Institute of Economic Affairs

Analysis of National Government Audit Reports FY 2019/20

Key messages

- In 2019/20, there has been an overall improvement in the way the financial statements were prepared which is attributed to use of IFMIS, guidance by The National Treasury through circulars and issuance of reporting templates to Ministries, Departments and Agencies (MDAs) by the Public Sector Accounting Standards Board (PSASB). The presentation of the financial statements is however, still below expectations when viewed holistically.

- In 2019/20, expenditure worth Ksh 14 billion was without supporting documentation thus casting doubt on the authenticity of the reported expenditure. It is also an indication of weak internal controls and governance in the entities affected.

- The audit also revealed numerous instances where prior year audit issues had not been resolved. Failure to resolve audit issues may result in loss of public funds especially where the issues involve irregular use of public resources.

- There is inadequate effective mechanisms (both at the oversight institutions such as National Assembly but also within the respective MDAs) to enhance further follow up on the implementation of audit recommendations to address the recurrence of audit queries in subsequent audit reports due to lack of adequate action.

- Failure to enforce the requisite sanctions has led to perennial failure by some Accounting Officers to adequately account for the management and use of public resources.

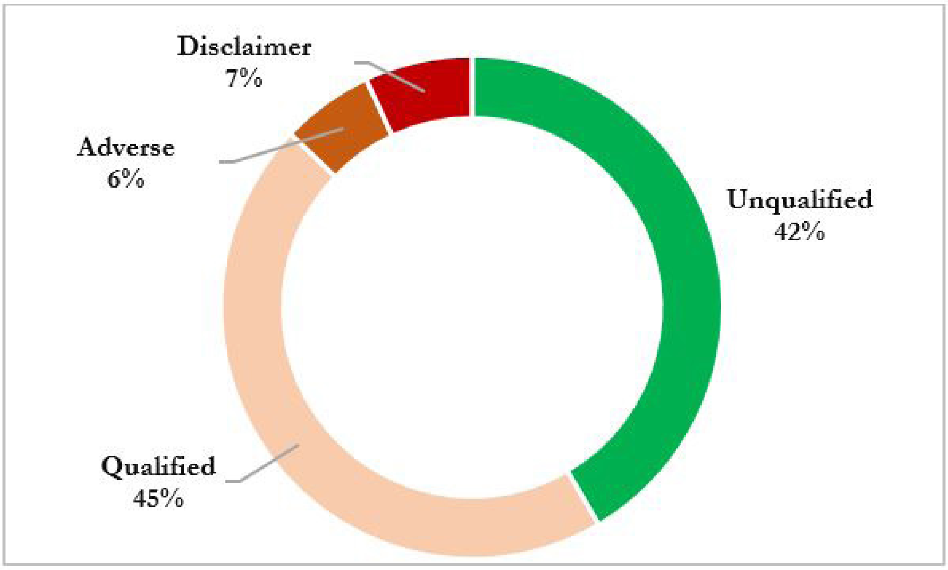
- Under-absorption of the budget has been on average at 8.2% of the gross estimated expenditure in the last five (5) years implying that some development programmes and delivery of services were not implemented as planned. This has been mainly been caused by overoptimistic revenue targets leading to shortfalls in revenue and hence delays in the disbursements to respective entities.

- State Owned Enterprises (SOEs) have continued to receive additional loans from government even when they are underperforming, thereby casting doubt on the criteria used to determine the advancement of additional loans.

- Various Ministries, Departments and Agencies (MDAs) are encumbered by huge pending bills, mainly attributed to inadequate exchequer releases and lack of vital supporting documents such as purchase orders, delivery notes, inspection and acceptance certificates among others. Failure to settle the bills during the year to which they relate adversely affects the subsequent year's budgeted programmes as it may lead to reallocation of funds or non-delivery of critical services

- The benefits of IFMIS are yet to be fully realized, numerous instances are noted where balances reflected in the financial statements and amounts extracted from IFMIS had huge variances when ordinarily the balances should be the same thus casting doubt on the accuracy of the system.

