

REPORT OF THE AUDITOR-GENERAL ON NATIONAL SOCIAL SECURITY FUND FOR THE YEAR ENDED 30 JUNE, 2019

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of National Social Security Fund (NSSF) set out on pages 1 to 44, which comprise of the statement of net assets available for benefits as at 30 June, 2019, statement of changes in net assets available for benefits, statement of changes in accumulated Members' Funds, 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 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 National Social Security Fund as at 30 June, 2019, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRS) and comply with the Public Finance Management Act, 2012 and the National Social Security Fund Act, 2013.

Basis for Qualified Opinion

1. Unaccounted for Members Contributions - Contributions in Transit

The statement of changes in net assets available for benefits reflects a net surplus from dealings with members amount of Kshs.10,163,269,208. In compliance with the Retirement Benefits Act, 1997, NSSF maintains employer contribution clearing accounts where total contributions are posted from the employers' accounts. It is from these clearing accounts that members' accounts are credited for benefits payment upon qualification. A review of Note 41 to the financial statements revealed that in the year under review, the contributions in transit representing contributions which had not been posted to individual members' accounts reduced from Kshs.663,000,000 as at 30 June, 2018 to Kshs.290,000,000 as at 30 June, 2019 being a net change by Kshs.373,000,000. Management has not provided explanations for failure to reconcile and post the amounts to the respective member's accounts.

Consequently, the accuracy, completeness and validity of the statement of changes in net assets available for benefits for the year ended 30 June, 2019 could not be confirmed.

2. Unreconciled Cash and Bank Balances

The statement of net assets available for benefits reflects cash and bank balance of Kshs.419,376,662. A review of the Fund's bank balances held by various financial institutions indicated a negative balance of Kshs.268,049,312 in respect of the National Bank

of Kenya while as the bank reconciliation statement reflected a positive balance of Kshs.198,407,296.

Further, an analysis of the Fund's bank reconciliation statements revealed the following unsatisfactory matters:

2.1 Unrecorded Receipts in Bank Statements and Cashbook

The bank reconciliation statements reflected receipts in the bank totalling Kshs.2,063,448,078.76 on 30 June, 2019 which was at variance with the amount reflected in the cashbook of Kshs.1,658,301,341.

2.2 Unrecorded Payments in Bank Statement and Cashbook

The bank reconciliation statements reflected payments in the bank not recorded in the cashbook amounting to Kshs.498,906,547.62 as at 30 June, 2019 which was at variance with amount reflected in the cashbook of Kshs.1,751,322,101.39. Further, included in this amount were payments amounting to Kshs.1,745,080,309.24 which had not been reconciled.

Management has explained that the above balances were held for prolonged periods without being cleared due to the inability of the accounting systems to clear the old balances.

In the circumstances, the accuracy and completeness of the cash and bank balance of Kshs.419,376,662 reflected in the statement of net assets available for benefits as at 30 June, 2019 could not be confirmed.

3. Unsupported Returned Benefits

The statement of net assets available for benefits reflects payables and accruals balance of Kshs.1,959,062,448 and as disclosed under Note 32 to the financial statements. The amount includes an amount of Kshs.269,378,392 in respect of returned benefits payable to members. It was not clear why the returned benefits have been outstanding for a long period of time without being investigated or beneficiaries identified, paid and cleared from the system.

Consequently, the accuracy, completeness and validity of payables and accruals balance of Kshs.1,959,062,448 reflected in the statement of net assets available for benefits as at 30 June, 2019 could not be confirmed.

4. Investments in Doubtful Bonds

As was reported in the previous year the financial statements reflected Kshs.7,807,297,038 on corporate bonds out of which a provision for doubtful investments of Kshs.666,900,000 was deducted, leaving net balance of Kshs.7,140,397,038.

A review of the status of investment in corporate bonds confirmed that the Fund entered into contractual agreements with four (4) Fund Managers namely; Old Mutual Investment Group

Ltd, Genesis Kenya Investment Management Limited (GenAfrica Asset Managers), British American Assets Managers Limited and Stanlib Kenya Limited in February, 2018 in line with Retirement Benefits (Managers and Custodians) Regulations. The Fund Managers were to have full control and unrestricted power to invest Fund's money as per the investment policy for maximum returns to Trustees.

