

# **REPORT OF THE AUDITOR-GENERAL ON NATIONAL CEREALS AND PRODUCE BOARD FOR THE YEAR ENDED 30 JUNE, 2019**

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## **REPORT ON THE FINANCIAL STATEMENTS**

### **Adverse of Opinion**

I have audited the accompanying financial statements of National Cereals and Produce Board set out on pages 25 to 45, 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 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, 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 National Cereals and Produce Board 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 (Accrual Basis) and do not comply with the Public Finance Management Act, 2012 and the National Cereals and Produce Board Act, 1985.

### **Basis for Adverse Opinion**

#### **1.0 Unreconciled Bank and Cash Balances**

The statement of financial position and as disclosed in Note 16 to the financial statements reflects bank and cash balances of Kshs.4,070,766,150 as at 30 June, 2019. However, the following anomalies were observed: -

- i. The bank balance of Kshs.4,037,872,639 differed with the cash book balance of Kshs.4,043,226,937 resulting in an unexplained and unreconciled variance of Kshs.5,354,293.
- ii. Included in cash in hand balance of Kshs.1,339,310 was Mpesa account balances of Kshs.67,380.29 that were not supported with Safaricom statements of account.
- iii. The bank reconciliation statements included stale cheques amounting to Kshs.294,025 as well as receipts in bank statements but not in cash book amounting to Kshs.4,582,794.

Consequently, the accuracy and completeness of the bank and cash balances of Kshs.4,070,766,150 could not be confirmed.

## **2.0 Unreconciled and Unsupported Bank Overdraft**

The statement of financial position reflects bank overdraft balance of Kshs.544,116,930 as at 30 June, 2019. However, this figure differed with cash book balance of Kshs.551,226,455 resulting in an unexplained and unreconciled variance of Kshs.7,109,525. Further, the bank overdraft of Kshs.544,116,930 was not supported by a bank reconciliation statement and bank confirmation certificate.

Consequently, the accuracy, completeness and fair statement of the overdraft balance of Kshs.544,116,930 as at 30 June, 2019 could not be confirmed.

## **3.0 Inaccuracies in Property, Plant and Equipment**

The statement of financial position and as disclosed in Note 10 to the financial statements reflects property plant and equipment balance of Kshs.6,041,210,862 as at 30 June, 2019. However, the following inaccuracies were noted: -

- i. The property, plant and equipment figure includes an amount of Kshs.8,540,920 relating to capitalized VAT contrary to Paragraph 16(a) of the International Accounting Standard (IAS) No.16. The standard requires that the cost of an item of property, plant and equipment comprises its purchase prices, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates. The 16% VAT charged on the assets is a refundable purchase tax as the Board is VAT registered.
- ii. Included in the property, plant and equipment figure are thirty-five parcels of land valued at Kshs.1,285,079,450 that do not have title deeds. In addition, there are fifty-five donor funded storage facilities whose ownership has not been clarified.
- iii. The work in progress opening balance of Kshs.51,414,759 includes an amount of Kshs.16,978,655 that relate to projects that had been completed and certificates issued.
- iv. Included in the work in progress figure of Kshs.36,618,713 are additions of Kshs.4,807,072 whose supporting documents were not provided for audit.

Consequently, the accuracy, completeness and ownership of the property, plant and equipment balance of Kshs.6,041,210,862 as at 30 June, 2019 could not be confirmed.

## **4.0 Inaccuracies in Inventory Records**

The statement of financial position reflects inventories balance of Kshs.402,684,031 as at 30 June 2019. However, the following issues were noted: -

- i. A comparison between balance reflected in the financial statements, the stock take report and the Navision system report revealed unexplained and unreconciled discrepancies.
- ii. There was no stock reconciliation to separate the government stocks from the Board's stocks.

