

REPORT OF THE AUDITOR GENERAL ON KENYA RURAL ROADS AUTHORITY FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

I have audited the accompanying financial statements of Kenya Rural Roads Authority set out on pages 21 to 52, which comprise the statement of financial position as at 30 June 2017, the statement of financial performance; the statement of changes in net assets and the statement of cash flows 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.

In my opinion, except for the effects of the matter described in the Basis for Qualified Opinion section of my report, the financial statements present fairly, in all material respects, the financial position of Kenya Rural Roads Authority as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards (Accrual Basis) and comply with the Kenya Roads Act, 2007 and Laws of Kenya.

In addition, as required by Article 229(6) of the Constitution, Except for the Matters described in the Basis for qualified Opinion section of my report, based on the procedures performed, I confirm that, nothing has come to my attention to cause me to believe that public money has not been applied lawfully and in an effective way.

Basis for Qualified Opinion

1.0 Nugatory Expenditures

As reported in the previous year, the Authority had incurred a total of Kshs.202,088,241 to pay interest on delayed payments as at 30 June 2016. A review of the matter in 2016/17 has revealed that a further amount of Ksh.4,253,404.04 was incurred to payment of interest bringing total nugatory expenditure to kshs.206,341,645.04. Although the management has explained that this was occasioned by delayed exchequer releases from the National Treasury, no evidence has been seen on action taken by management to prevent recurrence of this unfavorable situation which has constrained implementation of the Authority's programme by spending budgetary allocations on nugatory expenditure.

2.0 Rehabilitation and Repair of Kasoiyo – Saos - Society (D350) Road

The project was awarded to M/s. Bridgestone Construction Company Limited at a contract sum of Kshs.818,445,018 and commenced on 10 October 2012 with expected date of completion as 10 February 2016 revised to 10 April 2016.

Examination of the project file revealed the following:

2.1 Assignment of Works

On 28th January 2015, works valued at Kshs.504,824,286 were assigned to Guangxi Hydroelectric Construction Bureau an indication that the main contractor performance was poor.

2.2 Delayed Project Implementation

The latest progress report for 5 August, 2016 showed the overall progress achieved was at 99.91% against elapsed time of 130.2% of the contract period. Further, although the contractor requested for substantial completion inspection on 13 September, 2017 the management had not undertaken the same by the time of the audit.

3.0 Construction of Muranga – Gitugi (D427) and Njumbi- Mioro (E546)

The Project was awarded to M/s Nyoro construction co. ltd at contract sum of Kshs.2,120,325,200 with date of commencement as 31st July 2012 and expected date of completion as 2nd February 2015.

A review of the project file and the related records revealed some unsatisfactory matters as follows:

3.1 Delayed Project Delivery

Review of the project in the year under audit revealed that overall progress as at 30 June 2017 was at 47.23% against an elapsed contract period of 58.93 Months or 196.43% of contract period. This indicates the project is far behind schedule which could lead to escalation of costs.

3.2 Interest on Late Payments

The latest payment certificate (No. 20) dated 27 June 2017 indicated that interest on delayed payments totaling Kshs.7,001,678 had been incurred, which is a nugatory expenditure.

4.0 Construction of Kaptama-Kapsokwony-Sirisia (275/265) Road Contract No. RWC 023

As reported in the previous year the Road Project is situated in Kimilili, Bungoma West (both formerly in larger Bungoma) and Mt. Elgon Sub-Counties of Bungoma County. The project is approximately 67km long. The road is divided into 4 distinct portions with a total length of 67km as follows:-

1)	Kamukuywa- Kaptama (D285)	14.0km
2)	Kaptama- Kapsokwony- Namwela (D275)	40.32km
3)	Kapsokwony- Kimilili (D265)	8.37km
4)	Namwela- Chwele (C42)	5.1km

Review of the project files and the related records revealed the following unsatisfactory matters:

4.1 Delayed Project Delivery

The contract commenced on 22 June 2007 for a contract period of 35 months. The contract was to end by 13 May 2010 but the last progress report availed for audit was for 31 July 2015 by which time the contractor had attained a weighted average physical progress of 94% and there was no evidence of approval for extension of time from the Tender Committee. During the year under audit, the management did not avail information on the current status of the project.

