

REPORT OF THE AUDITOR-GENERAL ON KENYATTA NATIONAL HOSPITAL 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

Qualified Opinion

I have audited the accompanying financial statements of Kenyatta National Hospital set out on pages 97 to 155, which comprise the statement of financial position as at 30 June, 2023, and the statement of financial performance, statement of changes in net assets, 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 Kenyatta National Hospital as at 30 June, 2023 , and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards (Accrual Basis) and comply with the Legal Notice No.109 of 1987 and the Public Finance Management Act, 2012.

Basis for Qualified Opinion

1. Unsupported Secured Individual Debtors

Note 25 to the financial statements reflects gross medical services receivables balance of Kshs.13,139,787,000. The balance includes secured individual debtors balance of Kshs.562,353,542. However, verification of schedules revealed six hundred and seven-eight (678) patients with total unsecured debt amount of Kshs.74,556,613 did not have details of in-patient number, invoice number, folio number and guarantor. In addition, these debts have been outstanding for more than 360 days.

In the circumstances, the accuracy and recoverability of secured individual debtors of Kshs.74,556,613 could not be confirmed.

2. Un-Collected Rental Income

The statement of financial position reflects receivables from exchange transactions of Kshs.2,790,107,000 as disclosed in Note 25 to the financial statements. Included in the amount is rent receivables of Kshs.36,371,000 out of which Kshs.11,488,827 are rent receivables which have accumulated for over 360 days. Majority of the house occupants are public servants and it is not clear why the Hospital has not initiated rent recovery through checkoff system as required by the Kenyatta National Hospital (KNH) Housing Management Policy. Further, sixteen (16) debtors had a balance of Kshs.21,123,059 accounting for 58% of total rent receivables.

In the circumstances, the recoverability of uncollected rental income of Kshs.36,371,000 could not be confirmed.

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

1. Budgetary Control and Performance

The statement of comparison of budget and actual amounts reflects final receipts budget of Kshs.21,114,717,000 and actual on comparable basis of Kshs.20,291,252,000 resulting to an underfunding amounting to Kshs.823,465,000 or 4% of the budget.

Similarly, the Hospital spent Kshs.23,668,485,000 compared to the final expenditure budget of Kshs.21,114,717,000 resulting to an unapproved over expenditure amounting to Kshs.2,553,768,000 or 12% of the budget.

The underfunding affected the planned activities and may have impacted negatively on service delivery to the public whereas the over expenditure means there may have been expenditure on unbudgeted items.

2. Pending Accounts Payable

The statement of financial position reflects trade and other payables of Kshs.2,874,256,000 (2022 – Kshs.1,569,872,000) an increase by Kshs.1,304,384,000 or 83% as disclosed in Note 30 to the financial statements. Management has attributed this amount to unpaid suppliers.

Failure to settle bills during the year to which they relate distorts the financial statements and adversely affects the budgetary provisions for the subsequent year as they form a first charge.

My opinion however, is not modified in respect to these matters.

Key Audit Matters

Key audit matters are those matters that, in my professional judgment, are of most significance in the audit of the financial statements. There were no key audit matters to report in the year under review.

Other Matter

1. Forensic Audit on Payment System

The Office is currently undertaking a forensic audit on the payment system at the Hospital. The forensic audit was informed by a preliminary review of the payment system which pointed to possible fraudulent activities and loss of funds. As at the time of this report, the forensic audit had not been concluded.

2. Unresolved Prior Year Matters

In the audit report of the previous year, several issues were raised under the Report on the Financial Statements and Report on Lawfulness and Effectiveness in Use of Public Resources. However, Management has not resolved the issues.

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

1.0 Medical Services Contract Loss

1.1 Contracts with National Hospital Insurance Fund (NHIF)

The statement of financial performance includes medical services contracts loss of Kshs.569,237,000 out of which Kshs.379,100,000 relates to loss from National Health Insurance Fund (NHIF) as disclosed in Note 22 to the financial statements. The NHIF loss arises where the medical cost incurred on a patient who is a contributor to the Fund is greater than the rebate reimbursed by the Fund based on the existing medical service contracts.

It was noted that Management continued to engage NHIF and the Ministry of Health on the loss-making contracts from 2016 to 2022 as evidenced in several correspondences. Although a renegotiated contract commencing on 1 July, 2022 has enhanced the number of claimable services, the annual losses incurred during the year is still significant at Kshs.379,100,000.

In the circumstances, the Hospital has continued to bear the high cost leading to losses if the reimbursable amounts are not reviewed.

1.2 Linda Mama Program

The statement of financial performance includes medical services contracts loss of Kshs.569,237,000 out of which Kshs.190,137,000 relate to loss on Linda Mama Program offered by the Hospital, as disclosed in Note 22 to the financial statements. It was noted that the Government reimburses the Hospital Kshs.17,500 per delivery despite receiving complicated maternal referrals for specialized care services which include renal dialysis, critical care services and neonatal care whose medical cost could be way above Kshs.100,000. However, with effect from July 2017 the package was enhanced so that in case of complications the Hospital is allowed to claim a normal rebate rate of Kshs.4,000 per day in addition to the Kshs.17,500. This has however not been sufficient to cover the losses at Kshs.190,137,000 for the year under review.

