Institute of Certified Secretaries

'The Governance Profession'

Governance Audits for State Corporation

Operationalization of Governance Audits in State Corporations

Focus: Quality Assurance, Involvement of other Professional Bodies & Incubation Strategy

1.0 Background:

A Governance Audit is an independent assessment of an organization with a view to expressing an opinion on the adequacy and effectiveness of the organization's policies, systems, practices and processes within the legal and regulatory framework and in line with global best practices on corporate governance for the interest of its stakeholders. It is an objective assurance intended to add value by introducing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control, and governance processes. Governance Audit gives necessary assurance to the management, regulators and stakeholders, in regard to the governance standing of the organization.

Section 1.13 of Mwongozo recommends frequent governance audits by independent accredited governance auditor. The Institute commenced a consultative and intensive process of developing a proprietary Governance Audit framework and training programme. The programme is designed to train, refine and accredit its members as Governance Auditors to competently undertake Governance Audits and related assignments for both public and private sectors. Through a consultative process and after holding several review workshops and stakeholders' fora, governance guidelines, standards and tools have been developed.

2.0 Engagement with SCAC:

The Institute has had engagements with SCAC for a number of years on how to Operationalize the Governance Audits in State Corporations. In a meeting between Council and SCAC held on Tuesday July 5, 2021, to further this conversation, SCAC informed the institute that it was ready to operationalize the Governance Audits subject to the Institute addressing the following three issues:

1. Quality Control
2. Involvement of other Professional Bodies
3. Incubation Strategy

The Council would like to propose as follows to address the above areas subject to further stakeholder engagements.

3.0 Quality Assurance

a) The Institute has developed standards, guidelines and templates to guide governance auditors in their work.
b) The Institute has taken all its Accredited Governance Auditors through an intensive five-day course which comprises of research work, five days of face to face lectures, and group work.
c) While the course is open to all members of the Institute, only those members who have attained two years' experience since registration and awarded a practicing certificate by the Registration Board are accredited as governance auditors. The rest of the participants can only support the process under qualified auditors. This far, we have 443 successful participants of the course and of whom 312 are already accredited.
d) Participants of the course are further encouraged to participate as assessors in the Annual Champions of Governance Awards. This gives them practical experience in assessing of governance practices.
e) All members of the Institute, including governance auditors, are required to comply with CPD Policy, Professional Ethics and Conduct, as well as other directives issued by the Council from time to time.
f) A Disciplinary Committee is established under Section 25 of the CPSK Act Cap 534 as an independent tribunal. Governance Auditors who engage in unprofessional practices will be subjected to professional disciplinary procedures as provided for under the Act.
g) The Governance Audit Peer Review Mechanism (GAPRM) Board has been established to carry out an in-depth assessment of a Governance Auditor's performance and practice and thereby embed best practice in governance audit assignment execution, in-build competence and quality assurance in accordance with the governance guideline on Governance Audit Peer Review Mechanisms (GG 004).

4.0 Involvement of other Professionals

a) As part of the governance audit process, a governance auditor is required to utilize the work of other professionals such as internal and external auditors but subject to relevance, reliability and objectivity of the same. Notwithstanding such reliance on work of other professionals, the Governance Auditor retains the responsibility over the Governance Audit opinion.

b) Guidelines on alternative / accelerated membership route are being considered by the registration board (RCPSB). This will be extended to professionals who have the required governance expertise to join the Institute's membership through this alternative / accelerated membership programme. Once they join the profession, they will be required to undertake the governance auditors' accreditation course and comply with relevant professional standards, guidelines and policies. It is very important that all governance auditors are under one professional body for professional accountability and quality control.

c) The institute plans to sign MOU with other professional bodies involved in various audits or various stages of audit on the working modalities so that they are involved in the Governance Audits together with the members of the Institute.

5.0 Incubation Strategy

a) This being a fairly new area, it will need a proper incubation strategy to ensure it is sustained and is not subject to any abuses. As such there must be in place uniform standards. To be able to address any challenges, we propose that the process be closely monitored and controlled for the first three years. The Institute and SCAC will have a joint technical team that will oversee the entire process from engagement, pricing to reporting. Thereafter, forces of demand and supply should be allowed to take their course with the Institute only maintaining professional oversight.

b) The technical team shall allocate the state corporations to different governance auditors by observing the following criteria, among other considerations:
   (i) The number of state corporations allocated to a governance auditor will be subjected a limited number per given year.
   (ii) Each State Corporation will be audited by at least two Governance Auditors, where the more experienced Auditor will be the leader.
   (iii) Where the governance audit is being carried out by a consortium, such consortium shall be allocated the audits based on their combined portfolios.

(iv) The State Corporations assigned to Governance Auditors will be diverse including those that are in the upper and lower tiers, different locations, different sectors, and other complexities.

(v) The Governance Auditors' experience and seniority will be matched with the size and dynamics of the State Corporation.

c) The technical team shall review and improve the existing assessment and reporting templates as developed by the Institute to ensure uniformity of reporting structure by all auditors.

d) The Technical team shall review the governance auditors' reports and give comments for further improvements and therefore ensure that the final reports add value to organizations.

6.0 Pricing model

Option 1

Governance Audit fees should not act as an impediment to conducting governance audits neither should they incapacitate state corporations. The fees should take in to recognition the special circumstance of the organization, the state of the economy, the work involved and related costs.

