REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of County Assembly of Nakuru set out on pages 1 to 23, which comprise of the statement of financial assets and liabilities as at 30 June, 2019, statement of receipts and payments, 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 effects of the matter 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 County Assembly of Nakuru 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 comply with Public Finance Management Act, 2012 and County Governments Act, 2012.

Basis for Qualified Opinion

1.0 Accuracy of the Financial Statements - Variance Between the Financial Statements and IFMIS Trial Balance

Analysis of the balances reflected in the financial statements revealed the following variances with the balances reported in the IFMIS generated Trail Balance as follows: -

Component	IFMIS Trial Balance Figures Kshs.	Financial Statements Figures Kshs.	Variance Kshs.
Use of Goods and Services	712,508,676.10	595,865,447.00	116,643,229.10
System Required Expense	12,499,143.00	-	12,499,143.00
Acquisition of Assets	169,917,253.00	162,280,478.00	7,636,775.00
Domestic Lending and On-Lending	15,000,000.00	-	15,000,000.00
Ministry HQ Recurrent Bank A/C	1,041,322,586.85	-	1,041,322,586.85
Ministry HQ Development Bank A/C	421,201,957.00	-	421,201,957.00
Cash and Cash Equivalent	2,476,905,639.35	3,976,315.00	2,472,929,324.35
Other Liability	203,177.25	-	203,177.25
Consolidated Fund	2,046,096,323.55	-	2,046,096,323.55

From the above, it is also noted that a number of items appearing in the IFMIS trial balance had not been reported anywhere in the financial statements or explained what they relate to.

In the circumstances, the completeness and accuracy of balances reflected in the financial statements for the year ended 30 June, 2019, cannot be confirmed.

2.0 Use of Goods and Services

As reflected under Note 5 to the financial statements, the statement of receipts and payments reflects expenditure totalling to Kshs.595,865,447 on use of goods and services. A review of available records revealed the following unsatisfactory matters: -

2.1 Unreconciled Committee Expenses

Included in the expenditure is committee meeting expenses (sitting allowances) of Kshs.82,516,091 for plenary and respective committee sittings. Analysis of the payroll which records actual payments made by the County Assembly indicated an amount of Kshs.81,174,102.90 while the Clocking Sitting Allowance Management System reflected an amount of Kshs.55,257,800 resulting to unreconciled variance of Kshs.1,341,988.10 and Kshs.27,258,291 respectively.

2.2 Misclassification of Rentals of Produced Assets

Further, the expenditure includes an amount of Kshs.78,880,110 paid in respect of rentals of produced assets. The assembly increased ward offices operational costs from Kshs.60,000 to Kshs.100,000 per month with nominated Members of County Assembly being allocated Kshs.30,000 each per month. Examination of expenditure documents revealed that other operational costs and salaries and remuneration were charged under the item resulting to misclassification of expenditure. Further, a review of payments amounting to Kshs.45,837,410 for ward operational costs revealed that the expenditure returns supporting documents did not have the electronic tax register (ETR) receipts. In addition, there is no evidence to show that the activities were subjected to competitive procurement process for goods and services.

2.3 Unauthorized Expenditure on Subscription Fees

In addition, the expenditure includes an amount of Kshs.4,023,049 relating to membership fees, dues and subscription to professional and trade bodies. Included in this payment is Kshs.3,300,000 being part payment of Kshs.5,000,000 annual subscription fees to the County Assembly Forum (CAF). The payments were not budgeted for contrary to Section 37 of the Intergovernmental Relations Act, 2012 which provides that the operational expenses in respect of the structures and institution established by the Act shall be provided for in the annual estimates of the revenue and expenditure of the National Government.

2.4 Irregular Expenditure on Domestic Travel and Subsistence

The expenditure also includes domestic travel and subsistence expenditure of Kshs.117,200,531 which includes an amount of Kshs.70,635,545 paid in respect of committee meetings held outside the precincts of the County Assembly without the necessary approvals and justification.

Consequently, the validity, accuracy and completeness of the expenditure of Kshs.595,865,447 on use of goods and services reflected in the statements of receipts and payments for the year ended 30 June, 2019 could not be confirmed.

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

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. Budget Control and Performance

The statement of comparison of budget and actual amounts:-recurrent and development combined indicated that the County Assembly had a final budget of Kshs.1,287,000,637 but only received Kshs.1,076,825,789 leading to a budget shortfall of Kshs.210,174,848 or 16% of the approved budget. The statement further reflects actual expenditure of Kshs.1,100,724,601 against the budgeted expenditure of Kshs.1,287,000,637 resulting to under expenditure of Kshs.186,276,036 or 14% of the approved budget. The under expenditure mainly occurred under transfers to other government entities and acquisition of assets which recorded under expenditure of Kshs.7,336,468 or 76% and Kshs.162,280,478 or 45% respectively of their budgeted provisions.
Further, a review of the current budget compared to the previous year's budget revealed that the Management made huge budget allocations to various activities as follows:

