

REPORT OF THE AUDITOR-GENERAL ON COUNTY EXECUTIVE OF MACHAKOS FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of County Executive of Machakos set out on pages 1 to 97, which comprise the statement of financial assets and liabilities as at 30 June 2018 and the statement of receipts and payments, statement of cash flows and summary statement of appropriation: recurrent and development combined 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 County Executive of Machakos as at June 30, 2018 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 the County Government Act, 2012 and the Public Finance Management Act, 2012.

Basis for Qualified Opinion

1. Failure to Prepare Funds' Financial Statements

During the year under review, the Department of Education, Youth and Social Welfare operated two funds namely Machakos County Social Welfare Fund and Machakos County Bursary Fund. An amount of Kshs.52,248,016 was transferred to the Bursary Fund. The Funds' administrators failed to prepare and submit financial statements relating to the Funds.

2. Assets Inherited from the Defunct Local Authorities in Machakos County

As reported in previous years, the County's financial statements do not include the assets of the defunct local authorities located in Machakos County although the County Government has since taken possession of the assets. In addition, the Transition Authority (now defunct) did not formally handover the assets of the defunct local authorities to the County Government. Further, there are no ownership documents to the assets including title deeds and log books, among others. Consequently, it has not been possible to confirm the carrying values of the assets and their ownership status. The assets of the County Executive are therefore understated by an undetermined amount.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of County Executive of Machakos in accordance with ISSAI 30 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. Except for the matters described in the Basis for Qualified Opinion Section of my report and the conclusions on lawfulness and effectiveness as well as effectiveness of internal controls, risk management and governance, there were no other key audit matters to report.

Other Matter

1. Differences Between IFMIS and the Financial Statements Figures

The financial statements were prepared using a manual general ledger as opposed to an IFMIS ledger. There is no evidence that a reconciliation between the two records was undertaken to ensure that figures reflected in the financial statements agree with the IFMIS report. As a result, discrepancies were noted between the financial statements' figures and the IFMIS data in the following account balances:

Component	IFMIS	Financial Statements	Difference
	Kshs	Kshs	Kshs
Receipts	0	1,921,580,990	(1,921,580,990)
Transfers to Other Government Units	333,740,389	1,655,536,228	(1,321,795,838)
Proceeds from Domestic and Foreign Grants	59,626,172	109,997,189	(50,371,017)
Other Grants and Transfers	150,000	0	150,000
Exchequer Releases	5,937,353,280	7,398,999,999	(1,461,646,718)
Use of Goods and Services	869,402,022	992,913,236	(123,511,213)
Acquisition of Assets	794,069,222	850,694,781	(56,625,558)
Compensation of Employees	4,376,654,256	4,590,696,310	(214,308,053)
Social Security Benefits	3,665,770	0	3,665,770
Other Payments	12,710,269	0	12,710,269
Budget	8,730,834,395	10,078,517,468	(1,347,683,073)

In view of these discrepancies, the regularity, accuracy and completeness of the financial statements could not be confirmed.

2. Unsupported Accounts Payables – Deposits and Retentions

The statement of assets and liabilities reflects a balance of Kshs.106,247,155 in respect of accounts payables – deposits and retentions. However, the cash book and bank reconciliation statements in support of this balance were not provided for audit

review. As a result, it was not possible to confirm the existence, completeness and accuracy of the accounts payables-deposit and retentions balance that is reported in the financial statements

3. Long Outstanding Imprests

The statement of assets and liabilities reflects an amount of Kshs.51,667,748 as outstanding imprests as at 30 June 2018. The imprests date back to 2016/2017 financial year and have not been recovered, contrary to authorities that govern imprests. Management has not indicated the measures taken or intended to be put in place to recover the outstanding imprests.

4. Budget as a Control and Performance Tool

4.1 Failure to Meet Revenue Targets and Fully Absorb the Budget

During the year under review, the County Executive’s budgeted receipts and expenditure amounted to Kshs.10,078,517,469. The actual receipts amounted to Kshs.9,430,578,178 representing ninety-four (94%) percent of the budgeted amount and thus a shortfall of Kshs.647,939,289 while total payments amounted to Kshs.8,090,106,555 which translates to eighty (80) percent of the budgeted amount or under expenditure of Kshs.1, 988,410,912. The budget for the County’s own generated revenue was Kshs.1,571,446,504 and actual amount collected was Kshs.1,084,204,845 occasioning an under collection of Kshs.487,241,659. The County’s own generated revenue also declined by14% from the previous year’s collection of Kshs.1,259,304,944.

