Analysis of Nairobi City County Audit Report FY 2016/17

National Taxpayers Association (NTA)

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List of Abbreviations

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<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>CoK</td>
<td>Constitution of Kenya</td>
</tr>
<tr>
<td>IFMIS</td>
<td>Integrated Financial Management Information System</td>
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<tr>
<td>ISA</td>
<td>International Standards of Accounting</td>
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<tr>
<td>KShs</td>
<td>Kenya Shillings</td>
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<tr>
<td>MCA</td>
<td>Members of County Assembly</td>
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<tr>
<td>OAG</td>
<td>Office of the Auditor General</td>
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<tr>
<td>PAC</td>
<td>Public Accounts Committee</td>
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<td>PFMA</td>
<td>Public Finance Management Act 2012</td>
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<td>PSASB</td>
<td>Public Sector Accounting Standards Board</td>
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Executive Summary

Below are the findings of the analysis of the audit report for the Nairobi City Assembly for the FY 2016/17;

- Nairobi City County Assembly had an *Adverse Opinion* on the expenditure/ management of resources of the County Assembly

- The following are the basis for the Adverse Opinion are indicated in the audit report;
  - *Failure of the Audit Committee to hold meetings as required by the PFM Regulations (County Government), 2015;*
  - *Non-Disclosure of Non-Current Assets Balances;*
  - *Misclassification of Expenditure;*
  - *Un accounted for Receipts;*
  - *Over-Expenditure;*
  - *Under-Expenditure;*
  - *Un approved Budget Re-allocation*
  - *Unsupported expenditure;*
  - *Pending Account Payables; and*
  - *Variations in amount spent on compensation of employees*

- Other than the matters that formed the Auditor’s basis for Adverse Opinion, there are, in the opinion of the auditor, key audit matters in the FY 2016/17 report.

- The Financial Statements of Nairobi City County Assembly for the period under review was audited independent of the Financial Statements of Nairobi City County Assembly Service Board Car Loan Scheme Fund

- The County Assembly did not supply the Office of the Auditor General with all the supporting documentation necessary to undertake its work.

- Some of the audit queries (*Under-expenditure, over-expenditure, Un accounted for Receipts, Variations in amount spent on compensation of employees*) remain outstanding. They were raised in the FY 2015/16 report.
Background

An audit report is the independent examination of the financial statements and non-financial information of the government agency in order to ascertain fairness and accuracy of representation of the transactions undertaken by the government entity in this case, Nairobi City County Assembly1.

Section 164 of the Public Finance Management Act, 2012 (PFM Act 2012) requires the Accounting Officer of the public bodies to, upon completion of the financial year, to submit all financial reports of that concluded fiscal year to the Office of the Auditor General (OAG) within three months after the end of every financial year. The Audit reports are required by law to be made public six months (6) after the end of a financial year.

This is a review of the Nairobi City County Assembly Audit report produced by the Office of the Auditor General (OAG) of Kenya for the year ended June 2017 (FY 2016/17). This is a financial report aimed at checking the accuracy of financial statements prepared by Nairobi City County Assembly and not a report of corruption

It is important to highlight that the audit process does not involve assessment of every single transaction by the entity. It is rather based on risk evaluation as determined by the auditor’s objective judgment. The audit therefore promotes due diligence and accountability given that performance of agencies (in this case, county government) informs the budgeting process.

The Office of the Auditor General is established pursuant to article 229 of the Constitution of (CoK) 2010. The OAG is mandated with auditing of both the national and county financial statements. With respect to timelines, article 229 (4) provides that within six months after the end of each financial year, the Auditor-General shall audit and report, in respect of that financial year, on various accounts including those of the County. The OAG gives is findings in the form of certification or opinion. This is guided by the International Standards of Accounting (ISA).

The objective of audits on County financial statements is to assess whether or not public money entrusted to, in this case the, County Assembly were applied lawfully and in an effective way2 (CoK

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1 Parliamentary Initiatives Network (2016). A Guide to Understanding National and County Audit Reports
2 Article 229(6) of the Constitution of Kenya, 2010
The OAG is mandated to provide assurances on accountability of public resources through; certification of accounts, continuous audit presence and service delivery to all Kenyans.

