

REPORT OF THE AUDITOR-GENERAL ON NATIONAL CEREALS AND PRODUCE BOARD 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

Disclaimer of Opinion

I have audited the accompanying financial statements of National Cereals and Produce Board set out on pages 25 to 62, which comprise of the statement of financial position as at 30 June, 2021, and the statement of profit or loss and other comprehensive incomes, statement of changes in equity, 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 do not express an opinion on the accompanying financial statements. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for Disclaimer of Opinion

1. Gross Sales

1.1 Material Understatement of Gross Sales

The statement of profit or loss and other comprehensive incomes reflects gross sales amounting to Kshs.736,933,340 and as disclosed in Note 1 to the financial statements. However, an Enterprise Resource Planning (ERP) system in use reflects gross sales of Kshs.918,612,774 resulting in an unexplained material variance of Kshs.181,679,434. Further, the source of the amount of sales in the financial statements could not be confirmed.

1.2 Stock Losses Reported as Sales

The gross sales of Kshs.736,933,340 disclosed in Note 1 to the financial statements include stock losses amounting to Kshs.39,712,458 as per analysis of sales detailed transactions provided for audit. A part of the losses was attributed to transporters but Management did not explain how the losses occurred since the goods were already in the depot. Further, analysis revealed that more than half of the losses occurred at Nyansiongo sub-depot amounting to Kshs.19,165,300.

It was not clear how stock losses were treated as sales and how the stock losses for the earlier years were accounted for in the current year.

1.3 Unaccounted for Sales of Fertilizer

Review of documents relating to purchases of fertilizer in Meru revealed that purchase invoice numbers 81D4082138 of 45,000 bags of fertilizer for Kshs.128,250,000 and 81D4082679 of 45,000 bags of fertilizer for Kshs.115,421,760 both totalling Kshs.243,761,760 were raised and then cancelled using invoice numbers 16C4006134 and 16C4006127 for the same amounts, respectively. Review of detailed sales transaction revealed two sales orders number 11C4029817 of 45,000 bags and 11C4030107 of 45,000 totalling Kshs.270,000,000. However, review of stock cards provided no evidence of the stock movement as reported in the detailed sales transactions. The sales were also reversed in the ERP system with no explanation while the stocks were not traced in the stores.

1.4 Unsupported Sales of Maize

Scrutiny of the store records at Nakuru depot revealed undisclosed sales of white maize (commodity code 1066) amounting to Kshs.1,228,800. Further, the summary sales per product report generated from the ERP system revealed that 960 bags were sold, which differs with the physical stock card that indicated sales of 2001 bags. In addition, analysis of detailed sales transaction report revealed sales orders for 3145 bags of maize amounting to Kshs.4,025,600.

Further, records at the Eldoret depot indicated that sales totalling Kshs.1,281,000 were realized from sales of maize but this amount differed with the ledger at the headquarters that indicated nil sales.

In addition, the Board updates prices of various products on a monthly basis. However, the detailed sales transactions report revealed instances where the prices of some commodities amounting to Kshs.278,795 were set to zero and in other instances the prices were set below the market price index threshold for similar commodities during the year.

In the circumstances, the accuracy and completeness of the gross sales of Kshs.736,933,340 could not be confirmed.

2. Variances in Opening and Closing Stock Balances

2.1 Variances between Opening Stock in the Financial Statements and the ERP System

The statement of financial position reflects comparative inventories balance of Kshs.158,099,778 under the financial year 2019/2020 and as disclosed in Note 12 to the financial statements. However, comparison between the ERP system opening stock balance of Kshs.1,400,462,177 and the financial statements opening balance of Kshs.158,099,778 revealed a variance of Kshs.1,242,362,399. The Board attributed the variance to errors which occurred when migrating from Navision 2005 to Navision 2017 in February 2018 as well as inter-functional transactions that involved GOK transactions and third-party stocks. However, no justification was provided as to why the variances have taken too long to be investigated and reconciled.

