

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

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Machakos University set out on pages 1 to 37, the statement of financial position as at 30 June 2018, and statement of financial performance, statement of changes in net assets, 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 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 Machakos 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 Universities Act, 2012.

Basis for Qualified Opinion

1. Tuition and Other Related Incomes

Note 14 to the financial statements reflects Tuition and Other Incomes figure of Kshs.305,045,098 which included tuition fees balance of Kshs.151,812,781 out of which Kshs.3,998,230 relates to fees banked by students directly to the bank but have not been receipted in the cash book as at 30 June 2018. Some of these direct bankings have been outstanding since 2015.

In the circumstances, the validity, completeness and accuracy of the tuition and other related incomes could not be confirmed.

2. Cash and Bank Balances

The statement of financial position as at 30 June 2018 reflects cash and bank balances of Kshs.95,430,594 out of which an amount of Kshs.18,346,126 for National Bank Operations Account whose bank reconciliation statement had unrepresented cheques amounting to Kshs.1,163,038 that had not been reversed in the cash book as at 30 June 2018.

In the circumstance, the accuracy and completeness of cash and bank balances balance of Kshs.95,430,594 could not be ascertained.

3. Other Income

The statement of financial performance reflects Income Generating Activities and other income balance of Kshs.74,762,561 includes an amount of Kshs.72,294,387 being revenue from their restaurant. Out of this amount a balance of Kshs.1,596,896 relates to bank transfers that have not been receipted in the cash book.

In the circumstances, the validity and accuracy of other income balances of Kshs.74,762,561 could not be confirmed.

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 matter 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 and Performance

1.1 Budget Absorption

The University had an approved total budget of Kshs.1,508,844,000 for the financial year 2017/2018 against an actual of Kshs.1,150,408,017 resulting to an under absorption of Kshs.358,435,983 as detailed in the table below:

Item	Budget Allocation 2017/2018 (Kshs)	Actual 2017/2018 (Kshs)	Variance (Kshs)	Absorption Rate in %
Recurrent Grants	720,979,000	727,975,082	(6,996,082)	-1%
Development Grants	45,000,000	30,000,000	15,000,000	33%
Donor Grants	40,803,000	0	40,803,000	100%
Research Grants	50,000,000	12,625,275	37,374,725	75%
Tuition Fees	421,188,000	295,655,729	125,532,271	30%
Accommodation Income	3,100,000	3,589,876	(489,876)	-16%
Catering Income	15,280,000	5,799,493	9,480,507	62%
University Hotel Income	200,494,000	72,294,387	128,199,613	64%
Other Income	12,000,000	2,468,174	9,531,826	79%
Total Income	1,508,844,000	1,150,408,017	358,435,983	24%

It is evident that the University fell short of the budget by Kshs.358,435,983 due to shortfall of actual budget received from development grants, donor grants and research grants and revenue earned from tuition fees, accommodation income, catering income, University hotel and other income.

1.2 Recurrent Expenditure

Similarly, the University had a total recurrent expenditure of Kshs.1,069,163,063 against an approved budget of Kshs.1,404,576,000 resulting to under expenditure of Kshs.335,412,937 or 24% as detailed in the table below:

Item	Budget Allocation 2017/2018 (Kshs)	Actual 2017/2018 (Kshs)	Under Absorption (Kshs)	Absorption Rate in %
Personnel Emoluments	958,487,168	778,291,949	180,195,219	19%
Operations and Maintenance expenditure	446,088,832	290,871,114	155,217,718	35%
Total	1,404,576,000	1,069,163,063	335,412,937	24%

From the above analysis, the under absorption may have a negative impact on the implementation of the planned activities and service delivery to its stakeholders. The University management may also have over budgeted on the recurrent expenditure and therefore there is need for a more realistic budget in future.

1.3 Capital Expenditure Budget

In addition, the University incurred a total capital expenditure of Kshs.143,946,557 against an approved budget of Kshs.104,268,000 resulting to over absorption of Kshs.39,678,557 as detailed in the table below:

Item	Budget allocation 2017/2018 (Kshs)	Actual 2017/2018 (Kshs)	Variance (Kshs)	Absorption Rate in %
Extension of ADB Building	12,500,000	19,673,990	(7,173,990)	-57%
Tuition and other Blocks	30,000,000	36,767,890	(6,767,890)	-23%
Master Plan/Topo survey	1,500,000	0	1,500,000	100%
Furniture and Fittings	5,500,000	4,865,792	634,208	12%
ICT Equipment, Integration and Maintenance	12,168,000	17,470,268	(5,302,268)	-44%

