Fact Sheet

Institute of Economic Affairs

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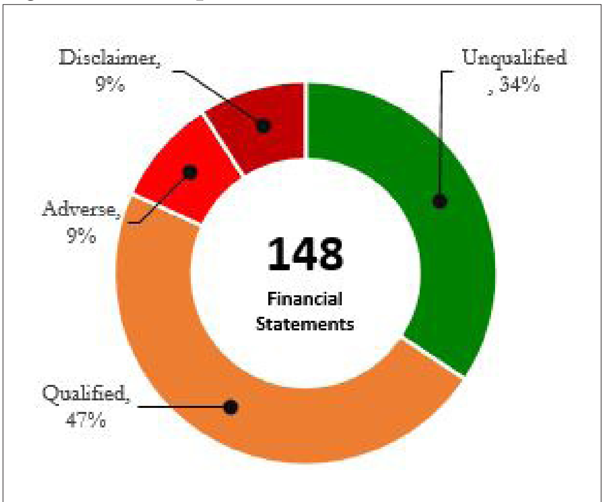
Summary of Key Audit Findings of the National Government Accounts, FY 2018/19

This brief highlights in a simplified way, key audit findings of IEA-Kenya's analysis of the Auditor General's report on the financial statements of the national government for 2018/19. The analysis starts with a big picture perspective on the distribution of audit opinions and further provides a breakdown from both a revenue and expenditure perspective for the reasons behind overall audit opinions.

Distribution of Audit Opinions across the Financial Statements (FS), 2018/19

Figure 1: Audit Opinions across FS, 2018/19



Source: Office of the Auditor General | National Government Audit Reports

About a third (34%) of these statements were awarded unqualified (clean) opinion. This means that about a third of the national government entities properly represent facts in accordance to financial rules. In other words, financial statements of these entities represent a true and fair view of the accounts (see fig 1).

Nearly a half (47%) of these statements had qualified opinion, hence they have cases of misrepresentation of facts which are significant but not widespread or persistent. Conversely, at least 9% (adverse opinion) are not only significant but also widespread and with persistent disagreement with the underlying books of accounts.

The remaining 9% (disclaimer opinion) of the entities have misrepresentation of facts that may arise from inadequate information, limitation of scope, inadequacy or lack of proper records such that the auditor is not able to form an opinion on the financial operations of the said entities.

For both cases of adverse and disclaimer opinions, considerable remedial interventions by the management are required and this should be a major concern for oversight institutions.

In 2018/19,148 financial statements (FS) exclusive of donor funded projects were audited.

These FS cover Ministries, Departments and Agencies (MDAs), revenue statements, national funds, and other unique accounts such as national exchequer accounts and amount in total to Ksh 2.91 trillion.

The specific financial statements with adverse (table 1) and disclaimer (table 2) of opinion are as follows:

Table 1: Financial Statements with Adverse Audit Opinion, 9% (14 out of 148)

National Funds & Other Unique Accounts	1. African Union and Other International Organization Subscription Fund
	2. Agricultural Information Resource Centre Revolving Fund
	3. Asian Officers Family Fund
	4. Commodities Fund
	5. European Widows and Orphans Fund
	6. Pensions and Gratuities
	7. Public Debt
	8. Provident Fund
	9. Rural Enterprise Fund
MDAs	10. State Department for Broadcasting and Telecommunications
	11. State Department for Information, Communications and Technology
	12. State Department for Planning
	13. The Judiciary
Revenue Statements	14. Government Investment and Public Enterprises (Outstanding Loans)

Source: Office of the Auditor General | National Government Audit Reports

Majority, 64% (9 out of 14) of the financial statements with adverse opinion are related to national funds and other unique accounts such as public debt; whereas 29% (4 out of 14) represent MDAs such as the Judiciary and State Department for Planning and the remaining 7% (1 out14) is for revenue statement specifically, the Government Investment and Public Enterprises (Outstanding Loans).