Figure 1: Overall Audit Findings, 2019/20



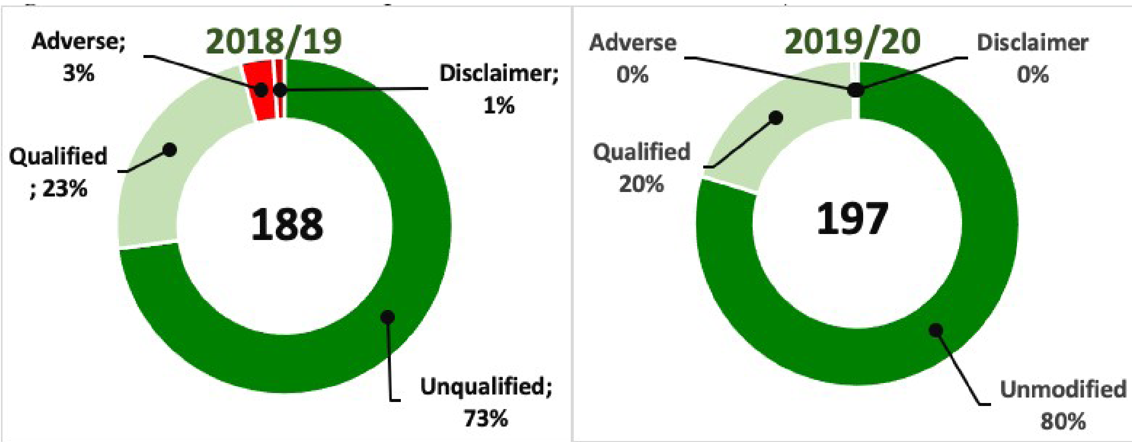
Source: Office of the Auditor General | National Government Audit Reports

- o A total of 156 financial statements[1] were audited in 2019/20
- o 42% of the statements were awarded unqualified opinion meaning that the statements presented a true and fair view of the financial position of the entities
- o Almost half of the statements (45%) were qualified, the statements contained significant misrepresentation of facts albeit not widespread
- o 6% of the statements were issued with an adverse opinion, the statements contained serious misrepresentation of facts which were widespread and persistent
- o 7% of the statements had a disclaimer of opinion, the statements exhibited serious and significant misrepresentation of facts which were widespread and persistent arising from inadequate information, limitation of scope, inadequacy or lack of proper records such that an opinion on the financial operations could not be expressed

[1]Excluding donor funded projects

Figure 2: Donor Funded Projects

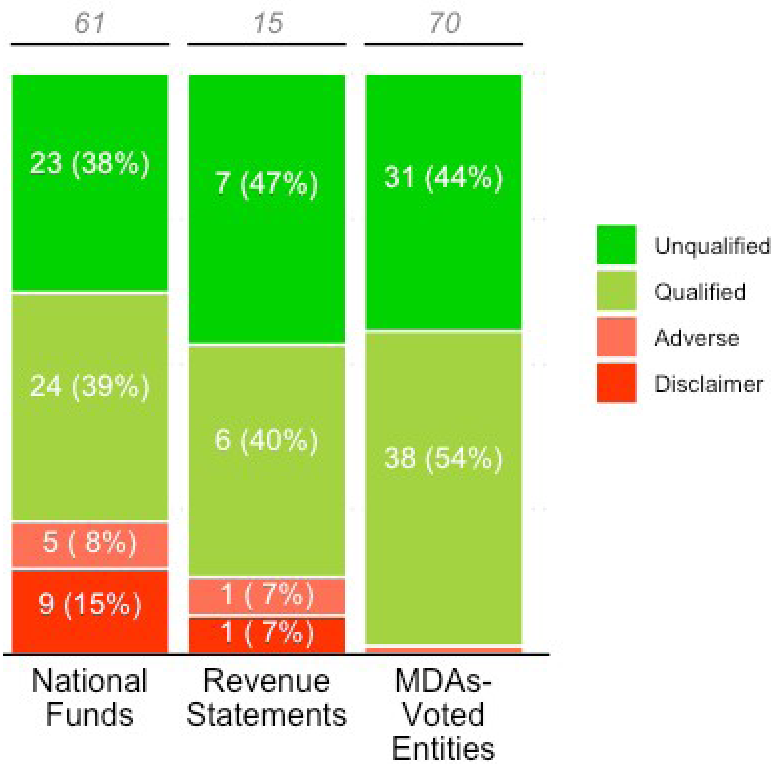
Approximately 197 donor projects were assessed in 2019/20 compared to 188 in the previous year



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

There is a huge improvement in the performing of Donor Funded Projects; none of the project was awarded an adverse opinion nor disclaimer in 2019/20 which is explained by relatively stricter monitoring of the projects and monitoring and evaluation of the projects has helped improve the reporting and financial management.