The analysis focuses on the Nairobi City County Assembly audit queries raised by the office of the auditor general in fiscal year 2016/17. In addition to reviewing the audit reports for FY 2016/17, the review also looked at the report of the County Assembly’s Public accounts Committee on review of the FY 2015/16 audit report.

Types of Audit Opinion

Upon undertaking an audit process, the OAG gives findings in the form of certification or opinion. These opinions only apply to financial audits. Whereas different jurisdictions might have variances on how some aspects of the opinions are defined, the OAG adopts the definition provided for by the International Standards on Auditing (ISA 705).

Audit Opinions are broadly categorized into two; Modified Opinion; and Unqualified Opinion. Modified Opinion can either be in the form of a qualified opinion, an adverse opinion or a Disclaimer of opinion. The decision regarding which type of modified opinion is appropriate depends upon:

- the nature of the matter giving rise to the modification, that is, whether the financial statements are materially misstated, (the transactions reflected are significantly affected by error or lack of sufficient audit evidence);
- the auditor’s professional judgement about the pervasiveness of the effects of the matter on the financial statements

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3 Pervasiveness refers to the spread of the error and how frequently it occurs in the financial statements
**Unqualified Opinion** - This is a clean opinion, expressed when the auditor concludes that the financial statements give a true and fair view (or are presented fairly, in all material respects) in accordance with the identified financial reporting framework;

**Qualified Opinion** – This is a modified opinion that is arrived at when the specific element(s) in the financial statements is material but not pervasive or the auditor is unable to obtain sufficient appropriate audit evidence but concludes that such undetected misstatement; if any, could be material but not pervasive;

**Adverse Opinion** is an opinion expressed when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements; and

**A disclaimer Opinion** is expressed when the auditor is unable to obtain sufficient audit evidence on which to base the opinion, and the auditor concludes that the possible effects of undetected misstatements on the financial statements, if any, could be both material and pervasive. In effect, the auditor is claiming that the financial statements should not be relied upon in any part, because the entity failed to provide the necessary audit evidence to facilitate the audit process, *thus enabling him to form an opinion.*

*Source: ISA 705*
Introduction

The analysis on the county Assembly seeks to assess adherence of the county transactions and management to the Constitution of Kenya 2010, Public Finance Management, the Public Audit Act 2015 and prudent management of public resources.

The Audit report shows that the Nairobi City County Assembly had an Adverse Opinion on the expenditure/ management of resources of the County Assembly. The OAG provides seven reasons underpinning the basis for Adverse Opinion.

A review of the OAG report for the period under review, indicates that the County Assembly’s total budget was Kshs 1.67 billion, out of which Kshs, 1.4 billion was received and spent representing 83.8% absorption rate.

Audit Queries

An analysis of the OAG report shows that the auditor general’s concerns on Nairobi County Assembly were:

- Failure of the Audit Committee to hold meetings as required by the PFM Regulations (County Government), 2015;
- Non-Disclosure of Non-Current Assets Balances;
- Un accounted for Receipts;
- Casting error;
- Omitted Expenditure;
- Over-Expenditure
- Under-Expenditure;
- Unsupported expenditure;
- Un-accounted for Provisional Sums
- Pending Account Payables
- Variations in amount spent on compensation of employees among other queries.

The following section looks into details of concerns raised by the OAG on the county assembly during the period under focus
Audit Committee Meetings

Section 155 of the Public Finance Management, Act 2012 provides that the county government entity makes appropriate arrangements for conducting internal audit according to guidelines issued by the Public Sector Accounting Standards Board. Further, Section 155(5) of the PFMA requires the County Government to establish an internal Audit Committee whose composition and functions are prescribed by the regulations. However, according to the auditor general’s report for FY 2016/17, it was established that despite the fact that the Nairobi City County Assembly complied with the law by having in place the said committee there was no evidence provided to indicate that Audit Committee met and conducted their business as required by law. This in deed was a breach of the provisions of section 172 of the Public Finance Management (County Government) Regulations, 2015.

Non-Disclosure of Non-Current Assets Balances

An analysis of the Audit report revealed that the statement of fixed assets provided by the County Assembly to the OAG only indicates the County Assembly’s total fixed assets as at the end of the FY 2016/17 were Kshs. 107.53 million. However, the audit report shows that these were fixed assets acquired during the FY 2016/17 only and as such the statements did not reflect the fixed assets that the county assembly acquired in the prior years pursuant to the Public Sector Accounting Standards Board (PSASB)’s reporting format.

