

# REPORT OF THE AUDITOR-GENERAL ON THE KENYA POWER AND LIGHTING COMPANY PLC FOR THE YEAR ENDED 30 JUNE, 2019

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## REPORT ON THE FINANCIAL STATEMENTS

### Opinion

The accompanying financial statements of The Kenya Power and Lighting Company PLC set out on pages 13 to 102, which comprise the statement of financial position as at 30 June, 2019, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information, have been audited on my behalf by PricewaterhouseCoopers, auditors appointed under Section 23 of the Public Audit Act, 2015. The auditors have duly reported to me the results of their audit and on the basis of their report, I am satisfied that all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit were obtained.

In my opinion, the financial statements present fairly, in all material respects, the financial position of The Kenya Power and Lighting Company PLC as at 30 June, 2019, and of its financial performance and cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Companies Act, 2015.

### Basis for Opinion

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of The Kenya Power and Lighting Company PLC Management in accordance with ISSAI 130 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 audit of financial statements in Kenya. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

### Emphasis of Matter

#### Material Uncertainty Relating to Going Concern

I draw attention to Note 2(a) to the financial statements which discloses that the Company's current liabilities of Kshs.115,190,801,000 exceeded its current assets of Kshs.44,220,940,000 by Kshs.70,969,861,000 as at 30 June, 2019 (2018: Kshs.56,012,987,000). The Company has remained in a negative working capital position for the third consecutive year. As disclosed by the Board and Management in the past and current financial statements, strategic initiatives have been undertaken to improve the financial results of the Company. However, these initiatives appear not to have yielded the intended results. These conditions indicate that a material uncertainty exists, which may cast significant doubt on the Company's ability to continue as a going concern.

My opinion is not qualified in respect of this matter.

### Key Audit Matters

Key Audit Matters are those matters which, in my professional judgment, were of most significance in the audit of the Company's financial statements for the current year. These matters were addressed in the context of the audit of the Company's financial statements as a whole, and in forming my opinion thereon, and I do not provide a separate opinion on these matters. For each matter below, a description of how the audit addressed the matter is provided in that context.

I have fulfilled the responsibilities described in the Auditor's Responsibilities for the Audit of the Financial Statements section of the report, including in relation to these matters. Accordingly, the audit included the performance of procedures designed to respond to the assessment of the risks of material misstatement of the financial statements. The results of the audit procedures, including the procedures performed to address the matters below, provide the basis for my audit opinion on the accompanying financial statements.

Key Audit Matter	How my Audit Addressed the Key Audit Matter
<p><b>Credit Risk and Provision for Expected Credit Losses (ECL) on Financial Assets</b></p> <p>The Company implemented IFRS 9, Financial instruments, on 1 July, 2018, which requires the recognition of expected credit losses on the Company's financial assets. Previously, under IAS 39, impairment losses on financial assets were recognised on incurred basis only if there was objective evidence of impairment.</p> <p>As disclosed in Note 4 of the financial statements, the determination of expected credit losses on financial assets involves significant judgments, assumptions and estimates by the management, and the use of complex mathematical models.</p> <p>The audit procedures focused on the following areas in the calculation of the expected credit losses whose outcomes have a significant impact on the financial performance and position of the Company:</p> <ul style="list-style-type: none"> <li>• the asset risk classifications at the reporting date, including identification of financial assets that have</li> </ul>	<ul style="list-style-type: none"> <li>• An understanding was obtained of the Company's IFRS 9 implementation process including the governance processes thereof through discussions with Management and review of related documentation.</li> <li>• A sample of financial assets was selected and tested for consistent application of asset segmentation and risk classification in accordance with IFRS 9 requirements and the Company policy.</li> <li>• Management's accounting policies were reviewed and assessed over key IFRS 9 concepts especially significant increase in credit risk, default definition, forecasting of forward looking macro-economic factors, and weighting of expected loss scenarios.</li> <li>• The basis and operation of the models and the data and assumptions used were tested.</li> <li>• Historical data trends were tested and an evaluation conducted on how they were applied to compute key expected credit losses parameters such as the probability</li> </ul>

