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Paper laid by the Hon. Jamleck Kamau on Tuesday 24/11/2015

GOVERNMENT OF KENYA THROUGH THE PARLIAMENTARY SERVICE COMMISSION

SUMMARY INDEPENDENT AUDITOR'S REPORT

OFFICE OF THE AUDITOR GENERAL (KENYA NATIONAL AUDIT OFFICE)

14 APRIL 2015

FINANCIAL AUDIT OF

THE OFFICE OF THE AUDITOR GENERAL KENYA NATIONAL AUDIT OFFICE (KENAO)

FOR THE PERIOD FROM 1 JULY 2012 TO 30 JUNE 2013

V. 30

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Abbreviations

OAG	Office of the Auditor General
AG	Auditor General
AiA	Appropriations In Aid
GoK	Government of Kenya
ICS	internal controls systems
IFAC	International Federation of Accountants
IFMIS	Integrated Financial Management Information System
IPSAS	International Public Sector Accounting Standards
ISA	International Standards on Auditing
KENAO	Kenya National Audit Office
SAI	Supreme Audit Institution

1 Executive Summary

The OAG in Kenya is an independent constitutional office and is the Country's SAI. The OAG is a constitutional office established under the Laws of Kenya and it draws its mandate from the Constitution of Kenya, 2010. The Office is established under Chapter 12, Part 6, and Article 229 of the Constitution of Kenya and is one of the independent offices as established by the Constitution

The OAG is headed by the AG who is appointed by President after public vetting and approval by the National Assembly It is not subject to direction or control by any person or authority

The AG and the OAG is enshrined in the Constitution of Kenya 2010 and the Public Audit Act 2003 Article 229, of the Constitution of Kenya 2010 outlines the mandate of the OAG It stipulates that the AG shall audit and report, in respect of that financial year, on the accounts of -

- The National and County governments;
- All funds and authorities of the National and County Governments,
- All courts;
- Every commission and independent office established by the Constitution,
- The National Assembly, the Senate and the county assemblies,
- Political parties funded from public funds;
- The public debt, and any other entity that legislation requires the Auditor-General to audit.

The AG is required to audit and report on all the accounts of any entity that is funded from public funds and is required to carry out audits and report to Parliament and the relevant Country Assemblies within statutory timelines It includes carrying out performance and effectiveness audits of all public funds referred to above under Article 229 (4) and Article 229(6) of the Constitution of Kenya 2010

2 Objectives and scope of the audit

2.1 Objectives of the Audit

The objective of the assignment is to carry out the annual audit of OAG for the year ended 30 June 2013 and to

a) Ensure that the audits are in accordance with the ISAs.

b) Check whether the financial statements have been prepared in accordance with the Government Financial Regulations and Procedures and in accordance with the International Standards

c) Express a professional opinion on the Auditor General's Office on the financial position at the end of each financial year and on funds received and expenditures incurred for the relevant accounting period

d) Prepare an audit report in line with pertinent constitutional provisions by Parliament.

e) To carry out the audit in accordance with the ISAs and as per the provisions of the provisions of the IFAC

f) Undertake internal controls testing to ensure that all funds received are used as per its purpose

g) Conduct thorough ICS testing to ensure that controls exist and are used effectively.

h) Conduct tests to ensure that books of account are kept as per the GoK Financial Regulations and are consistent with the statements of assets and liabilities and the AiA accounts

i) Conduct an exhaustive review of the internal control system to have sufficient knowledge procedures underpinning the systems, as contained in the various manuals of procedures or Government Guidelines and agreements signed by GoK.

j) Report the audit findings in a management letter

2.2 Scope of the Audit

The scope of the audit assignment was to ensure that,

a) All necessary supporting documents, records and accounts have been kept in respect of all project activities with clear linkages between the books of account and reports to ensure that OAG has maintained adequate supporting documentation to support claims for reimbursement of expenditures incurred

b) Goods and works services financed have been procured in accordance with the financing agreements including specific provisions of Government of Kenya Procurement Policies and Procedures

c) All necessary supporting documents, records and accounts have been maintained in respect of all activities, including expenditures reported using financial statements and to verify that respective reports issued during the period were in agreement with the underlying books of account

d) National laws and regulations have been complied with and that the financial and accounting procedures (Government Financial Regulations and procedures) were followed

e) Financial performance of the OAG is satisfactory

f) Assets procured from funds disbursed to the Office exist and there is verifiable ownership by the Office of the AG or beneficiaries in line with financing agreements.

g) The OAG procedures and sound and adequate and consistent with the normal course of operations

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3 Independent Auditor's Report

