

# **REPORT OF THE AUDITOR-GENERAL ON PYRETHRUM PROCESSING COMPANY OF KENYA FOR THE YEAR ENDED 30 JUNE 2018**

---

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Disclaimer of Opinion**

I have audited the accompanying financial statements of Pyrethrum Processing Company of Kenya set out on pages 11 to 28, which comprise the statement of financial position as at 30 June 2018, and the statement of comprehensive income, statement of changes in equity, 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 do not express an opinion on the accompanying financial statements. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

### **Basis for Disclaimer of Opinion**

#### **1. Undisclosed Material Uncertainty Related to Going Concern**

The statement of comprehensive income for the year ended 30 June, 2018 reflects a loss of Kshs.264,257,000 (2017: a loss of Kshs.147,251,000). The loss for the year under review eroded further the general reserve to negative Kshs. 1,126,140,000 as at 30 June 2018 from negative Kshs. 861,884,000 as at 30 June 2017. In addition, the statement of financial position as at 30 June 2018, reflects total current assets of Kshs. 443,644,000 and total current liabilities of Kshs. 1,161,032,000 resulting in a negative working capital of Kshs. 717,388,000 as at that date. The Company is, therefore, technically insolvent and its continued existence is dependent upon the financial support of the Government and its creditors. This material uncertainty that casts doubts on the Company's ability to continue as a going concern has, however, not been disclosed in the financial statements by the management

#### **2. Property, Plant and Equipment**

The statement of financial position reflects a balance of Kshs.2,545,450,000 in respect of property, plant and equipment as at 30 June 2018. This balance, as disclosed under Note 8 to the financial statements comprise of value of land, buildings, plant and machinery, work in progress, motor vehicles, furniture, equipment and computers. Examination of available records revealed the following:

- (i) During the year under review, the Company revalued its assets and paid an amount of Kshs.14,556,443 for the services. However, the revaluation of the

assets to Kshs.6,823,230,225 has not been adopted or approved by any authority or the board of directors.

- (ii) Included in the property, plant and equipment balance is a sum of Kshs.354,340,000 in respect of eighteen parcels of land which, however, are not registered in the name of the Company. Further, the balances include two parcels of land situated in Nakuru Municipality (Block 7/138) and Nyandarua County (Oljororok Farm Block 11322/1/2/3) valued at Kshs.7,500,000 and Kshs.45,800,000 respectively, but whose ownership is in dispute. Available information indicates that the land in Nyandarua was sold to a private developer at a cost of Kshs.30,050,000 and the matter has since been taken to court.
- (iii) Further, out of a total of fifty-eight motor vehicles and heavy machinery owned by the Company, only six motor vehicles were valued, while thirty-five, although serviceable had not been valued.
- (iv) A physical verification of the vehicles owned by Pyrethrum Company of Kenya revealed that eight vehicles were impounded and auctioned due to outstanding payments to a merchant who had carried out some works at the company in the financial year 2003/04. The eight vehicles had been purchased at a cost of Kshs.11,560,472.42. The disposal of the eight vehicles, which were auctioned in 19 May 2018, has not been recorded in these financial statements.
- (v) In addition, out of the existing fifty vehicles, logbooks for ten vehicles were not provided for audit. Consequently, their ownership remains doubtful.
- (vi) As disclosed under Note 8 to the financial statements, capital works in progress balance of Kshs.455,663,000 as at 30 June 2018 relates to a extraction plant purchased and installed in 2006 but which has never been commissioned. Although management has explained that the machine was purchased in anticipation of an increase in flower deliveries to the factory and that the plant will be commissioned in future once the industry is revived, no evidence has been presented for audit to show the steps taken to revive the industry. Further, technological changes and wear and tear are bound to affect the idle machines adversely and may result in the loss of Kshs.455,663,000 in taxpayers' funds invested in the assets.

In view of the above, it has not been possible to confirm whether, plant and equipment balance of Kshs.2,545,450,000 as at 30 June, 2018 is fairly stated.