Table 2: Financial Statements with Disclaimer of Opinion, 9% (13 out of 148)

National Funds & Other Unique a/cs	1. Kenya Local Loans Support Fund
	2. Government Clearing Agency Fund
	3. Land Settlement Fund
	4. National Government Affirmative Action Fund

	5. National Youth Service – Mechanical and Transport Fund
	6. East Africa Tourist Visa Fee Collection Account
	7. Statement of Outstanding Obligations Guaranteed by Government of Kenya
	8. Stores and Service Fund
	9. Strategic Food Reserve Trust Fund
	10. Uwezo Fund
	11. Youth Enterprise Development Fund
MDA	12. State Department for Crop Development
Revenue Statements	13. State Department for Crop Development

Source: Office of the Auditor General | National Government Audit Reports

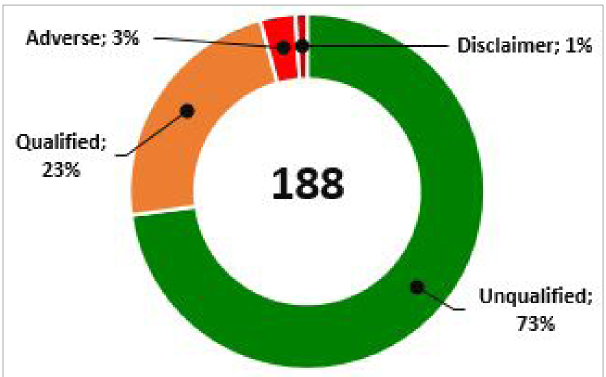
Again, the majority, 11 out of 14 (79%), of the financial statements that had disclaimer of opinion were related to national funds and other unique accounts such as Strategic Food Reserve Trust Fund and statement of outstanding obligations guaranteed by government of Kenya. One MDA: State Department for Crop Development and one revenue statement: State Department for Crop Development. To remedy the situation, these institutions require considerable interventions by the management including the need to strengthen their internal control systems.

Clearly, the national funds and other unique accounts, as the main culprit for both adverse and disclaimer opinions, point to the need for further investigation of the reasons behind these audit opinions. Some of the audit issues that may be attributed to these discrepancies include financial and procurement violations, no value for money and others. If not corrected, there are chances of funds being misappropriated and ultimately service delivery compromised.

Donor Funded Projects

A total of 188 financial statements for the donor funded projects were audited in 2018/19 and were distributed as follows: Unqualified Opinion (73%), Adverse (3%) and Disclaimer (1%).

Figure 2: Distribution of Audit Opinions of Donor Funded Projects, 2018/19



Source: Office of the Auditor General | National Government Audit Reports

Evidently, the donor funded projects have the highest unqualified (clean) opinion (approximately 7 out of every 10), signaling better performance compared to the government of Kenya entities including MDAs-voted entities, revenue statements, national funds, and other unique accounts such as national exchequer accounts. It is however noted that some MDAs did not disclose the counterpart funding from the government, therefore breaching the grant agreements/loan agreements.

Audit opinions are a key determinant by donors for continuous funding support. This is the main driver for comparatively higher clean audit opinions. Apparently their relatively higher audit compliance raises the question of whether that for government entities is by design.

This following section provides a breakdown and highlight of audit queries (questions not responded to adequately) by revenue and expenditure in further explanation of reasons behind audit opinions.

Audit of Revenue Statements, 2018/19

Audit of 14 revenue statements audited in 2018/19, 5(36%) had an unqualified opinion; 7 (50%) had a qualified opinion, 1 (7%) had an adverse opinion and one 1(7%) had a disclaimer of opinion. Hence, at least 64% of the statements did not fully comply with public financial rules.

Table 3: List of Revenue Statements, Corresponding Audit Opinions, Queries & Amounts, 2018/19

MDAs	Audit Opinion	Amount (Ksh Bn)	Audit Queries
1. The National Treasury –Development Revenue	Unqualified	50.1	
2. State Department for Immigration and Citizens Services		10.4	
3. Ministry of Defense		5.3	
4. Business Registration Service		0.8	
5. State Department for Fisheries and the Blue Economy		0.1	
Total		66.6	
1. The National Treasury – Recurrent Revenue		1,448	• Unsupported Adjustments • Variances between Revenue Statement and the General Ledger balances • Variance in Tax Receipts • Unsupported Non-Tax Revenue • Long outstanding reconciling items
2. State Department Interior		4.9	• Under-Charge of Licenses • Uncollected Revenue
3. Registrar of High Court (Judiciary)		3.0	• Long outstanding reconciling items • Unexplained variances • Revenue not banked • Unaccounted for revenue • Unresolved prior year issues
4. Ministry of Mining		1.7	• Unsupported Transfers to the Exchequer Account • Long outstanding arrears of Revenue

