

# **REPORT OF THE AUDITOR-GENERAL ON KENYA POST OFFICE SAVINGS BANK FOR THE YEAR ENDED 31 DECEMBER, 2019**

---

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Qualified Opinion**

I have audited the accompanying financial statements of the Kenya Post Office Savings Bank set out on pages 21 to 65, which comprise the statement of financial position, as at 31 December, 2019, and the statement of comprehensive income, statement of changes in equity, statement of cash flows and statement of comparison of budget and actual 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 effects 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 Kenya Post Office Savings Bank as at 31 December, 2019, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRS) and comply with the Public Finance Management Act, 2012.

### **Basis for Qualified Opinion**

#### **1. Overstatement in Stocks Balances**

The statement of financial position and as disclosed in Note 22 to the financial statements, reflects stocks balance of Kshs.14,145,662. Included in this balance is Kshs.3,247,794 in respect of drugs. However, the supporting physical stock count in respect of drugs revealed stock values of Kshs.317,626 resulting to an overstatement of Kshs.2,930,166.

Consequently, the accuracy of stocks balance of Kshs.3,247,794 as at 31 December, 2019 could not be confirmed.

#### **2. Variance in Customer Savings and Deposits**

The statement of financial position and as disclosed in Note 28 to the financial statements, reflects customer's savings and deposits balance of Kshs.21,779,302,505; (2018 - Kshs.20,018,428,733). However, the supporting schedules provided reflects a balance of Kshs.20,124,809,988 resulting to an unexplained and unreconciled variance of Kshs.1,760,873,773.

Further, the bank operations of customer's savings and deposits system maintained indicates a net variance of Kshs.26,144,196 in comparison with the reported balances in the financial systems as analyzed below: -

<b>Account Type</b>	<b>Financial Statements Balance (Kshs.)</b>	<b>System Balance (Kshs.)</b>	<b>Variance (Kshs.)</b>
Bidii Savings Account	8,766,726,286	8,735,821,024	30,905,262
Step Account	894,357,467	896,448,151	(2,090,684)
Pension Accounts (BSG)	5,202,736,305	5,238,588,249	(35,851,944)
Premium Savings Scheme	1,569,028	1,837,115	(268,088)
Premium Plus Account	3,821,054,970	3,818,760,657	2,294,313
Fixed Deposit Account	13,908,649	15,075,955	(1,167,306)
Save-As-You-Earn	994,051,399	1,013,547,236	(19,495,837)
Staff Salary Account	69,135,387	58,697,199	10,438,187
Salary Account	278,888,828	288,503,395	(9,614,567)
Postbank Junior Account	16,076,893	731,519	15,345,373
Corporate Clients	526,925,084	553,749,846	(26,824,762)
Smata Account	270,280,461	270,546,126	(265,665)
Pamoja Chama Account	92,897,036	92,914,959	(17,923)
Mzalendo Account	105,889	105,889	-
Waridi Account	625,935,534	627,881,132	(1,945,598)
Independent Agent Accounts	262,633	241,746	20,887
M-chama Savings Account	102,273,450	101,664,935	608,516
Mobile Savings Account	3,595,359	3,596,119	(760)
Akiba Account	1,432,103	1,432,603	(500)
Inua Jamii	63,422,793	63,410,793	12,000
Agent Control	20,413,726	21,044,286	(630,560)
ATM Retracted Cash	13,253,226	847,766	12,405,460
<b>Total</b>	<b>21,779,302,505</b>	<b>21,805,446,701</b>	<b>(26,144,196)</b>

The unreconciled variances points to the weaknesses in internal controls on accuracy of data maintained in the two systems.