- iii. Maize valued at Kshs.342,482,895 stored at the Board's depot was reported to contain high levels of aflatoxin by the Ministry of Health. This was declared to be unfit for human consumption. Management did not provide write down of the stocks to recognize the losses made during the year under review as prescribed in IAS 2.
- iv. Records maintained by the Strategic Grain Reserve Fund indicated stocks balance of 3,913,098 bags of maize as at 30 June, 2018 whereas the Board's store records reflected 6,521,481. The discrepancy of 82,608,383 bags has not been reconciled.

Consequently, the accuracy and completeness of the stock balances of Kshs.402,684,031 as at 30 June, 2019 could not be confirmed.

## **5.0 Inaccuracies in Trade Debtors and Pre-payments**

The statement of financial position and as disclosed in Note13 reflects trade debtors and pre-payment balance of Kshs.590,846,770 as at 30 June, 2019. However, the following inaccuracies were noted: -

- i. Note 4(f) on summary of significant accounting policies states that, provision for bad and doubtful debts is made on the basis of specific debtors and consists of 100% specific provision for some debtors and a general provision of 7.5% on all outstanding trade debts at the balance sheet date. However, examination of available information and Note 13 to the financial statements does not show that a general provision of 7.5% was made on all outstanding debts as at 30 June, 2019.
- ii. Note 13 to the financial statements reflects trade and other receivables gross figure of Kshs.1,582,311,179 before provisions for bad and doubtful debts. Included in this figure is Kshs.214,927,885 relating to sundry debtors and prepayments. However, the general ledger reflected Kshs.217,397,346 resulting in an unexplained and unreconciled variance of Kshs.2,469,461. Further, out of the total sundry debtors, an amount of Kshs.71,264,041 has been outstanding for more than seven years.
- iii. Included in this trade debtors and other receivables is Kshs.1,211,612,815 in respect to trade debtors. It was noted that a total of Kshs.750,033,616 or 61.9% of trade debtors that have been outstanding for more than seven years. Although a cumulative bad debts provision of Kshs.991,464,409 has been made in the financial statements, recoverability of the amount is in doubt.

Consequently, the accuracy, completeness and recoverability of the trade debtors and pre-payment could not be confirmed.

## **6.0 Unsupported Government Debtors - New Agency Account**

The statement of financial position and as disclosed in Note 14 to the financial statements reflects Government Debtors-New Agency Account balance of Kshs.9,275,250,160. It was noted that the debtors decreased by Kshs.1,846,439,800 from Kshs.11,121,689,843 reported in the previous financial year. However, management did not provide documents to support the reduction.

## **7.0 Unsupported Government Debtors - Ministry of Agriculture (MOA) Fertilizer Account**

The statement of financial position and as disclosed in Note 15 to the financial statements reflects Government Debtors - MOA Fertilizer Account balance of Kshs.7,593,776,111. Included in the balance is brought forward figures of Kshs.342,341,936 and Kshs.191,916,638 relating to Strategic Grain Reserve Programme - Old Account, and GOK 17 selected depots for Famine Relief respectively which have remained unpaid for over 17 years. It has not been possible to confirm whether the Board will be able to recover the amounts, Management did not make provisions for bad and doubtful debts.

Consequently, the accuracy and completeness of Kshs.7,593,776,111 in respect to Government Debtors-MOA Fertilizer A/c as at 30 June, 2019 could not be ascertained.

## **8.0 Unsupported Creditors-Due to GOK on Past Market Interventions**

The statement of financial position and as disclosed in Note 24 to the financial statements reflects a balance of Kshs.174,063,028 relating to creditors - due to GOK past market intervention. This balance relates to retained surplus from 1994/1995 maize intervention and subsequent maize export transaction in 1995/1996 and 1996/1997 retained to offset against other GOK debts which are still under review. However, Management did not provide supporting evidence in support of this amount.

In the circumstances, the accuracy and fair statement of the Government Market Interventions Account balance of Kshs.174,063,026 as at 30 June, 2019 could not be confirmed.