5. Ministry of Lands and Physical Planning		1.2	• Lack of Classification of Land Revenues • Undisclosed Deposits to Revenue Control Accounts • Failure to Provide Revenue Collection and Accounting Documents • Failure to Bank Revenue Collected • Non-Payment of Stamp Duty
6. The National Treasury – Pensions Department		0.3	• Discrepancies between Budget Statement and the Printed Estimates • Variance between the Revenue Statement and Trial Balance Figures
7. Office of the Attorney General and Department of Justice		0.2	• Discrepancy Between Integrated Financial Management Information System and Revenue Statements Balances • Unsupported Regional Revenues Long outstanding reconciling items
Total		1,489	
1. Government Investment and Public Enterprises – The National Treasury	Adverse	31.9	• Inaccurate Schedule of Outstanding loans • Unresolved Prior Year Matters
1. State Department for Crop Development	Disclaimer	0.0	• Unremitted Revenue • Inaccurate Arrears of Revenue
Total		1,588	

Source: Office of the Auditor General | National Government Audit Reports

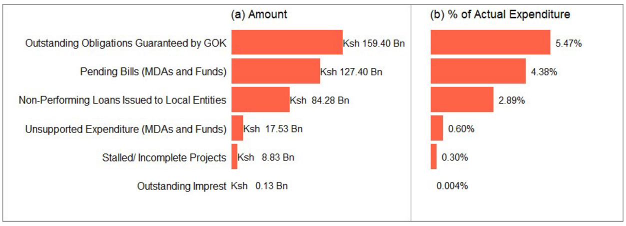
Total revenue receipts during 2018/19 amounted to Ksh 1.59 trillion, out of this, revenue statements worth Ksh 66.6 billion (4.2%) had unqualified opinion, Ksh 1.49 trillion (93.8%) had qualified opinion, Ksh 31.9 billion (2.0%) had an adverse opinion while one statement had a disclaimer of opinion. To a large extent, the majority of the receipts (93.8%) are in agreement with the public finance rules but contain some instances of misrepresentation of facts which even though are material, are not widespread or persistent. About 2% of the value of revenues was transacted in a manner exhibiting significant misrepresentation of facts with significant but widespread and persistent disagreements between the financial statements and the underlying books of accounts. As a result, these calls for considerable interventions by the management to rectify.

These overall audit findings regarding revenue statements characterize issues related to lack of transparency in revenue mobilization which manifest in under reporting especially for appropriations in aid (AiA), tax leakages and poor records for national assets and liabilities (see adverse opinion awarded to the Government Investment and Public Enterprises, among others.

Audit Queries on Expenditure

In 2018/19 a total of Ksh 398 billion of the spending was flagged as having been transacted unlawfully and/or ineffectively.

Figure 3: Audit queries and corresponding amounts, 2018/19



Source: Office of the Auditor General | National Government Audit Reports

The top three audited queries, outstanding obligations guaranteed by government (40%), pending bills (32%) and non-performing loans issued to the local entities (21.2%) added together constitute 93.2% of total audited queries. Unsupported expenditure, stalled/incomplete projects and outstanding imprest constitute the remaining portion.

Outstanding Obligations Guaranteed by GOK

Approximately, Ksh 159.4 billion was guaranteed by the government of Kenya to cover financial liability of its parastatals in case of default. Of importance to note is that the guaranteed obligation increases fiscal risk of contingent liabilities (loss) for the government in the event that the borrower (parastatals) defaults in payment of the debt.

Table 4: Outstanding Obligations Guaranteed by GOK as at 2018/19

Description	Amount (Ksh Bn)	Share (%)	Remarks
Kenya Airways	76.724	48.13%	Facing financial challenges
Kenya Electricity Generating Company PLC	43.035	27.00%	Facing financial challenges
Kenya Ports Authority (KPA)	34.061	21.37%	Loans issued under defunct authorities
Kenya Railways Corporation	4.603	2.89%	Facing financial challenges
Kenya Broadcasting Corporation (KBC)	0.357	0.22%	Facing financial challenges
East African Portland Cement PLC	0.346	0.22%	Court ruled that the company had no debt
Tana and Athi River Development Authority	0.279	0.18%	Under receivership
Total	**159.405**	**100.%**	