### **3. Intangible Assets**

As previously reported, the statement of financial position as at 30 June, 2018 similarly reflects intangible assets balance of Kshs.825,650,000 relating to an amount incurred on the cost of registering licenses and studies undertaken on impact of pyrethrum on the environment and human life. However, the management has not explained how the balance was determined.

In addition, the intangible assets have not been subjected to amortization or revaluation over the years. Although the management has explained that benefits from the assets will accrue indefinitely to the Company hence the reason for not amortizing them, technological and other changes are bound to affect the value of the intangible asset hence the need to amortize or revalue them over time.

#### **4. Fixed Deposit in Euro Bank Ltd**

As reported previously, the statement of financial position reflects under non-current liabilities, a long term provision relating to a fixed deposit balance of Kshs.150,000,000 placed with Euro Bank in 2001. The bank was subsequently placed under receivership and dissolved in 2003. Although the management has made a full provision for bad and doubtful debts for this deposit, no evidence has been presented to show steps taken by the Company to clear the unrecoverable amount of Kshs.150,000,000 from the books of account.

#### **5. Bank and Cash Balances**

The statement of financial position reflects bank and cash balances of Kshs.10,937,000 as at 30 June, 2018. The management has not provided bank confirmation certificate for Stanbic Bank – Mombasa Branch Account No. 014/00/300349/01 balance of Kshs.33,442, that has been outstanding since 2017. In addition, Note 12(a) to the financial statements reflects an amount of Kshs.41,000 in Other Bank Account whose details have not been disclosed.

Consequently, the accuracy and validity of bank and cash balances cannot be ascertained.

#### **6. Trade and Other Payables**

- (i) As reported also in the previous year, included in the trade and other payables balance of Kshs.736,385,000 as at 30 June 2018 are outstanding statutory deductions of Kshs.138,733,851 and Kshs.1,002,000 relating to pay as you earn (PAYE) for employees and board members, respectively that have remained unpaid, and thus continue to attract interest and penalties in line with the provisions of Section 37 (2) of the Income Tax Act Cap 470 of the Laws of Kenya.

- (ii) Further, the supporting documents and age analysis to the list of trade payables have not been provided.

In view of the foregoing, the validity and accuracy of trade and other payables figure of Kshs. 736,385,000 cannot be ascertained.

## **7. Inventories**

The statement of financial position as at 30 June 2018 reflects inventories balance of Kshs.204,262,000. This figure, however, includes other pyrethrum products valued at Kshs.104,168,000 brought forward from previous years and relates to sludge, green oil and carbon dust that is claimed to contain less than 3% pyrethrin. It was indicated that the value of Kshs.104,168,000 had been given by an Official from the Ministry and it has been difficult to either sell or dispose of the products.

In addition, the value of the total inventories balance of Kshs.204,262,000 has not been supported with any documentary evidence. Further, it has not been possible to confirm the method under which the stock was valued and whether in the valuation, adequate provisions for obsolescence were made since the quality of the unprocessed stock could deteriorate and eventually lose some or all its value.

Consequently, the valuation and accuracy of the inventories balance of Kshs.204,26,000 as at 30 June 2018 cannot be confirmed.

## **8. Trade and Other Receivables**

### **8.1. Unsupported Balances**

- (i) Trade and other receivables balance of Kshs.183,181,000 as at 30 June 2018 includes, as reported in the previous year, a sum of Kshs.7,180,000 relating to an abortive purchase of a stand at the Nairobi International Show Grounds. However, no documentary evidence has been provided to date to confirm the amount.
- (ii) Similarly, the trade and other receivables balance of Kshs.183,181,000 includes trade debtors amounting to Kshs.61,853,000 which have been outstanding for long and whose recoverability remain doubtful. Further, the management has not provided documentary evidence in support of this figure.
- (iii) The balance also includes staff debtors amounting to Kshs.43,604,000. The amount further includes unanalyzed debts totalling Kshs.36,798,000 owed by former staff members and which have been outstanding for more than fifteen years. The management has also not explained how the amount moved from Kshs.41,951,000 in 2013/2014 to Kshs.43,604,000 in 2017/2018. Provisions

for bad and doubtful debts necessary in relation to these uncertain debts have not been incorporated in these financial statements.