Information and explanations provided by the Fund Managers is that both Imperial Bank and Chase banks were cleared and approved by the Capital Markets Authority as the mandated regulators and supervised by the Central Bank of Kenya as legally viable investment vehicles in which Fund's money can be committed. However, approval to invest in the two Banks by The National Treasury was not availed for audit verification.

A five year, three months (5.25 years) fixed bond worth Kshs.132,200,000 was held by Imperial Bank but the Bank was placed under statutory management by the Central Bank of Kenya on 13 October, 2015. At the time, the Fund held corporate bonds totalling Kshs.666,900,000 through its Fund Managers. A provision for the entire amount has been made in the financial statements as tabulated below:

CORPORATE BONDS HOLDING AT IMPERIAL AND CHASE BANK					
Corporate Bond Position as at 30 June, 2019					
ID Number	Text ID Number	Portfolio	Nominal Amount (Kshs.)	Price (Kshs.)	Market Value (Kshs.)
Imperial_FXD	Imperial 5.25YR FXD BOND	Britam	90,000,000	100	90,000,000
Imperial_FXD	Imperial 5.25YR FXD Bond	Old Mutual	42,200,000	100	42,200,000
KE5000002104	FXDCHASE2015	Britam	100,000,000	100	100,000,000
KE5000002104	FXDCHASE2015	GenAfrica	160,000,000	100	160,000,000
KE5000002104	FXDCHASE2015	Old Mutual	174,700,000	100	174,700,000
KE5000002104	FXDCHASE2015	STANLIB	100,000,000	100	100,000,000
Total			666,900,000		666,900,000

In the circumstances, the realization of the investment in Corporate Bonds amounting to Kshs.666,900,000 invested by the Fund Managers could not be ascertained and members' contributions are at risk of being lost.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the National Social Security Fund 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.

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. Budget Control and Performance

The statement of comparative budget and actual amounts reflects final revenue budget and actual on comparable basis of Kshs.33,995,631,000 and Kshs.19,549,069,192 respectively resulting to an under-funding of Kshs.14,446,561,808 or 42% of the budget. Similarly, the statement reflects final expenditure budget and actual on comparable basis of Kshs.6,722,064,000 and Kshs.6,171,467,974 respectively resulting to under-utilisation of Kshs.550,596,026 or 9% of the budget. Management explained this fall to have arisen from investment management expenses of Kshs.235,393,947 occasioned by poor portfolio performance leading to lower amounts claimable. Further, the assets whose titles were revoked caused the variance of Kshs.40,431,395 or 41% on provisions.

2. Unresolved Prior Year Audit Matters

The following matters from previous years remained outstanding as at 30 June, 2019:

2.1 Irregular Disposal of Undeveloped Land - Mavoko

As previously reported, undeveloped land in Mavoko Municipality measuring 69.16 acres was subdivided into seven (7) plots of 9.88 acres and disposed-off at Kshs.18,000,000 each. The plots were sold to AMS Properties Limited on the basis of an agreement dated 21 November, 2011 at a total cost of Kshs.126,000,000. However, only Kshs.12,600,000 or 10% was paid vide Miscellaneous Receipt M010022315 dated 23 August, 2011. The balance of Kshs.113,400,000 which was to be paid within 90 days from the date of execution of the agreement has not been settled to date.

The Management has explained that the contract has not been terminated since the delay in completing the conveyancing process was caused by a dispute over physical location of the plots involving the Fund and other parties who claimed to have ownership documents of the land. The Fund Management has not adequately explained why it has taken a long time to resolve the disputes on the plot and what legal action has been taken to resolve the matter.

2.2 Kisumu Milimani Upmarket Houses

As previously reported, land LR.KISUMU/MUN/8/258 measuring 0.7740 Ha. situated in Milimani Estate, Kisumu County was on 26 November, 2012 swapped to offset a debt of Kshs.158,969,145.00 owed to the Fund by the then Municipal Council of Kisumu. The land is currently valued at Kshs.220,000,000. At the point of the swap in 2012 the land had been valued at Kshs.95,000,000 and Kshs.100,000,000 by Value Zone Limited and Tysons Limited respectively. Currently the National Social Security Fund does not have a policy on write-offs of penalties and swaps of property for contributions owed.