Source: Office of the Auditor General | National Government Audit Reports

Out of the total amount of Ksh 159.4 billion, Kenya Airways (48%), Kenya Electricity Generating Company PLC (27%) and Kenya Ports Authority (21.37%) make the first top three paratastals with a combined share of 96.5% of total queried amount. It is no wonder that the IMF is already putting pressure on the government to initiate structural reforms towards rationalization of parastatals, as this has been a recurring challenge for the country. On this point, the National Treasury recently provided updates on this exercise by identifying and clustering parastals in terms of whether they are profitable (commercially viable) such as KPA or the opposite, unprofitable and loss making such as KPLC and KBC. For the former, the objective of the government is to wean them off transfers and eventually stop any financial support as these parastatals are able to stand on their feet. As for the loss making ones, the National Treasury notes that it is going to gradually restructure them in a phased manner through divestiture, and privatization. There is however need for the government to make bold political decisions and dissolve the unredeemable parastatals in order to save the taxpayer from further losses.

Pending Bills (MDAs and Funds)

As at June 2019 unsettled financial obligation by the government entities across MDAs and some specific national funds totalled to Ksh 80.4 billion and are distributed as follows:-

Table 5: Distribution of Pending Bills across MDAs and Natioanl Funds, as at 2018/19

Description	Amount (Ksh Bn)	% of Total
1. Ministry of Health	41.93	52.10%
2. State Department for Devolution	6.74	8.37%
3. State Department for Correctional Services	6.28	7.80%
4. State Department for Interior	4.37	5.44%
5. Independent Electoral and Boundaries Commission	4.33	5.39%
6. State Department for Crop Development	4.09	5.09%
7. State Department for Regional and Northern Corridor Development	2.45	3.04%
8. State Department for Youth	1.91	2.38%
9. Parliamentary Service Commission	1.10	1.37%
10. The Judiciary	0.86	1.07%
Total	**80.48**	**100%**

Source: Office of the Auditor General | National Government Audit Reports

The Ministry of Health (MoH) had unsettled financial obligations worth Ksh 41.9 billion (52% of the total pending bills). Among other issues, late disbursement of funds is one of the main reasons attributed to failure to honour the financial obligations. Unsettled bills (delayed payments) in the case of the MoH and the other MDAs and national funds affects suppliers' and private sector cash flow and liquidity, and thus their smooth operation. Furthermore, these entities (MDAs and others) are obligated to make space for mandatory allocation of funds to be budgeted in the following financial year in order to offset these pending bills. This, roll over of spending to a new year is however a violation of the law given that it is only parliament that is legally mandated to approve appropriation of public funds.

Non-Performing Loans Issued to Local Entities

Non-performing loans (NPLs) issued to state-owned enterprises (SOEs) expected to be repaid had accumulated to Ksh 84.28 billion by June 2019 and are distributed as follows: -

Table 6: Distribution of Non-Performing Loans Issued to Local Entities as at 2018/19

Description	Amount (Ksh Bn)	Share (%)	Remarks
1 Kenya Airways	24.22	28.74%	Facing financial challenges
2 Lake Victoria South Water Services Board	13.12	15.57%	
3 Coast Water Service Board	12.24	14.52%	
4 Tanathi Water Services Board	9.71	11.52%	
5 Lake Victoria North Water Services Board	7.59	9.01%	
6 Tana Water Services Board	7.54	8.95%	
7 Mumias Sugar Company Limited	3.00	3.56%	
8 National Water Conservation & Pipeline Corp.	2.46	2.92%	Awaiting transfer of loan to Boards
9 National Irrigation Board	2.26	2.68%	Co. has requested for conversion to grant
10 Kenya Meat Commission	0.94	1.12%	Facing financial challenges
17 Miwani Sugar Company (1989) Ltd	0.02	0.02%	Facing financial challenges
18 Miwani Outgrowers Mills Limited	0.01	0.01%	Company is dormant
Total	84.28	100%	

Source: Office of the Auditor General | National Government Audit Reports

The leading SOEs with substantial quantum of NPLs are Kenya Airways (Ksh 24 Bn), Lake Victoria South Water Services Board (Ksh 13 Bn), Coast Water Service Board (Ksh 12 Bn), Tanathi Water Services Board (Ksh 9.7 Bn) and Lake Victoria North Water Services Board (Ksh 7.6 Bn). In fact, the NPLs for the top five SOEs make almost 80% of total NPLs.

The audit findings note that some of the of the entities given loans, continue to perform dismally and require government bailouts. Non-repayment of the loans has led to continued write offs of the loans as bad debts and eventual loss of public funds.