The Parliamentary Service Commission
P. O. Box 41842 - 00100
Nairobi, Kenya

Report on the statements of assets and liabilities and the Appropriations In Aid Accounts

We have audited the accompanying financial statements which comprised a Statement of Financial position, statement of comprehensive income, and notes to the financial statements of the OAG in accordance with the terms of reference and the requirements of Article 226 (4) of the Constitution of Kenya 2010 for the period from 1 July 2012 to 30 June 2013. The Statement of Financial position comprised transactions analysed using Ms Excel spread sheet whereas the statement of comprehensive income was derived from transactions captured into the OAG IFMIS accounting software on cash basis in which expenses are recognized when paid rather than when incurred Income was accounted for when received rather than when earned

Respective responsibility of the OAG and the auditors

The statement of financial position and the statement of comprehensive income are the responsibility of the OAG. The Office of The OAG is responsible for the preparation and fair presentation of these financial statements in accordance with International Public Sector Accounting Standards (IPSAS) and the requirements of the Constitution of Kenya 2010 This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error, selecting and applying appropriate accounting policies, and making accounting estimates that are reasonable in the circumstances. Our responsibility is to express an independent opinion on the financial statements based on our audit

We conducted our audit in accordance with the International Standards on Auditing (ISA's) These standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error

In making those risk assessments, the auditor considers internal controls relevant to the OAG preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of its internal control An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the OAG as well as evaluating the overall presentation of the financial statements

We believe that our audit provides a reasonable basis for our opinion We have highlighted our audit Findings and Recommendations in the management letter issued separately

Emphasis of matter

The opening balances of Recurrent Exchequer Kshs 229,897,425, Suspense account Kshs 21,456,538, and Bank balances Kshs. 197,099,229, General Account of Vote (GAV) Kshs 333,622,035 and Remittance to Exchequer Kshs 132,373 296 as at 1 July 2012 were omitted from the IFMIS cash book and general ledger as at 1 July 2012 The bank reconciliation statements for July 2012 had a difference of Kshs 751,497 and a persistent difference of Kshs 531,784 for the rest of the eleven months to 31 June 2013 as detailed in the management letter

Receivables in the Statement of financial position include Kshs 135.869,565 relating to amounts due from the old town councils which are over one year past due against which no provision for impairment has been made. The IPSAS financial statements prepared by the OAG had unsupportable general fund balance of Kshs. 414,294,049 and a capital reserve balance of Kshs 156,290,917 as at 30 June 2013 The unsupportable fund and reserve balances and the omission of the opening balances in the IFMIS cash book and general ledger and the persistent differences in the bank reconciliation statements from July 2012 to June 2013 presents significant doubt on the correctness of the IFMIS cash book for the years 2012 / 2013.

Opinion

In our opinion, except for the possible effect of the matter described in the emphasis of matter paragraph, the financial statements give a true and fair view of the state of the financial affairs of the OAG as at 30 June 2013 and of its deficit and cash flows for the period then ended in accordance with and comply with the requirements of the Kenyan Public Audit Act 2003, Public Financial Management Act and The Constitution of Kenya 2010 This report is solely, intended for the information and use by The Office of The Auditor General (Kenya National Audit Office) and Parliamentary Service Commission

Madhav Bhandari
Partner
Baker Tilly Merali's
Practicing Certificate No. 1213

Date:..........16.9.13...........

First Floor, New Rehema House
Rhapta Road, Westlands
P. O. Box 67486 – 00200
Nairobi, Kenya

4 Summary of Findings

A detailed audit report was issued. In this section we summarise the main audit findings noted from our audit for the period from 1 July 2012 to 30 June 2013.

4.1 Presentation of Financial Statements

The accounting framework applicable to KENAO is the International Public Sector Accounting Standards (IPSAS) The presentation of financial statements is governed by the provisions IPSAS 1 where accrual basis of accounting is used or the guidelines for financial reporting under the cash basis of accounting which supplement the IPSAS

Under the accrual basis of accounting, the IPSAS requires the following to be presented as part of financial statements.

a) Statement of financial position

b) Statement of financial performance

c) Statement of changes in net assets/equity

d) Cash flow statement

e) Comparison of budget versus actual amounts where the Entity makes public its approved budget

f) Notes, comprising a summary of significant accounting policies and other explanatory notes

The IPSAS requires the following to form the financial statements if the cash basis of accounting is applied·

a) Statement of cash receipts and payments

b) Accounting policies and explanatory notes

c) Comparison of budget versus actual amounts where the Entity makes public its approved budget

