REPORT OF THE AUDITOR-GENERAL ON KENYA ELECTRICITY TRANSMISSION COMPANY LTD FOR THE YEAR ENDED 30 JUNE, 2021

PREAMBLE

I draw your attention to the contents of my report which is in three parts:

A. Report on the Financial Statements that considers whether the financial statements are fairly presented in accordance with the applicable financial reporting framework, accounting standards and the relevant laws and regulations that have a direct effect on the financial statements.

B. Report on Lawfulness and Effectiveness in Use of Public Resources which considers compliance with applicable laws, regulations, policies, gazetted notices, circulars, guidelines and manuals and whether public resources are applied in a prudent, efficient, economic, transparent and accountable manner to ensure Government achieves value for money and that such funds are applied for intended purpose.

C. Report on Effectiveness of Internal Controls, Risk Management and Governance which considers how the entity has instituted checks and balances to guide internal operations. This responds to the effectiveness of the governance structure, the risk management environment, and the internal controls developed and implemented by those charged with governance for orderly, efficient and effective operations of the entity.

An unmodified opinion does not necessarily mean that an entity has complied with all relevant laws and regulations, and that its internal controls, risk management and governance systems are properly designed and were working effectively in the financial year under review.

The three parts of the report are aimed at addressing the statutory roles and responsibilities of the Auditor-General as provided by Article 229 of the Constitution, the Public Finance Management Act, 2012 and the Public Audit Act, 2015. The three parts of the report, when read together constitute the report of the Auditor-General.

REPORT ON THE FINANCIAL STATEMENTS

Qualified Opinion

The accompanying financial statements of Kenya Electricity Transmission Company Limited set out on pages 35 to 74, which comprise of the statement of financial position as at 30 June, 2021, statement of profit or loss and other comprehensive income, statement of changes in equity, statement of cash flows, and a summary of significant accounting policies and other explanatory information, have been audited on my behalf by Deloitte & Touché, 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, except for the effect of the matters described in the Basis for Qualified Opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the Kenya Electricity Transmission Company Ltd as at 30 June, 2021, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Public Finance Management Act, 2012 and the Companies Act, 2015**.**

Basis for Qualified Opinion

1.0 Deferred Grant Income

The statement of financial position reflects total deferred grant income of Kshs.189,891,542,000 which, as disclosed in Note 20 to the financial statements comprises of Kshs.70,915,400,000 and Kshs.118,976,142,000 in respect of direct and indirect grants respectively. Review of records revealed that the Company received an amount of Kshs.19,836,802 from the Ministry of Energy. However, records from the Ministry reflected an amount of Kshs.10,831,798,269 resulting to an unexplained variance of Kshs.9,005,004,000.

Further, the statements of profit or loss and other comprehensive income reflects amortized grant from Government income amounting to Kshs.2,192,104,000 which differs with the current grant amortization reported in the previous year as grant income to be amortized over 12 months of Kshs.2,233,745,000 resulting to an unexplained variance of Kshs.41,641,000.

In the circumstances, the accuracy of grants receipts and amortized grant income thereof could not be confirmed.

2.0 Capital Work in Progress

The statement of financial position as disclosed in Note 13 to the financial statements reflects an amount of Kshs.111,471,881,000 in respect of capital work in progress while the supporting schedule provided for audit indicated a balance of Kshs.111,015,936,000 resulting in an unexplained variance of Kshs.455,945,000. Review of the financial records revealed that projects valued at Kshs.17,015,210,520 were completed in the previous financial years but had not been capitalized. Management has not explained the reasons for not capitalizing the projects.

Further, projects valued at Kshs.25,566,410,286 were still ongoing but had exceeded their respective contract completion dates. However, Management has not explained the reasons for the delay in completion of the projects or provided evidence of approval of the contract extension as required by Section 139(2) of the Public Procurement and Asset Disposal Act, 2015.

In the circumstances, the accuracy and completeness of the capital work in progress balance of Kshs.111,471,881,000 could not be confirmed.

