

REPORT OF THE AUDITOR-GENERAL ON MERU COUNTY INVESTMENT AND DEVELOPMENT CORPORATION FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Meru County Investment and Development Corporation set out on pages 15 to 26, which comprise the statement of financial position as at 30 June 2017, and the statement of comprehensive income, statement of changes in equity, statement of cash flows 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 Meru County Investment and Development Corporation as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Public Finance Management Act, 2012 and the Meru County Investment and Development Corporation Act, 2014.

In addition, as required by Article 229(6) of the Constitution, except for the matters described in the Basis for Qualified Opinion and Other Matter sections of my report, based on the procedures performed, I confirm that, nothing has come to my attention to cause me to believe that public money has not been applied lawfully and in an effective way.

Basis for Qualified Opinion

1.0 Transfer of Non-Current Assets

During the year under review, the Meru County Executive transferred assets to Meru County Investment and Development Corporation in compliance to Section 32 (1) of the Meru County Investment and Development Corporation Act, 2014. The assets included the Meru County hotel, land for Meru rising tower project of unknown size, County Massionettes, petrol station land in Meru and Maua towns of unknown size. However, the assets were not registered under the name of the Corporation contrary to Section 32 (2) of the Meru County Investment and Development Corporation Act, 2014. Further the assets were not disclosed in the Corporation's financial statements as at 30 June, 2017.

In the circumstance, the ownership, security and valuation of the transferred assets as at 30 June 2017 could not be ascertained.

2.0 Irregular Consultancy Expenditure on Meru Rising Tower Project

Note 5 to the financial statements reflects Kshs.132,011,761 in respect to work-in-progress. Records made available showed that included in the Kshs.132,011,761 was Kshs.19,000,000 in respect of tender CGM/RFP/010/2014-2015 dated 20 November, 2015 for Consultancy services for the design and construction and supervision of proposed fifteen storey office block building in Meru Town. However, the land where the Meru rising tower was proposed to be constructed was not registered under the Corporation. Further, the consultancy fees computations were based on a project cost estimate of Kshs.1,990,878,979 whereas the estimate made available for audit reflected an estimated project cost of Kshs.1,770,663,000. This resulted in the consultancy fees for the project being overstated by Kshs. 5,489,632 as shown below:

Item	As per Invoice (Kshs)	As per Estimate (Kshs)	Variance (Kshs)
Project Cost Estimates	1,990,878,979	1,770,663,000	220,215,979
Architectural Consultancy (3.99% of Project cost + Kshs. 117,118)	79,553,189	70,766,572	8,786,618
Quantity Survey (QS) Fees (2.15% of project cost estimates + Kshs. 171,850)	42,975,748	38,241,105	4,734,644
Civil/Structural Engineering (CSE) Consultancy Fees	50,705,499	50,705,499	-
Total Consultancy Fees	173,234,436	159,713,175	13,521,261
Fees Due Upon Completion of Preliminary Designs (15 % of Total Consultancy)	25,985,165	23,956,976	2,028,189
Fees Due Upon Completion of Final Designs (20% of Arch and QS Consultancy fee)	24,505,787	21,801,535	2,704,252
Total Professional Consultancy Fees Due	50,490,953	45,758,512	4,732,441
Less Consultancy Previously Paid	15,700,345	15,700,345	-
Consultancy Fees now due	34,790,608	30,058,167	4,732,441
Add: 16% VAT	5,566,497	4,809,307	757,191
Total Consultancy Fees now due	40,357,105	34,867,473	5,489,632

Consequently, the correctness, completeness and accuracy of Kshs. 19,000,000 expenditure for consultancy services for the design and construction supervision of proposed fifteen storey office block building in Meru Town could not be ascertained.

