

REPORT OF THE AUDITOR-GENERAL ON KENYA MEDICAL RESEARCH INSTITUTE (KEMRI) FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Disclaimer of Opinion

I have audited the accompanying financial statements of Kenya Medical Research Institute set out on pages 1 to 28, which comprise the statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, statement of cash flows and 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.

In addition, as required by Article 229(6) of the Constitution, I have not been able to obtain sufficient appropriate audit evidence to confirm that public money has been applied lawfully and in an effective way.

Basis for Disclaimer of Opinion

1.0 Excess Exchequer Development Releases

Included in the statement of financial performance for the year ended 30 June 2017 is GOK funding balance of Kshs.1,834,962,265. This includes an amount of Kshs.35,500,000 received as development exchequer from the Ministry of Health. However, a review of the Institute's budget and the Ministry of Health approved development budget for the institute revealed that the only amount budgeted for was Kshs.5,000,000 for perimeter wall fence in Taita Taveta and Kirinyaga. The excess development exchequer of Kshs.30,500,000 has not been explained or reconciled.

Consequently, the propriety of GOK funding of Kshs.30,500,000 for the period ending 30 June 2017 could not be confirmed.

2.0 Unsupported Sundry Income-Overheads

Included in the statement of financial performance for the year ended 30 June 2017 is sundry income of Kshs.138,596,264 and whose supporting documents were not availed for audit review.

Consequently, it has not been possible to confirm the accuracy and completeness of sundry income amount of 138,596,264 included in the statement of financial performance for the year ended 30 June 2017.

3.0 Unsupported Interest on Investment

Included in the statement of financial performance for the year ended 30 June 2017 is revenue from exchange transactions of Kshs.104,186,750. As shown in note 6 to the financial statements, this includes interest on investment of Kshs.6,313,232 made up of Kshs.5,072,850.97 and Kshs1,240,381 from Family bank and Kenya Commercial Bank respectively. However, contract documents and deposit certificates supporting the income were not available for review.

Consequently, it has not been possible to confirm the accuracy and completeness of the interest on investment balance of Kshs.6,313,232 included under revenue from exchange transactions in the statement of financial performance for the year ended 30 June 2017.

4.0 Human Resources

4.1 Two Thirds Basic Rule

Included in employee costs of Kshs.1,513,076,142 in the statement of financial performance for the year ended 30 June 2017 is personal emoluments of Kshs.824,788,456. A review of the Institute's payroll revealed that fifty (50) employees suffered deductions beyond a third (1/3) of their basic salary contrary to Public Service Commission human resource policies and procedures manual (sec Ci sub sec 3) which require employees to retain at least a third of their salary.

The Institute is therefore in breach of the Law.

4.2 Accumulated Leave

Included in employee costs of Kshs.1,512,531,437 in the statement of financial performance for the year ended 30 June 2017 is passage and leave allowance of Kshs.6,948,500. A review of the Institute's leave schedule revealed that employees were accumulating leave days beyond the allowed maximum of 45 days in a year thus contravening Public Service Commission human resource policies and procedure manual and KEMRI HR policy.

4.3 Unreconciled Staff Cost

Included in the statement of financial performance for the year ended 30 June 2017 is employee costs of Kshs.1,512,531,437. A review of the payroll summaries for the year under review showed an amount of Kshs.1,506,038,686 which when compared

against the financial statements figure of Kshs.1,512,531,437 results to unreconciled variance of Kshs.6,492,751.

Consequently, it has not been possible to confirm the accuracy, validity and propriety of the employee cost of Kshs.1,512,531,437 included in the statement of financial performance for the year ended 30 June 2017.

5.0 Collaborators' Funds

5.1 Overpaid Personal Emoluments

Included in Collaborators' Funds Collaborators' Funds of Kshs.4,461,927,815 in the statement of financial performance for the year ended 30 June 2017 is an amount of Kshs.3,253,118,910 in respect of staff costs comprising of Kshs.3,243,128,312.00 and Kshs.9,990,598 for external and internal funding respectively. However, a review of schedule supporting external funding of Kshs.3,243,128,312.00 revealed that the stated amount is net of Kshs.9,840,934 being overpayments on the same. The Institute has not explained this state of affairs.

5.2 Credits on Bank Charges

Included in Collaborators' Funds of Kshs.4,461,927,815 is also an amount of Kshs.2,156,804 in respect of bank charges comprising of Kshs.2,014,888 and Kshs.141,916 for external and internal funding respectfully. However, a review of schedule supporting external funding of Kshs.2,014,888 revealed that the stated amount is net of Kshs.368,553 being credits on the same. The Institute has not also explained this state of affairs.