3.0 Trade and Other Payables

3.1 Unsupported VAT Payable

The statement of financial position as at 30 June, 2021 reflects trade and other payables balance of Kshs.18,069,482,000. However, the balance includes, VAT payable output tax amounting to Kshs.1,163,953,516 that was not supported by VAT returns duly acknowledged by Kenya Revenue Authority.

Under the circumstances, the accuracy and completeness of the VAT payable of Kshs.1,163,953,516 could not be confirmed.

3.2 Undisclosed Amounts Due To Kenya Electricity Generating Company Limited

The statement of financial position as at 30 June, 2021 reflects trade and other payables of Kshs.18,069,482,000. However, the amount excludes a balance of Kshs.4,481,056,467 in respect of transmission lines that were done during the financial year 2008/2009 or earlier by Kenya Electricity Generating Company (KenGen) and which are used in the furtherance of Company's business for revenue generation. Although the Company continues to generate revenue from the transmission lines, there was no evidence provided to indicate that the they have been included as part of the plant, property and equipment.

Further, although the transmission lines were financed through a loan, the Company has not recognized any interest charged on this loan since the takeover of the lines. Management of KenGen indicate that there has been negotiation for transfer of the assets to the Company which if concluded would increase the operations costs of the Company due to the accruing interest and impact cash outflows due to loan repayments every year.

Under the circumstances, the accuracy and completeness of the payables balance of Kshs.18,069,482,000 could not be confirmed.

4.0 Trade and Other Receivables

4.1 Unsupported Receivables Balances

The statement of financial position reflects trade and other receivables of Kshs.9,726,373,000 which is net of amounts due from related parties balance of Kshs.3,911,771,000. Review of the financial records revealed unsupported adjustments of Kshs.143,123,044 and Kshs.1,169,443,245 in respect of advance payments and litigation costs receivables respectively.

Further, included in the trade receivables are balances of Kshs.1,630,895,645, Kshs.3,392,580,798 and Kshs.1,008,597,136 in respect of advance payment, litigation cost receivable and assets under construction advance payment respectively, whose supporting documents were not provided for audit.

In addition, supporting schedule for trade and other receivables includes VAT input receivable of Kshs.1,302,920,502 that was not supported by VAT returns duly acknowledged by KRA.

Under the circumstances, the accuracy and completeness of the receivables balance of Kshs.9,726,373,000 could not be confirmed.

4.2 Amounts Due from Kenya Power and Lighting Company Limited

The statement of financial position and as disclosed in Note 21(a) to the financial statements reflects outstanding balances arising from services rendered to Kenya Power and Lighting Company Limited (KPLC) of Kshs.5,897,754,000. However, KPLC records indicated a balance of Kshs.5,546,379,000 resulting in a variance of Kshs.351,375,000.

In addition, there was no evidence of a payment plan from KPLC for the outstanding amounts at the end of the financial year under review.

In the circumstances, the full recoverability of the amounts due from Kenya Power and Lighting Company Limited could not be ascertained.

5.0 Unsupported Subsistence Allowances

The statement of profit or loss and other comprehensive income for the year ended 30 June, 2021 reflects administration costs of Kshs.1,520,724,000 which as disclosed in Note 6(a) to the financial statements includes other operating expenses amounting to Kshs.141,844,983 in respect of subsistence allowances-domestic, subsistence allowance-Staff travel expense and subsistence allowances-International travel. However, the expenditure was not supported with the details of the activities, dates of the activities, approved work plans, boarding passes, copies of passports and evidence of surrender of imprests.

In the circumstances, the accuracy, and propriety of the expenditure of Kshs.141,844,983 on other operating expenses could not be confirmed.

6.0 Unaccounted for Grants

The statement of financial position and as disclosed in Note 21(c)(ii) to the financial statements reflects recurrent grants of Kshs.6,816,300,000 received from the Ministry of Energy. However, Management did not provide documents to support how grants amounting to Kshs.3,407,118173 were accounted for.

Further, review of the financial records revealed that the Nanyuki-Isiolo-Meru project was allocated an amount of Kshs.100,000,000 during the year under review but only amount of Kshs.59,429,226 was incurred. However, records provided for audit indicated that the project was completed in the year 2014. Management did not explain why the project was allocated funds, yet it had been completed.