The shortfall in the revenue collection and the noted under expenditure in various items resulted in delays in the provision of services and failure to implement projects that had been planned and budgeted for.

4.2 Failure to Observe Budget Ceiling - Compensation of Employees

The County Executive made a budget of Kshs.4,613,606,356 towards compensation of employees for the year 2017/2018. This represents 46% of the total budget which is a contravention of the requirements of the Public Finance Management Act, 2012 which restricts such expenditure to 35 % of the total expenditure. In addition, the actual expenditure on compensation of employees amounted to Kshs.4,584,272,805 representing 57% of the total actual expenditure as shown below:

Employees Cost Analysis	Budget Amounts Kshs.	Actual Expenditure Kshs.
Compensation of Employees	4,613,606,356	4,584,272,805
Total Expenditure	10,078,517,467	8,090,106,556
% of Expenditure	46%	57%

Further, there was no evidence provided in terms of regulations approved by the County Assembly governing the ceilings of salaries, wages and benefits to public officers. Consequently, it was observed that a large amount of the budget was geared towards payment of employees' costs thus depriving funds to the most critical economic drivers which are domiciled in the development expenditure.

Additionally, the compensation of employees' figure includes an amount of Kshs.3,350,200 described as Top-Up house allowances to members of staff which however has not been explained or supported by way of authority and therefore remains unaccounted for. Consequently, the regularity and validity of the figure of Kshs.3,350,200 could not be confirmed.

5. Irregular Payment Made to Football Kenya Federation (FKF)

The Ministry of Tourism, Sports and Culture made a payment of Kshs.13,500,000 to Football Kenya Federation on 21 December 2017 as support for CECAFA games which were held in the County between 3 December and 17 December 2017. The Ministry did not have a budget for such an activity and the payment was not approved by the County Executive Committee Members' Cabinet. Further there was no memorandum on how the funds were to be used and the payment was done after the games had ended. There was also no acknowledgement from FKF of receipt of the money.

The regularity of the payment could therefore not be confirmed.

6. Failure to Settle Long Outstanding Pending Bills

Note 1.3.1 (other important Disclosures-Pending accounts payables) to the financial statements reflects pending bills of Kshs.954,194,940. Some of these bills date back to 2010/2011 and some of the reasons given for failure to settle the bills are that there were no funds. This is despite the fact that the statement of receipts and payments reflects a surplus of Kshs.1,340,471,622. It is also not clear why goods and services that had been included in the procurement plans and budgeted for lacked funds to pay once the services had been rendered. The budgeted amounts could have been diverted to other uses.

In addition, had these pending bills been settled during the year under review, the County Executive would have reported a reduced surplus of Kshs.386,276,682.

Management has not indicated the measures it has put in place to ensure that the long outstanding bills are cleared without affecting other normal operations of the County Executive.

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. Project Implementation and Management

1.1 Failure to Avail Information Relating to On-going Projects

As reported in the previous year, the County Executive initiated several projects mainly in the Department of Transport Roads and Public Works at an aggregate cost of Kshs.610,292,286. Of these, six projects were flagship projects worth Kshs.521,289,602. Majority of these projects were ongoing during 2016/2017 financial year. In the year under review, there were additional projects worth Kshs.89,002,689 under the Kenya Roads Board and Roads Maintenance Levy Fund.

However, the status report on these projects was not availed for audit review. Failure to complete projects on time ties up funds and denies the citizens the services that would make a difference in their lives.

In the year 2016/2017, the County Executive further allocated Kshs.205,812,124 for the upgrading of Kivandini - Masinga Road project. According to the project status report provided, the project was supposed to be completed within six months from the date of inception. However, during a site visit in November 2018, it was observed that the project was only 80%. Given that this was a 2016/2017 financial year project, the delay has resulted in failure to provide services to the citizens in time.

1.2 Incomplete Access Roads

The County Executive budgeted and planned to open up various access roads spread over all the eight (8) Sub-Counties at a cost of Kshs.21,054,400 during the year under review. A total of Kshs.13,475,409 was paid during the year to cover 511.1 KMs of roads.

However, as at 30 June 2018, only 65% of the work had been completed as per the project status reports availed for audit review. Failure to complete projects on time denies the citizens the services that they deserve.