Item	Budget allocation 2017/2018 (Kshs)	Actual 2017/2018 (Kshs)	Variance (Kshs)	Absorption Rate in %
Renovations of Buildings	2,500,000	4,595,360	(2,095,360)	-84%
Training Equipment and Machines	10,000,000	4,277,300	5,722,700	57%
Office Equipment	5,000,000	6,037,182	(1,037,182)	-21%
Motor vehicles	18,500,000	18,463,194	36,806	0%
Security Infrastructure & Street Lighting	1,000,000	0	1,000,000	100%
Development of Sports & Games facilities	5,600,000	1,438,000	4,162,000	74%
Lecture Hall & Classrooms (work-in-progress)	0	30,357,581	(30,357,581)	-100%
Total Development Expenditure	104,268,000	143,946,557	(39,678,557)	-38%

From the above analysis, the over absorption was as a result of the University management incurred unbudgeted capital expenditure in 2017/2018. This may also imply that the University management may also have under budgeted on the capital expenditure and therefore there is need for a more realistic budget in future.

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 matters described in the Basis for Qualified Opinion and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources sections 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. Unisol Enterprise Resource Planning (ERP) System Development of

The University entered into a service level agreement with M/s Abno Softwares International Limited for provision of Unisol Enterprise Resource Planning System support at a total cost of Kshs.958,000 payable annually. The service level agreement covered

ten ERP modules including Integrated Financial Management (IFM) of which a payment amount of Kshs.958,000 was paid on 29 January 2018. The system was installed in 2013/2014 financial year. However, the IFM generated statement of financial position balances as at 30 June 2018 differed with the financial statements submitted for audit as shown below:

Item	Financial Statement Balances Generated from Integrated Financial Management (Kshs)	Financial Statements balances Submitted for Audit (Kshs)	Variance Kshs
Cash and cash equivalent	(884,677,149)	95,430,594	(980,107,743)
Receivable from exchange transactions	134,263,739	140,207,228	(5,943,489)
Inventories	0	12,051,918	(12,051,918)
Receivable from non-exchange transactions	(50,278,063)	1,995,816	(52,273,879)
Trade and other payables	(791,536,271)	192,423,703	(983,959,974)
Property plant and equipment	513,449,142	2,371,499,293	(1,858,050,151)
Capital Reserves	252,308,751	2,606,063,018	(2,353,754,267)
Revenue reserves	(531,897,322)	(196,575,320)	(335,322,002)
Deferred income	500,000,000	19,273,448	480,726,552
Surplus (deficit) for the year	733,882,511	38,729,009	695,153,502

The resulting variances among the two sets of records had not been reconciled as at the time of our audit.

Consequently, it could not be ascertained whether the University obtained value for money for the expenditure of Kshs.958,000.

2. Property Plant and Equipment

Note 5 to the financial statements reflects property plant and equipment balance of Kshs.2,371,499,293 out of which an expenditure of Kshs.621,585,000 is in respect of buildings and site works. Examination of payment vouchers, payment schedules and interim certificates for Lecture Theatre and Classroom Complex Phase II indicate that the project was awarded to M/s Sinoe Construction Limited vide contract No. MUC/T/2/W/C/PH2/2013-2014 dated 9 January 2014 at a contract sum totaling Kshs.179,441,790. However, by the time of audit no landscaping had been done and the contractor of Phase II had vacated the site, yet the building was already in use.

Initially, these project had been awarded to Thwama Building Services Limited on 17 June 2013 at a contract sum of Kshs.40,330,307. The contractor of Phase I did not complete the works. Phase I was constructed up to the structural frame, at a cost of Kshs.49,364,073 with a variation of Kshs.9,033,766.50, being 22.39% of the initial contract.

University management had instructed the contractor of Phase II to complete the remaining works of Phase I. This was contrary to Public Procurement and Disposal Act 2015 section 153 (1) and (2) and Public Procurement and Disposal Regulations 2006, section 32, since the two contracts were separate and distinct from each other. No evidence was provided for audit review on the approval to terminate the Phase I contract by the tendering committee which authorized the original contract before Thwama Building Services Limited was released out of site.

In the circumstances, the University management was in breach of Public Procurement and Disposal Act 2015 section 153 (1) and (2); and Public Procurement and Disposal Regulations 2006, section 32 with regard to the termination of Lecture Theatre and Classroom Complex Phase I contract.

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 INTERNAL CONTROLS EFFECTIVENESS, GOVERNANCE AND RISK MANAGEMENT SYSTEMS

Conclusion

As required by Section 7 (1) (a) of the Public Audit Act, 2015, based on audit procedures performed except for the matter described in the Basis for Qualified Opinion section of my report, 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 University's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the applicable basis of accounting unless the management either intends to liquidate the University 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 University's 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.

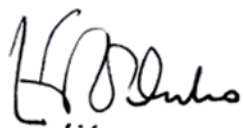
As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- 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 University'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 University 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 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

11 March 2019