Figure 3: Breakdown of Audit Opinions, 2019/20



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

Overall

- o National Funds relatively exhibit poorer performance compared to MDAs[2] and Revenue Statements
- o Nearly a quarter (23%) of the statements for the National Funds had adverse or disclaimer of opinion compared to 14% for Revenue Statements and 2% MDAs.
- o More than half (38 out of 70) of the statements for MDAs were awarded qualified opinion

Table 1: Financial Statements with Adverse Opinion, 2019/20

MDA/Fund	Recurrence
1. Ministry of Health	✗
2. Kenya Health Sector Programme Support III – DANIDA	✗
3. Consolidated Fund Services – Public Debt	✓
4. Revenue Statements – Government Investments and Public Enterprises	✓
5. Consolidated Fund Services – Pension and Gratuities	✓
6. Rural Enterprise Fund – The National Treasury	✓
7. Asian officers Family Pension Fund - The National Treasury	✓
8. Veterinary Services Development Fund - State Department for Livestock	✗
9. Agricultural Information Resource Centre Revolving Fund - State Department for Crop Development	✗
10. Youth Enterprise Development Fund - State Department for Youth	✗

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

Atleast 10 public entities had adverse opinion in 2019/20, denoting poor financial management. Out of these, entities that have continued to be awarded this opinion include the financial statement for the public debt, Government Investments and Public Enterprises, Consolidated Fund Services – Pension and Gratuities, Rural Enterprise Fund – The National Treasury and Asian Officers Family Pension Fund - The National Treasury.

Table 2: Financial Statements with Adverse Opinion, 2019/20

MDA/Fund	Recurrence
1. Statement of Outstanding Obligations Guaranteed by the Government of Kenya - The National Treasury	✗
2. Government Clearing Agency Fund – The National Treasury	✓
3. Kenya Local Loans Support Fund - The National Treasury	✓
4. Stores and Services Fund – State Department for Public Works	✓
5. Land Settlement Fund - Ministry of Lands and Physical Planning	✓
6. Revenue Statements – State Department for Crop Development	✓

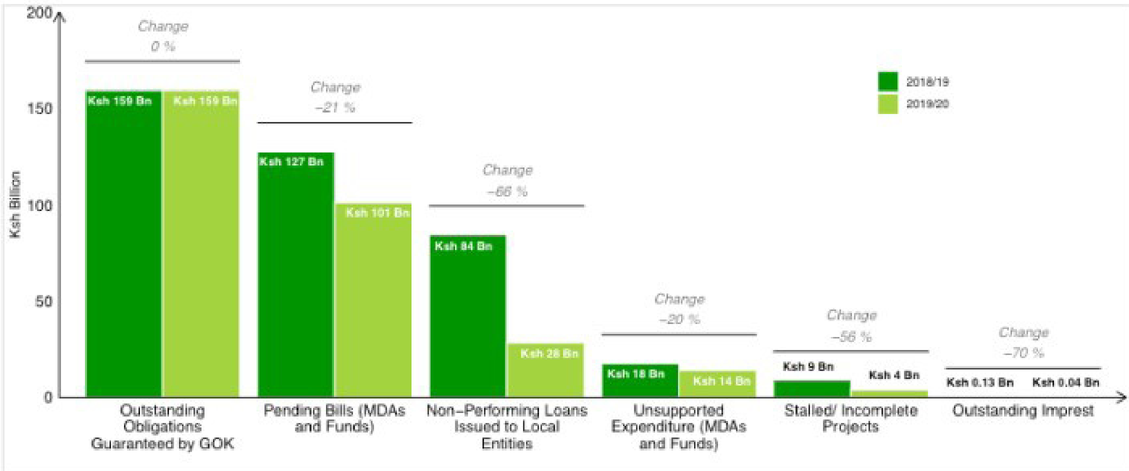
[2]Ministries, Departments and Agencies (MDAs)

7. Strategic Food Reserve Trust Fund - State Department for Crop Development	✓
8. Co-operative Societies Liquidation Fund – State Department for Co-operatives	✗
9. Management and Supervision Fund - State Department for Co-operatives	✗
10. Uwezo Fund – State Department for Gender	✓
11. Mechanical and Transport Fund - National Youth Service – State Department for Public Service	✓

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

It is also observed that most funds receiving this type of opinion are funds managed under the National Treasury they include: - Government Clearing Agency Fund – The National Treasury and Kenya Local Loans Support Fund - The National Treasury. Majority of the entities (8 out of 11) are consecutively being awarded this type of audit opinion thus depicting weak internal control systems and pervasiveness.

Figure 4: Distribution of queried amount on expenditure



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

In 2019/20, approximately Ksh 306 billion of the funds was established to have neither been spent lawfully nor effectively. However, this represents and improvement from Ksh 397 billion in the previous year. There was improved performance across pending bills, Non-Performing Loans, Unsupported expenditure, Stalled/Incomplete and Outstanding Imprests.