- (iv) The trade and other receivables figure of Kshs.183,181,000 also includes other debtors, growers' debtors, staff debtors and deposits held by courts all amounting to Kshs.86,238,000, Kshs.33,593,000, Kshs.43,604,000 and Kshs.4,454,000 respectively whose supporting documentation were not complete.

Under the circumstances, the completeness, accuracy and validity of the trade and other receivables balance of Kshs.183,181,000 as at 30 June 2018 cannot be confirmed.

## **8.2. Provision for Bad Debts**

- (i) The statement of financial position's trade and other receivables balance of Kshs.183,181,000 as at 30 June 2018 is net of provision for bad debts for the year of Kshs.56,241,000, while the trial balance reflects an amount of Kshs.52,680,159 resulting in unexplained difference of Kshs.3,560,841. Although the management has been making a general provision for bad debts of Kshs.56,241,000 per year over the last three years, no policy on provision for doubtful debts was provided for audit scrutiny. It is, therefore, not clear how the accumulated provision for bad and doubtful debts is accounted for.
- (ii) It is also not clear how the provision was accounted for in the statement of comprehensive income as the provision for the year could not be traced to the cost of sales, administration costs or other costs in the statement of comprehensive income.

In the circumstances, it has not been possible to confirm the validity and accuracy of the provision for bad debts.

## **9. Deferred Pyrethrum Costs – Irregular Charge of Amortization Cost**

As reported in the previous years, the deferred pyrethrin costs resulted from losses in the pyrethrin content in the crude pyrethrin extract (OR) inventories held between 1999 and 2003. Reconciliations made in the financial year 2005/2006 revealed substantial loss in pyrethrum totalling 180,859 kilograms and valued at Kshs.1,357,922,110. According to Section 18 of the Pyrethrum Act Cap 340 (now repealed), such losses should have been born by the farmers. However, the Board of Directors passed a resolution to amortize the losses over a period of 30 years with effect from 2007/2008. The management has, however, not explained over the years the cause of the huge loss or justified how the 30-year amortization period was determined.

## **10. Other Income**

### **10.1. Rent Income**

The statement of comprehensive income reflects an amount of Kshs.16,521,000 under Other Income. As disclosed in Note 4 to the financial statements, the amount includes rent income of Kshs.15,309,000. However, a detailed review of the ledger revealed that rent amounting to Kshs.18,082,720 was collected during the year and thus, resulting in undeclared receipts of Kshs.2,773,720. In addition, the following documents were not provided or audit scrutiny:

- (i) A list of all properties owned by the Company and the rent receivable from each of the properties.
- (ii) Lease agreements for leased properties.

A review of some of the physical rental properties revealed that the Company has a capacity to collect more rent than disclosed in these financial statements. Based on the enquiries done to existing tenants, the Company could be collecting up to Kshs.29,872,800 in rent on at least 189 of its rentable properties leased out to third parties, including two state entities, Commodities Fund and Pest Control Board. The rent collectable and collected is therefore not only under-declared but part of it is also not accounted for.

Further, in the previous year, the Company contracted an agent to collect rent on its behalf. During request for quotation, it was mandatory for the bidders to provide the following supporting documents:

- (i) Company's certificate of incorporation;
- (ii) Pin certificate;
- (iii) Tax compliance certificate;
- (iv) Certificate of registration for youth, woman or disabled; and
- (v) Certificate of registration as an estate agent by Agents Registration Board and Trade or Business License.

The required relevant documents for the company that won the tender for rent collection agency service were not however provided for audit review. The validity of the award and contract for rent collection cannot be confirmed under the circumstances.

## **11. Irregularities on Staff Costs**

### **11.1. Non-disclosure of Staff Expenditure**

The statement of comprehensive income reflects an amount of Kshs.219,474,000 under administration costs. As disclosed in Note 5(b) to the financial statements, the

amount includes Kshs.68,691,000 relating to staff costs. However, a review of available records revealed that the company spent Kshs.147,812,802 on staff costs, and the balance of Kshs.79,121,802 was charged to cost of sales. No reason has been given for this misleading disclosure.

