

REPORT OF THE AUDITOR-GENERAL ON SCHOOL EQUIPMENT PRODUCTION UNIT FOR THE YEAR ENDED 30 JUNE, 2019

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of School Equipment Production Unit set out on pages 1 to 18, which comprise the statement of financial position as at 30 June, 2019, and the statement of profit or loss and other comprehensive income, statement of changes in equity, 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 School Equipment Production Unit 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 and comply with the Companies Act, 2015.

Basis for Qualified Opinion

1. Receivables and Prepayments

As previously reported and as disclosed in Note 16 to the financial statements, the statement of financial position reflects a balance of Kshs.84,054,800 under receivables and prepayments. The balance includes trade receivables totalling to Kshs.33,942,817, out of which an amount of Kshs.22,621,361 has been outstanding for more than ten (10) years. Supporting documents for the amount were not provided for audit review. Further, the balance of Kshs.84,054,800 includes staff advances of Kshs.982,040, out of which an amount of Kshs.829,984 was in respect of staff advances due from deceased employees and those who had since left the Unit. Recoverability is therefore, doubtful.

The Management explained that a fire broke out in the Unit's Headquarters in 2007 and destroyed supporting schedules relating to receivables hindering recovery of the debtors due to lack of evidence. Additional information indicated that the Management wrote to the parent Ministry in November, 2017 requesting for authority to write off the outstanding debts but lack of the relevant information and documentation has delayed the write off process.

In the circumstances, it has not been possible to confirm the validity, accuracy and full recoverability of the receivables and prepayments amount of Kshs.22,621,361.

2. Trade and Other Payables

As previously reported, the trade and other payables balance of Kshs.23,991,099 reflected in the statement of financial position includes trade payables of Kshs.8,239,115, out of which payables totalling to Kshs.7,209,565 has been outstanding for more than ten (10) years. Further, supporting documents for the payables totalling to Kshs.7,209,565 were not availed for audit review. The Management explained that the fire of 2007 in the Unit's Headquarters destroyed supporting schedules relating to the payables. The Management placed advertisements in the daily newspapers in November, 2016 requesting creditors to present documents supporting the services offered to the Unit but with little success. Further, the Management wrote to the Parent Ministry in November, 2019 for concurrence and approval by The National Treasury to write off the outstanding creditors. However, no such approval had been availed as at the date of this report.

In the circumstances, it has not been possible to confirm the validity and accuracy of the trade and other payables amount of Kshs.7,209,565.

3. Land

As disclosed in Note 14 to the financial statements, the property, plant and equipment balance of Kshs.93,350,238 reflected in the statement of financial position includes land at a cost of Kshs.63,000,000. The parcel of land identified as plot No. LR.209/14009 and measuring 5.1 hectares, is situated at Imara Daima Estate, Industrial Area and is registered under the Unit's name. Although the land was allocated to the Unit in 1996, the Unit has not been able to develop it due to subsequent invasion by informal settlers. Although Management has requested the National Land Commission to reclaim the land for development by evicting the informal settlers, progress made in this regard has not been disclosed.

In the circumstances, it has not been possible to ascertain the ownership status of the piece of land and to confirm that the property, plant and equipment balance of Kshs.93,350,238 is fairly stated.

4. Supply of School Equipment

As reported in the previous years, the Unit entered into a contract in the year 2006 with a local Company for the supply of various pieces of laboratory equipment, chemicals and teaching aids to 1,457 secondary schools across the Country, at a contract price of Kshs.226,772,450. According to records available, the Unit in 2008/2009 financial year received an amount of Kshs.261,326,532 from the Ministry of Education for the purpose. The Unit used direct procurement and made an advance payment of Kshs.75,086,880 to the supplier.

Additional information indicates that the Ethics and Anti-Corruption Commission (EACC) intercepted and four (4) officers of the Unit were arraigned in court for not following procurement procedures. The case was concluded on 28 August, 2013 and the supplier was directed to surrender Kshs.70,000,000 to The National Treasury and pay an additional balance of Kshs.5,086,880 plus undetermined interest as a fine. Documentary

evidence availed by Management confirmed that a refund of Kshs.70,000,000 was received by The National Treasury in 2013/2014 financial year leaving a balance of Kshs.5,086,880 and undetermined interest on the principal amount.

A review of the matter indicated that another judgement was entered in favour of the supplier on 7 December, 2017 for a sum of Kshs.150 million cost and interest. However, the Unit obtained stay of the judgement and orders pending hearing and determination of the intended appeal. However, there is no disclosure of the contingent liability in the financial statements.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the School Equipment Production Unit 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.

Emphasis of Matter

Financial Performance

The statement of financial performance reflects a loss of Kshs.18,840,675 (2018: Kshs.28,567,266) thereby reducing the retained earnings from Kshs.31,536,455 to Kshs.12,695,780. The loss-making trend of the Unit, if not reversed, may wipe out the accumulated reserves.

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. I have determined that there are no Key Audit Matters to communicate in my report

Other Matter

Budgetary Control and Performance

The statement of comparative budget and actual amounts reflects final receipts budget and actual on comparable basis of Kshs.93,000,000 and Kshs.73,692,327 respectively, resulting to an under-funding of Kshs.19,307,673 or 21% of the budget. Similarly, the Unit incurred an expenditure of Kshs.64,882,110 against an approved budget of Kshs.63,770,000 resulting in an over-expenditure of Kshs.1,112,110. The under-funding and over-expenditure affected the planned activities of the Unit and may have impacted negatively on service delivery to the public.

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.

Investment in Call Deposits

As disclosed in Note 18 to the financial statements, the statement of financial position reflects a balance of Kshs.22,231,649 representing investment in a call deposit at a local bank. This is contrary to The National Treasury Circular Ref. DMD 4/02 'H' (63) of 26 March, 2018 which directed all State Corporations and SAGAs to invest surplus funds in Treasury Bills and/or Treasury Bonds directly through Central Bank of Kenya without intermediaries.

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, I confirm that, nothing has come to my attention to cause me to believe that internal controls, risk management and governance were not effective.

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 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.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Kenya Companies Act, 2015, I report based on my audit, that:

- (i) 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;
- (ii) In my opinion, proper books of account have been kept by the Unit, so far as appears from my examination of those books; and,

(iii) The Unit's financial statements are in agreement with the books of account.

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 Unit's ability to continue as a going concern disclosing, as applicable, matters related to going concern and using the applicable basis of accounting unless Management is aware of intention to terminate the Unit 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.

Those charged with governance are responsible for overseeing the Unit'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 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 the Unit's 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 Unit's ability to continue as a going concern or to sustain its services. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence

obtained up to the date of my audit report. However, future events or conditions may cause the Unit to cease to continue as a going concern or to sustain its services.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Unit 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

05 July, 2021