

REPORT OF THE AUDITOR-GENERAL ON THE NATIONAL IRRIGATION BOARD (NIB) FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of the National Irrigation Board (NIB) set out on pages 1 to 21, which comprise the statement of financial position at 30 June 2017, and the statement of financial performance, statement of changes in equity, statement of cash flows and statement of comparative 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 the National Irrigation Board as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards (Accrual Basis) and do not fully comply with the Irrigation Act, Cap 347 of the Laws of Kenya.

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, I confirm that public money has been applied lawfully and in an effective way.

Basis for Qualified Opinion

1. Property, Plant and Equipment

1.1 Freehold Land

As previously reported, the property, plant and equipment balance of Kshs.5,210,433,820 as at 30 June 2017 excludes the value of trust land in seven (7) schemes equivalent to 75,509 Acres but in respect of which ownership documents have not been obtained. Further, the parcels of land have been omitted in the fixed asset register.

1.2 Unsupported Compensation for Land

As previously reported, the freehold land balance of Kshs.1,189,586,063 as at 30 June 2017 includes compensation payments for Thiba Dam, Lower Sio and Lower Kuja of Kshs.357,895,014, Kshs.10,922,017, Kshs.6,331,485 respectively for which no supporting documents have been provided on who was compensated, rate of compensation and acreage of land acquired.

In consequence, it has not been possible to confirm validity and legality of the total amount of Kshs.375,148,516 included in the financial statements as at 30 June 2017.

1.3 Buildings

Examination of the fixed assets register revealed that the balance reported under buildings of Kshs.78,304,130 as at 30 June 2017 included the cost of building materials amounting to Kshs.28,787,614. However, the building materials in question are not attributed to any specific building. Further, the asset register does not have a list of the Board's buildings.

In view of the foregoing, it has not been possible to confirm the accuracy, valuation and completeness of the property, plant and equipment balance of Kshs.5,210,433,820 as at 30 June 2017.

2.0 Cash and Cash Equivalents.

The statement of financial position reflects a cash and cash equivalents balance of Kshs.1,388,540,391 as at 30 June 2017. The following issues were noted:

2.1 Barclays Bank of Kenya-Queensway House(BBK826) Account No. 0945036826

The reconciliation statement for June 2017 includes payments in the bank but not recorded in the cash book amounting to Kshs.2,555,402. It was not possible to ascertain what the payments relate to and why they have not been recorded in the cashbook as required.

2.2. Barclays Bank of Kenya- Kisumu A/C No. 0091010127

Included in the reconciling items in the bank reconciliation statement as at 30 June 2017, is an amount of Kshs.415,787 described as historic uncredited receipts. The amounts were not analyzed and thus could not establish what they relate to and for how long they have been outstanding. Also included in the reconciling items is an amount of Kshs.44,076 described as a cash book overcast which is not dated. No explanation was offered as to what it relates to.

Under the circumstances, it has not been possible to confirm the accuracy and completeness of the cash and cash equivalents balance of Kshs.1,388,540,391 as at 30 June 2017.

3.0 Receivables from Exchange Transactions

3.1 Long Outstanding Debts

Included in the receivables from exchange transactions (Note 15) balance of Kshs624,814,720, is Kshs.501,257,096 (2016: Kshs.518,364,597) or 80% provision for bad debts. However, the trade debtors, farmers and other debtors were all historical figures carried forward for unknown number of years. No reason has been given for the huge provision of 80% of receivables.

3.2. Suspense Account-Sundry Debtors

Also included in the other debtors' balance of Kshs.230,882,623 is an amount of Kshs.34,280,229 which does not relate to any specific debtor but instead classified as other trade debtors (Kshs.11,098,612), sundry debtors (Kshs.23,142,118) and other debtor

(Kshs.39,500) which has been outstanding but the Board has not reconciled or explained the suspense amount.

