

REPORT OF THE AUDITOR-GENERAL ON KENYA INDUSTRIAL RESEARCH AND DEVELOPMENT INSTITUTE FOR THE YEAR ENDED 30 JUNE, 2019

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Kenya Industrial Research and Development Institute set out on pages 1 to 22, which comprise of the statement of financial position as at 30 June, 2019, statement of financial performance, statement of changes in net assets, 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, 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 Kenya Industrial Research and Development Institute 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 (Accrual Basis) and comply with the Science, Technology and Innovation Act, 2013 and the Public Finance Management Act, 2012.

Basis for Qualified Opinion

1. Lack of Revaluation of Property, Plant and Equipment

As disclosed in Note 13 to the financial statements, the statement of financial position reflects property, plant and equipment balance of Kshs.4,076,195,410. However, other than motor vehicles with a net book value of kshs.32,572,500 which were revalued in course of the year, the other assets with a net book value of Kshs.4,043,622,910 had its last valuation conducted in 1980, over thirty-nine (39) years ago. The long delay contravenes International Accounting Standard No.16 which stipulates that property, plant and equipment be revalued after every five (5) years.

Consequently, the value of property, plant and equipment balance of Kshs. 4,043,622,910 reflected in the statement of financial position as at 30 June, 2019 could not be confirmed.

2. Unsupported Retentions

As disclosed in Note 20 to the financial statements, the statement of financial position reflects contractor's retention money of Kshs.218,248,140. However, Management did not provide supporting documents such as bank certificates to confirm the availability of the amounts for discharging the liabilities when they fall due.

Consequently, the accuracy and completeness of contractor's retention money of Kshs.218,248,140 reflected in the statement of financial position as at 30 June, 2019 could not be confirmed.

3. Long Outstanding Accounts Receivables

As disclosed in Note 15 to the financial statements, the statement of financial position reflects account receivables balance of Kshs.8,722,485. Included in the balance is Kshs.4,754,436 being excess medical expenditure due for recovery from some members of staff. Out of this balance, an amount of Kshs.1,581,599 relates to officers who have since passed on. The Institute does not have policies that give clear guidance on provisions to be made in case of death of a staff member. In addition, the rate of the recovery of the outstanding dues is low with some balances having not been recovered at all.

In the circumstances, the recoverability of the excess medical receivable balance of Kshs.4,754,436 cannot be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Kenya Industrial Research and Development Institute 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

Material Uncertainty Related to Going Concern

I draw attention to page xxii where Management has put up a justification for the continued preparation of the financial statements on a going concern basis. However, a review of the Institute's financial performance for the year ended 30 June, 2019 indicated a net deficit of Kshs.29,173,978 (2017/2018 - deficit of Kshs.164,721,477). This is despite the fact that the Government disbursed a recurrent grant of Kshs.535,707,396 to the Institute during the year under review. Further, the Institute's statement of financial position as at 30 June, 2019 reflects current liabilities of Kshs.171,219,445 which exceeded current assets of Kshs.119,739,934 by Kshs.51,479,511 resulting into a negative working capital. The Institute is likely to face significant financial difficulties in meeting its financial obligations as and when they fall due and the future survival as a going concern will be dependent on creditors' and Government support.

These events or conditions, indicate that a material uncertainty exists that may cast significant doubt on the Institute's ability to continue as a going concern.

My opinion is not modified in respect of this matter.

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. Long Outstanding Debt

1.1. Debt from Kenya National Cleaner Production Centre

The Institute entered into a Memorandum of Understanding (MOU) with Kenya National Cleaner Production Centre (KNCPC) in October, 2013 for a period of two (2) years where the Centre was to be hosted by the Institute. At the end of the MOU and through a Board of Directors resolution dated 6 April, 2017 the Management wrote to the Centre for claim of rent and utility costs. An amount of Kshs.58,950 per month was to be paid from 1 January, 2018 and Kshs.257,163 from 1 January, 2019 as per letter dated 15 November, 2017 and invoice No.6909 dated 15 January, 2019. However, review of the Institute's records showed that a receivable has not been recognized in respect of the rent and utility costs of Kshs.2,250,378 (Kshs.707,400 for year 2018 and Kshs.1,542,978 to June, 2019).

Management should engage the Centre with a view to signing a binding contract that is enforceable in a court of law in order to recognize the amounts owing.

1.2. Amount due from a Court Ruling

The Institute was involved in a court case with one of its staff where the staff took the Institute to court for contempt in 2014. The case was dismissed with costs and the court issued a certificate of taxation on 23 November, 2018 where the Institute was to claim Kshs.104,540 from the staff. However, the amount has neither been recovered, despite the time lapse, nor has it been captured as a receivable.

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. Delay in Completion of the Proposed Techno Centre

The Institute contracted a firm for implementation of the proposed Techno Centre in Nairobi, that commenced on 25 February, 2013 at an estimated contract sum of

Kshs.3,933,008,763. The contract was to take 156 weeks with a completion date of 3 March, 2016. According to the Architect's progress report as at 30 June, 2019, the project was approximately 63.5% complete having taken 329 weeks while the project contract price had been revised to Kshs.4,812,400,054. There was no notable progress on site for as at 30 June, 2019.

Further, there were extra costs incurred due to idle staff and machinery and interest on delayed payments, which amounted to Kshs.33,805,849 as per certificate No.34 dated 11 October, 2019.

In the circumstances, the public may not get value for money for the delayed project as well as loss arising from continued penalties and interests on delayed payments which could be avoided.

2. Unutilized Resource Centres

The Institute planned for the construction of Research, Technology and Innovation (RTI) Laboratories at the Kisumu Western Region Centre. This was to be composed of Leather Pilot Plant and Research Laboratories, Food Processing Research Laboratories, Energy Resource Testing and Research Laboratories, Natural Products Pilot and Research Laboratories and, Administration offices & Business Incubation Unit, for purposes of enhancing and achieving its mandate.

The contract was awarded to a firm commenced on 15 April, 2011 at a contract sum of Kshs.641,410,058 and completed on 25 October, 2016 at a final costs of Kshs.783,138,524.

Physical verification undertaken during the month of October, 2019 revealed that the Food Processing, Energy Resource Testing and Natural Products Pilot Research Laboratories were not being utilized despite being complete due lack of machinery.

In the circumstances, the buildings did not achieve the intended purpose, showing lack of proper use of public resources.

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

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 Directors

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 overall governance.

In preparing the financial statements, Management is responsible for assessing the Institute's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management is aware of the intention to liquidate the Institute 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 Directors is responsible for overseeing the Institute's financial reporting process, reviewing the effectiveness of how the Institute 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 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 Institute’s ability to continue as a going concern. 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 Institute to cease to continue as a going concern.
- 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 Institute 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
AUDITOR-GENERAL

Nairobi

19 August, 2021