3.0 Meru County Hotel Project

During the financial year 2015/2016, the Corporation awarded tender No. MCIDC/TO4/2015/2015 for refurbishment of Meru County Hotel at a contract sum of Kshs.186,390,006 and tender No. MCIDC/RFP/001/2015-2016 for the provision of consultancy services for detailed design, preparation of bidding documents and supervision of the refurbishment of Meru County Hotel. During the financial year under review, the Corporation spent Kshs.67,860,714 for the two contracts which was included in the work-in-progress of Kshs. 132,011,761. However, a physical verification done on 23 February 2018 established that the works already done were being demolished to change the use of the building from hotel to offices. The Corporation did not avail new contracts and bill of quantities for the changed works. Further, it was not clear why the Corporation approved and started a project which it changed midway resulting in wastage of public funds totaling to Kshs.67,860,714.

In consequence, the propriety and value for money for the Kshs. 67,860,714 expenditure in respect to Meru County Hotel refurbishment as at 30 June 2017 could not be ascertained.

4.0 Irregular Expenditure on Conferences and Seminar

Note 4 to the financial statements indicates Conference and Seminars expenditure of Kshs.4,456,446 which included unsupported payments amounting to Kshs.4,165,169. In the circumstance, the propriety of the expenditure of Kshs.4,165,169 for Conference and Seminars as at 30 June 2017 could not be confirmed.

5.0 Overpayment of Board Allowances

During the financial year under review, the Corporation paid board allowances totaling to Kshs. 990,000 for eleven (11) board meetings based on the rates approved by the County Treasury in compliance with Section 9 of the Meru County Investment and Development Act, 2014. However, these allowances were above the Kshs.415,000 that would have been paid if the Corporation had adopted the rates prescribed by the Salaries and Remuneration Commission (SRC) in the circular referenced SRC/ADM/CIR/1/13(122)- dated 16 April 2014. By Kshs.575,000. However, the Corporation, did not seek an approval from the Salaries and Remuneration Commission (SRC) for the higher rates contrary to Article 230 (4) of the Constitution of Kenya, 2010.

Consequently, the Corporation contravened applicable regulations and the Kshs.575,000 overpayment as at 30 June 2017 was not a proper charge to public funds.

6.0 Irregular Project Implementation

Note 6 to the financial statements reflected investments totaling to Kshs. 37,871,370 as at 30 June 2017 which included Kshs 3,702,429 for partitioning of offices and purchase equipment's for Mugambo Jwetu radio station. However, the Project of Mugambo Jwetu was not in accordance with the investment strategy and plan contrary to Section 25 (4) of the Meru County Investment and Development Act, 2014. Further, no investment or project appraisal and financial analysis for Mugambo Jwetu was undertaken before implementation of the project contrary to Section 26 of the Meru County Investment and Development Act, 2014. In addition, the ownership documents of Mugambo Jwetu were not availed for audit to determine the shareholding and

ownership of the radio station and therefore it was not possible to ascertain that the Kshs.3,702,429 expenditure was a proper charge to public funds.

In view of the foregoing, the ownership, propriety, security and accuracy of the investments balance of Kshs. 37,871,370 as at 30 June 2017 could not be ascertained.

7.0 Irregular and Unbudgeted Staff Cost

The financial statements for the year under review show compensation of employees' balance of Kshs.28,597,537 as at 30 June 2017. However, the salaries had not been approved by Salaries and Remuneration Commission (SRC) contrary to Article 230(4) of the Constitution of Kenya. Further, included in the staff cost was Kshs.1,002,000 being salaries and allowances for Meru County Oils Ltd and Mugambo Jwetu staff recruited as the Corporation staff. However, it was not certain why the Corporation recruited on behalf of the two institutions and paid staff salaries using the Corporation staff budget contrary to Section 19 (4) of Meru County Investment and Development Corporation Act, 2014.

Further, the Meru County Oils Ltd Petrol Station Manager was recruited in September 2016 eight (8) months before the petrol station was operationalized in April, 2017. No reason or evidence of work done for the eight months was availed for audit to justify the recruiting of the station manager before the operation of the Petrol Station leading to wasteful expenditure of Kshs.45,000 per month all totaling to Kshs.360,000 for the 8 months the petrol station was not operational.

