REPORT OF THE AUDITOR-GENERAL ON COUNTY ASSEMBLY OF NAIROBI CITY FOR THE YEAR ENDED 30 JUNE, 2020

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of County Assembly of Nairobi City set out on pages 8 to 32, which comprise the statement of financial assets and liabilities as at 30 June, 2020 and the statement of receipts and payments, statement of cash flows, statement of comparison of budget and actual amounts and 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 audit.

In my opinion, because of the significance of the matters discussed in the Basis for Adverse Opinion section of my report, the financial statements do not present fairly, the financial position of the County Assembly of Nairobi City as at 30 June, 2020, and of its financial performance and its cash flows for the year then ended in accordance with International Public Sector Accounting Standards (Cash Basis) and do not comply with the Public Finance Management Act, 2012 and the County Governments Act, 2012.

Basis for Adverse Opinion

1.0 Presentation of Financial Statements

The financial statements contain the following errors and discrepancies:

(i) The statement of financial assets and liabilities incorrectly reflects Notes 13, Note 14 and Note 15 as providing further disclosures on Accounts Receivables - Outstanding imprests, Accounts Payables – Deposits and Retentions, and Fund Balance brought forward respectively. However, the actual disclosures on these accounts are denoted in the Notes to the financial statements as Notes 14, 15 and 16 respectively.

(ii) Note 17 on prior year adjustments is incorrectly reflected as Note 16 in the statement of financial assets and liabilities.

(iii) The cover page refers the financial statements as “amended” but the designation is not recognized in the reporting format prescribed by the Public Sector Accounting Standards Board or the in IPSAS.

In view of these issues, the financial statements do not conform to IPSAS and the presentation format prescribed by the Public Sector Accounting Standard Board (PSASB).

2.0 Unconfirmed Balances

Review of the financial statements revealed the following inaccuracies:

2.0.1 Compensation of Employees

The statement of receipts and payments reflects payments on compensation of employees totalling Kshs.623,426,791. The balance contains the following anomalies:

2.0.1.1 Unreconciled Variance

Whereas statement of receipts and payments reflects Kshs.623,426,791 in respect to compensation of employees, Note 4 to the financial statements reflects Kshs.684,054,221 on the account resulting to a variance of Kshs.60,627,430 which was not explained.

2.0.1.2 Allowances to Members of County Assembly

The compensation of employees expenditure totalling Kshs.623,426,791 reflected in the statement of receipts and payments includes personal allowances totalling Kshs.226,709,669 paid as part of salary.

Audit examination of records on the payments indicated that Kshs.75,761,400 was paid as sitting allowances to Members of the County Assembly (MCAs) during the year under review. However, attendance reports, including biometric data on the MCAs, and the dates the respective Committee meetings were held, were not provided for audit review.

As a result, the propriety of payments totalling Kshs.75,761,400 could not be confirmed.

2.0.2 Use of Goods and Services

The statement of receipts and payments reflects payments on use of goods and services totalling Kshs.470,626,447, as further reflected in Note 4 to the financial statements. However, examination of records on the expenditure disclosed the following unconfirmed balances:

2.0.2.1 Miscellaneous Payments

Payments for various items totalling Kshs.72,146,593 were not supported with relevant documents contrary to Regulation 104(1) of the Public Finance Management (County Governments) Regulations, 2015.

As a result, the accuracy, completeness and validity of the payments could not be confirmed.

2.0.2.2 Legal Fees

Included in use of goods and services balance totalling Kshs.470,626,447 is Kshs.44,987,494 paid to various legal firms in respect of legal fees. However, records indicating how the firms were identified and the respective service agreements signed with them, if any, were not provided for audit. Further, the proceedings or outcomes of the court cases or affairs that the firms provided legal services in were not provided for audit verification.

As a result, the occurrence, propriety and value for money on the expenditure totalling Kshs.44,987,494 could not be confirmed.

2.0.2.3 Foreign Travel and Subsistence Allowances

Records provided for audit indicated that the County Assembly spent Kshs.97,802,709 on foreign travel and subsistence in the year under review. However, payment vouchers for the expenditure were not supported with travel documents to confirm the occurrence and validity of the expenditure.

As a result, the occurrence, accuracy and propriety of the payments totalling Kshs.97,802,709 could not be confirmed.