<b>Key Audit Matter</b>	<b>How my Audit Addressed the Key Audit Matter</b>
<p>experienced significant increase in credit risk or default;</p> <ul style="list-style-type: none"> <li>• the determination of key inputs in calculating the expected credit losses such as the probabilities of default, the loss given default, exposures at default, and the forward-looking information overlays; and</li> <li>• the conceptual logic and accuracy of the expected credit losses calculation models used by the Company.</li> </ul>	<p>of default, Loss Given Default and Exposures at Default.</p> <ul style="list-style-type: none"> <li>• An assessment was carried out on the consistency of application of the principles, judgments and assumptions on transition opening balances and the closing balances at the year end.</li> <li>• A review was conducted on Management’s ECL related financial statement disclosures especially sensitivities on areas of estimation.</li> </ul>

**Other Information**

The other information comprises the Chairman’s Statement and the Managing Director & CEO’s Statement, which I obtained prior to the date of this report, and the rest of the other information in the Annual Report which is expected to be made available to me after that date, but does not include the financial statements and my auditor’s report thereon. The Directors are responsible for the other information. My opinion on the financial statements does not cover the other information and I do not express any form of assurance conclusion thereon.

In connection with my audit of the financial statements, my responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit, or otherwise appears to be misstated. If, based on the work I have performed on the other information obtained prior to the date of this auditor’s report, I conclude that there is a material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

When I read the rest of the other information in the annual report and I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance.

**REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES**

**Conclusion**

As required by Article 229(6) of the Constitution, based on the audit procedures performed, except for the matters described in the Basis for Conclusion on Lawfulness and Effectiveness in Use of Public Resources Section of my report, I confirm that, nothing else has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

## **Basis for Conclusion**

### **1. Non-compliance with the Unclaimed Financial Assets Act, 2011**

As reported in the prior year and as disclosed in Note 27 to the financial statements, the Company as at 30 June, 2019 held in their books financial assets amounting to Kshs.922,000,000 (2018:Kshs.1,729,000,000) under other payables of Kshs.10,319,188,000 (2018:Kshs.10,302,192,000). These assets include deposit refunds, unidentified receipts, unpaid customer electricity deposits, unpaid wayleaves compensation, unclaimed dividends and stale cheques, which ought to have been reported and submitted to the Unclaimed Financial Assets Authority (UFAA), as required by the Unclaimed Financial Assets Act, 2011. According to the Act, failure to comply attracts a penalty of 25% of the assets held, in addition to a daily penalty of between Kshs.7,000 and Kshs.50,000 for each day a report is late in submission. Although Management is confident that the outstanding balance will drop following an ongoing review and audit of the assets, this aspect of non-compliance may cost the Company up to Kshs.1,765,000,000 in interest and penalties as at 30 June, 2019.

### **2. Non-compliance with the Capital Markets Authority Listing Rules**

As reported in the prior year, the First Schedule of the Capital Markets (Securities) (Public Offers, Listing and Disclosures) Regulations, 2002 (Amended 2016) sets out the minimum requirements for a company at the time of listing, as well as continuing obligations of the listed entity. The First Schedule provide that the listed company must have prepared financial statements for the latest accounting period on a going concern basis and that the related audit report must not contain any qualification or emphasis of matter in this regard.

Further, the Company must not be in breach of its loan covenants, particularly in regard to the maximum debt capacity and should have adequate working capital. However, the Company was in breach of certain borrowing covenants ratios as at 30 June, 2019. Management however obtained from the lenders the necessary waivers before 30 June, 2019, confirming the waiver of the lenders' right to demand immediate repayment of the loan, due to the breach of borrowing covenants.

In addition, the Company's current liabilities of Kshs.115,190,801,000 exceeded current assets of Kshs.44,220,940,000 by Kshs.70,969,861,000 resulting in a negative working capital of a similar margin.

### **3. Non-compliance with the Public Procurement and Asset Disposal Act, 2015**

Article 227(1) of Constitution of Kenya provides that a procuring entity shall uphold the principles of fairness, equity, transparency, competitiveness and cost effectiveness in the process of procurement of public goods and services.

Further, the Public Procurement and Asset Disposal Act, 2015, Section 103(1) provides that; a procuring entity may use direct procurement as allowed under Sub-Section (2) as long as the purpose is not to avoid competition. Sub-Section (2) further provides instances where the direct procurement method may be used to include, among others, where;

goods, works or services are available only from a particular supplier or contractor, or a particular supplier or contractor has exclusive rights and procuring entity, having procured goods, equipment, technology or services from a supplier or contractor, determines that additional supplies shall be procured from that supplier or contractor for reasons of standardization or need for compatibility with existing goods, equipment, technology or services.