In the circumstances, the propriety of the expenditure of Kshs. 28,597,537 for staff cost as at 30 June 2017 could not be confirmed.

8.0 Presentation of Financial Statements

Section 164 of the Public Finance Management Act, 2012 (1) requires that at the end of each financial year, the accounting officer for a county government entity shall prepare financial statements in respect of the entity in formats to be prescribed by the Accounting Standards Board. The Corporation prepared financial statements for the financial year ended 30 June 2017 and presented for audit review. However, the financial statements included a Summary Statement of Appropriation instead of a Statement of Comparison of Budget and Actual Amounts. Further, the Corporation did not disclose if it had adopted any new or revised International Financial Reporting Standards.

In the circumstances, the Corporation was in breach of Section 164 of the Public Finance Management Act, 2012.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Meru County Investment and Development Corporation 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 and Other Matter sections of my report, I confirm that there were no Key Audit Matters to communicate in my report.

Other Matter

1.0 Budget and Budgetary Control

The Corporation budget for the year under review of Kshs. 242,453,134 was approved on 19 September 2016 over two months after the commencement of the year contrary to Section 19 of the of the Meru County Investment and Development Corporation Act, 2014 which requires the budget to be prepared at least three months before the commencement of the financial year and approved before the commencement of the financial year. Further, there was no evidence of budget approval by the County Executive Committee as required by Section 20 (3) of the Meru County Investment and Development Corporation Act, 2014. The budget is as shown below:

TITLE AND DETAILS	Final Supplementary Budget (Kshs.)	Actual Expenditure (Kshs.)	Under/Over (Kshs.)	Absorption rate (%)
Revenue	242,453,134	242,453,135	-	100%
TOTAL REVENUE	242,453,134	242,453,135	-	100%
Recurrent Expenditure	69,725,511	53,665,195	16,060,316	77%
Development Expenditure	172,727,624	110,225,857	62,501,766	64%
TOTAL EXPENDITURE	242,453,134	163,891,052	78,562,082	68%

The Kshs.62,501,766 development under-expenditure translated to a denial of equivalent services to Meru residents.

2.0 Audit Findings on Internal Control Effectiveness

2.1 Reserve Funds

Section 19 (2) (h) of the Meru County Investment and Development Act, 2014 requires the Corporation to create such reserve funds to meet future or contingent liabilities in respect of retirement benefits, insurance or replacement of buildings or equipment. During the year under review, no reserve funds were created and set aside as required. The Corporation was therefore in breach of the law. It was also not clear how the Corporation intended to finance future replacement of its depreciable Non-current Assets balance of Kshs.138,188,412 as at 30 June 2017 in absence of the reserve funds.

2.2 Failure to Establish an Audit Committee

The Corporation did not have an audit committee in place, contrary to Section 155 (5) of the Public Finance Management Act, 2012 which states that a County Government entity shall establish an internal audit committee whose composition and functions are set out in Section 167 (1) of the Public finance management (County Governments) regulations 2015.

In the circumstances, the Corporation was in breach of Section 155 (5) of the Public Finance Management Act, 2012.

2.3 Dividend Policy

Section 30 of the Meru County Investment and Development Corporation Act, 2014 states that the Corporation shall, in consultation with the County Executive Committee establish a dividend policy, which shall be reviewed annually. However, the Corporation did not establish a dividend policy during the year under review.

In the circumstances, the Corporation was in breach of Section 30 of the Meru County Investment and Development Corporation Act, 2014.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards (IFRS) and for such 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.

In preparing the financial statements, management is responsible for assessing the Corporation's ability to continue as a going concern/ sustain services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless the management either intends to liquidate the Corporation's 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.

Those charged with governance are responsible for overseeing the Corporation's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

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

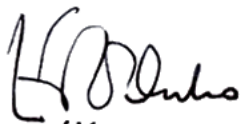
or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances and for the purpose of giving an assurance on the effectiveness of the Corporation's 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 Corporation'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 Corporation's 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 Corporation's 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

27 June 2018