The OAG prepared the financial statements based on accruals based IPSAS The accruals based IPSAS financial statements were generated from the IFMIS based cash book from which receipts from the Exchequer, Appropriations In Aid and other income and expenses were recorded. Except for the bank balances, the other statement of financial position balances i e property, plant and equipment, inventories / stores, receivables and payables were extracted from a Microsoft Excel spread sheet maintained, as the IFMIS modules had not been fully installed. This resulted into incomplete record keeping and the related risk of omission of transactions as not all the debit entries could be traced into their corresponding credit entries and vice versa

We recommend a full implementation of IPSAS in subsequent years

4.2 Financial Reporting

We noted that opening balances of Recurrent Exchequer Kshs. 229,897,425, Suspense account Kshs. 21,456,538, and Bank balances Kshs 197,099,229, General Account of Vote (GAV) Kshs 333,622,035 and Remittance to Exchequer Kshs 132,373,296 as at 1 July 2012 were omitted from the IFMIS cash book and general ledger as at 1 July 2012. The bank reconciliation statements for July 2012 had a difference of Kshs 751,497 and a persistent difference of Kshs 531,784 for the rest of the eleven months to 31 June 2013 as detailed in the management letter

The IPSAS financial statements prepared by the OAG had unsupportable general fund balance of Kshs. 414,294,049 and a capital reserve balance of Kshs 156,290,917 as at 30 June 2013. The unsupportable fund and reserve balances and the omission of the opening balances in the IFMIS cash book and general ledger and the persistent differences in the bank reconciliation statements from July 2012 to June 2013 presents significant doubt on the correctness of the IFMIS cash book for the years 2012 / 2013

4.3 Management of Receivables

Receivables in the statement of financial position include Kshs 135,869,565 relating to amounts due from the old town councils which are over one year past due, against which no provision for impairment has been made. Also, a general ledger was not maintained for each customer / account receivable In addition, we noted that Kenya Government Regulations require imprests to be retired 48 hours after returning from the mission. We however, noted retirement of imprests in some cases exceeded this time limit.

We recommend immediate strengthening of the finance function to ensure that appropriate provisions for impairment are made for receivables deemed to be irrecoverable.

4.4 Management of non-current assets

The fixed assets register provided did not show the value of all the motor vehicles. Thus the motor vehicles shown in the financial statements at gross carrying value of Kshs. 147,059,433 and net carrying value of Kshs.98,956,575 is materially understated in the statement of financial position as it does not include the value of the 41 vehicles. A separate list provided with a total of Kshs. 45,352,000 relate only to 38 (number) motor vehicles.

The OAG lacks asset capitalisation policy. Some of the assets included in the assets register are either of very low values or have a lifespan of less than one year, or both.

4.5 General weaknesses in the internal control systems

We also noted general weaknesses in the OAG systems of internal controls especially regarding procurement processes, human resource practises, budgeting and property plant and equipment as detailed below;

(i). Procurement

We reviewed a number of procurement files and noted instances in which the requisite three quotations were not obtained from the pre-qualified lists of suppliers and compared as required. In one case, the approval of the procurement transaction by the tender committee was done several months after the items were ordered while some of the suppliers who were awarded the supply contracts were not in the pre-qualified lists of suppliers under the various supply categories.

(ii). Human resource

The entity uses IFMIS accounting software which is controlled by the treasury, a G-pay accounting system for making payments whose control is vested with Central Bank of Kenya and Memory Soft payroll accounting software which is fully controlled by the entity. We noted that although IFMIS and G-Pay software are integrated online, the Memory Soft payroll software is not integrated to the IFMIS and G-Pay. Therefore there is an increased likelihood or risk of errors as the payroll information is recorded into IFMIS manually through the payment voucher recording procedures. We also requested for but were not provided with a number of staff personnel files.

(iii). Budgeting

Some of the OAG transactions for the period 1 July 2012 to 30 June 2013 were posted to the incorrect budget lines while a number of expenditure budget lines were either under or overspent.

5 Recommendations

We recommend as follows

a) The Entity should take measures to move towards full implementation of the IFMIS by activating all the modules of IFMIS that can capture the income, expenses, assets and liabilities This would ensure preparation of more accurate IPSASs based accounting and financial reporting

b) A full review / valuation is carried out with a view to ensure that all the remaining 41(number) vehicles are correctly included in the financial statements. A balance sheet clean up exercise should be carried out.

c) The IFMIS accounting system is currently in use for purposes of accessing Treasury budgets It is not appropriate, nor independent, for purposes of running KENAO's operations and assuring OAG's independence An independent and integrated ERP should be sought and implemented as soon as possible so as to address the operational challenges faced by the officers in application of controls and preparation of accounts An independent ERP would enhance OAG's independence of the core system that drives accounting in MDAs that it audits. The policies and procedures on administration of receivables should be reviewed to include the following controls.