Further, the ERP system generated ledgers reflects negative stock balances on various stock items amounting to Kshs.217,543,763 which have been reflected as having a nil opening balance to conceal the negative stock. No explanation was provided on how the system to reflected a negative stock balance and the effect of negative stock in the financial statements.

In addition, the stock records reflect opening stocks with no prices and no change or movement during the year despite the financial statements reflecting procurement of the stock items costing Kshs.1,684,563,251.

2.2 Variances Between Closing Stock in the Financial Statements and the ERP System

The statement of financial position reflects inventories balance of Kshs.1,227,094,135 and as disclosed in Note 12 to the financial statements. However, comparison between the ERP system closing stock balance of Kshs.1,410,085,751 and the financial statements amount revealed unexplained variance amounting to Kshs.182,991,616. Further, closing stocks amounting to Kshs.115,997,475 had negative balances.

In addition, examination of the closing stocks for various items revealed stocks with no prices and change or movement during the year despite the reported purchases costing Kshs.1,684,563,251 and sales of Kshs.736,933,339 on the stock items.

In the circumstances, the existence, accuracy and completeness of the opening and closing stocks balances of Kshs.158,099,778 and Kshs.1,227,094,135 respectively, could not be confirmed.

3. Directors Expenses

The statement of profit or loss and other comprehensive incomes reflects directors expenses amount of Kshs.10,702,825 as disclosed in Note 7 to the financial statements. Review of Board expenses records revealed that the entity held seven (7) full board meetings during the period under review against the restricted maximum of six (6) for each financial year contrary to Paragraph A (2) of Circular no. OP/CAB.9/1A of 11 March, 2020 which states that board meetings shall be restricted to a maximum six (6) for each financial year.

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

4. Decline in Performance

The statement of profit or loss and other comprehensive incomes disclosed a decline total revenue from Kshs.1,659,790,172 that was reported in 2019/2020 financial year to Kshs.774,010,342 realized in the current year, resulting in a decline in sales of Kshs.885,779,830 or 53%. Similarly, the operating loss increased from Kshs.1,098,935,685 reported in 2019/2020 to Kshs.3,128,788,783 in the current year under review.

In the circumstances, the Board may not internally generate enough revenue to finance its operations in future without relying on the Government support.

5. Property, Plant and Equipment

The statement of financial position reflects a balance of Kshs.19,139,275,369 in respect of property, plant and equipment as disclosed in Note 10 to the financial statements which includes leasehold land balance of Kshs.5,748,184,763. However, the following unsatisfactory matters were noted:

5.1 Lack of Ownership Documents on Land

As previously reported, the leasehold land includes thirty-four parcels that do not have title deeds. In addition, the leases for three plots in Kericho had not been renewed thus making a total of thirty-seven properties valued at Kshs.581,364,000 whose title documents were not in the custody of the Board.

In addition, the document of title for the land on which the Nakuru Cyprus Bins are located, was not provided for audit. Though Management explained that the surveyors had established that the title had been issued at the Land's Registry, the same was not in the custody of the Board.

Although the Board has title deeds for five parcels of land in Kisii County, which have been fenced and marked with the NCPB signpost, there was encroachment on all the parcels of land.

In Kericho, there was encroachment on one of the parcels of land and a temporary structure constructed by a school. Another parcel along Kericho-Kisumu highway has also been encroached by KENHA as well as one of the neighbors whose perimeter wall extended into the Board's compound.

The Board's land in Sagana Town indicated that the land had been fenced but there was encroachment on one section of the land whereby commercial and residential houses have been constructed. There was no sign post to show that the land belongs to the Board.

Further, it was noted that there is a restraining order on a parcel of at Narok that was issued by the High Court in 2013. Though the Board was allocated 20 acres of this land, it was not possible to physically identify the portion that belongs to the Board.

5.2 Failure to Update the Fixed Assets Register and Tag Assets

Some office furniture, fittings, computers and other equipment held at the depots were not tagged or labeled with a unique number for identification and tracking purposes. Although the staff quarters and other buildings were marked with unique numbers, the same were not reflected in the asset register.