2.3 Tassia I and Tassia II Scheme

As previously reported, the Fund holds titles for Block 97, 21190 and 21189 in Tassia along Outering Road measuring 350 Acres. The land was acquired at a cost of Kshs.2.2 Billion from Tassia Coffee Estate Ltd and Nokin Investment Ltd and in 2005. The Fund sold 5,500 plots to informal settlers as un-serviced plots. Further, there were contributions made by the plot owners for infrastructure development to service the plots.

However, at the time of audit in June, 2020, the title deeds had not been processed and neither had the infrastructure development been carried out as expected.

Consequently, the delay in resolving the issue on titles and laying of infrastructure could attract claims and prolong disputes from the plot owners.

2.4 Fixed Deposits held to Maturity

Note 17(b) to the financial statements reflects Kshs.6,104,878,400 in relation to fixed deposits (held to Maturity) as at 30 June, 2019 and which is net of provision for doubtful deposits held in Chase Bank and Imperial Bank at Kshs.70,000,000 and Kshs.259,500,000 respectively. These deposits were invested between 08 September, 2015 and 03 March, 2016 and were expected to mature between December, 2015 and May, 2016. This however, and as previously reported, did not materialize since both Chase Bank and Imperial Bank were placed under Statutory Management by the Central Bank of Kenya on 07 April, 2016 and 13 October, 2015 respectively. A review of the matter during the year ending 30 June, 2019 revealed that Kshs.53,373,740.10 and Kshs.52,970,671.10 were recovered from Imperial Bank and Chase Bank respectively both totalling Kshs.106,344,411.20 as illustrated in the table below:

Imperial/Chase Bank Ltd Redemptions as at 30 June, 2019						
		Deposits		Corporate Bonds		
Bank		Imperial Bank (Kshs.)	Chase Bank (Kshs.)	Imperial Bank (Kshs.)	Chase Bank (Kshs.)	Total (Kshs.)
Holding		259,500,000.00	70,000,000.00	132,200,000.00	534,700,000.00	996,400,000.00
Received	2018/2019	26,691,232.15	52,970,671.10	-	-	79,661,903.25
	2017/2018	26,682,507.95	-	-	-	26,682,507.95
Balance		206,126,259.90	17,029,328.90	132,200,000.00	534,700,000.00	890,055,588.80

In the circumstances, the recoverability of the balance of Kshs.666,900,000 on Investments in Corporate Bonds from Imperial Bank and Chase Bank as at 30 June, 2019 is doubtful.

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 Construction of Hazina Trade Centre

Included in the assets under construction balance of Kshs.3,213,440,907 is an amount of Kshs.2,480,782,310 in respect of Hazina Trade Centre whose construction was ongoing as at the time of audit. The was awarded at an initial contract sum of Kshs.6,715,218,188 for construction of thirty-six (36) floors tower which was subsequently scaled down to 15 floors at a reduced contract sum of Kshs.4,095,862,434. The project has had a number of extensions, the last authorized one being 31 December, 2019.

As at the time of audit in May, 2020, eleven (11) certificates had been paid totalling Kshs.3,406,865,723.11 representing eighty-three percent (83%) of the total project cost. A physical inspection of the building on 07 May, 2020 indicated that the construction was approximately seventy percent (70%) done. During the exercise, the contractor was at early stages of laying floor tiles and roofing, with major interior works still outstanding.

The Management explained that Covid-19 pandemic and the resultant restrictions had adversely affected the contractors supply chain and hence the slow pace at which the project was being implemented. This was despite the fact that the completion date for the project had earlier been extended to 31 December, 2019. The period has since lapsed with the construction still in progress without an extension.

In addition, perusal of other relevant project documents revealed a claim of Kshs.871,697,124 by the contractor arising from idle stoppage of works. The financial claim remained outstanding as at the time of audit as Management and the Board of Trustees held the view that it is an independent process separate from completion of the construction works which would be dealt with as a final account issue. Further, the claim was going through various stages of vetting and approval before payment could be processed.