3.2.1.0 Inter Company Transactions

3.2.1.1 Mwea Rice Mills Ltd

Included in other debtor's balance of Kshs.230,882,623 as at 30 June 2017, is a balance of Kshs.67,737,278 being balance owing from Mwea Rice Mills Limited. In the books of Mwea Rice Mills Limited the same balance is reflected as Kshs.40,410,431 resulting in an unexplained difference of Kshs.27,326,847.

3.2.1.2 Western Kenya Rice Mills Ltd

Similarly, included in the debtors' balance is an amount of Kshs.73,457,601 being a balance due from Western Kenya rice Mills Ltd. In the books of the company, the same balance is given as Kshs.26,426,152 resulting in an unexplained and unreconciled balance of Kshs.47,031,449. In view of the foregoing, it has not been possible to confirm the accuracy and recoverability of the receivables from exchange transactions balance of Kshs.123,557,624 as at 30 June 2017.

4. Current Liabilities

4.1 Outstanding Kenya Revenue Authority Dues

As previously reported, included in the payables from exchange transactions balance of Kshs.3,560,750,127 as at 30 June 2017 is a balance of Kshs.973,391,569.29 due to Kenya Revenue Authority which has been outstanding over a long period. This amount has risen considerably by 36% as compared to the previous year amount of Kshs.623,242,634. Further, interest and penalties on the outstanding balance have not been recognized in the Board's books of account thus understating the balance reported by accrued interest/levies which Kenya Revenue Authority may impose.

Management has not explained how it intends to settle the balance.

4.2 Long Outstanding Trade Payables

Included in current liabilities-payables from exchange transactions balance of Kshs.3,560,750,127 as at 30 June 2017 is an amount totaling Kshs.407,257,813 due to various contractors, consultants and other trade payables which has remained outstanding for more than one year without supporting documents. The audit could not establish why the Board has not prioritized the settlement of those outstanding amount and the criteria it uses to settle debts.

Consequently, the accuracy and completeness of the trade payables account balance of Kshs.407,257,813 could not be ascertained as at 30 June 2017.

4.3 Retention Money

Included in the balance for current liabilities trade payables is an amount of Kshs.392,448,788 referred to as retention money. However, the analysis provided for the retention account and reconciliation statement of the account which is held at Co-operative Bank Account No.01136128012902 as at June 2017, both reflects a balance of Kshs.109,528,989 resulting in an unexplained and unreconciled difference of Kshs.282,919,799.

4.4 Water Resources Management Authority (WARMA)

Included in the statement of financial position is payables from exchange transactions balance of Kshs.3,560,750,127 as at 30 June 2017 comprising of various outstanding balances. Included in trade payables amount is Kshs.20,981,308 indicated as owing to Water Resources Management Authority. However, upon verification from WARMA books, the amount indicated as receivable from the Board is Kshs.26,820,104 resulting in an unexplained variance of Kshs.5,838,796.

In view of the foregoing, it has not been possible to confirm the accuracy, completeness and validity of the Current liabilities (payables from exchange transactions) of Kshs.3,560,750,127 as at 30 June 2017.

5. Under-utilization of leased land at Galana Kulalu Food Security Project

During the year under review the Board spent Kshs.1,597,068,997 on Galana Kulalu Food Security Project. However, an examination of information and documents availed indicated that the model farm is covering 10,000 acres out of the 20,000 acres leased. The remaining 10,000 acres are idle and will remain idle since they were not included in the model farm programme. Management did not explain as to why they leased 20,000 acres of land when they required only 10,000 acres.

The Board from the inception of the Project has paid Kshs.150, 000,000 as analyzed below:

Financial Year	Amount(Kshs)
2013-2014	50,000,000
2014-2015	70,000,000
2015-2016	30,000,000
<u>TOTAL</u>	<u>150,000,000</u>

In consequence, it has not been possible to establish why the Board leased 20,000 acres and only utilized 10,000 acres but making lease payments for 20,000 acres resulting to an apparent loss of Kshs.75,000,000 as at 30 June 2017.