In addition, the failure of Management of the County Assembly to provide the OAG with the Assets Register for audit verification on the authenticity of financial statements therefore raises transparency and accountability concerns on the part of the county assembly. The figure below shows the County Assembly’s summary of fixed asset;
From the figure above, it is evident that the summary of the fixed register provides very scanty information with respect to the County Assembly’s fixed Asset portfolio. From the note provided at the end of the table, the Assembly indicates that the information supplied related to the cumulative cost of all the assembly’s assets (bought and inherited since its inception). However, this is not supported by the data in the summary table. For instance, there is no information relating to the cost assets acquired or owned by the assembly as at FY 2015/16 whose column appears blank. Again, it is not clear whether the difference between the balances provided under the column on historical cost C/F for FY 2016/17 and the additions during the year FY 2016/17 represents the cost of fixed assets for all the other years since inception of the county assembly but with the exclusion of the period under review.

**Pending Account Payables**

The excerpt below shows that during the period under review, the County Assembly’s pending account payables was Kshs. 79.94million. However, the audit report indicates that the supporting documents provided by the Assembly on the same, shows that the pending account payables figure for the period was Kshs. 182.6million thus resulting to unsupported difference of Kshs. 102.7million.
Further, an analysis of the pending accounts payable schedule indicates pending bills in respect of acquisition of assets worth Kshs. 130.3 million and unanalyzed withholding tax worth Kshs. 1.91 million. The failure on the part of the assembly to supply documentation in support of some of the pending account payables therefore casts the authenticity of pending bills balances of Kshs. 79.9 millions in doubt.

**Over Expenditure**

The Audit reports shows that during the FY 2016/17, the County Assembly had over expenditure amounting to Kshs. 113.97 million. In addition, the Assembly made overpayment worth Kshs. 5.2 million in respect of the Speakers house contrary to the advisory by the *Salaries and Remuneration Commission (SRC)*. The Assembly paid Kshs 350,000 per month for 26 months for the Speaker’s house whose rental value according to the SRC advisory⁴ was to be not more than Kshs. 150,000 per month. It must be noted that the query on over-expenditure was raised by the auditor even in

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⁴ The SRC Circular SRC/TS/CGOV/3/61 dated 24th October 2016 limits the Speaker’s House rent to Kshs. 150,000 per month.
FY 2015/16 and not even the recommendations of the Public Accounts Committee on the review of the FY 2015/16 audit report prevented the assembly from overspending.

**Figure 3: Summary of Over-Expenditure**

<table>
<thead>
<tr>
<th>Item</th>
<th>Budgeted Amount (Kshs.)</th>
<th>Expenditure (Kshs.)</th>
<th>Over Expenditure (Kshs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic Travel and subsistence</td>
<td>153,869,910.00</td>
<td>156,555,208.00</td>
<td>2,685,298.00</td>
</tr>
<tr>
<td>Printing, advertisement and information</td>
<td>-</td>
<td>9,919,595</td>
<td>0</td>
</tr>
<tr>
<td>supplies</td>
<td>9,919,595</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hospitality supplies and services</td>
<td>16,229,167.00</td>
<td>35,314,228</td>
<td>19,085,061.00</td>
</tr>
<tr>
<td>Insurance costs</td>
<td>66,094,242.00</td>
<td>72,736,784</td>
<td>6,642,542.39</td>
</tr>
<tr>
<td>Office and general supplies and services</td>
<td>8,876,363.00</td>
<td>43,197,828</td>
<td>34,521,434.57</td>
</tr>
<tr>
<td>Rentals of Produced Assets</td>
<td>15,555,000.00</td>
<td>19,782,000</td>
<td>4,227,000.00</td>
</tr>
<tr>
<td>Basic Salaries of Temporary Employees</td>
<td>72,647,000</td>
<td>72,687,700</td>
<td>40,700.00</td>
</tr>
<tr>
<td>Personal Allowances paid as part of salary</td>
<td>225,361,061</td>
<td>243,848,729</td>
<td>18,487,668.00</td>
</tr>
<tr>
<td>Personal Allowances paid as reimbursement</td>
<td>0</td>
<td>7,752,000</td>
<td>7,752,000.00</td>
</tr>
<tr>
<td>Pension and other Social Security</td>
<td>125,416,155</td>
<td>134,593,617</td>
<td>9,177,462.00</td>
</tr>
<tr>
<td>contributions</td>
<td>0</td>
<td>1,434,520</td>
<td>1,434,520.00</td>
</tr>
<tr>
<td>Other Personnel Payment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>683,848,928</td>
<td>797,822,209</td>
<td>113,973,281</td>
</tr>
</tbody>
</table>