   - Each customer should have a ledger created on the accounting system through which transactions involving the customer are recorded This would enable the effective tracking of amounts of receivables due at any date A receivables aged analysis / report should be generated and receivables deemed doubtful or irrecoverable are either provided for or written off

   - Measures are taken to ensure adherence to the timelines for retirement of imprest. Such measures include ensuring prior imprests are retired before issuance of a new imprest and surcharge against staff salaries for delayed accounting for imprest

d) The Internal Audit function of KENAO is strengthened by ensuring adequate manpower and planned reviews of the branch offices,

e) Until an ERP is fully implemented, the Entity may also consider further training of personnel on the effective use of the IFMIS even though this is currently applied simply because the budget of the Office is not a one line budget at the Treasury.

f) We recommend that the Entity implements modalities to ensure all required procurement documentations are readily available and that all purchases should be undertaken only after requisite approvals, such as from the tender committee, are obtained. All the staff personnel files should be maintained and readily available for verification and payroll system and accounting software fully integrated All the motor vehicles should be disclosed in the OAG statement of financial position and a proper asset capitalization policy put in place

ANNEXES

ANNEX I – Statement of financial position

	Annexes	2013
		Kshs
ASSETS		
Current assets		
Cash and cash equivalents	III	24,298,601
Receivables	IV	453,433,259
Inventories		2,727,841
Total current assets		**480,459,701**
Non-current assets		
Property, plant and equipment	V	229,072,551
Intangible assets	VI	4,613,357
Total non-current assets		233,685,908
Total assets		**714,145,609**
LIABILITIES AND EQUITY		
Current liabilities		
Payables	VI	150,406,184
Retention money		50,516
Total current liabilities		**150,456,700**
Net assets / equity		
General fund	VIII	414,294,049
Revenue reserve	VIII	(5,721,886)
Capital reserve	VIII	155,116,747
Total net assets / equity	VIII	563,688,910
Total liabilities and equity		**714,145,609**

The OAG financial statements were authorized for issue on ....14 April 2015........ and were signed on its behalf by:

....

Auditor General of Kenya **Deputy Auditor General (Corporate Services)**

ANNEX II – Statement of comprehensive income

		2013	2012
	Annexes	**Kshs**	**Kshs**
Revenue			
Receipts from the Exchequer	IX	1,580,000,000	1,198,000,000
Audit fees	IX	195,109,406	242,460,811
Other operating income	IX	1,190,600	3,041,842
Total operating revenue		**1,776,300,006**	**1,443,502,653**
Expenses			
General and administrative expenses	IX	1,600,338,131	1,209,937,880
Establishment expenses	IX	279,089,775	157,720,683
Total operating expenses	IX	1,879,427,906	1,367,658,563
(Deficit) / surplus for the period		(103,127,900)	75,844,090
Transfer from Capital Grants received from the Government		26,987,500	-
Net surplus / (deficit) for the period		**(76,140,400)**	**75,844,090**

ANNEX III – Cash and cash equivalents

	Kshs
Petty cash	2,381,570
Bank balances	21,917,031
	24,298,601

ANNEX IV – Receivables

	Kshs
Amounts receivable from customers	434,489,689
Staff medical expenses recoverable	2,642,249
Outstanding imprests from staff	12,926,095
Staff advances	875,226
Deposits	2,500,000
	453,433,259

ANNEX V – Property, plant and equipment

	Furniture, Fittings & Equipment	Motor Vehicles	Computer Equipment	Office Equipment	Total
	Kshs	**Kshs**	**Kshs**	**Kshs**	**Kshs**
Fiscal year ended 30 June 2013					
Cost:					
As at 1 July 2012	32,943,915	45,352,000	59,521,430	9,835,305	147,652,650
Additions in2012 / 2013	9,567,960	101,707,433	102,331,084	5,399,051	219,005,528
Reversals to intangible assets			(5,766,696)		(5,766,696)
As at 30 June 2013	**42,511,875**	**147,059,433**	**156,085,818**	**15,234,356**	**360,891,482**
Accumulated depreciation:					
As at 1 July 2012	4,117,989	11,338,000	19,642,072	1,229,413	36,327,474
Depreciation	5,313,984	36,764,858	51,508,320	1,904,295	95,491,457
As at 30 June 2013	**9,431,973**	**48,102,858**	**71,150,392**	**3,133,708**	**131,818,931**
Net carrying value					
As at 30 June 2013	**33,079,902**	**98,956,575**	**84,935,426**	**12,100,649**	**229,072,551**