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

Emphasis of Matter

1. Construction works of Rahole Canal Phase (ii) Irrigation Scheme Development Project (NIB/T/160/2012-2013), Kshs.300,356,375

- **Deferment of works to defects liability period**

The defects liability period for the above phase was for the period starting from 30 January 2015 to 30 January 2016.

Substantial completion certificate of phase II was issued of Kshs.25,879,739. The remaining items which include the following were to be done during the defects liability period;

SNAG LIST

S/NO.	BILL NO.	DESCRIPTION	AMOUNT (Kshs.)
1	1(1.3)	Purchase and supply of office furniture	500,000
2	1(1.5)	Allowance for supervision of works	1,519,494
3	1(1.9)	Allow for farmers sensitization	5,000,000
4	2(2.4)	Rock blasting	3,248,000
5	4(4.2.5)	Construction of riprap	4,517,240
6	4(4.2.8)	Installation of gabion protection	32,961,750
7	4(4.2.9)	Fabricate and fix screen for gully crossing	50,000
TOTAL			47,796,484

The audit could not establish if the contractor would be in a position to finish the above outstanding works as at end of the defects liability period although a payment of Kshs.32,017,134 was made to the contractor in the year under review.

As a result, it has not been possible to establish the accuracy and value for money for the payment of Kshs.32,017,134 as at 30 June 2017.

2. Bura irrigation settlement scheme rehabilitation project (NIB/T/046/2010-2011), Kshs. 7,355,829,104

i. Failure to carryout geotechnical investigation

It was highlighted that soil strata differed from that of the tender and the contractor met with hard soils/ soft rock in the new gravity canal works, which had reduced the productivity per working set of equipment's deployed. The audit could not establish why investigation was not carried out in the new gravity canal works section.

ii. Delay in completion of the project

As reported previously, the company was awarded the project despite its bad past record. As at 30th June 2017, two years after the expected completion date, the project is still lagging

behind.

iii. Pricing risk

The contractor was executing works at quoted rates which were worked out on the baseline pricing of 2011. This therefore exposing the project to possible escalation on the cost of non-specified materials as some of them the cost might have already shot up.

Key Audit Matters

Key audit matters are those matters that, in my professional judgement, are considered of significance in the audit of the financial statements. Except for the matters described in the Basis for Qualified Opinion, Emphasis of Matter and Other Matter sections of my report, I have determined that there are no other Key Audit Matters to communicate in my report.

Other Matter

1. Bank Loan for Galana Kulalu Food Security Project

As previously reported, the Board took a bank loan of US \$ 71,408,014 (Kshs.7,283,617,428) from the Bank of Leumi Isreal for the construction works for 10,000 acres' model farm for the Galana Kulalu Food Security Project. However, most of the loan terms are not to the best interest of the Kenyan tax payers. The loan interest will be determined from time to time by the bank depending on the prevailing economic conditions (Clause 6). The borrower will pay any additional costs the bank will incur while mobilizing the funds for loan disbursement (Clause 7). The Board confirms the Bank's books and account entries in relation to this loan to be correct and binding to the Board (Clause 24). The borrower will not be entitled to contest any payment made by the Bank and may not justify its failure to fulfil its payment obligation in accordance with the terms and conditions of the agreement. Therefore, the conditions, of this loan are in favor of the Bank and not the Board. Also the repayment of the loan principal and interest are not clearly defined in the loan agreement.

In the circumstances, the National Irrigation Board and the Government of Kenya risks paying more than expected in the absence of clearly spelt out borrowing terms.

2. Delay in completion of the following projects

2.1 Galana/Kulalu Food Security Project Kshs.14,545,106,963

Examination of files correspondences and contract documents revealed the following anomalies;

- The project contract was signed was signed on 20 August, 2014 between the Board and Green Arava Limited and the site handed over on 11 September,2014 as is indicated in a Memo reference GM/G/548 dated 3 February,2015 which means therefore that the

project had at the time of audit taken forty-four months (44) had not been handed over to client. fourteen (14) months down the line.