The decision of the Assembly to overspend is a manifestation of the fact that the County Assembly could have overfunded some expenditure items at the expense of the other. Some of the expenditure items such as *Personal Allowances paid as reimbursements, printing advertisement and information supplies, Other Personnel Payment*, were funded despite not being budgeted for.

In addition, the County Assembly budgeted Kshs. 88 million towards sitting allowances for its members but it emerged that the actual expenditure on sitting allowance amounted to Kshs. 100.3 million thus resulting to an over-expenditure of Kshs. 12.5 million, a complete non-adherence to budget and budgetary controls provided for by the PFM Act 2012. *(This is a case of Un approved Budget Re-allocation)*

**Unsupported Expenditure**

Expenditure amounting to Kshs. 115.29million did not have documentation to support the expenditure. The table below shows a summary of the Unsupported Expenditure by the County Assembly for the period under review;
Table 1: Summary of Unsupported Expenditure (Kshs. Millions)

<table>
<thead>
<tr>
<th>Audit Query</th>
<th>Total Expenditure</th>
<th>Supported Expenditure</th>
<th>Unsupported Expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-Disclosure of Current Asset Balances</td>
<td>107.53</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Un accounted for Receipts</td>
<td>1,447.00</td>
<td>1,446.10</td>
<td>0.90</td>
</tr>
<tr>
<td>unsupported Inter accounts borrowing</td>
<td>44.03</td>
<td>-</td>
<td>44.03</td>
</tr>
<tr>
<td>Compensation to Employees (payment to Lap fund)</td>
<td>780.48</td>
<td>710.12</td>
<td>70.35</td>
</tr>
<tr>
<td>Totals</td>
<td>2,379.05</td>
<td></td>
<td>115.29</td>
</tr>
</tbody>
</table>

Adapted from the 2016/17 OAG Audit Report for Nairobi City County Assembly

The Kshs. 115.29 million unaccounted for were on the following activities: Compensation to Employees (Payment to Lap Fund) at Kshs 70.35 million; Inter-account borrowing at Kshs.44.03 million and unaccounted for Receipts at Kshs. 900,000.

Under-Expenditure

A review of the assembly’s financial statements shows that the assembly had an approved budget of Kshs. 1.7 billion. However, according to the audit report, the Integrated Financial Management Information System (IFMIS) account analysis report showed that the Assembly had an under-expenditure amounting to Kshs.157.8 million. The under-expenditure is a manifestation of funds not utilized fully besides indicating that the approved programmes were not implemented despite funds being available.

Misclassification of Expenditure

An analysis of the financial statements supplied to the OAG shows that the assembly had other operating expenses under the use of goods and services vote amounting to Kshs. 166.7 million (as shown below). However, the same operating expenses have been captured under compensation of employees, uniforms and fuel, and oil and lubricants. This therefore makes it difficult to confirm the authenticity of the operating expenses.

Figure 4: Summary of Misclassified Expenditure
It is imperative for the county assembly to address the issues raised by the office of the Auditor General. In addition, the County Assembly’s Public Accounts Committee needs to take punitive action on the Accounting officers of the County Assembly under whose watch public funds are not prudently applied.
Concern and Recommendation

From the analysis above, it is clear that the county assembly engagements with respect to public finance management raises transparency and accountability concerns. Unlike in previous year, in which the county failed to address issues raised by the auditor general and further perpetrated some of the same issues of concern raised by the OAG, it is paramount that county Assembly consider addressing issues raised by the office of the auditor general conclusively in order to allow for prudent management of the limited resources for enhanced service delivery to the citizen of Nairobi County and Kenyans at large.
References