In setting such prices, it should be noted that governance audit is more broad based than most of the traditional audits and would therefore generally involve more work and resultant costs. Secondly, the benefits accruing to governance audits, including supporting organizations for future improved performance, should be appreciated.

During the incubation period discussed above, pricing may be loosely regulated where the governance auditors will be allowed some room to negotiate with the State Corporations but within the limits provided as per different categorization. Currently, state corporations are categorized as Financial; Commercial/manufacturing; Regulatory bodies; Public Universities; Training and Research institutions; Service institutions; Regional Development Authorities; and Tertiary Education and Training Institutions categories.

For pricing purposes, they may be categorized and priced according as follows:

Size	Large	1,000,000	1,500,000	2,500,000	3,500,000
	Medium	700,000	1,000,000	1,500,000	2,500,000
	Small	500,000	700,000	1,000,000	1,500,000
	Micro	400,000	500,000	700,000	1,000,000
		Insolvent	Deficit/Loss	Neutral	Surplus/Profitable

Performance

In addition to size and performance as above, the following parameters may form room for negotiations for additional fees but subject to the set maximum.

Parameter	Additional fee in Kshs
Branches/outstations	50,000 per branch/outstation subject to a maximum of 400,000.
Location, distance from Nairobi	Subject to a maximum of 200,000
Listed on the NSE and other securities exchanges	Subject to a maximum of 200,000
Any other special factors	Subject to a maximum of 50,000

For illustrations purposes on the highest possible fees, consider the scenario below:

Super Eagle is a large and very profitable state corporation with 10 outstations is located in Turkana. The Super Eagle is listed on NSE and five other exchanges. The Governance Auditor considers the Super Eagle as very risky due to past numerous scandals, interference from politicians, high interests from diverse stakeholders and generally poor governance.

Below is the maximum governance audit fees as may be negotiated and agreed upon between the governance auditor and Super Eagle.

Parameter	Maximum possible fees in Kshs
Large and Profitable	3,500,000
Branches	400,000
Location	200,000
Listing	200,000
special factors	50,000
	4,350,000

Note: The purpose of the guideline is to set maximum, and not minimum, possible fees.

For purposes of this section, terms are defined as follows:

Term	Definition
Micro[1]	• whose annual turnover does not exceed five hundred thousand shillings; • employs less than ten people; and • The total assets and financial investment or the registered capital of the enterprise does not exceed Ksh 10 million in the manufacturing sector and does not exceed Ksh 5 million the service and farming sector.
Small[2]	• annual turnover ranges between five hundred and five million shillings; • which employs between ten and fifty people; • In the manufacturing sector, investment in plant and machinery should be between Ksh 10 million and Ksh 50 million and registered capital of the enterprise between Ksh 5 million and Ksh 25 million in the service and farming sector.
Medium[3]	• annual turnover is between five million shillings and one hundred million shillings; • employs between fifty one and two hundred and fifty employees; • in the manufacturing sector, the investment in plant and machinery or the registered capital of the enterprise does not exceed two hundred and fifty million shillings; and the service sector and farming enterprises, the investment in equipment or registered capital of the enterprise does not exceed one hundred and twenty-five million shillings;
Large	• annual turnover is more than one hundred million shillings; • employs more than two hundred and fifty employees; • in the manufacturing sector, the investment in plant and machinery or the registered capital of the enterprise exceeds

[1] Ibid
[2] section 2 of the Micro and Small Enterprises Act, No. 55 of 2012
[3] Public Finance Management Act No. 18 of 2012

	two hundred and fifty million shillings; and the service sector and farming enterprises, the investment in equipment or registered capital of the enterprise exceeds one hundred and twenty-five million shillings;
Insolvent	A state corporation declared as insolvent by the Auditor general
Deficit/Loss	A state corporation which, though not declared as insolvent by the Auditor general, has been making losses for the previous five consecutive years
Neutral	A state corporation which has mixed fortunes, may be recording deficits /losses in some years and surpluses/profits in other years. Also included here are all state corporations which are fully funded by the exchequer
Surplus/Profitable	State corporations that are generally profitable, notwithstanding that they have recorded deficits in some isolated years.
special factors	Such special factors may include a reputation of corruption, week governance structure, extraordinary interference, and any other special circumstances that may add into the work and costs of governance audit etc

Option 2

This is the current official categorizations of State Corporations.

The State Corporations Categorization:

I. Financial.

8 A
8 B
8 C

II. Commercial and Manufacturing.

7 A
7 B
7 C

III. Regulatory Corporations.

6 A
6 B
6 C

IV. Public Universities.

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V. Training and Research Corporations.

4A
4B
4C

VI. Service Corporations.

3A
3B
3C
3D

VII. Regional Development Authorities/ Tertiary Education and Training Corporation.

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Due to the affordability and the market dynamics, a governance Auditor may charge from a fee of 400,000 to 3,500,000. For the extras, the auditor may use the rates, applicable to board members as issued by SCAC.

For any clarifications, please feel free to contact the undersigned on line +254 20 3597841 or e-mail address info@ics.ke.

We look forward to your feedback on this proposal.

Yours sincerely,

CS Obare Nyaega

CHIEF EXECUTIVE OFFICER