In addition, the company hired casuals and spent an amount of Kshs.20,090,000 on the same yet there was no processing of flowers that took place in the year under review.

## **11.2. Non-remittance of Statutory Deductions**

The Company received from the parent ministry Kshs.144,000,000 vide a letter referenced MOA/CORP/II/16/2/VOL.II dated 5 April 2017 towards settlement of statutory obligations. However, examination of the payroll and payment vouchers revealed that the Company only paid the net salaries and statutory deductions relating to NHIF and NSSF and an amount of Kshs.6,728,849 in respect of PAYE. No explanations were given for failure to settle statutory deductions like workers' union subscriptions, pension scheme contributions and bank and loan repayments, and yet there was an allocation for the same in May 2017.

## **12. Government of Kenya Loan**

The statement of financial position as at 30 June 2018, reflects a long term Government of Kenya loan of Kshs.863,368,000 and current portion of Kshs.424,647,000. According to the information available, the loan was given by the Government of Kenya through the National Treasury in the 2006/2007 financial year and was to be repaid within 10 years. It was, however, noted that the principal amount of Kshs.863,368,720 has not been repaid and has attracted accumulated interest of Kshs.424,647,000 and accumulated penalty of Kshs.195,448,022. In addition, although the loan balance has been categorized into a long term and a current portion, the total amount is now due and payable as the full sum ought to have been settled in full by the end of 30 June 2017.

## **13. Inaccurate Statement of Cash Flows**

The statement of cash flows reflects a negative amount of Kshs.38,857,000 being net cash flows from operations activities. However, the cash and cash equivalents balance of Kshs.10,937,000 cannot be confirmed as increase in trade and other payables figure of Kshs.89,680,000 differs with the calculated figure of Kshs.89,728,000 by Kshs.48,000, which has not been reconciled or explained. The cost of assets disposed of amounted to Kshs.744,000 but the same was not captured in other income.

Consequently, the accuracy of the statement of cash flows as presented and the balance of cash and cash equivalents cannot be confirmed.

## **Other Matter**

### **1. Grants from National Government**

In the report for the previous year, it was indicated that the statement of comprehensive income for the year ended 30 June 2017 reflected an amount of Kshs.244,000,000 in respect of grants from National Government. As disclosed in Note 3 to the financial statements, these were capital grants. It is still, however, not clear how the amount was to be expended as no supporting documents have been provided to date regarding the same.

Out of the amount, Kshs.100,000,000 was transferred to Agriculture and Food Authority (AFA). No documentary evidence has however been provided for audit verification to show how the balance of Kshs.144,000,000 was utilized.

It was also indicated that the Company received funds from Agriculture and Food Authority (AFA) amounting Kshs.50,000,000 during the same period. However, no records have provided to show how the two transactions were effected and recorded in the books of account of the two entities.

Consequently, the completeness and validity of the transactions involving receipt and expenditure of government grant totalling to Kshs.244,000,000 and the additional amount of Kshs.50,000,000 received from AFA still cannot be ascertained.

### **2. Legal Fees**

The statement of comprehensive income for the year ended 30 June 2017 reflected administration costs amounting to Kshs.208,438,000. The amount included legal fees and court awards totalling Kshs.20,094,000, out of which Kshs.18, 810,703 was paid to a legal firm for court case No. 16 of 2013 - Fredrick Ngori and 98 others against Pyrethrum Board of Kenya. The court awarded the plaintiffs Kshs.61,919,493. A review of documents, however, revealed an additional amount of Kshs. 13,702,361 was also paid to the plaintiff, and was described as interest. It is not clear why the interest on decretal amount was paid and the method used to compute the interest paid. No explanation has been provided as at 30 June 2018.

## **REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES**

### **Conclusion**

I do not express a conclusion on the lawfulness and effectiveness in the use of public resources as required by Article 229(6) of the Constitution. Because of the



significance of the matters described in the Basis for Disclaimer of Opinion, Other Matter and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources and sections of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit conclusion.

