REPORT OF THE AUDITOR-GENERAL ON COUNTY ASSEMBLY OF MACHAKOS FOR THE YEAR ENDED 30 JUNE, 2019

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of County Assembly of Machakos set out on pages 1 to 25, which comprise the statement of financial assets and liabilities as at 30 June, 2019, statement of receipts and payments, statement of cash flows and the 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, because of the significance of the matters discussed in the Basis for Adverse Opinion section of my report, the financial statements do not present fairly, the financial position of the County Assembly of Machakos as at 30 June, 2019, and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards (Cash Basis) and do not comply with the Public Finance Management Act, 2012 and the County Governments Act, 2012.

Basis for Adverse Opinion

1. Variances between Financial Statement and IFMIS Balances

Several balances reflected in the financial statements presented for audit differ with those shown against identical accounts in the trial balance extracted from the Integrated Financial Management Information Systems (IFMIS) as at 30 June, 2019, as detailed in the attached Appendix 1.

Management did not provide reconciliations for the variances and as a result, the accuracy, validity and completeness of the account balances, and the financial statements in whole, has not been confirmed.

2. Unconfirmed Bank Balances

The statement of assets and liabilities as at 30 June, 2019 reflects bank balances totaling Kshs.421,325, as disclosed in Note 13 A to the financial statements. The balance is comprised of account balances in development, recurrent and imprest bank accounts amounting to Kshs.141,001, Kshs.140 and Kshs.280,183 respectively. However, the cash books presented in support of the balance were dated 31 July, 2019 instead of 30 June, 2019 which was the reporting date. Further, the bank balance reflected in the respective cashbook as at 30 June, 2019 was Kshs.1,903,770 comprised of Kshs.150,001 development vote account, Kshs.1,175,858 recurrent vote account, and Kshs.577,911 imprests account.

In view of these anomalies, the accuracy and completeness of the bank balance totaling Kshs.421,325 reflected in the statement of assets and liabilities as at 30 June, 2019 has not been confirmed.

3. Unconfirmed Accuracy of Statement of Cash Flows

The statement of cash flows reflects nil opening cash and cash equivalents balance for the year which, however, differs with the closing cash and cash equivalents credit (negative) balance amounting to (Kshs.43,725,317) for the financial year ended 30 June, 2018. No restatements have been disclosed in the financial statements that would explain the reported change of the opening balance. In addition, the reported comparative balance amounting to Kshs.43,725,317 differed with the audited balance of Kshs.31,627,749 by Kshs.75,353,067 which has not been explained.

In view of the unexplained variances, the accuracy of the statement of cash flows for the year ended 30 June, 2019 has not been confirmed.

4. Incomplete Compensation of Employees Balance

The statement of receipts and payments for the year ended 30 June, 2019 reflects compensation of employees costs totaling Kshs.360,447,006, as further disclosed under Note 4 to the financial statements. However, salaries totaling Kshs.342,778,508 incurred on staff employed on permanent terms incorrectly included several sub-items. These were; basic wages for temporary employees, personal allowances paid as part of salary as well as pension and social benefits contributions.

In the absence of sufficient disclosure, the completeness and accuracy of the expenditure totaling Kshs.360,447,006 shown in the financial statements as having been incurred on compensation of employees during the year under review has not been confirmed.

5. Insufficient Disclosure of Pending Bills

Annex 1 to the financial statements reflects pending accounts payables totaling Kshs.76,066,531 as at 30 June, 2019. However, the pending bills have not been disclosed in the financial statements under other disclosures as required by the International Public Sector Accounting Standards (Cash Basis) accounting framework. Had the pending bills been paid and charged to the relevant budget lines in the year under review, the statement of receipts and payments would have reflected a deficit of Kshs.75,645,207 instead of the surplus amounting to Kshs.421,325 reported in the year under review.

Further, examination of the pending bills schedule revealed a debt amounting to Kshs.3,123,500 owed to a local University. The bill arose from training services rendered to the County Assembly's Budget Appropriation, Public Investment and Accounts committees during a trip to South Africa in 2014. Management has not explained why the pending bill was not disclosed and paid in previous years even though the University is reported to have issued several demand notices on the debt, over the years.

In the circumstance Management has breached the law and has not managed its pending bills in an effective way.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of County Assembly of Machakos 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 adverse opinion.

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. Except for the Matters described in the Adverse Opinion Section, I have determined that there are no other key audit matters to communicate in my report.

Other Matter

Budgetary Control and Performance

The statement of comparison of budget: recurrent and development combined for the year ended 30 June, 2019 reflects final revenue budget and actuals on comparable basis amounting to Kshs.1,230,776,339 and Kshs.951,103,579 respectively resulting in a shortfall of Kshs.279,672,760 or 23% of the budget. Management explained the underfunding as having resulted from delay in receipt of Exchequer releases.

In addition, the County Assembly incurred expenditure totaling Kshs.360,447,006 on compensation of employees against its budget amounting to Kshs.354,795,858 resulting in over-expenditure of Kshs.5,651,148. In the circumstance, Management did not adhere to the approved budget. No plausible explanation has been provided for the anomaly.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, because of the significance of the matters discussed in the Basis for Adverse Opinion and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources sections of my report, based on the audit procedures performed, I confirm that public resources have not been applied lawfully and in an effective way.