5.3 Unsupported Revaluation Adjustment

Although the statement of financial position reflects a balance of Kshs.19,139,275,369 in respect of property, plant and equipment, a summary of the assets' revaluation report submitted for audit indicated a revaluation amount of Kshs.19,523,400,000. The resultant variance of Kshs.384,124,631 was not explained or reconciled.

In addition, the statement of changes in equity reflects a revaluation reserve adjustment of Kshs.14,233,513,389 and as disclosed in Note 18 to the financial statements that was not supported with any documentation.

5.4 Irregular Procurement of Repairs and Maintenance Works

The property, plant and equipment balance of Kshs.19,139,275,369 includes additions to work in progress of Kshs.100,519,052 in 2020/2021 financial year. The additions of Kshs.100,519,052 includes an amount of Kshs.64,067,080 that was incurred on the carpeting of NCPB compound and associated drainage works at GCP depot. The Board advertised through the local dailies, a tender notice for these works on 5 June, 2020. Following an evaluation of responsive bids, the tender evaluation committee recommended the award of the contract to the lowest evaluated bidder, at a contract sum of Kshs.62,262,012. Both parties signed a contract agreement on the 15 July, 2020. A certificate of practical completion was issued by the Chief Architect on 21 May, 2021.

However, as soon as the contract performance began it emerged that there was water beneath the base and the pre-existing drainage channel was too narrow. This called for a wider area of excavation and expansion of the drainage system to avoid the perennial flooding of the stores. The contractor notified the Board about the additional civil works that needed to be undertaken for the project to be completed in the most efficient and

effective way. This entailed approval of 3 No. contract variation orders. Following a financial appraisal, the additional works were estimated to cost Kshs.12,055,800. However, the Accounting Officer approved the engagement of the contractor for the additional works of Kshs.12,055,800 through a direct procurement method.

Though the Board explained that the required services could not be sourced from different contractor as this could bring about conflict in execution of project; and that the contract could not be canceled mid-way as this would have resulted in unnecessary litigation, the only options available was through direct procurement method for the reason of standardization and compatibility.

However, there was no justification for commencement of the repairs before carrying out a proper prior feasibility study and assessment of the project.

In the circumstances, the accuracy, completeness, and ownership of property, plant and equipment balance of Kshs.19,139,275,369 could not be confirmed.

6. Inaccuracies of Inventory and Stores Records

The statement of financial position reflects inventories balance of Kshs.1,227,094,135 and as disclosed in Note 12 to the financial statements. The stock card for maize item code PP1066 at the Eldoret Depot reflected a nil balance which differed with the physical count of 494 bags of 50kg each as at 30 June, 2021. In addition, the running balances in the stock ledgers at Mwea and Embu Depots were not consistent with the additions and reductions of stock, thereby making it impossible to compare the balances in the stock ledgers against the stock cards balances as well as tracking the stock movement from the stock ledgers.

Further, inspection of sampled depots revealed that the stock card for sindano paddy 45kgs item code 5212 at Sagana Depot with a balance of 7,555 bags valued at Kshs.12,579,075 was omitted from the stock-take aggregation and valuation report for the year under review.

In addition, analysis of opening stock showed stock balances which were classified as goods in transit. Management did not provide explanation on what comprised the goods on transit and how they were cleared during the year.

In the circumstances, the accuracy, existence and completeness of the inventories balance of Kshs.1,227,094,135 could not be confirmed.

7. Long Outstanding Trade Debtors and Prepayments

The statement of financial position reflects trade debtors and prepayments net balance of Kshs.611,529,746 and as disclosed in Note 13 to the financial statements. However, Note 13 to the financial statements reflects trade debtors and prepayments gross balance of Kshs.1,604,675,205 which includes trade debtors of Kshs.1,175,533,409. Included in the amount are debtors totalling Kshs.725,641,237 that have been outstanding for more than eight years.