1.3 Irregular Advance Payment - Construction of a Commercial Development Centre

The County Executive under the Ministry of Transport, Roads, Public Works and Housing awarded the construction of a Commercial Development Centre to a construction firm on 1 March 2018 at a contract sum of Kshs.55,495,943. The site was handed over to the contractor on 8 March 2018 and the project duration was 26 weeks. The Contractor requested and was paid an advance payment of Kshs.5,549,594 (10% of the contract sum) on 15 May 2018 for mobilization of resources and equipment to

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the site. A site visit in November 2018 revealed that the work was at the foundation stage and the contractor had abandoned site.

The level of completion was at 5%, although as per the contract it should have been completed by September 2018. There was also no inception report from the contractor in support of this advance.

1.4 Stalled Project-Construction of Microwave and Shredder House

The County Executive was to construct a microwave and shredder house for machines donated by the National Government to ensure that they were not exposed to the vagaries of weather. The contract was not advertised even though the engineer's bill of quantities was Kshs.10,801,440. The contract was awarded to a local contractor on 23 January 2017 at a contract sum of Kshs.11,127,131. It was not clear how the bidders were invited, evaluated and awarded the contract.

Certificate no.1 for Kshs.3,646,610 raised and approved on 25 April 2017 was paid on 12 June 2017 and a second payment of Kshs.1,259,213 that was not supported by any certificate was made on 17 April 2018. Inspection of the microwave and shredder house in November 2018 revealed that the project had stalled and the contractor had abandoned site.

Under the circumstances, there was no value for money realized on this contract.

1.5 Failure to Prepare a Performance Report

Section 164(f) of Public Finance Management Act, 2012 requires county governments to prepare and submit to the Auditor-General reports on their own performance. Management did not prepare and submit a report on performance against pre-determined objectives for submission to the Auditor-General. The management was therefore in breach of this requirement.

2. Unresolved Prior Year Issues

2.1 Installation of a Substandard Tartan Track at Machakos Stadium

The Ministry of Tourism, Sports and Culture contracted a company to install a tartan track (all-weather synthetic track surfacing made of polyurethane used for track and field competitions) at contract price of Kshs.37,946,172. By 30 June 2017, the County Executive had paid a cumulative amount of Kshs.25,000,000 to the contractor. However, site visits revealed that approximately one third of the running track had started wearing out, barely less than a year after installation.

Consequently, value for money in respect of this project was not realised.

2.2 Stalled Construction of Office Block at Ministry of Transport and Public Works

On 17 April 2014, Machakos County Government entered into a contract with a construction firm for the construction of an office at the Ministry of Transport, Roads, Public Works and Housing at a contract sum of Kshs.24,537,266. The contractor was

given possession of the site on 29 April 2014 and the works commenced soon after. However, a default notice was issued to the contractor on 17 June 2015 as a result of failure by the contractor to complete works within the stipulated contract period, failure to maintain qualified number of personnel on site, failure to proceed regularly and diligently with works as per the conditions of the contract, failure to provide a revised program of works, continuous negligence and refusal to comply with instructions from the technical team and non-authorized stoppage of works for more than 30 days. As at the time of issue of the default notice, the contractor had lodged an interim certificate No. 1 of Kshs.11,225,070.

The skeleton building is currently under the devastating effects of weather and the public risks losing money tied in the stalled project.

2.3 Grounded Motor Vehicles

The audit of 2016/2017 revealed that seventeen vehicles attached to the Ministry of Decentralized Units County Administration Water and Irrigation (Department of Solid Waste Management and the Inspectorate) were either grounded or not operational. It was not clear what measures the county had taken to repair the grounded motor vehicles since some of the vehicles were hardly more than three years' old. It was also found that a fire engine GKA 036X (Mercedes Actros) had stalled at Mavoko Sub-County Offices which greatly hampered the ability of the County to respond to fire and emergency services.

Further, physical inspection of the Athi River Health facility revealed that the facility had been allocated two ambulances. It was also found that the road insurance for an ambulance registration number KBY 281G expired on November 2017 which meant that despite it being in good condition, the ambulance could not be used in case of an emergency. The other ambulance registration number KBY 091G was grounded hence not operational. In the absence of the two ambulances allocated to the facility, emergency cases could not be attended to promptly.

2.4 Lack of Ownership Documents for Tractors

As reported in 2015/2016 and 2016/2017 financial years, the County Government procured forty (40) units of tractors, 32 of them Massey Ferguson and the rest of different makes and models meant to assist farmers to plough their farms. Ownership documents for fourteen units have not been provided for audit verification by 30 June 2017. In addition, the existence of twenty-five units had not been confirmed.