## **9.0 Unsupported Government Agency Programme (Old Account)**

The statement of financial position and as disclosed in Note 25 to the financial statements reflects a balance of Kshs.143,195,039 in respect to Government Agency Account – Operating Results (Old Account). This balance relates to amounts held on behalf of the Government from cereal sales by the Board prior to the liberalization of cereals in 1993. However, Management did not provide documentary evidence for audit in support of the balance and reason why the Board has not remitted this amount to the Government since 1993.

In the circumstances, the accuracy and completeness of the Government Agency-Old Account balance of Kshs.143,195,039 as at 30 June, 2019 could not be confirmed.

## **10.0 Undisclosed Value Added Tax Arrears**

The statement of financial position reflects total current liabilities balance of Kshs.19,653,832,902 as at 30 June, 2019. Included in this figure is an amount of Kshs.964,765,588 in respect of Value Added Tax arrears payable to Kenya Revenue Authority on agencies services to government. This figure includes Kshs.464,430,643.61 tax arrears that have remained outstanding since 2002. Further, the long-term taxation account does not include withheld VAT that may have accrued in the last three years. Although the tax arrears continue to attract penalties and interest, the same have not been assessed and incorporated in these financial statements.

Consequently, the accuracy and completeness of the total current liabilities of Kshs.19,653,832,902 cannot be confirmed.

## **11.0 Unsupported Cost of Sales**

The statement of profit and loss and other comprehensive income and as disclosed in Note 2 to the financial statement reflects Kshs.1,885,230,200 in respect to cost of sales. Included in this figure are purchases of Kshs.629,997,952. Review of the purchases revealed that a total of Kshs.496,089,500 was incurred on procurement of 10,000 metric tonnes (MT) of Government fertilizer under the assignment contract. However, the assignment contract details indicated that the cost of the fertilizer was Kshs.427,980,000 resulting in an unexplained and unreconciled variance of Kshs.68,109,500 as shown below:

	<b>Unit Price Per Mt (Kshs.)</b>	<b>Order Per Mt</b>	<b>Quantity ordered Bags</b>	<b>Cost (Kshs.)</b>
NPK 17:17:17	48,268.50	5,000	100,000	241,342,500
CAN 26%	37,327.50	5,000	100,000	186,637,500
<b>Total</b>		<b>10,000</b>	<b>200,000</b>	<b>427,980,000</b>

Consequently, the accuracy of the cost of sales amount of Kshs.1,885,230,200 as at 30 June, 2019 could not be confirmed.

## **12.0 Disclosure of Contingent Liability**

As previously reported, the Board entered into a fixed sum contract of Kshs.730,968,000 on 26 November, 2004 for the supply of 40,000 Metric Tons (MT) of white maize at US Dollars 229 per MT which was not executed. The supplier sought for arbitration with the Kenya Chapter Institute of Chartered Arbitrators and in July, 2009 was awarded US\$ 3,106,000 for breach of contract. On appeal by the Board, the award was increased to US\$ 6,140,859 being equivalent to Kshs.552,677,382 of which the amount of Kshs.264,864,285 has since been settled through bank attachments. The case is in court

awaiting its hearing and determination. Management has not disclosed the contingent liability relating to this matter.

Consequently, the financial statements do not have full disclosure.

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

### **Key Audit Matters**

Key audit matters are those matters that, in my professional judgment, are of most significance in the audit of the financial statements. There were no key audit matters to report in the year under review.

### **Other Matter**

### **Prior Year Matters**

In the audit report of the previous year, several issues were raised under the Report on Financial Statements, Report on Lawfulness and Effectiveness in Use of Public Resources, and Report on Effectiveness of Internal Controls, Risk Management and Governance. Although the Management has provided comments on annexure XVI on progress on follow-up of auditor recommendation, the matters have remained unresolved as parliament has not met to deliberate on the same.

### **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, Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources and Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance sections of my report, based on the audit procedures performed, I confirm that public resources have not been applied lawfully and in an effective way.