In addition, it was noted that an amount of Kshs.2,2522,000 was disbursed to four (4) projects that had no activities and the funds could not be accounted for.

In the circumstances, the accuracy of expenditure on recurrent grants of Kshs.3,407,118,173 could not be confirmed.

7.0 Unsupported Expenditure

The statement of financial position and as disclosed in Note 13 to the financial statements reflects an amount of Kshs.2,696,820,000 in respect of transfer from works in progress for construction of transmission lines. Included in the balance is an amount of Kshs.701,416,727 that was incurred on construction of the Loyangalani Suswa transmission line. However, the expenditure was not supported with a certificate of completion and commissioning.

In the circumstances, validity of the expenditure of Kshs.701,416,727 for construction of transmission lines could not be confirmed.

8.0 Pending Way-Leave Compensations

Review of way-leave compensations revealed that the Company had outstanding compensation to landowners for way-leaves amounting to Kshs.2,724,649,715. However, Management explained that delayed payment was due to insufficient budgetary allocation from The National Treasury and long negotiations between land owners, the Company and various County Governments. Delays in compensating Project Affected Persons, (PAPs) may lead to legal suits, cost escalations and project delays.

Further, it was noted that the way-leave compensation balance includes debit balances of Kshs.11,940,000 which has been occasioned by a mismatch of invoices against the corresponding payable balance. Management indicates that the matching is an ongoing process but does not indicate the controls put in place to ensure that the errors are eradicated in future.

In the circumstances, the accuracy and completeness of the pending way-leave compensations could not be confirmed.

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Kenya Electricity Transmission Company Ltd 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 qualified opinion.

Emphasis of Matter

1.0 Provisions and Contingent Liabilities

I draw attention to Note 29(a&b) to the financial statements which discloses that the Company's estimated contingent liabilities consist of ongoing court cases relating to acquisition of wayleaves and contractors' claims beyond the original contract period, amounting to Kshs.6,723,093,000. According to Management, the status of these exposures is evaluated on a regular basis to assess the probability of incurring related liabilities. However, in the event that these contingent liabilities crystalize, the Company may be exposed to unforeseen project cost overruns, resulting to inability to meet its obligations when they fall due. This may affect service delivery capacity of the Company.

My opinion is not modified with respect to these matters.

2.0 Material Uncertainty Relating to Going Concern

I draw your attention to the statement of financial position at 30 June, 2021 which indicated the company's current liabilities balance of Kshs.27,479,514,000 exceeded current assets balance of Kshs.21,655,789,000 by an amount of Kshs.5,823,725,000.

In view of the negative working capital, the Company may not be in a position to meet its short-term maturing obligations, thereby exposing it to going concern risks.

My opinion is not modified with respect to this matter.

3.0 Court Award on Terminated Contract

During the year under audit, an arbitration case between the Company and a contractor for the termination of contract for the construction of 132KM of 400KV double circuit transmission line from Lessos substation in Kenya to Tororo substation in Uganda has remained unresolved since April, 2016. The tribunal issued an award in favour of the contractor on 30 July, 2019 amounting to Euro 37,365,691 or approximately Kshs.4.5 Billion, which included termination costs, legal cost and other claims amounting to Kshs.2,223,137,553. Management considered the decision to be against public interest and sought assistance from Attorney General's office in setting aside the Tribunal's award. However, the award was upheld by the High Court of Kenya on 16 February, 2020.

Further, it was not possible to confirm whether the project would be completed in the near future, and the additional costs which would be necessary to complete the project, or the losses which the Government of Kenya would suffer in the event that the project is not completed.

In the circumstances, the award has resulted to unforeseen legal and arbitration costs, termination charges, and other claims.

My opinion is not modified with respect to this matter.

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. There were no key audit matters to report in the year under review.

Other Information

The Directors are responsible for the other information, which comprises of corporate information, Chairman's statement, report of the Chief Executive Officer, Statement of performance against predetermined objectives, Management discussions and analysis, report of the Directors and the statement of Directors' responsibilities.