2.0.3.0 Outstanding Imprests

The statement of financial assets and liabilities reflects Kshs.128,072,586 in respect of accounts receivables – outstanding imprests whereas Note 14 to the financial statements reflects accounts receivables totalling Kshs.129,809,586 resulting to an unreconciled variance of Kshs.1,737,000.

Further, an analysis of imprests balance showing the names of the imprest holders, issue and due dates for the imprests, amounts surrendered and balances as at 30 June, 2020 was not provided for audit verification.

Consequently, the accuracy, completeness and validity of the outstanding imprests balance totalling Kshs.128,072,586 as at 30 June, 2020 could not be confirmed.

2.0.4.0 Fixed Assets

Annex 4 to the financial statements reflects a summary of fixed assets register that depicts assets with historical values totalling Kshs.21,873,599 as at 30 June, 2019. However, information on asset additions, disposals and transfers in the year under review was not disclosed. In addition, Management did not maintain an updated asset register contrary to Section 149(2) of the Public Finance Management Act, 2012.

In view of these omissions, the existence, location, and accuracy of the assets balance totalling Kshs.21,873,599 as at 30 June, 2020 could not be confirmed.

2.0.5.0 Pending Bills

Note 1 of other important disclosures reflects pending accounts payables (pending bills) totalling Kshs.8,941,436 as at 30 June, 2020 whereas Annex 1 reflects a nil balance in respect to the account resulting to an unreconciled variance of Kshs.8,941,436.

Further, the pending bills balance was not supported by source documents and supporting schedules indicating the nature of the payables and payments made thereof if any, and the outstanding balance as at 30 June, 2020. Further, analyses showing the ages of the payables was not provided for audit.

In view of these discrepancies the accuracy and propriety of the accounts payables totalling Kshs.8,941,436 as at 30 June, 2020 could not be confirmed.

Delays in settling pending bills may slow down economic activity and discourage traders and other private parties from doing business with public entities.

2.0.6.0 Prior Year Grants

The statement of receipts and payments reflects prior year other grants and transfers totalling Kshs.1,558,992 whereas Note 8 to the financial statements, that seeks to explain the balance, reflects a nil balance resulting to an unreconciled variance of Kshs.1,558,992. As a result, the accuracy and fair presentation of the prior years grant balance totalling Kshs.1,558,992 could not be confirmed.

2.0.7.0 Budgeted Receipts Payments

The statement of comparison of budget and actual amounts: recurrent and development combined reflects an original budget of Kshs.5,500,000 on Other Grants and Transfers, whereas the final budget reflects a nil balance resulting to an unexplained difference of Kshs.5,500,000 between the two records.

The statement further reflects final budgeted payments totalling Kshs.1,473,673,965 but a recast of the balances included therein yields Kshs.1,393,462,525 resulting to an unreconciled variance of Kshs.80,211,440.

In view of these discrepancies, the accuracy of the statement of comparison of budget and actual amounts: recurrent and development is doubtful.

2.0.8.0 Prior Year Adjustment

Note 17 to the financial statements reflects prior year adjustments totalling Kshs.118,980,141, which Management attributed to adjustments of bank account balances and receivables erroneously included in previous audited financial statements.

However, the adjustments were effected against balances for the year under review contrary to International Public Sector Accounting Standard No.3. The Standard requires every material error for prior periods be corrected retrospectively in the first set of financial statements authorized for issue upon its discovery by restating the comparative amounts for the prior period in which the error occurred. The adjustment has, similarly, been made in error in the statement of cash flows.
Therefore, the financial statements are not fairly stated.

2.0.9.0 Total Payments

The statement of receipts and payments reflects payments totalling Kshs.1,154,646,327 whereas the Integrated Financial Management System (IFMIS) ledger reflects payments totalling Kshs.375,542,403 for the year under review resulting to an unexplained variance of Kshs.779,103,924.

As a result, the accuracy of the financial statements is doubtful.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of County Assembly of Nairobi City 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 adverse 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. I have determined that there are no key audit matters to report in the year under review.

Other Matter

Budgetary Control and Performance

The approved budget of the County Assembly for the year under review totalled Kshs.1,473,673,965 comprised of recurrent and development estimates totalling Kshs.1,343,262,525 and Kshs.44,700,000 respectively. Actual expenditure totalled Kshs.1,154,646,327 as indicated in the summary statement of appropriation recurrent and development combined . This was, equivalent to an absorption rate of 83%.

The failure to absorb Kshs.238,816,198 or 17% of the budget may have constrained delivery of the legislative and oversight mandate of the County Assembly.