## **Basis for Conclusion**

### **1. Legal Status**

The Company uses three different names in its operations as indicated below:

- (i) Pyrethrum Processing Company of Kenya – Financial statements
- (ii) Pyrethrum Regulatory Authority – Bank statements
- (iii) Pyrethrum & Other Industrial Crops Company– Payment vouchers

According to paragraph 3 of the transition provisions of the Agriculture and Food Authority Act, 2013 (revised) under the first schedule-

- (i) The regulatory part of the defunct Pyrethrum Regulatory Authority would be Pyrethrum and Other Industrial Crops Directorate under AFA.
- (ii) The commercial function transforms into to a company to be registered under the Companies Act.

It is not clear how the management chose to operate under the name Pyrethrum Processing Company of Kenya (PPCK) which was registered in August 1963 instead of registering the company under the Companies Act as required under the new legislative framework.

The management of the Company has presented the financial statements for 2017/2018 under the name Pyrethrum Processing Company of Kenya (PPCK) without taking cognizance of the new legislative framework.

### **2. Company Operating Without a Substantive Board**

The Company has been operating without a substantive board of directors. As a result, the Company is in breach of Section 6(1) of the State Corporations Act.

### **3. Approval of the Company's Budget**

The Company's budget for the year 2017/2018 was not approved by the National Treasury or the parent Ministry. Consequently, the basis for collecting revenue and incurring expenditure cannot be confirmed.

### **4. Unexplained Budget Deficit and Unapproved Disbursement**

The statement of comparison of budget and actual amounts for the year ended 30 June 2018 reflects total budgeted income of Kshs.423,268,000 with a comparable total budgeted expenditure of Kshs.762,258,000 and a deficit of Kshs.338,990,000. No explanation has been provided for the fact that the Company had anticipated a budget deficit.

Further, examination of the same statement revealed that although the Pyrethrum Processing Company of Kenya had budgeted for receipts of Kshs. 90,000,000 from the Government, the Ministry went ahead and disbursed Kshs.99,000,000 to Company without the National Treasury's approval. This resulted to disbursement of unapproved amount of Kshs.9,000,000.

## **5. Operating Performance**

The statement of comprehensive income for the year ended 30 June 2018 reflects sales totalling Kshs. 43,885,000 (2017: Kshs.45,295,000), while the cost of sales was Kshs.146,210,000 (2017: Kshs.187,816,000) a situation that does not make any business sense. Management has not explained the reasons for such a situation.

## **6. Under Collection of Revenue**

The statement of comparison of budget and actual amounts for the year ended 30 June 2018 reflects an under collection of revenue by Kshs.263,862,000. This represents 62.34% of the gross estimates of Kshs.423,664,000. The under collection of revenue was attributed to failure to attain sales targets by Kshs.253,765,000 and other income by Kshs.19,097,000. However, no reasons were given by the Company for failure to achieve the set targets.

## **REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE**

### **Conclusion**

I do not express a conclusion on the effectiveness of internal controls, risk management and governance as required by Section 7(1) (a) of the Public Audit Act, 2015. Because of the significance of the matters described in the Basis for Disclaimer of Opinion, Other Matter and Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources and sections of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit 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 Financial Reporting Standards 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 of Pyrethrum Processing Company of Kenya 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 Company 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**

My responsibility is to conduct an audit of the financial statements in accordance with International Standards of Supreme Audit Institutions (ISSAIs) 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. However, because of the matters described in the Basis for Disclaimer of Opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

In addition, my responsibility is 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. I also consider internal control, risk management and governance processes and systems in order to give an

assurance on the effectiveness of internal controls, risk management and governance 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. However, because of the matters described in the Basis for Conclusions on Lawfulness and Effectiveness in Use of Public Resources, and Internal Controls, Risk Management and Governance sections of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit conclusion.

I am independent of Pyrethrum Processing Company of Kenya 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.



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

**Nairobi**

**11 April 2019**