4.2 Financial Distress of the Contractor

The contractor, KSL International Ltd was put under receivership as indicated in the Daily Nation on Monday 23 February 2015 page 37. The contractor's yard including the site offices at Kamkuywa, was placed under a Receiver Manager and all site operations brought to halt.

The Contractor had been unable to settle rent arrears owed to the Authority amounting to Kshs.3,028,125 for Mwatunge Camp in Taita Taveta which was used in a previous contract.

4.3 Requests for Mutual Winding up of the Contract

The Receiver Manager vide Letter ref HG/JKM/RBH/JGM/62 dated 9 July 2015 requested for mutual winding up of the contract citing balance of funds to the contract sum is insufficient to complete the outstanding works based on design specifications. In a letter ref KeRRA/05/1/VOL.1/RWC023/2536 dated 16 July 2015 the General Manager (Design and Construction) requested the Resident Engineer to comment on mutual winding up of the contract and also undertake a project appraisal and submit a report with recommendations before 27 July 2015. Further, the Attorney General in a letter Ref:AG/CONF/21/6/12 VOL.I (7) dated 1st September, 2016 advised the management to terminate the contract forthwith in accordance with clause 63.1 of the conditions of contract but there was no evidence to show what action had been taken as at the time of audit.

In the circumstances, it has not been possible to confirm whether the public obtained value for money for the expenditure of Kshs.2,622,131,272 already incurred.

A review of the matter in 2016/17 revealed that the issue is still unresolved.

5.0 Construction to Bitumen Standard of Naromoru - Munyu - Karisheni Road Contract No RWC 040.

As reported in the previous year, the project scope was construction of four roads with a total length of 45.9km and was awarded to M/S Kirinyaga Construction (K) Limited at a contract sum of Kshs.2,468,815,445 and commenced on 1 October 2012 with expected date of completion as 30th September 2014.

5.1 Assignment of Works

On 21 April the contractor entered into agreement with East African Development Engineering Trading Co. Ltd to assign to the latter part of the works valued at Kshs.2,064,537,961 after approval from Director General through letter ref. KeRRA/D&C/3679 dated 9 March 2015. A total of 39.9 KMs were assigned to M/s East African Development as follows:

1)	Road D448 km 6+000 to km 21+200 (Karisheni)	15.2km
2)	Road E171A Lusoi- Munyu- Kakuret	7.3km
3)	Road RAR27 Giting'a- Kamburuaini- Sarafina	7.3km
4)	Road RAR29 Ibauini- Mwicwiri- Njoguini	<u>10.1km</u>
	Total	<u>39.9km</u>

5.2 Delayed Project Delivery

The main contractor, Kirinyaga Construction Ltd, whose scope was reduced to 6 km after assignment of works, had only realized a progress of 72.1% as at 30 June 2017 and by that time 57 months equivalent to 227.5% of contract period had elapsed. The assigned contractor's progress was at 71.23% with elapsed time of 25 months equivalent to 104% of contract period. The combined overall progress for the two contractors as at 30 June 2017 was 73.1%.

The project is therefore behind schedule .

6.0 Rehabilitation and Repair of Eldoret – Ziwa – Kachibora – Eldoret-Kabenes Road

The Project was awarded to M/s Kimillili Hauliers at a contract sum of Kshs.1,435,212,465 and commenced on 1st September 2011 with expected date of completion as 1st March 2014 which was later revised to 1st March 2016. A review of the project files and related records revealed the following:

6.1 Scaling down of Works

The initial contract was repackaged into three components as follows:

- (i) Eldoret - Kabenes 24KM- Kshs. 974,301,651
- (ii) Kabenes-Kachibora 31KM- Kshs. 1,064,762,019
- (iii) Moi's Bridge – Kachibora 20 KM- kshs.536,046,915

The first section was repackaged as addendum No. 2 which was approved by the CTC on 12 September 2014 and is to be completed under the current contract. The second section was subjected to open tender and awarded to M/s China International Cooperation on 19 June 2015 at a contract sum of Kshs.1,313,914,382. The third section is estimated to cost Kshs.536,046,915 and will be implemented through an annuity programme.