Consequently, the accuracy of customers' savings and deposits balance of Kshs.21,779,302,505 reflected in the statement as at 31 December, 2019 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Kenya Post Office Savings Bank Management in accordance with ISSAI 130 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAI and 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**

### **Material Uncertainty in Relation to Going Concern**

The statement of comprehensive income for the year reflects a loss of Kshs.1,400,244,912; (2018-Kshs.1,589,099,239), a slight improvement from the prior year. The loss continued to impact negatively on the revenue reserves worsening further to negative Kshs.14,027,788,796;(2018-Kshs.12,588,190,816). The Bank continued to record a negative shareholder's equity of Kshs.10,606,330,604; (2018 – Kshs.9,192,821,813). The Bank's dependence on government to defray these losses is uncertain and the bank's ability to continue as a going concern is doubtful.

Further, the statement of financial position for the year ended 31 December, 2019 reflects customers' savings and deposits of Kshs.21,779,302,505 which exceeds the total assets of the bank of Kshs.14,484,906,047 by Kshs.7,294,396,458. This reflects a low liquidity ratio of the Bank thus, rendering it technically insolvent unless the Government supports their operation by extending credit facilities and assisting the Bank to manage its fixed costs which the Management has not been able to manage in the past.

My opinion is not qualified in respect of this matter.

### **Key Audit Matters**

Key audit matters are those matters that, in my professional judgement, 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 Information**

The Board of Directors is responsible for the other information. The other information comprises the information included in the annual report and financial statements, but does not include the financial statements and my audit report thereon.

My opinion on the bank financial statements does not cover the other information and I do not express any form of assurance conclusion thereon.

### **Other Matter**

#### **Prior Year Matters**

##### **1. Overdue Accounts Receivable**

As reported previously and as disclosed under Note 24 to the financial statements, the statement of financial position reflects accounts receivable balance of Kshs.2,610,326,854;(2018-Kshs.2,637,847,618). Included in the amount is rent receivables balance of Kshs.73,000,353 of which Kshs.47,113,844 is owed by tenants who have since vacated the Bank's premises without recourse as provisioned for in the lease agreements being exercised. The likelihood of the amount being collected is

doubtful, and adjustments necessary by way of provisions for the uncertainty have not been incorporated in the financial statements.

In the circumstances, the accuracy of the accounts receivable balance of Kshs.73,000,353 as at 31 December, 2019 could not be confirmed.

## **2. Loss of Cash Through Fraud/Cash Loss**

### **2.1 Fraud**

As reported previously and as disclosed under Note 25, included in the prepayments & other assets balance of Kshs.2,531,312,171 is an amount of Kshs.81,128,628 indicated as fraud customers and fraud others. The money was lost through fraud and no meaningful efforts have been undertaken by Management to recover the money so far. This is failure on part of the Management to recover the lost money.

### **2.2 Cash Shortage**

Further, included in Note 25 pre-payments and other assets balance of Kshs.2,531,312,171 is Kshs.35,228,987 being cash shortages attributable to working cashiers. The Human resource policy of the Bank requires such cash shortages to be made good within forty-eight (48) hours by the concerned.

Under the circumstances, the Board and Management has not implemented the policy to safeguard the customers' savings & deposits.

## **3. Property and Equipment**

As reported in the previous year and as disclosed in Note 26 to the financial statements, the statement of financial position reflects property and equipment balance of Kshs.2,263,288,081;(2018-Kshs.2,360,260,775). The following unsatisfactory issues were however noted:

### **3.1 Encroached Land without Title Deed**

Included in the land balance of Kshs.805,000,000, is a parcel of land valued at Kshs.5,000,000 located in Dandora Phase II allotted to the Bank in 1993. Physical visit to the land during the audit revealed that the land has remained unfenced and has since been encroached on by informal settlers. There is no evidence of action taken by Management to secure the land and obtain a title deed. The Bank's ability to access the land in the future as its rightful owner is doubtful.

In the circumstances, the security and ownership of the parcel of land by the Bank could not be confirmed.

