REPORT OF THE AUDITOR-GENERAL ON COUNTY ASSEMBLY OF MOMBASA FOR THE YEAR ENDED 30 JUNE 2018

REPORT ON THE FINANCIAL STATEMENTS

Adverse Opinion

I have audited the accompanying financial statements of County Assembly of Mombasa set out on pages 2 to 43, which comprise the statement of financial assets as at 30 June 2018, and the statement of receipts and payments, statement of cash flows and statement of comparison of budget and actual amounts-recurrent and development combined 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 County Assembly of Mombasa as at 30 June 2018, 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 Government Act, 2012.

Basis for Adverse Opinion

1.0 Car Loans Fund

1.1 Deposits for Car Loans

As reported previously, the County Assembly of Mombasa placed a deposit of Kshs.20 Million in respect of car loans to Members of the County Assembly with Chase Bank. However, this amount has been omitted from the balance of receivables and it is not clear and the management has not explained how the deposit has been accounted for in these financial statements. In addition, audit review of Chase Bank loan repayment schedule revealed that a total of Kshs.7,317,336 was owing from twenty-one (21) former Members of the County Assembly as at 30 June 2018. In the circumstances, Public funds amounting to Kshs.7,317,336 may be lost in case of loan default by the twenty-one (21) former members of the County Assembly.

As a result, the accuracy, completeness and validity of deposit for car loan of Kshs.20 million as at 30 June 2018 could not be confirmed.

1.2 Financial Statements for Car Loan Fund

Financial statements for the Car Loan Fund were not submitted to the Auditor-General for audit contrary to Section 167 (1) and (3) of the Public Finance Management Act, 2012 which requires the administrators of funds to prepare financial statements for each financial year and submit the same to the Auditor General.

Consequently, the County Assembly is in breach of the law.

2.0 Pending Bills

As reported previously, Annex 1 to the financial statements reflects pending accounts payables amounting to Kshs.61,539,200 as at 30 June 2018 out of which Kshs.53,759,977 relates to accounts payable pending for more than one year. Further, Annex 3 to the financial statements reflects other pending payables in respect to unremitted statutory deductions amounting to Kshs.35,673,479 and unremitted staff pension contributions amounting to Kshs.12,325,957: all totalling Kshs.47,999,436.

In the circumstances, the accuracy and validity of the pending bills totalling Kshs.109,538,636 as at 30 June 2018 could not be ascertained.

3.0 Finance Costs

Note 11 to the financial statements reflect finance costs amounting to Kshs.1,501,520. This amount relates to Kenya Revenue Authority penalties for non-remittance of Pay As You Earn (PAYE) deductions. It is not clear why the management of the County Assembly could not remit the deductions in time to avoid unnecessary costs.

In the circumstances, the validity of the finance costs amounting to Kshs.1,501,520 for the year ended 30 June 2018 could not be confirmed.

4.0 Variance between Financial Statement and Ledger

The statement of receipts and payments for the year ended 30 June 2018 reflects payments of Kshs.62,463,769.66 compared to the ledger balance of Kshs.66,298,078.15 resulting to unexplained nor reconciled variance of Kshs.3,834,308.49 as shown below:

Item Description	Note	FS Figure (Kshs)	Ledger Figure (Kshs)	Variance (Kshs)
Pension and other social security contributions	4	19,724,859	22,265,633	(2,540,774)
Rentals of produced assets	5	37,080,000	37,300,000	(220,000)
Hospitality supplies and services	5	5,658,910	6,732,445	(1,073,535)
Total		**62,463,769**	**66,298,078**	**3,834,309**

In the circumstance, the accuracy and completeness of the expenditure totalling Kshs.3,834,309 for the year ended 30 June 2018 could not be confirmed.

5.0 Transfers from the County Treasury/Exchequer Releases

Note 1 to the financial statements for the year ended 30 June 2018 reflects transfers from the County Treasury or Exchequer releases of Kshs.525,366,107. However, audit review of the bank statements for the County Assembly bank accounts revealed that the County Assembly only received Kshs.225,560,047 resulting to a variance of Kshs.299,806,060 which was paid directly by the County Executive to pay staff salaries. Management indicated that since inception of the County Government, the County Executive has been paying salaries for all departments, the Assembly included. The management has not provided evidence of any agreement with the County Executive to make payments on their behalf.

In the circumstances, the accuracy and completeness of transfers of Kshs.299,806,060 during the year and the financial independence of the County Assembly and independence of the County Assembly in performance of its oversight role to the County Executive could not be confirmed.

6.0 Variance between Statement of Comparison Budget and Receipts and Payments

The statement of comparison of budget and actual amounts: recurrent and development combined reflects total actual on comparable basis amount of Kshs.519,248,629. However, the statement of receipts and payments reflects total payments of Kshs.520,750,148 as a result of omitting finance cost (penalty) of Kshs.1,501,519 which had not been budgeted for.

Consequently, the accuracy and completeness of the statement of comparison of budget and actual amounts: recurrent and development combined for the year ended 30 June 2018 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the County Assembly of Mombasa 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 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. Except for the matter(s) described in the Basis for Adverse Opinion section, I have determined that there are no other Key Audit Matters to communicate in my report.

