

REPORT OF THE AUDITOR-GENERAL ON MUNICIPALITY OF KILIFI FOR THE YEAR ENDED 30 JUNE, 2021

PREAMBLE

I draw your attention to the contents of my report which is in three parts:

- A. Report on the Financial Statements that considers whether the financial statements are fairly presented in accordance with the applicable financial reporting framework, accounting standards and the relevant laws and regulations that have a direct effect on the financial statements.
- B. Report on Lawfulness and Effectiveness in Use of Public Resources which considers compliance with applicable laws, regulations, policies, gazette notices, circulars, guidelines and manuals and whether public resources are applied in a prudent, efficient, economic, transparent and accountable manner to ensure Government achieves value for money and that such funds are applied for intended purpose.
- C. Report on Effectiveness of Internal Controls, Risk Management and Governance which considers how the entity has instituted checks and balances to guide internal operations. This responds to the effectiveness of the governance structure, the risk management environment, and the internal controls developed and implemented by those charged with governance for orderly, efficient and effective operations of the entity.

An unmodified opinion does not necessarily mean that an entity has complied with all relevant laws and regulations, and that its internal controls, risk management and governance systems are properly designed and were working effectively in the financial year under review.

The three parts of the report are aimed at addressing the statutory roles and responsibilities of the Auditor-General as provided by Article 229 of the Constitution, the Public Finance Management Act, 2012 and the Public Audit Act, 2015. The three parts of the report, when read together constitute the report of the Auditor-General.

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Municipality of Kilifi set out on pages 25 to 50, which comprise of the statement of financial position as at 30 June, 2021, and the statement of financial performance, statement of changes in net assets, statement of cash flows and the 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, except for the effects of the matter described in the Basis for Qualified Opinion Section of my report, the financial statements present fairly, in all material

respects, the financial position of the Municipality of Kilifi as at 30 June, 2021, and of its financial performance and its cash flows for the year then ended, in accordance with the International Public Sector Accounting Standards (Accrual Basis) and comply with the Urban Areas and Cities Act, 2011 and Kilifi County Subsidiary Legislation, 2019 and the Public Finance Management Act, 2012.

Basis for Qualified Opinion

Inaccuracy in Surplus for the Year

The statement of financial performance reflects a surplus balance of Kshs.39,596,698 while the statement of changes in net assets reflects surplus balance of Kshs.49,943,782 resulting in an unreconciled variance of Kshs.10,347,084.

In the circumstances, the accuracy and completeness of the reported surplus balance of Kshs.39,596,698 could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Municipality of Kilifi 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 qualified 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

Budgetary Control and Performance

The statement of comparison of budget and actual amounts reflects a final revenue budget and actual on comparable basis of Kshs.124,567,916 and Kshs.116,010,258 respectively, resulting in an underfunding of Kshs.8,557,658 or 7% of the budget. Similarly, budgeted expenditure was Kshs.121,750,100 against an actual expenditure of Kshs.66,066,476, resulting in an under expenditure of Kshs.55,683,624 or 46% of the budget.

In the circumstances, the under performance affected the planned activities and may have impacted negatively on service delivery to the public.

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 effect of the matters described in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources section of my report, 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. Irregular Roads Contract

As disclosed in Notes 4A and 4B to the financial statements, the statement of financial performance reflects expenditure on Urban Development Grant Projects accrued balance of Kshs.49,152,720 and Kshs.10,347,084 respectively, both totalling to Kshs.59,499,804. The expenditure relates to refurbishment of Oloititip Market and Service Road by the County Executive for a period of eight (8) months, from 13 March, 2019 upto 12 November, 2019. The contract sum was Kshs.95,362,190. Records provided indicated that Management reviewed the contractor's final account on 18 October, 2021. However, the following anomalies were noted:

1.1 Failure to Account for Provisional Sums

The bill of quantities provided for a provisional sums for electrical installations and contingency amount of Kshs.3,250,000 and Kshs.8,669,290 respectively, all totalling to Kshs.11,919,290. However, the contractor's final account did not account for these provisional sums.

1.2 Irregular Contract Variation

The contractor's final account included consultancy services amounting to Kshs.9,436,870 that were not part of the contract. This was contrary to Section 82 of the Public Procurement and Asset Disposal Act, 2015 which provides that, the tender sum as submitted and read out during the tender opening shall be absolute and final and shall not be the subject of correction, adjustment or amendments.

1.3 Undelivered Supplies

The contract also included supply of twenty-five (25) forty-foot (40) steel used containers at a cost of Kshs.28,485,000 as per the bill of quantities. However, the containers were not seen during physical verification.

1.4 Unrecovered Liquidated Damages

The project's expected practical completion date was 12 November, 2019 which was delayed by over one and a half years. It was completed and in use in November, 2021. However, the reviewed contractor's project final account did not factor in the savings for liquidated damages of Kshs.11,700,000 at the rate of Kshs.20,000 per day for the 585 days delay. This was contrary to Paragraph 43.1 of the Appendix to the conditions of the signed contract which provides for the liquidated damages.

In the circumstances, Management was in breach of the law.

2.0 Delayed Remittance of Withholding Tax

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Review of Withholding Tax remittances revealed that tax totalling to Kshs.4,309,667 was remitted late by more than five (5) months. This was contrary to Section 42.A (4B) of the Value Added Tax (VAT) Act which provides that, “the tax withheld under this section shall be remitted to Commissioner on or before the twentieth day of the month following the month in which the deduction is made”.

In the circumstances, Management was in breach of the law.

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 effect of matters described in the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance section of my report, 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

1. Weaknesses in Municipality Board

The Municipality Board of Kilifi is composed of seven (7) members, out of whom only three (3) members were appointed through a competitive process, contrary to the requirement of the Section 9 of the Municipality of Kilifi Charter, 2019 which provides that the Board of the Municipality shall be comprised of not more than nine (9) members, four (4) of whom are women and shall be appointed through a competitive process by County Executive Committee and approved by County Assembly.

In the circumstances, effectiveness of the governance structure could not be confirmed.

2. Weaknesses in Management of the Municipality

Review of records indicated that the control over budget and actual performance were still domiciled in the parent Department including the development budget allocation totalling to Kshs.96,750,100 for Urban Development Grant that was fully under the control of the of Department of Lands, Energy, Housing, Physical Planning and Urban Development.

Further, the Municipality had total approved substantive positions of three hundred and eighty four (384). However, it had filled only one (1) substantive position while eleven (11) members of staff were on secondment.

In the circumstances, the Municipality might not fully meet its mandate.

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 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 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 (Accrual 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 overall governance.

In preparing the financial statements, Management is responsible for assessing the Municipality of Kilifi'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 terminate the Municipality 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 Municipality'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 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 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 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 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 Municipality'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 Municipality to cease 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 Municipality to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

I communicate with 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

07 September, 2022