In the circumstances, it is not clear when the project will be completed and whether the public will get value for money on the investment.

2. Delay in Sale of Milimani Executive Apartments in Nairobi

Included under Note 29 to the financial statements on Investment Property are additions during the year amounting to Kshs.3,881,755,189 in respect of Milimani apartments project. The project comprises of one hundred and four (104) spacious apartments on Five Blocks A-E with initial estimated cost of Kshs.1,550,000,000. The contractor completed the project at a pre-measured works value of Kshs.1,692,262,919 and handed over the project on 9 April, 2019.

The Board approved the sale of the apartments categorized into 3-bedroom unit with a DSQ and a 3 bedroom without DSQ at Kshs.35,000,000 and Kshs.31,000,000 respectively. The expected total sales amounted to Kshs.3,600,000,000 at the time of hand-over. However, as at the time of the audit in April, 2020, total sales were Kshs.831,246,302 as follows:

Type	No. of Units	Initial Deposit of 10% (Kshs.)	Expected Amount (Kshs.)
House with DSQ	94	828,046,302	3,290,000,000
House Without DSQ	10	3,200,000	310,000,000
Total	104	831,246,302	3,600,000,000

Further, documentation and records provided revealed that nine (9) prospective house owners partially paid minimum ten percent (10%) amounting to Kshs.5,092,000 of the cost required. Besides, most of the houses were fully booked and the requisite deposit of ten percent (10%) of the selling price paid for at the completion date except the aforementioned prospective buyers. This was in contravention of the sale agreement which required payment of 10% deposit. Further, the partial payment may also have affected the Fund's cash flows and thus negatively impacted on service delivery.

It was however, noted that the progress in occupancy of the houses has been low with only twelve (12) or eleven percent (11%) buyers having fully paid and sixty-eight (68) or sixty-five percent (65%) having made partial payments. Out of the buyers who had paid the ten (10%) deposit at the completion date, seventeen (17) prospective buyers withdrew their interest and were refunded their deposit amounting to Kshs.94,950,000.

Management has indicated measures taken to enable prospective buyers to finance the remainder and vacant units at favourable terms, including advertisement in print media besides partnering with commercial banks on financing loans.

In the circumstances, it is not clear when the public will get value for money on the investment.

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 matter 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

1. Unremitted Members Contributions

Review of the members contributions status as at 30 June, 2019 revealed that contributions receivable estimated at Kshs.5,702,745,355.40 had been included in the financial statements under contingent assets. This comprised of mandatory contributions of Kshs.580,759,618.45 and penalties of Kshs.5,121,985,736.95.

Although the Management has indicated that recovery efforts are in progress, as at the time of audit in April, 2020 the contributions receivable of Kshs.5,813,336,648.95 was still outstanding and no satisfactory explanation was provided for non-recovery.

This was an indication of weak controls over recovery of unremitted contributions.

2. Ineffective Systems

Note 29 to the financial statements reflects Kshs.3,177,008,287 in respect of assets under construction out of which Kshs.167,945,837, Kshs.64,998,224 and Kshs.29,914,248 were for Social Security and Pensions Administration System (SSPAS) Reimplementation, Electronic Document and Records Management System (EDRMS) System and the SAP Additional modules respectively. The modules were meant for production of financial statements by the Fund. However, the system could not generate financial statements as expected of an end-to-end system. Failure by the system to independently generate financial statements has occasioned interventions through manually preparing the financial statements leading to numerous errors in the presented financial statements.

In addition, analysis of the expenditure schedules produced using the SAP system revealed that they do not include payee names making it difficult to relate the schedules generated against payment vouchers or files availed for audit verification.

In the circumstances, the reliance of the systems to conclusively generate results without manual interventions is in doubt.

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 Trustees

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards (IFRS) 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 Fund'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 Fund 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 Trustees is responsible for overseeing the Fund's financial reporting process, reviewing the effectiveness of how the Fund 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 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 Fund'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 Fund 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 Fund 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

24 June, 2021