Consequently, it has not been possible to confirm the accuracy, validity and propriety of the collaborators fund of Ksh.4,461,927,815 included in the statement of financial performance for the year ended 30 June 2017.

5.3 Overpaid Laboratory Supplies

Included in Collaborators' Funds of Kshs.4,461,927,815 is an amount of Kshs.93,172,932 in respect of Laboratory supplies comprising of Kshs.49,552,097 and Kshs.43,620,835 for external and internal funding respectively. However, a review of schedules supporting external funding of Kshs.49,552,097 revealed that the stated amount is net of Kshs.236,342 being overpayments on the same. The institute has not supported overpayments of Kshs.236,342 and the reason for the net off of the actual amount on Laboratory supplies.

5.4 Overpaid Travelling and Accommodations

Included in Collaborators' Funds Collaborators' Funds of Kshs.4,461,927,815 is an amount of Kshs.211,468,521 in respect of travelling and accommodation comprising of Kshs.162,006,661 and Kshs.49,461,860 for external and internal funding

respectively. However, a review of schedule supporting external funding of Kshs.162,006,661 revealed that the stated amount is net of Kshs.33,853 being overpayments on the same that has not been supported or explained.

5.5 Overpaid Other Operating Expenses

Included in Collaborators' Funds Collaborators' Funds of Kshs.4,461,927,815 is an amount of Kshs.821,797,042 in respect of other operating expenses comprising of Kshs.819,736,078 and Kshs.2,060,962 for external and internal funding respectively. However, a review of schedules supporting external funding of Kshs.819,736,078 revealed that the stated amount is net of Kshs.91,907,241 being overpayments on the same that has not been supported.

Consequently, it has not been possible to confirm the accuracy, validity and propriety of the collaborators fund of 4,461,927,815 included in the statement of financial performance for the year ended 30 June 2017.

6.0 Administrative Costs

6.1 Legal Expenses

Included in the administrative costs of Kshs.326,732,231 in the statement of financial performance for the year ended 30 June 2017 is Kshs.11,083,790.75 paid to private legal firms. However, the Institute had not sought approval and issuance of no-objection from the Attorney General's Office to continue using the services of the same private law firms.

Consequently, the institute did not comply with Attorney General's Circular reference AG/CON/6/D/144/VOL. II of 6th April 2017 on legal expenses and the propriety of the administrative costs of Kshs.326,732,231 included in the statement of financial performance for the year ended 30 June 2017 could, therefore, not be determined.

7.0 Cash and Cash Equivalents

7.1 Operating Unlawful and Undisclosed Bank Accounts

Included in the statement of financial position as at 30 June 2017 is cash and cash equivalents of Kshs.1,029,775,253. A review of bank accounts operated by the Institute revealed that the Institute operated a total of twenty five (25) bank accounts held in Kenya Commercial Bank of Kenya, Co-operative Bank of Kenya and Family Bank of Kenya without Treasury approval.

The Institute failed to comply with the Public Finance Management Act, 2012 Section 28(1) which require the National Treasury to authorize the opening, operational and closing of bank accounts and sub-accounts for all National Government entities.

Further, a review of bank accounts operated by the Institute and the supporting documents revealed that the Institute excluded from the cash and cash equivalents of Kshs.1,029,775,253 an amount of Kshs.22,331,178 for KEMRI-Oxford University as analysed below;

Account Name	Bank	Certificate No.	Account No.	Amount as per Cert
KEMRI-Oxford University	KCB	CERT1718814268	1179013859	Ksh22,331,178.90

It was also noted that RCTP Account No.1104166879 changed signatories in the course of the year. The Institute has neither explained why the amounts could not form part of cash and cash equivalent balance of Kshs.1,029,775,253 nor accounted for the transactions on these financial statements.

Consequently, it has not been possible to confirm the accuracy, validity and propriety of the cash and cash equivalent balance of Kshs.1,029,775,253 included in the statement of financial position as at 30 June 2017.

7.2 Bank Reconciliation

7.2.1 Exchequer Account 1104161362

The bank reconciliation statement for the exchequer cash book (**Account No.1104161362**) as at 30 June 2017, reflects payments in cash book not recorded in the bank statement totaling Kshs.27,322,287.51 which includes an amount of Kshs.45,459.43 in respect of stale cheques. No reason has been given for failure to replace the cheques or having the same credited back in the cash book. The statement also reflects receipts in the bank statement not recorded in the cash book totaling Kshs.657,747.20 out of which an amount of Kshs.108,145.27 has been outstanding for more than six months. No reason has been given for delay in entering the amount in the cash book. The statement further reflects payments in bank statement not in cash book totaling to Kshs.3,662,825.24 out of which Kshs.2,532,148.74 has been outstanding for more than six months. No reason has been provided for the delay in recording these payments in the cash book. The statement also reflects receipts of Kshs.194, 689.40 in the cash book but not recorded in the bank statement. No explanation has been given for the delay in recording the payments in the cashbook. The management has not provided an explanation on this state of affairs.