Further, the gross balance of Kshs.1,604,675,205 also includes an amount of Kshs.115,941,063 relating to staff debtors. Included in the staff debtors is an amount of Kshs.62,606,484 that has been outstanding for more than eight years.

Though a cumulative bad debts provision of Kshs.993,145,460 has been made in the financial statements, it was not possible to confirm if the Board will be able to recover the amounts.

In the circumstances, the recoverability of the trade debtors and prepayments balance of Kshs.611,529,746 could not be confirmed.

8. Bank Overdraft

The statement of financial position reflects a bank overdraft balance of Kshs.6,729,563,152 which represents an increase by Kshs.1,292,203,413 or 24% from previous year's balance of Kshs.5,437,359,739. The bank overdraft is related to Government Fertilizer Subsidy Programme that was being implemented by the Board on behalf of Ministry of Agriculture. As previously reported, Kenya Commercial Bank (KCB) continued to charge 12.5% interest and 10% default rate on the outstanding loan. The overdraft is negatively impacting on the Board's operations.

In the circumstances, the Board continues to incur default charges and interest on the bank overdraft balance of Kshs.6,729,563,152 which may affect its liquidity.

9. Irregular Termination of Employment

The Board carried out a restructuring process during the year under review that resolved to merge the Monitoring and Evaluation section with Research and Development. However, before the Board obtained the necessary approval from State Corporations Advisory Committee, the Management implemented the changes and retired the Manager, Monitoring and Evaluation from service on 3 August, 2020 on grounds of abolition of office without approval as per Clause 11.10 of the HR Manual - Retirement on Abolition/Re-organization of office. Further, the decision of the Board to pay the officer terminal dues as per Clause 11.7 of the HR manual on retirement under the 50-year rule was contradictory since the officer did not apply for it.

In the circumstances, the Board incurred an expenditure of Kshs.1,688,250 for wrongful dismissal which was awarded by the Employment and Labour Relations Court on 24 November, 2021 as well as undetermined charges on legal fees.

10. Non-Operationalization of National Food Reserve and National Trading Divisions

The Board was supposed to operationalize the National Food Reserve and National Trading Divisions as per Circular Ref: MOA/B.1/6A dated 29 April, 2020. The divisions were to deal with matters of Strategic Food Reserve and undertake commercial storage and trading in food commodities. However, the Board has not operationalized the two divisions.

In the circumstances, Management is in breach of the law and the assurance of food security in the country could not be confirmed.

11. Unresolved Prior Year Matters

In the audit report of the previous year, several issues were raised covering inability to confirm true and fair view of the financial statements, lawfulness and effectiveness in use of public resources, and effectiveness of internal controls, risk management and governance. However, the Management has not resolved the issues or given any explanation for failure to adhere to the guidelines issued by the Public Sector Accounting Standards Board.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

I do not express a conclusion on the lawfulness and effectiveness in the use of public resources as required by Article 229(6) of the Constitution. Because of the significance of the matters described in the Basis Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit conclusion.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

I do not express a conclusion on the effectiveness of internal controls, risk management and governance as required by Section 7(1)(a) of the Public Audit Act, 2015. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for my audit conclusion.

Responsibilities of Management and the Board of Directors

Management is 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 its assessment of the effectiveness of internal control, risk management and overall governance.

In preparing the financial statements, Management is responsible for assessing the Board's ability to continue to sustain services, disclosing, as applicable, matters related to sustainability of services and using the applicable basis of accounting unless the Management is 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.

The Board of Directors is 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

My responsibility is to conduct an audit of the financial statements in accordance with International Standards of Supreme Audit Institutions (ISSAIs) 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. However, because of the matters described in the Basis for Disclaimer of Opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

In addition, my responsibility is 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. I also consider internal control, risk management and governance processes and systems in order to give an assurance on the effectiveness of internal controls, risk management and governance 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. However, because of the matters described in the Basis for Disclaimer of Opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit conclusion on lawfulness and effectiveness in use of public resources, and on effectiveness of internal controls, risk management and governance.

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.



CPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

02 September, 2022