Unsupported Expenditure

Table 7: Unsupported Amount (MDAs) as at 2018/19

Description	Ksh Bn	Share (%)
1. State Department for ICT	12.747	74.43%
2. State Department for Crop Development	2.821	16.47%
3. Ministry of Health	0.336	1.96%
4. Parliamentary Service Commission	0.324	1.89%
5. State Depart. for Public Service & Youth	0.199	1.16%
	....	....
Total	17.126	100%

Source: Office of the Auditor General | National Government Audit Reports

MDAs with highest unsupported spending are: State Department for ICT (74%), State Department for Crop Development (16%) and Ministry of Health (2%). Failure by the entities to fully support payments and / or reconcile the records casts doubt on the authenticity of the reported expenditure. In some cases, this implies that goods and services in the MDAs mentioned in table 7 may not be verified as received.

Stalled/ Incomplete Projects

In 2018/19, the total queried amounts on stalled and incomplete projects amounted to Kshs.8.8 billion as seen in the table below.

MDA	Queried Amount (Ksh Bn)	Stalled/ Incomplete Projects
1. State Department for Regional and Northern Corridor Development	3.669	Advance payments for Kimwarer Multipurpose Dam Development Project and Sigor Wei Wei Project
2. The Judiciary	3.492	Delayed completion of thirty-nine courts
3. State Department for Public Works	0.802	Several stalled and incomplete projects: • Voi Pool Housing • Mathare Nyayo Hospital • Headquarters for Nyandarua County at Ol Kalou • Nyanza Headquarters • Kagumo Teachers Training College
4. Ministry of Health	0.745	Upgrading of Othaya District Hospital
5. State Department for Vocational and Technical Training	0.046	Kakrao Technical Training Institute abandoned
6. State Department for Early Learning & Basic Education	0.028	Contractor had abandoned the construction at Kaimosi Teachers Training College after being paid Kshs.27,749,758
7. State Department for Irrigation	0.023	Stalled projects & dry boreholes for schools (Ksh 16.7 Mn) Construction of Lakasuyuni Water Pan (Ksh 6.3 Mn

8. State Department for Mining	0.021	Head Office refurbishment
Total	8.826	

Stalled projects are a typical example of cases of no value for money with major opportunity cost implications. For all the stalled/incomplete projects flagged in the table above, it implies that ineffective use of public funds as the projects are not realizing their intended purposes. The two biggest culprits are the State Department for Regional and Northern Corridor Development and Judiciary. This is a serious indictment on the governments' planning and budget decisions. It also exposes lack of due diligence and appraisal of projects' viability on the part of government, with the hope that this will be redressed following the recently established of Public Investment and Management Unit (PIMU) at the National Treasury.

Key Messages

The National Treasury in collaboration with relevant stakeholders should ensure that the IFMIS balances with balances reflected in the financial statements and reporting templates configured to conform with the system in order to enhance the accuracy, in the financial controls and reporting.

MDAs should put in place strict measures to minimize the occurrence of pending bills. Failure to settle the bills has had an effect of withholding circulation of cash in the economy and affects the smooth operations of suppliers and Small Medium Enterprises (SMEs). All these factors viewed holistically call for the Executive to put in place strict measures, including budget controls to minimize the occurrence of pending bills.

MDAs should further strengthen internal control systems in order to give an assurance on the effectiveness of the application of public funds and manage related risks, public entities should strengthen the internal controls, in accordance with the provisions of Section 7(1)(a) of the Public Audit Act, 2015.

Parliament should strengthen the sanction enforcement mechanisms and follow up on the implementation of its audit recommendations for punishment of those culpable.

Ensure Unresolved Prior Year Audit Issues are addressed and the Lag in the timing of the Audited Accounts reduced: National Assembly should put in place measures to ensure that audit reports are approved and reviewed at least within a year which is instrumental in ensuring that the unresolved prior year issues are adequately addressed.

The National Treasury should ensure more realistic and effective forecasts of revenue and cash flows. The revenue shortfall is a critical contributor to delayed exchequer releases and budget under absorption. In order to enhance the quality and accuracy of fiscal forecasting, there is need to ensure greater coordination between the National Treasury and other stakeholders contributing critical information and macro-economic data for fiscal forecasting, especially the Kenya Revenue Authority (KRA).

MDAs should adopt a more rigorous criteria in determining the advancement of additional loans. This is important in order to minimize awarding loans to underperforming institutions which results to continued write offs of the loans as bad debts and eventual loss of public funds.

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