ANNEX VI – Intangible assets

	License	Software	Total
	Kshs	**Kshs**	**Kshs**
Fiscal year ended 30 June 2013			
Cost:			
As at 1 July 2012			
Additions	687,410	5,079,286	5,766,696
As at 30 June 2013	**687,410**	**5,079,286**	**5,766,696**
Accumulated depreciation:			
As at 1 July 2012			
Amortisation charge for the year	137,482	1,015,857	1,153,339
As at 30 June 2013	**137,482**	**1,015,857**	**1,153,339**
Net carrying amount:			
As at 30 June 2013	**549,928**	**4,063,429**	**4,613,357**

ANNEX VII – Payables

	2013
	Kshs
Computer Software	19,083,840
ICT Networking and Com Equipment	25,742,602
MAINT OF COMPUTERS	5,882,965
Maint of Office Furniture & Equip	448,850
CMC Motors Ltd	56,000,000
Maint Expenses - Motor Vehicles	3,019,449
Contracted Professional Services	5,909,971
CONTRACTED GUARDS	23,205
REFINED FUEL	116,923
Supplies & Accessories for Computers	5,638,108
General Office Supplies & Publishing	255,072
Medical Insurance	24,437,404
TUITION AND TRAINING	903,128
RENT	2,334,884
ACCOMM EXP & Subsistence Allow	285,010
Courier & Postal Services	110,014
WATER & SAN	214,759
	150,406,183

ANNEX VIII – Net assets / equity

	General Fund	Capital Grants	Capital Reserves	Revenue Reserves	Total
	Kshs	Kshs	Kshs	Kshs	Kshs
Fiscal year ended 30 June 2012					
At 1 July 2011	414,294,049				414,294,049
Surplus for the year				75,844,090	75,844,090
At 30 June 2012	**414,294,049**			**75,844,090**	**490,138,139**
Fiscal year ended 30 June 2013					
At 1 July 2012	414,294,049			75,844,090	490,138,139
Restatement of revenue reserve				(5,425,576)	(5,425,576)
Surplus / (deficit) for the year				(76,140,400)	(76,140,400)
Property, plant & equipment purchased		26,987,500	155,116,747		182,104,247
Transfer to the statement of comprehensive income		(26,987,500)			(26,987,500)
At 30 June 2013	**414,294,049**		**155,116,747**	**(5,721,886)**	**563,688,910**

ANNEX IX – Detailed schedule of income and expenditure

	2013	2012
Revenue	**Kshs**	**Kshs**
Receipts from the Exchequer	1,580,000,000	1,198,000,000
Audit fees	195,109,406	242,460,811
Other operating income	1,190,600	3,041,842
	1,776,300,006	**1,443,502,653**
General and administrative expenses		
Staff cost	1,220,067,801	863,298,965
Commission expenses	3,160,000	3,248,548
Travelling and accommodation	135,650,854	155,598,350
Advertising, printing and stationery	13,042,876	11,296,330
Fuel and lubricants	19,164,782	19,775,628
Telephone & communication supplies	41,713,191	36,005,544
Entertainment and hospitality	3,584,192	3,656,400
Training expenses	25,298,112	16,896,279
Office general expenses	24,674,784	19,176,410
Subscriptions	804,847	519,500
Pension and retirement benefits	3,596,639	900,000
Medical expenses	99,537,104	72,875,227
Other operating Expenses	10,042,949	6,690,699
	1,600,338,131	**1,209,937,880**
Establishment expenses		
Water and electricity	1,176,951	555,861
Repairs and maintenance	76,849,140	33,687,889
Rent	104,418,888	91,727,241
Depreciation of property, plant and equipment	95,491,457	31,749,692
Amortisation of intangible assets	1,153,339	-
	279,089,775	**157,720,683**

6 Persons contacted or involved in the audit

The Auditor – Baker Tilly Merali's Certified Public Accountants	
Madhav Bhandari	Partner
Rishi Bhandari	Associate Partner
Erastus Ochieng	Audit Supervisor
Edith Mutua	Audit Supervisor
Samuel Muigai	Audit Senior
Lucy Wainaina	Audit Senior

The Entity subject to audit – Office of The Auditor General (OAG)	
Edward Ouko	Auditor General
Agnes C. Mita	Deputy Auditor General (Corporate Services)
Martha Wanjiru Mbau	Manager (Accounts)
Stephen Makau	Assistant Manager
Samuel Muchiri	Senior supervisor - Audit

Parliamentary Service Commission (PSC)	
Justin N. Bundi	Clerk of The National Assembly