### **3.2 Land in Dispute**

Disputed land reference No. 209/11908(I.R No.59328) in Nairobi, Upper Hill, Mara Road, is registered in the name of the Bank valued at Kshs.550,000,000 but has its title deed encumbered (The encumbrance was registered vide a caveat dated 15 August, 2014 claiming interest absolutely). Review of information indicates that this dispute relates to an ongoing court case No.2834 of 1995 between the Bank and a plaintiff. The outcome of the case had not been determined as of the date of my audit report. However, Management has not disclosed this by way of contingent liability in the financial statements.

In the circumstance, ownership of the two parcels of land by the Bank could not be confirmed.

### **3.3 Motor Vehicle without a Log Book**

Also included in the property and equipment balance of Kshs.2,263,288,081 as at 31 December, 2019 are motor vehicles valued at Kshs.19,361,255. As reported previously, the motor vehicles schedule includes a motor vehicle registration number KAJ 078Y valued at Kshs.400,000 whose log book has not been issued to the Bank by the National Transport and Safety Authority (NTSA). This is despite the Bank having paid the requisite duty to register the vehicle in its own name in November, 1997.

In the circumstances, the accuracy of motor vehicles balance of Kshs.19,361,255 as at 31 December, 2019 could not be confirmed.

## **REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES**

### **Conclusion**

As required by Article 229(6) of the Constitution, based on the audit procedures performed, except for the matters described in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section of my report, I confirm that, nothing else has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

### **Basis for Conclusion**

#### **1. Anomalies in Employee Expenses**

The statement of comprehensive income reflects employees' expenses of Kshs.1,153,873,508 which is approximately 53% of the total expenditure of the Bank for the year under review. This is above the set limit of 35% as stipulated in Regulation 26(a) of PFM Regulations, 2015. Further, contrary to the provisions of Section 19(3) of the Employment Act, 2007, four hundred and twenty-eight (428) (65.5%) employees of the Bank out of the total six hundred and seventy-four (674) employees received net pay less than a third (1/3) of their basic pay. No explanation has been provided for the anomaly.

In the circumstances, the Management failed to comply with the provisions of the law.

## **2. Staff Over-Establishment**

The approved staff establishment for the Bank is six hundred and ten (610) officers, while the actual staff in post are six hundred and seventy-four (674) exceeding the staff establishment by sixty-four (64) employees. This has contributed to high cost of compensation to staff and hence, the Bank continued to record operating deficits. The Management failed to comply with the approved staff establishment for the year.

## **3. Unassessed Contingency Liability over Legal Cases**

During the year under review, the bank made provisions of Kshs.1 Billion in the books in respect of the anticipated crystallization of numerous legal cases against the bank. Based on the information available, the Management believes that at the determination of all the cases, the bank is not likely to suffer any financial loss. The land dispute case between Postbank and a plaintiff has taken so long to be concluded. The contingency liability risk should be properly assessed and addressed by Management.

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

## **REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE**

### **Conclusion**

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, except for the matter described in the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance section of my report. I confirm that, nothing else has come to my attention to cause me to believe that internal controls, risk management and overall governance were not effective.

### **Basis for Conclusion**

#### **Lack of Updated Business Continuity Policy**

A review of business continuity policy revealed that the Bank is not prepared to adapt to disruptions incidents that may occur in order to maintain continuous operations and to protect its assets. The bank continues to use an outdated business continuity policy and backups which have not been tested to ensure recoverability in the event of disruption.

Consequently, the Bank's recoverability of operations and assets in the event of disruption could not be confirmed.

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 overall 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 Board of Directors**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards (IFRS) 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 overall governance.

In preparing the financial statements, Management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management is aware of the intention to liquidate the Bank 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.

The Board of Directors is responsible for overseeing the Bank's financial reporting process, reviewing the effectiveness of how the 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 overall 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 overall 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 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 Bank's ability to continue as a going concern. 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 Bank to cease to continue as a going concern.
- 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 Bank 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.



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

**Nairobi**

**29 June, 2022**