.26,944,000 could not be confirmed.

### **5. Other Statutory Deductions**

As disclosed in Note 26 to the financial statements, the statement of financial position reflects trade and other payables balance of Kshs.4,889,932,000. Out of this balance, Kshs.4,426,911,000 is in respect of other payables and accrued expenses which includes other statutory deductions totaling Kshs.453,200,652 which had not been remitted to the relevant bodies. Non-remittance of the statutory deductions may attract heavy penalties and interests for non-compliance.

The respective penalties and interest for non-compliance have not been provided in these financial statements. Further in the absence of probable penalties and interest provided for in these financial Statements,

Consequently, it has not been possible to confirm that the trade and other payables balance of Kshs.4,889,932,000 is fairly stated.

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

#### **Material Uncertainty in Relation to Going Concern**

I draw attention to a disclosure in Note 4 to the financial statements, which indicates that the Company incurred a net loss after tax of Kshs.1,656,308,000 (2019: Kshs.1,358,342,000) during the year and had accumulated losses of Kshs.6,322,810,000 as at 30 June, 2020 (2019: Kshs.4,666,502,000). In addition, the Company's current liabilities of Kshs.6,219,899,000 exceeded its current assets of Kshs.848,411,000 resulting to negative working capital of Kshs.5,365,488,000 (2019: Kshs.4,473,753,000). These conditions indicate the existence of a material uncertainty, which may cast significant doubt on the Company's ability to continue as a going concern.

In addition, the Management has indicated that the Company's going concern depends on implementation of various strategies, whose success is yet to be realized.

Under the circumstances, the financial statements have therefore been prepared on the going-concern basis on the assumption that the Company will continue to get financial support from the Government, shareholders, banks and creditors.

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**

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

### **Conclusion**

As required by Article 229(6) of the Constitution, based on the audit procedures performed, except for the matters described in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section of my report, I confirm that, nothing else has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

## **Basis for Conclusion**

### **1. Payment of Board and Director Costs**

As disclosed in Note 10 to the financial statements, the statement of profit or loss and other comprehensive income reflects administration expenses Kshs.581,244,000 which includes Kshs.11,878,000 relating to board expenses. However, information provided indicated that the board had eleven (11) board meetings instead of four (4) recommended by Mwongozo code and Treasury Circular No. 2020(OP/CAB.9/1A). The higher number of meetings above the approved number significantly contributed to higher board expenses in a period the company is experiencing financial difficulties.

In addition, the Company paid an officer from Inspectorate of State Corporations Kshs.560,000 as allowance for attending board meetings in a supervisory capacity as part of her regular duties contrary to the Attorney General Circular AG/CONF/6/D/73 dated 22 August, 2013 that advised that sitting allowances or other remuneration is only payable to duly appointed chairperson and members of board attending a board meeting.

Consequently, the Management was in breach of the law.

### **2. Deposits with Suppliers**

As disclosed in Note 18 to the financial statements, the statement of financial position reflects trade and other receivable balance of Kshs.74,421,000 other receivable and prepayments of Kshs.238,518,000 before impairment losses of Kshs.169,536,000. As indicated in prior years, included in this figure is deposits with suppliers' balance of Kshs.106,227,487 contrary to section 146 of Public Procurement and Asset Disposal Act, 2015 which states that no works, goods or services shall be paid before they are executed or delivered and accepted by the accounting officer of a procuring entity.

Consequently, the Management was in breach of the law.

### **3. Trade and Other Payables**

As disclosed in Note 26 to the financial statements, the statement of financial position reflects trade and other payables balance of Kshs.4,889,932,000 which includes Kshs.4,426,911,000 in respect of other payables and accrued expenses. The balance includes outstanding Value Added Tax (VAT) and PAYE payables totaling Kshs.1,320,447,140 spanning several months of non-payment of principal amount, interest and penalties.

As similarly reported in the previous year, the management has continued to indicate that some of the outstanding obligations had been paid and that it intends to approach the Kenya Revenue Authority for waiver of applicable interest and penalties.

Consequently, the Management was in breach of the law.

#### **4. Long Outstanding Borrowings**

As disclosed in Note 27 of the financial statements, the statement of financial position reflects borrowing balance of Kshs.2,081,817,000 which includes Kshs.818,969,000 in respect of Government of Kenya (GOK/ODA) loan and Kshs.477,321,000 being Commodity Fund (SDF) loan which had fallen due by the end of 30 June, 2020.

Non-payment of loans is a breach of contract agreements which may attract heavy penalties and interests for non-compliance.

Consequently, the Management was in breach of the law.

#### **5. Officers Appointed in Acting Capacity**

Audit verification of personnel records revealed that the Company had nine (9) who had been appointed in acting capacity for a period beyond the stipulated six (6) months, with some officers acting since 2015 in contravention of the Section C.14(1) of Public Service Commission Human Resource Policies and Procedures Manual, which prohibits an officer from acting to a position for more than six (6) months. No explanation was provided for the failure to confirm the officers to the posts or advertise the vacancies.

Lack of substantive leadership in the respective departments and units may have constrained their contribution in fulfilling the Company's objectives. The Management was also in breach of the law

#### **6. Ethnicity and Regional Distribution**

Audit of the staff records revealed that 86% of the staff are from the dominant ethnic community contrary to requirement Section 7(1) and (2) of the National Cohesion and Integration Act, 2008 which states that all public establishments shall seek to represent the diversity of the people of Kenya in the employment of staff and no public establishment shall have more than one third of its staff from the same ethnic community.

Consequently, the 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 under 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**

### **Lack of Business Continuity Plan**

A review of the Company's business continuity plan and disaster recovery plan revealed that they have not been approved by the Board and consequently these documents have not been operationalized contrary to section 92(1) and (3) of the Public Finance Management Act, 2012 which state that if a State organ or other public entity encounters a serious financial problem or anticipates serious challenges in performing its financial function or meeting its financial commitments, it shall immediately seek solutions to resolve the financial problems.

The Company is therefore, highly exposed to business risks and unmitigated losses in the event of occurrence of a disaster.

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 processes and systems of internal control, risk management and 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 the 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 my audit;
- (ii) In my opinion, proper books of account have been kept by the Company, so far as appears from the examination of those records;
- (iii) The Company's statement of financial position and statement of profit or loss and other comprehensive income are in agreement with the accounting records; and
- (iv) In my opinion the information provided in the report of the Directors is consistent with the financial statements.

## **Responsibilities of 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 the requirements of the Kenyan Companies Act, 2015 and for maintaining effective internal control 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 assessment of the effectiveness of internal control, risk management and governance.

In preparing the financial statements, the Management is responsible for assessing the Company's ability of 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.

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 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 financial reporting process, reviewing the effectiveness of how the entity 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 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 ability of the Company 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 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 the 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.



**CPA Nancy Gathungu, CBS**  
**AUDITOR-GENERAL**

**Nairobi**

**16 February, 2022**