Sub Item Name	Approved Budget 2017/2018 Kshs.	Budget 2018/2019 Kshs.	Change (increase/ (Decrease) Kshs.	% Change
Training Allowances	500,000	15,000,000	14,500,000	2900
Domestic Travel and Subsistence Allowances	12,500,000	58,000,000	45,500,000	364
Foreign Travel and Subsistence Allowances	17,500,000	40,000,000	22,500,000	129
Advertising, Awareness and Publicity Campaigns	4,000,000	9,000,000	5,000,000	125

Superannuation Fund/Gratuity	21,150,990	42,708,488	21,557,498	102
Electricity	3,000,000	6,000,000	3,000,000	100
Rents and Rates - Non-Residential	41,500,000	76,400,000	34,900,000	84
Membership Fees, Dues and Subscriptions to	4,000,000	7,000,000	3,000,000	75
Catering Services (Receptions), Accommodation, Gifts, Food & Drinks	23,000,000	33,000,000	10,000,000	43
Medical Insurance	29,425,840	38,200,000	8,774,160	30
Committee Meeting Expenses	90,000,000	111,000,000	21,000,000	23

There was no evidence of changes in activities to necessitate the above budget adjustments.

Consequently, the Management did not adhere to budget and budgetary controls.

2. Pending Bills

Annex 1 to the financial statements reflects pending bills of Kshs.57,390,196 as at 30 June, 2019. Management has not provided reasons for non-payment of the bills. Failure to settle bills during the year in which they relate to distorts the financial statements and adversely affects the budgetary provisions for the subsequent year.

3. Unresolved Prior Year Matters

In the audit report of the previous year, several paragraphs were raised under the Report on Financial Statements, Report on Lawfulness and Effectiveness in Use of Public Resources, and Report on Effectiveness of Internal Controls, Risk Management and Governance. However, although the Management has indicated that some issues have been responded to, the matters have remained unresolved as the Senate has not met to deliberate on the matters.

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. Unauthorized Hire of Legal Services

Pending accounts payables reported under other disclosures to the financial statements for the year ended 30 June, 2019 reflected a balance of Kshs.57,390,196 which included Kshs.32,136,908 in respect to outstanding legal fees as at 30 June, 2019. Management did not provide evidence to show that it sought and got approval to engage the services of a consultant to render legal services contrary to Section 17(1) of the Office of the Attorney-General Act No. 49 of 2012.

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

2. Unspent Funds Not Transferred to County Exchequer Account

As disclosed under Note 6 to the financial statements, the statement of receipts and payments reflects transfers to County Treasury (CRF Account) of Kshs.7,336,468. However, the statement of cash flows reported Kshs.26,944,266 being cash and cash equivalent at year end of 2017/2018 as well as the cash and cash equivalents at the beginning of the financial year 2018/2019. The Management did not explain why only Kshs.7,336,468 was returned and which was not disclosed as per the template. The reporting of Kshs.26,944,266 implies that the County Assembly did not comply with Section 136(2) of the Public Finance Management Act, 2012.

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

3. Valuation of Inherited Assets from the Defunct Local Authority

Annex 3 of the financial statements reflected fixed assets with historical costs of Kshs.505,861,058 (2018-Kshs.343,580,580). It was noted that the Assembly inherited fixed assets including land and buildings from the defunct County Council of Nakuru. However, there is no evidence of handover report indicating the assets and their values.

In the circumstances, the completeness and accuracy of the fixed assets totalling to Kshs.505,861,058 as at 30 June, 2019 cannot be confirmed.

4. Non-Adherence to the Thirty Per Cent (30%) Reservation Rule

Section 53(6) of Public Procurement and Asset Disposal Act, 2015 states that every procuring entity shall ensure that at least thirty (30%) percent of its procurement budget in every financial year is reserved for the youth, women and persons with disability. During the year under review, Management made procurement contracts amounting to Kshs.438,955,821 but only Kshs.35,700,000 worth of contracts was reserved for the youth, women and persons with disability. This translates to eight (8%) per cent reservation contrary to Section 53(6) of the Public Procurement and Asset Disposal Act, 2015. No reasons were given for not adhering to this provision.

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

5. Unauthorized Variations of a Contract

The Management entered into a contract agreement with a firm for the construction of executive residential house for the Speaker at a contract sum of Kshs.42,649,273.40 and paid Kshs.22,737,191.55. A review of the contract and verification of the payment indicated that there were variations to the roof, swimming pool, pump house among other items which had not been deliberated on. Although the contract agreement did not specify the completion date, board minutes reflect that the Project is behind schedule and no reasons were given for the delay in completion of the Project.

Under the circumstances, effective use of public resources 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. Lack of a Functional Audit Committee

The established Audit Committee has not been operationalized to support the accounting officer on their responsibilities for risk, control and governance and to follow up on the implementation of the recommendations of internal and external auditors as required under Section 168 of the Public Finance Management (County Governments) Regulations, 2015.

In the circumstances, I am unable to confirm the effectiveness of the overall governance.

2. Lack of a Risk Policy

The Assembly does not have a Risk Management Policy which should guide on assessment and evaluation of risk and development of the strategies for mitigation.

In the circumstances, I am unable to confirm the effectiveness of the overall governance.

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 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 assessment and overall governance.

In preparing the financial statements, Management is responsible for assessing the County Assembly ability's 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 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 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 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 County Assembly'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 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 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.

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

Nairobi

09 December, 2020