A review of procurement processes revealed that the Company executed a contract with a local firm for the provision of creative, production and media buying services at a cost of Kshs.55,890,600 in January, 2018. The services were procured through Direct Procurement contrary to Article 227 of the Constitution of Kenya and Section 103(1) of the Public Procurement and Asset Disposal Act, 2015.

No justification for the direct procurement method used was availed as there existed other providers of similar services in the market and there were no exclusively held rights for them, in the case of the services procured

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance on whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities which govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

## REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

### **Conclusion**

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, except for the matter described in the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance section of my report, I confirm that, nothing else has come to my attention to cause me to believe that Internal Controls, Risk Management and Governance, were not effective.

### **Basis for Conclusion**

#### **Control Weaknesses in Information Technology**

The Company has implemented a number of Information Technology (IT) systems for its various operations. Review of these systems revealed control weaknesses, as listed below:

- (i) There was inconsistent monitoring of super-user activity for four IT applications. Activities in the applications should be monitored using three software tools at both application and database levels. However, the operating system level activities were not being monitored while three of the four main IT applications had not been configured on the monitoring tool for user activity at application and database levels. Similarly, the monitoring tools were yet to be configured, thus individual accounts/user IDs with powerful rights layer were not being monitored.
- (ii) Reports generated by the tools and data maintained by the trigger tables were

not reviewed frequently and in a timely manner by Management so as to understand issues flagged and how they were responded to by the information security team. This means that unauthorized or malicious activities performed in the databases, applications and operating systems may not be detected on time.

- (iii) Audit logs and audit settings were not protected from access by privileged users making such users capable of changing audit settings without authorization and enabling unauthorized changes without being held accountable.
- (iv) There were inadequate logical access controls and weak passwords parameters whereby password configurations of the operating systems databases and application of in-scope applications were not set in line with the password policy.

In view of the above lapses in IT controls, it was not possible to rule out existence of weaknesses in internal control and related risks, during the year under review.

The audit was conducted in accordance to ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance on whether effective processes and systems of internal control, risk management and overall governance, were operating effectively, in all material respects. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

## REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by the Companies Act, 2015, I report based on the audit that:

- (i) In my opinion, the information given in the report of the Directors on pages 2 to 3 is consistent with the financial statements.
- (ii) In my opinion, the auditable part of the Directors' remuneration report on pages 4 to 6 has been properly prepared in accordance with the Kenyan Companies Act, 2015.

## Responsibilities of Management and those Charged with Governance

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for maintaining effective internal control as Management determines is necessary to enable the preparation of financial statements which are free from material misstatement, whether due to fraud or error and for assessment of the effectiveness of the internal control, risk management and overall governance.

In preparing the financial statements, Management is responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless Management is aware of the intention to liquidate the Company or to cease operations.

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.

In addition to the responsibility for the preparation and presentation of the financial statements described above, Management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them, and that public resources are applied in an effective way.

Those charged with governance are responsible for overseeing the Company's financial reporting process, reviewing the effectiveness of Management's systems for monitoring compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

### **Auditor-General's Responsibilities for the Audit**

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report which 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. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

In addition to the audit of the financial statements, a compliance review is planned and performed to express a conclusion on whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them and that public resources are applied in an effective way, in accordance with the provisions of Article 229(6) of the Constitution, and submit the audit report in compliance with Article 229(7) of the Constitution.

Further, in planning and performing the audit of the financial statements and audit of compliance, I consider internal control in order to give an assurance on the effectiveness of internal controls, risk management and governance processes and systems in accordance with the provisions of Section 7(1) (a) of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. My consideration of the internal control would not necessarily disclose all matters in the internal control which might be material weaknesses under the ISSAIs. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level, the risk that misstatements caused by error or fraud in amounts which would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Because of its inherent limitations, internal control may not prevent or detect misstatements and instances of non-compliance. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become

inadequate because of changes in conditions, or that the degree of compliance with the Company's policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence which is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.
- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner which achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Company to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

I communicate with the Management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control which are identified during the audit.

I also provide Management with a statement that I have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters which may reasonably be thought to bear on my independence, and where applicable, related safeguards.

From the matters communicated with Management, I determine those matters that were of most significance in the audit of the financial statements and internal control of the current period and are therefore the key audit matters. These matters are described in my auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, I determine that a matter should not be



communicated in my report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.



**Nancy Gathungu**  
**AUDITOR-GENERAL**

**Nairobi**

**04 September, 2020**