Table 3: Outstanding Obligations Guaranteed by Government

Description	2019/20[3] Ksh Bn	Remarks
1. Kenya Airways	76.724	Facing financial challenges
2. Kenya Electricity Generating Company PLC	43.035	Facing financial challenges

[3]MDAs did not prepare and submit for audit, their respective statements of outstanding obligations guaranteed by the Government of Kenya as at 30 June, 2020 contrary to Sections 81(1) and 81(2) (c) of the PFM Act, 2012.

3.	Kenya Ports Authority	34.061	Loans issued under defunct Authorities
4.	Kenya Railways Corporation	4.603	Facing financial challenges
5.	Kenya Broadcasting Corporation (KBC)	0.357	Facing financial challenges
6.	East African Portland Cement PLC	0.346	Court ruled that the Company had no debt
7.	Tana and Athi River Development Authority	0.279	Under Receivership
	Total	**159.41**	

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

Kenya Airways, Ken Gen and Kenya Ports Authority are the leading State-Owned enterprises (SOEs) with outstanding obligations guaranteed by government. Majority of these SOEs continue to face significant financial challenges.

Table 4: Non-Performing Loans Issued to Local entities

Description		Ksh Billion	
		2018/19	2019/20
1.	Kenya Airways	24.22	?
2.	Kenya Electricity Generating Company PLC	13.12	2.03
3.	Coast Water Service Board	12.24	6.75
4.	Tanathi Water Services Board	9.71	4.38
5.	Lake Victoria North Water Services Board	7.59	2.68
6.	Tana Water Services Board	7.54	1.85
7.	Mumias Sugar Company Limited	3.00	3.00
8.	National Water Conservat. & Pipeline Corp.	2.46	2.46
9.	National Irrigation Board	2.26	2.26
10.	Uchumi Supermarket	-	1.20
11.	Kenya Meat Commission	0.94	0.94
12.	Agricultural Finance Corporation	0.48	?
13.	Water Resource Management	0.36	0.36
14.	East African Sugar Industries Ltd, Muhoroni	0.18	0.18
15.	Miwani Sugar Mills Limited	0.08	0.08
16.	Kenya Urban Transport Various Towns	0.04	0.04
17.	Halal Meat Products	0.03	0.03
18.	Miwani Sugar Company (1989) Ltd	0.02	0.02
19.	Miwani Outgrowers Mills Limited	0.01	0.07
Total		**84.28**	**28.28**

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

Despite the reduction in the overall amount of the Non-Performing Loans issued to local entities, from Ksh 84.3 billion to Ksh 28.3 billion, there have been new entrants such as Uchumi Supermarket with a loan of Ks 1.2 billion. Other entities such as Kenya Airways and Agricultural Finance Corporation are missing with not clear updates on their status as of 2019/20.

It can still be observed that most entities facing challenges in servicing of their loans from government are mainly Water Service Boards and Sugar Companies thus calling for further investigation to ascertain their viability.

Table 5: Incomplete/Stalled projects

Description	2019/20 (Ksh Billion)
1. State Department for Regional and Northern Corridor Development	3.49
2. The Judiciary	0.1
3. State Department for Public Works	0.1
4. Drought Resilience and Sustainable Livelihoods Programme	0.100
5. State Department for Correctional Services	0.022
6. Uwezo Fund	0.020
7. Prison Industries Revolving Fund	0.015
8. State Department for Fisheries, Aquaculture and The Blue Economy	0.0094
Total	**3.9**

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

Kimwarer Dam development project under the State Department for Regional and Northern Corridor Development has been pending despite payment of Ksh 3.49 billion. Other leading projects that are incomplete beyond their timelines as stipulated in the contracts include; The Judiciary (Ksh 0.1 billion), State Department for Public Works (Ksh 0.1 billion) and Drought Resilience and Sustainable Livelihoods Programme (Ksh 0.1 billion).

Table 6: Outstanding Imprests

MDA	Ksh Mn
1. Parliamentary Service Commission	13.8
2. Ministry of Health	10.4
3. State Department for Labour	10.3
4. The National Land Commission	1.2
5. State Department for Infrastructure	1.1
6. State Department for Broadcasting and Telecommunications	0.8
7. State Department for Vocational &Technical Training	0.5
8. State Department for East African Community	0.2
9. Ministry of Lands and Physical Planning	0.1
Total	**38.3**

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

It is evident that a number of MDAs have failed to adhere to financial rules and regulations regarding the management of imprests. In 2019/20 a total of Ksh 38.3 million value of imprests was not surrendered due to weak control measures. It is also noted that during the year under audit, some entities did not avail breakdowns of the reported amounts relating to imprests and advances.