7.2.2 RGA Account No. 1104174529

The bank reconciliation statement for the RGA cashbook (**Account No. 1104174529**) as at 30 June 2017 reflects payments in cash book not recorded in the bank statement totaling Kshs.764,880 which includes an amount of Kshs.719,986 in respect of stale cheques. No reason has been given for failure to replace the cheques or having the same credited back in the cash book. The statement also reflects receipts in the bank statement not recorded in the cash book totaling

Kshs.7,892,608.10 out of which an amount of Kshs.2,335,462 has been outstanding for more than six months. No reason has been given for the delay in entering the amount in the cash book. The statement further reflects payments in bank statement not in cash book totaling to Kshs.1,082,963.60 out of which Kshs.254,388.30 has been outstanding for more than six months. No reason has been provided for the delay in recording these payments in the cash book. Also the statement reflects receipts of Kshs.1,917,994.70 in the cash book but not recorded in the bank statement. As in the previous instance, no explanation has been given for the inordinate delay.

7.2.3 KEMRI EAST AFRICA Account No.1128126671100

The bank reconciliation statement for the KEMRI East Africa cashbook (**Account No. 1128126671100**) as at 30 June 2017 reflects payments in bank statement not in cash book totaling to Kshs.68,255 out of which Kshs.63,910 has been outstanding for more than six months. No reason has been provided for the delay in recording these payments in the cash book.

7.2.4 KEMRI JICA Production Department Account 1104166194

The bank reconciliation statement for KEMRI JICA production department cashbook (Account 1104166194) as at 30 June 2017 reflects payments in cash book not recorded in the bank statement totaling Kshs.223,377.20 which includes an amount of Kshs.92,627.20 in respect of stale cheques. No reason has been given for failure to replace the cheques or having the same credited back in the cash book.

Consequently, it has not been possible to confirm the accuracy, validity and propriety of the cash and cash equivalent balance of Kshs.1,029,775,253 included in the statement of financial position as at 30 June 2017.

7.3. Unexplained Foreign Currency Translation Rate

Included in the cash and cash equivalents amount of Kshs.1,029,775,253 is an amount of Kshs.17,467,856 (€ 149,591.98) and Kshs.4,693,750 (\$46,044.24) and whose translation rate and reconciliations were not availed for audit review.

Consequently, it has not been possible to confirm the accuracy, validity and propriety of the cash and cash equivalent balance of Kshs.1,029,775,253 included in the statement of financial position as at 30 June 2017.

8.0 Unsupported Short Term Deposit

Included in the statement of financial position as at 30 June 2017 is short term deposits amounting to Kshs.530,000,000 which comprises of Kshs.500,000,000 invested in CBK Treasury bills and Kshs.30,000,000 invested in Kenya Commercial bank. Analysis of two years financial statements 2015/2016 and 2016/17 reflects a gap/deficit of Kshs.66,769,206 and Kshs.28,565,808 respectively. The management has not provided the basis of recognizing Kshs.530,000,000 as a surplus and thus

available for investment. Further, no Treasury approval has been provided for investing Kshs.30,000,000 in KCB. A further review of the end year support documents show that the bank confirmation Certificates from CBK showed a nil balance for the Treasury Bills investment of Kshs.500,000,000 while the certificate of balance availed for the fixed deposit account in KCB reflected Kshs.35,817,808.20. The Institute has not reconciled the resulting differences.

Consequently, the accuracy, validity and existence of the short-term deposit balance of Kshs.530,000,000 included in the statement of financial position as at 30 June 2017 could not be determined.

9.0 Trade and Other Receivables

9.1 Deposit with the Institute Lawyers

As reported in 2015/2016, trade and other receivables balance of Kshs.510,735,379 included in the statement of financial position as at 30 June, 2017 is net of an amount of Kshs.120,000,000 in respect of a deposit placed with the Institute of lawyers in the year 2000 while the Institute was following up issues related to the stalled residential staff housing project. Although the institute has fully provided for this amount as doubtful debts, the matter is still under police investigation. A further review of the statements indicates that the interest accumulated over time on the amount of Kshs.120,000,000 was not taken into account in arriving at the balance.