In addition, revenue records indicated that the County Assembly received exchequer releases for the year under review totalling Kshs.311,831,896 between the months of June, 2020 and July, 2020 . The receipts were for the recurrent vote. Delay in receipt of the exchequer releases may, to a large extent, explain the expenditure shortfall recorded in the year under review .

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, because of the significance of the matters discussed in the Basis for Adverse opinion and Basis for Conclusion on Lawfulness and Effectiveness in Use of public Resources sections of my report, I confirm that that public resources have not been applied lawfully and in an effective way.

Basis for Conclusion

1.0 Irregularities in Compensation of Employees

Examination of records on compensation of employees disclosed the following irregularities:

1.0.1 High Wage Bill

The statement of receipts and payments reflects expenditure totalling Kshs.623,426,791 on compensation of employees, which is 48% of the County Assembly`s total revenue amounting to Kshs.1,303,785,480 for the year ended 30 June, 2020. The expenditure on wages and benefits therefore exceeded the thirty-five percent (35%) threshold prescribed under Regulation 25(1)(b) of the Public Finance Management (County Governments) Regulations, 2015.

In the circumstances, the Management was in breach of the law. In addition, excessive use of limited resources in payment of personnel emoluments may have constrained the capacity of the County Assembly to fund its legislative and oversight operations and development projects.

1.0.2 Excessive Deductions on Staff Pay

In the year under review, forty (40) employees were paid net salaries that were less than a third (1/3) of their respective basic pay. Nineteen (19) of the officers were members of staff whereas twenty-one (21) were Members of County Assembly (MCAs). In allowing the excessive deductions, Management contravened provisions of the Nairobi City County Assembly Human Resource Manuals and Section 19(3) of the Employment Act, 2007 both of which prohibit employers from making deductions in excess of two thirds of their employees' wages.

In the circumstances, the Management breached the law and also exposed the Officers to the risk of pecuniary embarrassment.

1.0.3 Payments to Staff by County Executive of Nairobi

As similarly reported in the previous year, examination of expenditure documents for the year under review revealed payments totalling Kshs.142,857,111 made to the staff of the County Assembly by Management of the County Executive of Nairobi City for undisclosed duties. The authority if any, granted for the payments was not provided for audit review and as a result, the validity and propriety of the expenditure could not be confirmed.

2.0 Irregular Payments for Use of Goods and Services

Examination of records on use of goods and services disclosed the following irregular expenditures:

2.0.1 Domestic and Subsistence Allowances

Examination of imprest records indicated that the County Assembly made payments totalling Kshs.2,963,807 to various members of staff in the year under review. The payments were for refunds of costs the staff had reportedly incurred on domestic travel and subsistence while on official duty away from the County Assembly. However, the refunds were made contrary to the provisions of Regulations 91(2) and 93(4) of the County Government Regulations, 2015 which requires such expenditures to be incurred through imprests issued to Officers beforehand.

No explanation was provided by Management on why the staff were not issued with imprests before they embarked on the said duties.

2.0.2 Payment to County Assembly Forum

Expenditure records indicated that Management paid a voluntary contribution of Kshs.5,000,000 to the County Assemblies Forum in the year under review. However, the Forum is not recognized in law as deserving to receive grants drawn from public funds.

In the circumstance, the payment was irregular.

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements, 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, because of the significance matters described in the Basis for Adverse Opinion and Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance sections of my report, I confirm that, internal controls, risk management and overall governance were not effective.

Basis for Conclusion

Unapproved Risk Management Policy

Review of risk management in the County Assembly indicated that Management was yet to approve the draft risk management policy for the County Assembly. Failure to establish a risk management policy contravened Regulation 158(1) of the Public Finance Management (County Governments) Regulations, 2015. Further, in the absence of the policy, Management lacked objective means to identify, measure and mitigate risks that the County Assembly may face.

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.

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 Public Sector Accounting Standards (Cash Basis) 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 County Assembly'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 Management is aware of the intention to dissolve the County Assembly.

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 following 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

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 County Assembly's policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional scepticism 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 Management's use of the applicable 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 County Assembly's ability to continue to sustain its services. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the County Assembly to cease to continue to sustain its services.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the County Assembly 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 communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.

CPA Nancy Gathungu, CBS
<u>AUDITOR-GENERAL</u>

Nairobi

24 December, 2021