Other Matter

1.0 Budgetary Control and Performance

1.1 Budget Absorption

The County Assembly of Mombasa had a total budget of Kshs.662,085,836 voted for the financial year 2017/2018, comprising Kshs.44,268,615 for development and Kshs.617,817,221 for recurrent expenditure. Actual expenditure amounted to Kshs.519,248,629, as summarized below:

Item	Approved Budget Kshs.	Actual Expenditure Kshs.	Under Absorption Kshs.	Under Absorption (%)
Development Vote	44,268,615	42,367,069	1,901,546	4.3
Recurrent Vote	617,817,221	476,881,560	140,935,661	22.8
Total	**662,085,836**	**519,248,629**	**142,837,207**	**21.5**

In overall, the County Assembly under spent to a tune of Kshs.142,837,207 or 21.5% of the total budget allocation. The funds could have been allocated to other deserving areas that would improve goods and services delivery to the residents of Mombasa County.

This may also be an indication of improper planning and the management may need to re-think on its budget making process in view of focusing on more priority areas.

1.2 Development Budget

During the year, under review, the County Assembly allocated Kshs.44,268,615 for development projects and spent Kshs.42,367,069, resulting to net under expenditure of Kshs.1,901,546 or 4.3%. The under-utilization of the budget by 4.3% affected service delivery to the residents of Mombasa County.

1.3 Recurrent Budget

During the year under review, the County Assembly allocated Kshs.617,817,221 for recurrent expenditure and spent a total of Kshs.476,881,560, resulting to an overall under expenditure of Kshs.140,935,661 or 22.8% of the budget as summarized below:

Expenditure item	Budget Amount Kshs.	Actual Expenditure Kshs.	Under-absorption Kshs.	% Under-absorption
Compensation of Employees	289,499,217	230,333,406	59,165,811	20.4%
Use of goods and services	328,318,004	246,548,153	81,769,851	24.9%
Total	**617,817,221**	**476,881,560**	**140,935,661**	**22.8%**

The County Assembly's under-utilization of the budget by Kshs.140,935,661 or 22.8% affected service delivery to the residents of Mombasa County.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

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 section of my report, based on the audit procedures performed, I confirm that public resources have not been applied lawfully and in an effective way.

1.0 Rentals of Produced Assets

1.1 County Wards Bank Accounts

Note 5 to the financial statements for the year ended 30 June 2018 reflects rentals of produced assets of Kshs.37,080,000. These funds were paid to cater for wards' operations to pay staff salaries and office rent. Audit revealed that each ward operates a bank account. However, prior County Treasury authority to open the bank accounts in accordance with Section 119(1) of the Public Finance Management (County Government) Regulations, 2015 which states that the County Treasury is responsible for authorizing the opening, operating and closing of bank accounts for the county government and its entities was not availed for audit verification.

1.2 Recruitment of County Wards Staff

Further, the County Assembly recruited ninety (90) staff at the Member of County Assembly's offices. However, recruitment records, contract agreements, appointment letters for the employees and procurement records for the Member of County Assembly's offices were not availed for audit verification.

2.0 Outstanding Imprest

Note 14 to the financial statements for the year ended 30 June 2018 reflects outstanding imprests of Kshs.23,270,625. Audit review of imprest register revealed that imprest amounting to Kshs.2,178,976 had been outstanding for over one year. This is contrary to Section 93 (5) of the Public Financial Management (County Government) Regulations, 2015 which require a holder of a temporary imprest to account or surrender it within seven (7) days after returning to duty station. In addition, the audit examination revealed that Kshs.18,025,027 was held as multiple imprest by twenty-seven officers contrary to Section 93 (4) (b) of Public Finance Management (County Government) Regulations 2015 which requires the Accounting officer to ensure that the applicant has no outstanding imprest. Although management indicates that the imprest shall be recovered through payroll, it was not clearly explained why it had taken long to effect the recoveries.

In the circumstances, the propriety and recoverability of accounts receivables-outstanding imprest balance of Kshs.23,270,625 as at 30 June 2018 could not be confirmed.

3.0 Failure to Constitute Audit Committee

As reported previously, the County Assembly of Mombasa had not constituted audit committee contrary to Section 167 of the Public Finance Management (County Government) Regulations, 2015. It was not clear who carries the financial oversight role for the County Assembly.

In addition, the internal audit department has no internal audit charter creating functions, roles and powers of the function. It was also observed that the head of internal audit function reports administratively and functionally to the Clerk which casts doubt on the independence of the department.

In the circumstances, the County Executive was in breach of law and assurance on the risk management, control and governance of the County Assembly is in doubt due to lack of an effective audit committee.

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 SYSTEMS AND GOVERNANCE

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 and Basis for Conclusion on compliance with lawfulness and effectiveness in use of public resources sections of my report, based on the audit procedures performed, I confirm that internal controls, risk management and governance were not effective.

The audit was conducted in accordance with ISSAI 1315 and ISSAI 1330. 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, 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 Assembly's ability to sustain 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 Assembly or to cease operations, or have no realistic alternative but to do so.

Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 47 of the Public Audit Act, 2015.

In addition to the responsibility for the preparation and presentation of the Assembly's 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 Assembly'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 review is planned and performed to express a conclusion with limited assurance as to 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 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 review 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 noncompliance. 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 Assembly'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 Assembly'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 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 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 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
<u>AUDITOR-GENERAL</u>

Nairobi

18 February 2019