REPORT OF THE AUDITOR-GENERAL ON KENYATTA UNIVERSITY FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Kenyatta University set out on pages 49 to 88, which comprise the statement of financial position as at 30 June 2018, and the statement of financial performance, statement of cash flows, statement of changes in net assets 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 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 Kenyatta University as at 30 June 2018 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 University's Act, 2012 of the Laws of Kenya.

Basis for Qualified Opinion

1.0 Going Concern

During the year under review, the University recorded a deficit of Kshs.2,109,408,510 (2017-deficit of Kshs.43,902,999) thus reducing accumulated surplus from kshs.8,631,815,399 in June 2017 to kshs.6,522,406,889 as at 30 June 2018. Further, the current liabilities of Kshs.4,339,760,367 as at 30 June 2018 exceed the current assets of Kshs.847,650,317 resulting to a negative working capital of Kshs.3,492,110,050 which indicates that the University was unable to meet its financial obligations as and when they fall due. In particular, the University was unable to remit pension and taxes amounting to Kshs.1,826,407,015, audit fees Kshs.3,400,000 and other deductions of Kshs.204,381,264 to the respective beneficiaries thereby risking fines and penalties.

The University is therefore operating under financial difficulties and currently it has resulted to financing its operations using costly short term borrowings which may further worsen the liquidity position. Therefore, the University is technically insolvent and if no urgent positive steps are taken to improve the financial position, it may not be able to meet its mandate in future.

The financial statements have therefore been prepared on a going-concern basis on assumption that it will continue to receive financial support from Government, creditors and donors.

2.0 Property Plant and Equipment

2.1 Encroached Land

As similarly reported in the previous years, the property, plant and equipment balance of Kshs18,169,653,855 reflected in the statement of financial position as at 30 June 2018 includes land registration No. 11026/2 measuring 445.17 hectares on which the main campus of the University stands. Included in the 445.17 hectares is a portion of land measuring 12.472 hectares valued at Kshs.123,281,555 that has been illegally encroached upon by squatters. Although the University has filed a case in a Court of law against the illegal encroachment, the matter has not been determined and the squatters continue to erect buildings on the land as at the date of this report.

2.2 Land without Ownership Documents

The property, plant and equipment balance of Kshs.18,169,653,855 further includes land measuring thirty two hectares whose registration fees of Kshs.880,000 was paid and allocated from Lagdera Constituency Development Fund in Garissa County. However ownership documents for the land were not availed for audit verification and as a result, it has not been possible to confirm that the land is owned by the university.

In the circumstances, it has not been possible to ascertain the ownership status of the said land in dispute and that the Property, Plant and Equipment balance of Kshs.18,169,653,855 is fairly stated as at 30 June 2018.

3.0 Receivables from Non-exchange Transactions

3.1 Car Loans

As similarly reported in the previous year, the receivables from non-exchange transactions balance of Kshs.232,126,977 reflected in the statement of financial position as at 30 June 2018 includes an amount of Kshs.6,437,627 in respect of staff debts out of which Kshs.1,421,445 relates to car loans due from four (4) officers who have since left the University which have been outstanding for long period of time. The loans were issued by National bank of Kenya and guaranteed by the University but the staff defaulted in repayment after they left the University. The bank however recovered the amounts owed together with accrued interest from the fixed deposit account of the University. It is not clear how the vehicle logbooks were released to ex-staff and how the ex-employees were cleared by the management before the University had fully recovered the outstanding loans from them.

3.2 Outstanding Imprest

Note 19 to the financial statements reflects outstanding imprests totaling Kshs.15,397,702 out of which imprest amounting to Kshs.15,003,769.65 has been outstanding for over a year. This is contrary to Public Finance Management Act, Section 93(4B) 6 which requires that before issuing temporaty imprests the accounting officer shall ensure that the applicant has not outstanding imprests and failure to account for or surrender of the imprest the full recovery to be made on the salary of the defaulting officer.

In the circumstance it has not been possible to confirm the full recoverability of the receivables from no-exchange transactions totaling Kshs.232,126,977.

4.0 Nugatory Expenditure - Closure of Kigali and Arusha Campus

Kenyatta University had incurred Kshs.518,174,359 to set up both Kigali campus in Rwanda (Kshs.420,749,207) and Arusha campus in Tanzania (Kshs.97,425,152). It was however established that the University closed down the two campuses due to operational challenges apparently imposed by change in legislation by both the Rwandan and Tanzanian governments after the University had just met all the requirements and ready to roll out their programmes.

Although the university has explained that all the due diligence was done before the decision to open up the two campuses, the management has not made any recovery on the amount so far incurred totaling Kshs.518,174,359 as at 30 June 2018 and the investment of Kshs.518,174,359 may turn out to be a sunk cost.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Kenyatta University 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 judgement, are of most significance in the audit of the financial statements. Except for the matters described in the Basis for Qualified Opinion section, I have determined that there are no other Key Audit Matters to communicate in my report.

Other Matter

1.0 Budgetary Control & Performance

1.1 Revenue

According to the statement of comparison of budget and actual amounts, the University had an approved Revenue budget of Kshs.9,979,017,618 for the financial year 2017/2018 against actual receipts of Kshs.9,053,537,878 resulting to a deficit of Kshs.925,479,740. This was attributed majorly to the fact the University did not receive the anticipated tuition fees revenue due to the staff strike that disrupted learning, reduction in number of students and non-facilitation of the programmed third semester. However there is a need by the University to refocus on the budgeting on its own locally generated funds to avoid over budgeting and its own challenges.

