

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

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Kenya Medical Research Institute set out on pages 1 to 49, 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 Medical Research 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. Unsupported Finance Income – External Investments

As disclosed in Note 8 to the financial statements, the statement of financial performance reflects finance income-external investments balance of Kshs.30,506,394. The balance includes Treasury Bills interest income of Kshs.26,114,784 whose supporting certificates were not availed for audit review.

Consequently, the accuracy and validity of interest income from treasury bills of Kshs.26,114,784 for the year ended 30 June, 2019 could not be confirmed.

2. Recoverability of Staff Advances

As disclosed in Note 21 to the financial statements, the statement of financial position reflects receivables from non-exchange transactions balance of Kshs.446,925,910. The balance includes staff advances amounting to Kshs.38,437,671 which constitutes imprests totalling to Kshs.5,736,759 owed by officers who have since separated with the Institute through termination of service, resignation and death rendering the amount irrecoverable.

In the circumstance, the validity and recoverability of receivables from non-exchange transactions balance of Kshs.38,437,671 as at 30 June, 2019 could not be confirmed.

3. Unsupported Property, Plant and Equipment

As disclosed in Note 23 to the financial statements, the statement of financial position reflects property, plant and equipment balance of Kshs.20,035,378,571. The balance includes various parcels of land totalling to Kshs.4,152,168,160 whose title/ownership documents were, as previously reported, not provided for audit review.

Further, as previously reported, the balance also includes land and buildings for a staff housing project valued at Kshs.476,001,556. The vendor of the land who is also the developer had initially used the title documents as collateral to borrow funds from a commercial bank. In an effort to have the documents discharged, the Government spent a sum of Kshs.280,000,000 in 1993 and a further amount of Kshs.142,000,000 in 2000 all totalling Kshs.422,000,000 towards settling the developer account with the bank. Available information indicates that the ownership documents have since been released to the National Treasury but the title has not been discharged by the bank and remains in the name of the vendor as at 30 June, 2019.

In the circumstances, the ownership status of the parcels of land of Kshs.4,152,168,160 and staff housing project valued at Kshs.476,001,556 as at 30 June, 2019 could not be confirmed.

4. Unsupported Intangible Assets-Software

As disclosed in Note 24 to the financial statements, the statement of financial position reflects intangible assets net book value of Kshs. 33,129,095 which includes Kshs.22,904,126 relating to a payment for an Enterprise Resource Planning (ERP) software. As previously reported the Institute had sourced for this service from a company on 24 August, 2011 at a contract sum of Kshs.24,865,500. The installation and commissioning of this software was to take one year up to 2 July, 2012. Despite the 92% payment of the contract sum by 30 June, 2019, only four (4) out of fourteen (14) modules had been installed. It was further noted that even the installed modules were not operational as at 30 June, 2019.

Consequently, the validity and accuracy of intangible asset net book value Kshs.33,129,095 reflected in the statement of financial position as at 30 June, 2019 could not be confirmed.

5. Unsupported Investments and Grant Fund

As disclosed in Note 22 to the financial statements, the statement of financial position reflects investments balance of Kshs.416,661,800. The balance includes fixed deposit balance of Kshs.30,000,000 whose supporting certificate was not availed for audit review.

Similarly, and as disclosed in Note 28 to the financial statements, the statement of financial position reflects grant fund balance of Kshs.926,881,060 which includes a fixed

deposits balance of Kshs.379,238,750. The supporting certificates were not availed for audit review.

Consequently, the accuracy and validity of fixed deposit balance of Kshs.30,000,000 and grant fund balance of Kshs.379,238,750 as at 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 the Kenya Medical Research 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

Financial Performance

During the year under review, the Institute reported a deficit of Kshs.164,395,118 (2017/2018-deficit Kshs.132,621,755) resulting in reduction in accumulated surplus from Kshs.1,489,571,089 as at 30 June, 2018 to Kshs.1,325,175,971 as at 30 June, 2019. The Institute's performance therefore is on a downward trajectory and if strategies are not put in place to reverse the trend, the Institute is likely to experience financial difficulties in future.

My opinion is not modified based on the effects of the 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. Budgetary Control and Performance

The statement of comparison of budget and actual amounts reflects final revenue budget and actual on comparable basis of Kshs.7,479,401,243 and Kshs.6,641,432,170 respectively, resulting to an under-funding of Kshs.837,969,073 or 11% of the budget. Similarly, the statement reflects final expenditure budget and actual on comparable basis of Kshs.7,479,401,243 and Kshs.6,688,117,984 respectively resulting to an under expenditure of Kshs.791,283,259 or 11% of the budget.

The underfunding and underperformance affected the planned activities and may have impacted negatively on service delivery to the public.

2. Unresolved Prior Year Matters

In the audit report of the previous year, several issues were raised. However, the Management has not resolved all the issues or given any explanation for failure to adhere to the provisions of the Public Sector Accounting Standards Board templates and The National Treasury's Circular Ref. No. PSASB/1/12/(44) of 25 June, 2019.

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. Non-Compliance with the Attorney General's Circular

As disclosed in Note 18 to the financial statements, the statement of financial performance reflects general expenses amounting to Kshs.463,923,464. The balance includes legal expenses to private legal firms of Kshs.23,043,896. However, the Management did not provide, for audit review, approval and issuance of no objection from the Attorney General's office on engagement of the private legal firms as required by the Attorney General's Circular reference AG/CON/6/D/144/VOL.II dated 16 April, 2014.

In the circumstance, it has not been possible to determine compliance with the law.

2. Contracted Services

As disclosed in Note 15 to the financial statements, the statement of financial performance reflects contracted services-cleaning of Kshs.20,833,319 paid to a company. As previously reported, the Institute had contracted a company in September, 2014 for cleaning services which was to run for eleven (11) months up to 31 July, 2015 at a monthly charge of Kshs.1,602,563. The Management extended the contract for four (4) months to November, 2015 to allow for a fresh tender. However, it was noted that the company continued offering services from December, 2015 up to the time of this audit in January, 2020. Available information indicated that a dispute arose between the contractor and the Management where upon the company sought legal redress. The Institute was directed to pay the company for services rendered from December, 2015. The Management did not provide evidence of action it intends to ensure there is a valid contract is consummated with the company or another service provider.

In the circumstances, it has not been possible to determine whether value for money has been achieved and the payments amounts to wasteful utilization of public resources.

3. Non-Compliance with the One Third of Basic Salary Rule

During the year ended 30 June, 2019, two hundred and fifty-six (256) employees earned a net salary of less than a third (1/3) of the basic salary contrary to Section C.1(3) of the Public Service Commission (PSC) Human Resource Policies, 2016. The Management has not given explanation for failure to comply with the policy.

In the circumstances, Management is in breach of the law

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 Conclusion on Effectiveness of Internal Controls, Risk Management and Governance 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

Long Outstanding Receivables

The statement of financial position reflects receivables from non-exchange transactions balance of Kshs.446,925,910 which includes capitation balance of Kshs.139,371,856 which has been outstanding for more than two (2) years. No supporting documents were provided to confirm the recoverability of this amount. Further, the receivables from non-exchange transactions balance includes customers/suppliers control account balance of Kshs.40,471,198 which has also been outstanding for more than two years and recoverability appears doubtful.

In the circumstances, I am unable to confirm existence of effective debt management mechanisms at the Institute.

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 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 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 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 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 Institute'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 Institute 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 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