This repackaging of the works brings up the contract sum from an original price of Kshs.1,435,212,465 to a sum of Kshs.2,575,110,585.

6.2 Delayed Project Implementation

The revised contract period lapsed on 1st March 2016 but the latest progress report dated 30th June 2017 showed that the overall progress was at 96% with only 88.2% of the contract sum certified.

The project is behind schedule which could lead to cost overruns.

7.0. Construction of Kibunja-Molo-Olenguruone Road (D316)

The project which is located in Molo, Nakuru County and is approximately 51 km long was awarded to M/S Kimilili Hauliers at a contract sum of Ksh.742,290,293 revised to Kshs.844,344,347,348 and commenced on 6th August 2010 with expected date for completion of 6th February 2016.

7.1 Assignment of works

The contractor agreed to sub-contract works valued at Kshs.113,137,134,730 to another contractor, Raflo Services to speed up the progress but the arrangement has still not delivered the project.

7.2 Failed Project Delivery/Termination

The project was to be completed on 6th February 2012 but as per the last progress report for December 2014, only 67.73% physical progress had been achieved. There was no progress report from December 2014 to date and no evidence of approval for extension of contract period and evidence of action taken by management in line with the terms of contract.

8.0 Construction of Sigalagala – Musoli-Sabatia – Butere Roads (D260/E390)

The project is in Kakamega County and the road length is approximately 34.25 km. The contract was awarded to M/s Associated on 28th March 2011 at a contract price of Kshs.1,809,465,663. Works commenced on 6th June 2011 and was to be completed by 6th June 2013.

8.1 Assignment of Part of the Works

In December 2014, the contractor entered into an agreement with another contractor, East African Development Engineering and Trading Co. Ltd to assign part of the works in line with Clause 3.1 of the conditions of contract. Out of the total road length of 34.25 KM, the assignee was to construct 20 KM at a contract sum of Kshs.1,113,658,598. The main contractor was left to handle 14.25 kilometers only. The assignee was given 18 months to complete the works.

8.2 Advance payment

The main contractor was paid an advance of Kshs.180,946,566 and out of which only Kshs.22,808,548 had been recovered by the time of the audit leaving an outstanding amount of Kshs.158,138,018.69 (same as the previous year).

8.3 Delayed Project Completion

The project was to be completed by 6th June 2013 but this was revised to 9th July, 2013 through an extension of the contract period. The latest progress report dated 31st July 2017 showed that only 74.3% combined progress had been realized by both the main contractor and the assignee, an indication that the project was behind schedule which could lead to escalation of costs.

9.0 Construction of Sigiri Bridge and Approach Roads on Road R43 - RW-C092

The above contract was awarded to China Overseas Engineering Group Co. Ltd on 5th March, 2015 at a contract sum of Kshs.992,546,146.28. The project had a contract period of 18 Months starting from 12th August 2015 and the project was expected to be completed by 12th February 2017.

The following observations were made from review of the project files and related records:

9.1 Slow Progress

The contract period for the project elapsed on 12th February 2017 and there was no evidence for approval of extension of time but as per the latest progress report dated 31 October, 2017, the overall progress was at 81.27% against an elapsed contract time of 24 Months equivalent to 133.33% of the contract period. Although management has indicated that the project is substantially complete, no evidence was availed in support of this and it was not possible to confirm the status of the project as at 29th May 2018.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Kenya Rural Roads Authority 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. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Key Audit Matters

Key audit matters are those matters that, in my professional judgment, are of most significance in the audit of the financial statements. Except for the matters described in the Basis for Qualified Opinion section, I have determined that there are no Key Audit Matters to communicate in my report.

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 Authority'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 the management either intends to liquidate the Authority 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 Authority's financial reporting process.

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

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 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 of Kenya. 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.

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 that 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.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, and for for the

purpose of giving an assurance on the effectiveness of the Authority's 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 Authority's ability to continue to sustain its services. 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 Authority to cease to continue to sustain its services.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Authority 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 that are identified during the audit.

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



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

Nairobi

28 June 2018