- The General Manager vide his letter to the Cabinet Secretary Ref: NIB/HQ/G1/51(107) dated 19 December,2017 enumerated various issues which brought about the delay and heavily impacting on the Board and the Government. The General Manager pointed out four (4) aspects which have consequently brought about the delay viz avis;
 - i. weakness of the contract
 - ii. weakness of the contractor
 - iii. challenges faced by the employer
 - iv. time analysis

The letter by the General Manager revealed the procurement process of the project was flawed and was poorly planned.

Under the weakness of the contract the following anomalies were sighted;

- i. The financing agreement is tied to the Contractor and therefore all proceeds of the loan due to the contract can only be channeled through the Contractor. This gives the Contractor an upper hand and leaves the Employer at the mercy of the Contractor,
- ii. Single sourcing of the contractor. This favoured the contractor against competitive bidding, pricing, capacity and competence,
- iii. The Contract provides for advance payment under Operation and Maintenance bill e.g. payment for experts under operation and maintenance which may lead to underperformance,
- iv. The Contract provides for payment for items on account of Bill of Lading before installation. This may lead to delay to implementation,
- v. Exclusion of operation and maintenance bill out of the performance bond for exposing the Employer to under security,
- vi. Conflict of interest as the designing firm is associated with the implementing firm (Contractor) leading to poor designs requiring frequent reviews and interpretations,
- vii. The production component of the contract was pegged on area without emphasizing on production output targets which has sometimes led to underperformance.

Further, the letter highlighted the weaknesses on the part of the contractor are as enumerated below;

- i) Low Capacity to implement the contract as per the work programme resulting to the contract works being behind schedule,

- ii) Failure to avail key personnel to man various sections as per the contract requirements,
- iii) Failure to comply with instructions within reasonable time issued contractually for the works thus leading to disputes on payment, especially, on lump sum items. So far 70 instructions have been issued with unsatisfactory compliance.

In contract document between the Board and Green Arava it was noted that a very key ingredient of such technologically advanced project there was no mention of transfer of knowledge of manning the infrastructure installed after the contractor exits the site.

2.2 Kalundu Kitui clusters Irrigation Scheme Development Project, Phase II, Kitui County

Examination of documents in regard to Kitui Clusters Irrigation Project, Phase II revealed the following observations/findings;

The contract No. NIB/T/106/2013-2014 awarded to Aventure Ltd at an amount of Kshs.16,982,900 and notification for the award dated 18 December,2014 was to take twelve (12) months that is from 1 March,2015 to 1 March, 2016. However, the contract was signed on 10 February, 2015 and the Board modified the completion date from 1 March, 2016 to 30 September,2016.The contractor Aventure Ltd was to take twelve (12) months but has taken over thirty six (36) months without the project being completed.

A default notification letter dated 30 June, 2017 was written by the Deputy General Manager(ES) Ref: NIB/HQ/K1/74A (33) bringing to the attention of the Contractor on the

following issues; On failure to secure an extension of the contract period which ended on 30 September 2016; Failure to extend the performance bond which is not valid since 26 July,2015; Failure to resume work on site despite numerous reminders by the Resident Engineer.

The delay by the contractor to complete the projected slated to take one year but delayed for another two years puts into question the competence of the contractor

In consequence, the Board has not achieved its operational and strategic objectives for the year under review.

3. Budgetary Controls Over-Expenditure

Audit examination of the budget verses actual revealed that the Board in the year under review had overshoot her budget for repairs and maintenance by Kshs.21,967,163. No reason has been provided for failure to spend within the approved budget nor formalizing the over expenditure through supplementary budget as required.

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 Public Sector Accounting Standards (Accrual Basis) 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 to sustain its 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 Board 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 Board'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 of Kenya. 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.

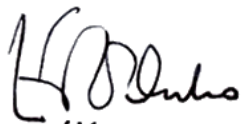
As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- 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 Board'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 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 Board'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 Board to cease to continue as a going concern or 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 Board 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 the 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

28 September 2018