Revenue Analysis

	Original Budget	**Adjustment**	**Final Budget**	**Actual on Comparable Basis**	**Over/(Under)**	**Percentage Difference**
Revenue	**2017-2018**	**2017-2018**	**2017-2018**	**2017-2018**	**2017-2018**	
Government Grant	4,090,781,105	82,457,108	4,008,323,997	4,148,305,985	139,981,988	3.49
Tuition & Other Fees	5,991,174,751	599,117,475	5,392,057,276	4,347,821,552	(1,044,235,724)	(19.37)
Other Income (IGAs)	595,304,882	16,668,537	578,638,345	557,410,341	(21,226,004)	(3.67)
Total Income	**10,677,260,738**	**698,243,120**	**9,979,017,618**	**9,053,537,878**	**(925,479,740)**	

1.2 Expenditure

The University had an approved expenditure budget of Kshs.9,561,794,820 for the financial year 2017/2018 against actual spending of Kshs.11,162,946,388.This occasioned an excess expenditure of Kshs.1,051,263,010 translating to 10.99%.This occurred mainly due to Increase in staff cost as a result of the implementation of the 2013-2017 Collective Bargaining Agreement (CBA).However the University management had not sought approval from the line Ministry and the National Treasury for exceeding budget by 11% as per requirement of Section 4.1 of Treasury circular No.14/2016 dated 13 July 2016.

Expenditure Analysis

	Original Budget	**Adjustment**	**Final Budget**	**Actual on Comparable Basis**	**(Over)/Under**	**Percentage Difference**
Expenses	**2017-2018**	**2017-2018**	**2017-2018**	**2017-2018**	**2017-2018**	
Telephone, Electricity and Water	262,452,311		262,452,311	249,050,363	13,401,948	5.11
Personal Emoluments			6,399,824,889	7,726,090,829	(1,326,265,940)	(20.72)
Council Allowances	11,705,496		11,705,496	9,777,840	1,927,656	16.47
Depreciation				549,888,557		
Repairs and Maintenance	655,314,313		655,314,313	616,729,470	38,584,843	5.89
Contracted Professional Services	37,000,000		37,000,000	36,918,502	81,498	0.22
Operation Expenses	2,344,860,000	(262,762,188)	2,082,097,812	1,861,096,802	221,001,010	10.61
Finance Cost	113,400,000		113,400,000	113,394,025	5,975	0.01

	Original Budget	Adjustment	Final Budget	Actual on Comparable Basis	(Over)/Under	Percentage Difference
Total Expenditure	3,424,732,120	(262,762,188)	9,561,794,820	11,162,946,388	(1,051,263,010)	10.99

2.0 Property Plant and Equipment

The Statement of Financial Position balance of Kshs.18,169,653,855 as at 30 June 2018 excludes the value of Kenyatta University Teaching, Research and Referral Hospital that stands on the Universities 7.97 hectares of land. The Hospital was built after the Kenya Government entered into a concessional loan agreement with Export-Import Bank of China for a concessional loan of Kshs.8,756,625,600.

The supporting documentation of the construction of this Hospital were not availed for audit verification.

Also the Government of Kenya through Legal Notice No.4 of 25 January 2019, Kenya University Teaching, Research and Referral Hospital was turned into a state corporation.
In view of the foregoing, it has not been possible to confirm that Universities Property, Plant and Equipment balance of Kshs.18,169,653,855 as at 30 June 2018 is fairly stated.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

As required by Article 229(6) of the Constitution, based on 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 has come to my attention to cause me to believe that public Resources has not been applied lawfully and in an effective way.

Basis for Conclusion

1.0 Ethnic Diversity

A review of the university staff data as of 30 June 2018 revealed that one ethnic community accounted for 40% of council members, 45.4% of senior management and 39.6% of permanent staff. This is contrary to paragraph 7(2) of the National Cohesion and Integration Act, 2008 which states that no public establishment shall have more than one third of its staff from same ethnic community. The University has failed to improve the ethnic balance as similar percentages remain relatively un-changed compared to last years.

The University management is therefore in breach of the law.

2.0 Human Resource Management

Noncompliance to a Third Rule on Salary Deductions.

Analysis of the payroll data for the year ended 30 June 2018 revealed that there were six thousand eight hundred and eighty four (6,884) University employees who were being paid net salary that is less than a third (1/3) of their basic pay. This contravenes Employment Act, 2007 CAP.226 Section 19(3) which states that ‘Without prejudice to any right of recovery of any debt due, and notwithstanding the provisions of any other written law, the total amount of all deductions which under the provisions of subsection (1), may be made by an employer from the wages of his employee at any one time shall not exceed two-thirds of such wages or such additional or other amount as may be prescribed by the Minister either generally or in relation to a specified employer or employee or class of employers or employees or any trade or industry’. In the circumstances, the University was 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, I confirm that, nothing has come to my attention to cause me to believe that internal controls, risk management and overall governance were not effective.

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.

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 (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 governance.

In preparing the financial statements, management is responsible for assessing the ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the management either intends to liquidate the entity 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 noncompliance. 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 University 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 University 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.

FCPA Edward R. O. Ouko, CBS
AUDITOR-GENERAL

Nairobi

13 March 2019