9.2 Temporary Imprest

The trade and other receivables balance of Kshs.510,735,379 as at 30 June, 2017 includes temporary imprests amounting to Kshs.18,308,554.60 which had not been surrendered at the close of the financial year. Further, this amount for unsurrendered imprests included Kshs.7,625,903.65 as advances to centres and long outstanding temporary imprest of Kshs.2,795,258.61 which relates to officers who have since left the Institute.

The Public Finance Management (National Government) Regulation, 2015 Section 93(5) requires a holder of temporary imprest to account or surrender the imprest within seven working days after returning to duty station.

Consequently, the management failed to comply with the Public Finance Management (National Government) Regulation, 2015 Section 93(5) on requirement of temporary imprest.

9.3 Unsupported Impairment Allowance

Excluded from trade and other receivables balance of Ksh.510,735,379 is Kshs.163,609,492 in respect of impairment allowance which has not been supported.

9.4 Unsupported Over Remitted Statutory Deductions

Included in trade and other receivables balance of Kshs.510,735,379 is Kshs.276,563 which relates to over remitted statutory deduction (withholding tax) which has not been explained or supported.

In the circumstance, it has not been possible to confirm the validity and accuracy of the trade and other receivables balance of Kshs.510,735,379 included in the statement of financial position and whether the same is fairly stated as at 30 June, 2017.

10.0 Property, Plant and Equipment

10.1 Land

As previously reported, the property, plant and equipment balance of Kshs.19,920,505,937 included in the statement of financial position as at 30 June 2017 includes various parcels of land totaling Kshs.4,240,135,760 as summarized below:

No	Location	County	Acreage	Valuation (Kshs)
1	Mbagathi Road	Nairobi	2.4282 Ha	4,143,768,160
2	Taita Taveta	Taita Taveta	15 Acres	8,400,000
3	Busia	Busia	100 Acres	87,967,600
Total				4,240,135,760

However, the title/ownership documents in respect of the above parcels of land were not availed for audit verification.

10.2 Residential Staff Housing

As similarly reported in year 2014/2015, the property, plant and equipment balance of Kshs.19,920,505,937 as at 30 June, 2017 also includes a staff housing project valued at Kshs.476,001,556 located on a 2.4282 ha area along Mbagathi Road - Nairobi and against which a developer had used the title documents as collateral to borrow funds from the National Bank of Kenya. In an effort to have the documents discharged, and as similarly reported in 2014/15, the Government spent a sum of Kshs.280 million in the year 1993 and a further amount of Kshs.142 million in the year 2000 towards settling the developer account with the Bank. However and in spite of payments totaling Kshs.422 million having been made thus settling the debt in full, the documents had not been discharged to KEMRI as at 30 June 2017.

In the circumstance, it has not been possible to ascertain the ownership status of the parcels of land and whether the property, plant and equipment balance of Kshs.19,920,505,937 as at 30 June 2017 is fairly stated.

11.0 Intangible Assets Software

11.1 Payment for Intangible Assets not Delivered

As reported in the year 2014/2015, included in the statement of financial position as at 30 June, 2017 is intangible asset which had cost Kshs.68,151,763 as per note 22 and out of which Kshs.22,904,126 relate to payment for an Enterprise Resource Planning (ERP) software for use in KEMRI 14 modules. KEMRI had sourced for this service from M/S Alliance Technologies on 24th August 2011 at a contract sum of Kshs.24,865,500. The installation and commissioning of this software was to take one year up to 2nd July 2012. Despite the 92% payment of the contract sum by 30th June, 2017 it was observed that only 4 out of 14 modules had been installed. It was further noted that even the 4 modules installed were not in operation. KEMRI, therefore, had paid and amortized intangible assets not received.

A review of the Intangible assets movement schedule disclosed in note 22 to the financial statements revealed an impairment loss of Kshs.5,822,232 which had not been supported nor explained.

Consequently, it has not possible to confirm the validity and accuracy of the intangible asset net book value of Kshs.3,085,093 in the statement of financial position as at 30 June, 2017.

12.0 Trade and Other Payables

Included in the trade and other payables balance of Kshs.212,760,116 in the statement of financial position as at 30 June 2017 is Kshs.787,928 in respect of advance to centres, Kshs.240,000 in respect of salary in advance, Kshs.27,618 in respect of salary advance to employees and Kshs.5,246,854 in respect of temporary imprests which were not supported.

Further, the trade and other payables balance of Kshs.212,760,116 includes unremitted statutory deductions of Kshs.5,136,244 as disclosed in note 14 to the financial statements which is payable to Kenya Revenue Authority and which has not been supported.