Compliance and Governance Issues

The weaknesses revealed by the compliance audits during 2019/20 include: -

- Non-compliance with the Public Procurement and Asset Disposal Act, 2015 and the Public Procurement and Disposal Regulations, 2006.

The main issues include the following:

- Contract and Tender documents were not provided for audit
- Use of non-competitive procurement practices
- Goods received were not inspected or taken on charge in the stores
- Irregular variations of contracts

- Value for Money Issues

  - Delays in projects completion
  - Unapproved over expenditures
  - Idle cash in bank accounts
  - Unauthorized allowances

- Other Compliance and Governance Issues

  - Fixed assets registers not in existence or poorly maintained
  - Non-establishment of Audit Committees
  - Ineffective Internal Audit and Audit Committees
  - Entities not maintaining documented enterprise wide risk management process
  - Non-establishment of IT Strategic Committees

The Equalisation Fund

The National Treasury had not remitted the remaining balance of Kshs.14.5 billion to the Fund as at 30 June, 2020 and is, therefore, in breach of Article 204(1) of the Constitution. Given the low level of disbursements as indicated above, the country is not likely to achieve the objectives of the Equalisation Fund, which is to improve the quality of requisite services in the marginalized areas within the set timelines, as envisaged by the Constitution.

Underfunding of the Approved Expenditure

Table 7: Underfunding of Approved Expenditure, 2019/20

Description	Approved Net Expenditure (Ksh Billion)	Actual Issues (Ksh Billion)	Underfunding (Ksh Billion)	% Variance
Recurrent	1,076	1,030	46	4%
Development	440	386	53	12%
County Governments	348	316	32	9%

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

In 2019/20, development budget was underfunded by 12% mainly due to constraints in revenue and delayed disbursement of donor funds. This is likely to affect the rate of development in the Country as envisaged in the National Development Plan, Vision 2030. Underfunding on recurrent expenditure of 4% is also likely to have negatively affected the timeliness and quality of services delivered to the citizens during the year. Overall, counties are disproportionately delayed compared to National government. Consistency in the shortfall in revenue is an indicator of lack of comprehensive revenue forecasting indicating poor budgeting which in turn has led to disruptions in budget implementation.

Ineffectiveness and inefficiency of the IFMIS

Balances reflected in the financial statements and amounts extracted from IFMIS have huge variances pointing to both control weaknesses in the system and transactions processed manually outside the system. The discrepancies are of material concern on the effectiveness and efficiency of the system. It may also be an indicator to lack of adequate internal controls and governance where supervision nor consistent monthly reconciliations.

Unresolved Prior Year Audit Issues

Numerous instances where prior year audit issues had not been resolved by the concerned entities. Such issues include, instances where no supporting evidence were availed. Failure to resolve audit issues may result in loss of public funds especially where the issues involve irregular use of public resources.

Recommendations

- National Assembly should develop an effective mechanism for follow up on implementation of audit recommendations to address the recurrence of audit queries in subsequent audit reports due to lack of adequate action.

- National Treasury should invoke sanctions to public entities that have perennially failed to adequately account for the management and use of public resources address cases of fiscal indiscipline including misallocations, wastage of resources and lack of value for money in implementation of projects.

- National Assembly should ensure MDAs have rigorous criteria used to determine the advancement of additional loans to State Owned Enterprises (SOEs) to minimize issuance of loans to Non-Performing Entities

- National Assembly and The National Treasury should enhance budgetary allocation for the Office of the Auditor General to enable it build technical capacity, expand its presence in the counties, widen the scope and comprehensiveness of audit and address other audit needs at the counties level. This is also key in ensuring timely reporting of the audit findings atleast withing six months as required by the PFM Act.

- National Treasury should enhance the quality and accuracy of fiscal forecasting. There is need to ensure greater coordination among stakeholders contributing critical information and macroeconomic data for fiscal forecasting, especially the Kenya Revenue Authority (KRA). This will ensure more realistic and effective forecasts of revenue and cash flows to facilitate smooth budget implementation.

- National Assembly should ensure that the Public Sector Accounting Standards Board has a functional Board of Directors to provide strategic direction and oversight.

- National Treasury should fast-track the migration from cash to accrual accounting for National and County Government entities, envisaged as critical for enhancing accountability in the use of public resources.

- The National Treasury which is charged with the governance of IFMIS should therefore, design and implement proper controls to ensure the completeness, accuracy and reliability of the financial information generated from the system and that there is value for money for the huge investment.

NOTES

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