2.5 Failure to Secure County Residential Houses

As reported previously, the National Housing Corporation developed a Housing Scheme, Depot Housing Scheme in Machakos Municipality Block 1/197-214 comprising of 25 (twenty-five) units on behalf of the defunct Masaku County Council. Information available from National Housing Corporation indicates that the Scheme was developed through a loan to the defunct Council which was fully paid. However, the entire housing units were later taken over by the National Government under the Ministry of Housing and Urban Development and allocated to civil servants who have

in effect been paying rent to the Ministry. However, no evidence has been provided to indicate how these houses were taken over by the Ministry and further what action the County Executive is contemplating to repossess the houses.

2.6 Failure to Secure Ownership of Immovable Assets

As reported in the 2015/2016 and 2016/2017, an undetermined number of land parcels and buildings belonging to the County Government valued at Kshs.961,451,472 did not have title deeds and were prone to grabbing or encroachment by unscrupulous persons who might be privy to this fact. Further, records available show that 18 parcels of land of various sizes recognized by the defunct Municipal Council of Mavoko as public utilities in Syokimau and Numerical area of Mavoko Sub-County had been subdivided and allocated to individuals and institutions under unexplained circumstances. A physical check revealed that most of the land had been developed by private developers and others fenced off while a few still remained vacant. However, no evidence has been provided to confirm that the County Executive has followed up on title deeds to secure ownership of these properties.

In addition, no documents in support of the sub-division of the 18 parcels of land allocated to the individuals/private developers have been made available for audit verification.

The audit was conducted in accordance with ISSAI 1315 and ISSAI 1330. 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.

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 Appoint an Audit Committee

During the year under review, the County Executive did not have an operational audit committee. Although the committee members were appointed vide Gazette Notice No.9038.dated 16 August, 2018, it is still not operational. As a result, the internal audit function, which should report to this committee in order to work effectively and independently from the management in identifying risks, ensuring adherence to internal

controls and safeguarding loss of public funds failed to fulfill these functions. The objectives of the audit committee as outlined in the County Financial Accounting and Reporting Manual were also not achieved. The County Executive was therefore in breach of authorities that govern establishment of audit committees.

2. Lack of a Risk Management Policy

Machakos County Executive lacks a Risk Management Policy contrary to the requirements of the Public Finance Management- County Governments Regulations, 2015, 158. (1) which stipulates that a County Government entity should develop risk management strategies, which include fraud prevention mechanism; and that the County Government entity develops a system of risk management and internal control that builds robust business operations. Failure to develop a risk management policy means that the County executive does not have a framework for management of risk and hence it is not possible to identify, assess and control risk. As a result, it is not possible to define the entity's risk appetite and set the risk tolerance levels by identifying boundaries against unacceptable exposure to risk.

3. Lack of a Disaster Recovery Plan

The County Executive lacks a Disaster Recovery Plan/ Business Continuity Plan contrary to provisions of Section 99 of the Public Finance Management Act, 2012 which stipulates that the role of a disaster recovery plan is to secure the County Government's ability to meet its obligations to provide basic services or its financial commitments, identify the financial problems and be designed to place the County Government in a sound and sustainable financial condition as quickly as possible. Lack of this plan puts the County Executive at a risk of not being able to pick up and continue with its operations in case of a disaster.

The County Executive is in breach of the Public Finance Management Act, 2012.

4. Lack of an ICT Policy

The county executive has not prepared and implemented an ICT policy as a commitment to the process of implementing digital technology. An ICT policy and strategy would also provide guidance and framework that would ensure confidentiality, integrity and availability of the entity's data.

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 governance.

In preparing the financial statements, management is responsible for assessing the ability to continue to sustain services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless the County Executive either intends to liquidate the or to cease operations, or have no realistic alternative but to do so.

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 entity monitors compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

Auditor-General's Responsibilities for the Audit

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

In addition to the audit of the financial statements, a compliance audit is planned and performed to express a conclusion about whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities that govern them and that public resources are applied in an effective way, in accordance with the provisions of Article 229(6) of the Constitution and submit the audit report in compliance with Article 229(7) of the Constitution.

Further, in planning and performing the audit of the financial statements and audit of compliance, I consider internal control in order to give an assurance on the

effectiveness of internal controls, risk management and governance processes and systems in accordance with the provisions of Section 7 (1) (a) of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. My consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under the ISSAIs. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Because of its inherent limitations, internal control may not prevent or detect misstatements and instances of non-compliance. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the ability to continue as a going concern or 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 Executive to cease to continue as a going concern or 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 Executive 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 Edward R. O. Ouko, CBS
AUDITOR-GENERAL

Nairobi

28 February 2019