Basis for Conclusion

1. Inter-Account Borrowing Classified as Receipts

The statement of receipts and payments for the year ended 30 June, 2019 reflects other receipts totalling Kshs.10,000,000, as further disclosed in Note 3 to the financial statements. Examination of records of the receipts revealed that these were funds borrowed from the County Assembly Housing Fund. Although, Management explained that the borrowing was occasioned by delays in receipt of Exchequer releases, the County Assembly was not requested to approve the transaction before it was effected. In addition, there was no evidence to show that the borrowed funds were refunded to the Fund by the County Assembly.

In view of the foregoing, the borrowing amounting to Kshs.10,000,000 made by Management from the County Assembly Fund was irregular. Further, Management has not explained why the monies were not paid back to the Fund.

2. Irregular Reallocation of Compensation of Employees Budget

During the year under review, Management reallocated funds totaling Kshs.75,040,000 budgeted for compensation of employees. The reallocations were made contrary to the provisions of Section 154(1c) of the Public Finance Management Act, 2012 which prohibits Accounting Officers from reallocating funds meant for wages to other expenditure items.

In the circumstance, Management acted contrary to the Law.

3. Non-Adherence to a One Third of Basic Pay Rule

Review of monthly payrolls during the year revealed that non-statutory deductions on the salaries of two employees exceeded two-thirds (2/3) of their basic pay contrary to Section19(3) of the Employment Act, 2007. Management therefore, acted contrary to Law and exposed the staff to the risk of pecuniary embarrassment.

4. Failure to Promote Equitable Staffing

Analysis of the County Assembly staff compliment revealed that out of two hundred and twelve (212) employees, employed by the County Assembly as at 30 June, 2019, one hundred and ninety-eight (198) representing 93% of the establishment were from the dominant ethnic community in the County. This was contrary to the requirements of Section 7(2) of the National Cohesion and Integration Act, 2008 which provides that no public establishment shall have more than a third (1/3) of its employees from one ethnic community.

In the circumstance, the County Assembly has breached the Law on retention of a staff compliment that promotes national cohesion.

5. Non-Adherence to End of Year Cut-off Date

Examination of expenditure records indicated that payments totaling Kshs.13,849,114 were made to various suppliers and contractors after the end of year cut-off date of 30 June, 2019, as detailed in the attached Appendix II.
The payments were made contrary to Regulation 97(1) of the Public Financial Management (County Government) Regulations of 2015, which states that the accounts

of the County Government entities shall record transactions which take place during the financial year running from 01 July to 30 June.

6. Failure to Submit Performance Report

Contrary to the provisions of Section 164 (f) of the Public Finance Management Act, 2012, the annual financial report submitted to the Auditor-General for audit does not discuss the County Assembly's performance against its objectives for the year under review. Therefore, the report does not provide sufficient information on the County Assembly and does not conform to the Law. As a result, it is not possible to confirm whether the County Assembly met its objectives for the year.

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, because of the matters described on the Basis for Adverse Opinion and Basis for Lawfulness and Effectiveness in Use of Resources sections of my report, I confirm that the internal controls, risk management and governance were not effective.

Basis for Conclusion

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 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 those Charged with Governance

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Public Sector Accounting Standards (Cash 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 overall governance.

In preparing the financial statements, Management is responsible for assessing the County Assembly's ability to continue to sustain its services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless Management is aware of the intention to dissolve the County Assembly 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.

Those charged with overall governance are responsible for overseeing the financial reporting process, reviewing the effectiveness of how the County Assembly 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 overall 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 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 ability of the County Assembly 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 County Assembly 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 County Assembly 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.

Nancy Gathungu
<u>AUDITOR-GENERAL</u>

Nairobi

12 November, 2020

Appendix I – Unexplained Variances Between Financial Statement and IFMIS Balances

Item	Financial Statements Balance (Kshs.)	IFMIS Balance (Kshs.)	Variance (Kshs.)
Compensation of Employees- basic salaries for permanent staff	342,778,509	279,053,150	63,725,359
Compensation of Employees -Social Benefit Schemes	17,668,497	19,668,497.00	-2,000,000
Use of Goods and Services	481,044,180	447,995,552	33,048.628
Item	**Financial Statements Balance (Kshs.)**	**IFMIS Balance (Kshs.)**	**Variance (Kshs.)**
Acquisition of Assets	24,186,539	81,254,059	-57,067,520
Transfers to other Government units	85,000,000	75,000,000	10,000,000
Bank Balances	421,325	1,922,333,230	-1,921,911,905
Cash in Hand Balance	0	2,407,202,753	-2,407,202,753
Accounts receivables	0	124,021,811	-124,021,811
Accounts payables	0	1,865,638,721	-1,865,638,721

Appendix II – Non-Adherence to Cut-off Dates

Date Paid	Payment Voucher No.	Payment Details	Amount paid (Kshs)
16/7/2019	D 17/1	Payment for Supply and Fixing of Curtain Blinds	2,587,072
16/7/2019	D 15/1	Payment for Supply of Furniture	150,000
16/7/2019	D18/1	Provision of Electrical Works	1,998,700
01/8/2019	D19/1	Provision of Electrical Works	3,167,925
23/7/2019	D20/1	Provision of Building, Plumbing and Civil Engineering Works.	3,892,616
25/7/2019	D21/1	Stair Landing Opening and Aluminum Partition.	2,202,801
Total			**13,849,114**