In the circumstances, the Hospital has continued to bear the high cost of free maternity programs which has negatively impacted on the overall performance.

2. Incomplete Pediatrics Emergency and Burns Management Centre

Note 41 to the financial statements on contingent liabilities reflects projected contractor's cost of Kshs.3,368,624,780 and consultant costs of Kshs.263,959,541 totaling Kshs.3,632,584,321. However, the contract was awarded at project cost of Kshs.2,959,511,555 and consultant cost at Kshs.39,927,200 totaling Kshs.2,999,438,755. This implies an increase by Kshs.633,145,566 or 21% of the original costs. This escalation of costs is largely attributed to delays in making prompt payments which continues to persist. This was demonstrated in the contractor's letter dated 18 April, 2023 on delay in payment by the employer, release of certificate of financial claims to the employer and delay in submission of clear details and instructions from the consultant

resulting to slow work progress. Further, there was no evidence of ongoing negotiations with both the contractor and consultant.

It was noted that the project was to be financed through a concessionary loan from development partners at Kshs.1,235,724,580 or 41.8% and Government of Kenya at Kshs.1,723,786,975 or 58.2% with an initial completion date of 20 August, 2020 which has lapsed.

However, one of the extended loan agreements with the financiers expired on 31 December, 2023 while the second expires on 31 July, 2024 and there is no evidence of additional extensions.

In the circumstances, value for money on amounts spent on construction of pediatrics emergency and burns management center could not be confirmed.

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 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 overall governance were not effective.

Basis for Conclusion

1. Failure to Adjust Rent Rates

The statement of financial performance reflects rental revenue from facilities of Kshs.135,378,000 as disclosed in Note 11 to the financial statements out of which Kshs.100,062,000 relates to residential properties revenue from the hospital staff. It was noted that the Hospital has 968 staff houses but the rates charged have not been reviewed since the year 2001 to align them to market rent rates. Analysis revealed projected estimated annual rent of Kshs.318,060,000 compared to the current annual rent of Kshs.57,199,200 which results to difference (rental revenue loss) of Kshs.260,860,800.

In the circumstances, the effectiveness of internal controls on management of house rents could not be confirmed.

2. Inadequate Segregation of Duties

Review of the system processes revealed that a supply chain officer could amend orders, perform inspections and receive stocks. In addition, a finance officer could register suppliers, could change supplier account numbers, commit orders and make direct cash payments. Further, there was no clear distinction between human resource and payroll staff.

In the circumstances, the effectiveness of internal controls in procurement and human resource section could not be confirmed.

3. Weaknesses in the Payment System

Review of the Hospital payment systems revealed that the same payment voucher would appear in different systems with different amounts and details. Further, analysis revealed amounts of Kshs.19,269,324 were processed in the QuickBooks System but the amount paid in the bank was Kshs.22,048,014 resulting to an overpayment by Kshs.2,778,689.01.

In the circumstances, the effectiveness of internal controls in the system used for processing payments and reporting could not be confirmed.

4. Weaknesses in Use of Manual Processes

The Hospital uses four (4) different systems one for processing payments and reporting, the second for uploading of payments for onward remittance to individual accounts, the third to manage human resource and payroll processes and fourth to manage operations of supply chain, management of cashier shifts, revenue collection, patient registration and processing of imprest. However, these systems are not integrated and rely on manual interventions to link them. These manual interventions are done multiple times which hampers smooth business workflow and greatly poses a high risk to data integrity.

In addition, the information relating to staff creditors' banks details and processing of their payments is maintained manually.

In the circumstances, the effectiveness of internal controls and risk management could not be confirmed.

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance about whether effective processes and systems of internal control, risk management and overall governance were operating effectively, in all material respects. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

Responsibilities of Management and Board of Management

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Public Sector Accounting Standards (Accrual Basis) and for maintaining effective internal control as Management determines is necessary to enable the preparation of financial statements that are free from material

misstatement, whether due to fraud or error and for its assessment of the effectiveness of internal control, risk management and governance.

In preparing the financial statements, Management is responsible for assessing the Hospital's ability to sustain services, disclosing, as applicable, matters related to sustainability of services and using applicable basis of accounting unless the Management is aware of the intention to dissolve the Hospital 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 Management is responsible for overseeing the Hospital'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 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 applicable 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 Hospital's ability to continue to sustain its services. 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 Hospital to cease to continue to sustain its services.
- 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 Hospital to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

I communicate with the Management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

I also provide Management with a statement that I have complied with relevant ethical requirements regarding independence and to communicate with them all relationships and other matters that may reasonably be thought to bear on my independence and where applicable, related safeguards.



FCPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

05 March, 2024