In the circumstance, it has not been possible to confirm the accuracy of trade and other payables balance of Kshs.212,760,116 included in the statement of financial position as at 30 June 2017.

13.0 Unsupported Deferred Income

Included in the statement of financial position as at 30 June 2017 is deferred income of Kshs.25,125,898. Information available indicate that a total of Kshs.224,000,000 was deferred in 2015-2016 financial year and with a change to Kshs.25,125,898 an amount of Kshs.198,874,102 was expected to be a transfer to statement of financial performance. A review of statement of financial performance for the period ending 30 June 2017, showed there was no transfer from deferred income. It was therefore not possible to confirm how Kshs.198,874,102 deemed to have been transferred from deferred income was accounted for.

In the absence of support documents, it has not been possible to confirm the accuracy of the deferred income balance of Kshs.25,125,898 included in the statement of financial position as at 30 June 2017.

14.0 Unsupported Collaborators Funds

Included in the statement of financial position as at 30 June 2017 is collaborators fund balance of Kshs.834,772,884. A review of schedules supporting the same showed an opening and closing balance of Kshs.491,402,509 and Kshs.376,975,507 which when compared against the prior year and current year closing balances of Kshs.507,885,802 and Kshs.834,772,884 result to unsupported difference of Kshs.16,483,293 and Kshs.457,797,377, respectively, which has not been explained. A further review of the supporting schedules showed unexplained debt or overpayments brought forward and carried down of Kshs.56,002,126 and Kshs.161,400,478, respectively, that have been used to net off the schedule's opening and closing balances respectively.

In the absence of supporting documents, it has not been possible to confirm the accuracy of the collaborators funds balance of Kshs.834,772,884 in the statement of financial position as at 30 June 2017.

15.0 KEMRI NCG – Service Level Agreement Loss

As previously reported in the year 2015/2016, the Institute signed an MOU with Nairobi City Government (N.C.G) and subsequently entered into a Service Level Agreement (SLA) effective 11th March 2015 with an objective to collaborating with one another to improve standards of testing food handlers in the county of Nairobi with a view of ensuring provision of quality and hygienic services to the residents of the County.

The Institute committed itself to clause 7.7 (service level credits/penalties) that stipulated that KEMRI were to examine 50,000 food handlers per month which translate to Kshs.50,000,000 at the charge rate of Kshs.1,000 per client. The amount was to be shared at the ratio of 75:25 for KEMRI and Nairobi County Government respectively. Out of the KEMRI share of Kshs.750 per client, Kshs.500 was to cater for operational costs. The clause further stipulated that should KEMRI fail to reach the target of 50,000 people they were to forfeit their share of the proceeds so as to cover Nairobi County Government share fully. This clause appears to have favoured

the Nairobi County Government given that the target of 50,000 people that KEMRI was expected to certify was unrealistic and was not based on any baseline survey.

Further, a scrutiny of the implementation process for the last 10 months revealed that only a target of 83,665 people was realized as opposed to a target of 518,000 people expected translating to a shortfall of 434,335 people. The shortfall resulted to KEMRI owing Kshs.120,000,000 to Nairobi County Government emanating from this biased Service Level Agreement. This may result to a loss of Kshs.120,000,000 should KEMRI pay Nairobi County Government since there was no service rendered on the amount owing.

16.0 Partial Deliveries – Food Handlers Programme

As previously reported, included in the administrative costs of Kshs.396,657,988 in the statement of financial performance for the previous year ended 30 June 2016 is a payment of Kshs.10,123,000 paid in full value payment vouchers numbers, 38 and 56 for consumables ordered from various suppliers. It was, however, established that the consumables worth Kshs.5,119,952 paid for had not been delivered. Further, the inspection and acceptance certificate, goods receipts notes and delivery notes used to support this irregular payment had been acknowledged by the KEMRI management.

In the circumstance, it has not been possible to confirm what action the management has initiated to recover the amount involved.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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 such 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.

In preparing the financial statements, management is responsible for assessing the Institute's ability to continue as a going concern/ sustain services, disclosing, as applicable, matters related to going concern/sustainability of services and using the going concern basis of accounting unless the management either intends to liquidate the Institute's or to cease operations, or have no realistic alternative but to do so.

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.

Those charged with governance are responsible for overseeing the Institute's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

My responsibility is to conduct an audit of the Institute's 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 matter 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.

I am independent of Kenya Medical Research Institute (KEMRI) in accordance with ISSAI 30 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.



FCPA Edward R. O. Ouko, CBS
AUDITOR-GENERAL

Nairobi

19 April 2018