## **Basis for Conclusion**

### **1.0 Encroachment on the Board's Property**

Field inspection undertaken on a number of depots revealed that there is encroachment on the Board's property as detailed below: -

- i. In Bungoma a portion of plot number 485 where the Bungoma silos are located has been encroached by a third party who has fenced the land and leased it to a garage operator. It was not possible to ascertain the effort the Board is making to get back its land.
- ii. In Nakuru the Board did not have any ownership documents for land LR/No 3490/16 measuring 0.0878 hectares and it was not possible to physically identify the said land for audit verification.
- iii. In Kericho there were permanent residential houses constructed and occupied by third parties who claim to own the properties and have allotment letters for three of the Board's properties Blk.5/65 or L.R NO.631/488, Blk.5/66 or L.R NO.631/505 and Blk.5/67 or L.R NO.631/504 measuring 0.03ha, 0.0389ha and 0.0335 ha, respectively. It is not clear under what circumstances that the land ceased to belong to the Board.
- iv. Properties Blk.5/138, Blk.2/49 and Blk.5/165 measuring 0.0654ha, 0.7284ha, and 0.0654ha are each encroached from one side by pushing in the boundary beacons.
- v. In Kakamega Depot it was noted that the tenant has built permanent structures on the open space and also repainted the NCPB office. However, there was no evidence provided to show that these developments on the property Blk.1/640 were approved by the Board of Directors.

The Board Management did not demonstrate measures instituted to ensure that adequate control and safeguards for its assets are implemented. This was contrary to Regulation 139 (1) (a) of the Public Finance Management (National Government) Regulation 2015.

Consequently, Management was in breach of law and risks losing valuable assets.

### **2.0 Acting Allowances**

The Board paid acting allowances of Kshs.24,351,167.95 out of which Kshs.17,255,180 was paid to members of staff who were in acting capacity for more than six (6) months. This was contrary to Section C.14(1) of the Public Service Commission (PSC) Human Resource Policy, 2016 and the Board's own Human Resource Policy which provides that acting appointment shall automatically lapse after six (6) months.

Consequently, the Management is in breach of the human resource policies and procedures.

### **3.0 Non-Compliance with the One Third of Basic Salary Rule**

Review of the payrolls revealed that some employees' salary deductions fell below 1/3 of the basic salary. This was contrary to Section 19(3) of the Employment Act, 2007 which requires that deductions made by an employer from the wages of his employee at any one time shall not exceed two thirds of such wages.

Consequently, Management was in breach of law.

### **4.0 Procurement, Delivery and Distribution of Fertilizer on Behalf of Parent Ministry**

During the financial year 2018/2019, the Board procured 10,000 metric tonnes of fertilizer valued at Kshs.496,089,500. However, Management did not provide for audit documents in support of the importation and certificate of conformity issued by Kenya Bureau of Standards.

Consequently, it was difficult to ascertain that value for money was realised in the procurement of the fertilizer.

The audit was conducted per 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 comply, 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, because of the significance of the matters discussed in the Basis for Adverse Opinion, Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources and Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance sections of my report, based on the audit procedures performed, I confirm that internal controls, risk management and governance were not effective.

### **Basis for Conclusion**

#### **Composition of the Board Audit Committee**

Review of the appointment of members to the Board Audit Committee revealed that the appointment failed to meet the criteria set under Part 1.1.6 Mwongozo the Code of Governance for State Corporations. The Mwongozo the Code of Governance for State Corporations requires that at least one of the members of the Audit Committee should financial expertise and be a member of professional body regulating the accountancy professionals.



The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standard requires 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 Directors and those Charged with Governance**

The Directors are 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 assessment of the effectiveness of internal control, risk management and governance.

In preparing the financial statements, Management is responsible for assessing the Board'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 Directors are aware of the intention to terminate the Board 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 Board's financial reporting process, reviewing the effectiveness of how Management 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 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 Directors.
- Conclude on the appropriateness of the 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 Board'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 Board 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 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.



**CPA Nancy Gathungu, CBS**  
**AUDITOR-GENERAL**

**Nairobi**

**14 January, 2022**