The other information does not include the financial statements and my auditor's report thereon.

My opinion on the financial statements does not cover the other information and I do not express any form of assurance or conclusion thereon.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Section 7(1)(a) of the Public Audit Act, 2015, 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

1.0 Construction of Loyangalani - Suswa Transmission Interconnector Line

In the special audit concluded in April 2021 a number of issues were raised in the procurement and execution of the above contract as indicated below:

i) Management did not undertake both technical and financial due diligence as provided under Section 68(1) PPDA Act 2015 leading to irregular payment of Kshs.10,827,072 to a Contractor which subsequently filed a petition for bankruptcy.

ii) After bankruptcy of the original Contactor, Management engaged yet another Contractor. However, the procurement was not included in the annual procurement plan and valuation of the pending works for the purposes of preparing the bills of quantities was not provided for audit.

iii) Engagement of subcontractors at a cost of Kshs.1,524,059,296 which was not accompanied with certificates of completion.

iv) Acquisition of materials from the subcontractors at a cost of Kshs.26,220.329 without a valuation report and subsequently taking them on charge.

In the circumstances, Management was in breach of law and value for money could not be confirmed.

2.0 Payments made for Terminated and Stalled Projects

Review of the project status report indicated that an amount of Kshs.3,976,801,443 had been paid to a contactor in respect of Bomet-Sotik, Mwingi-Kitui-Wote-Sultan Hamud,Nanyuki-Nyahururu and Olkaria transmission lines for contracts that have since been terminated while an amount of Kshs.8,714,632,590 was incurred on construction of the Lessos-Tororo-Transmission line which had stalled. Management has not explained the reasons for the termination and measures instituted to recover the payments made to the contractors.

In the circumstances, it was not possible to confirm whether value for money was obtained on the expenditure of Kshs.12,691,434,033 on the four (4) transmission lines.

3.0 Non-Compliance with Loan Novation Agreement

As previously reported, loan liability on the construction of the Kamburu-Meru transmission line was transferred from Kenya Power and Lighting Company (KPLC) to Kenya Electricity Transmission Company (KETRACO), on 19 October, 2016. According to the novation agreement, KETRACO was required to make bi-annual payments to the Government of Kenya (GoK) on account of outstanding interest at a rate of 2.5% per annum. However, the Company had not made any payments to the Government, as stipulated in the novation agreement. Management has indicated that a moratorium for twenty-four (24) months had been sought from The National Treasury but the matter was yet to be considered by the National Treasury.

In the circumstances, Management was in breach of the law.

4.0 Income from Disposal of Motor Vehicles

Note 5 to the financial statements reflects income from disposal of motor-vehicles of amounting to Kshs.20,025,000. However, the disposal was not supported with an approved disposal plan, minutes of asset disposal committee, a technical report to support the disposal of the assets and the reserve price as required by Regulations 176 and 177 of the Public Procurement and Asset Disposal Regulations, 2020.

In the circumstance, Management was in breach of the law.

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 about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that 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, except for the matters described in theBasis 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

Weak Information Technology Internal Controls

Review of the KETRACO financial information system revealed some internal control weaknesses, which could result to unauthorized access and manipulation of the entity's financial data, thus negatively impacting on the data integrity. It was noted that password parameters in relation to password complexity and account lockout duration have not been appropriately defined.

In the circumstances, the effectiveness of the ICT infrastructure could not be confirmed.

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance about 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 Kenyan Companies Act, 2015 I report based on the audit, that:

(i) I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of my audit;

(ii) In my opinion, proper books of account have been kept by the Company, so far as appears from the examination of those books;

(iii) The Company's statement of financial position and statement of comprehensive income agree with books of account.

Responsibilities of Management and Board of Directors

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 that are free from material misstatement, whether due to fraud or error and for its assessment of the effectiveness of 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.

The Board of Directors is responsible for overseeing the Company's financial reporting process, reviewing the effectiveness of how Management monitors 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 overall 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 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. 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 audit is planned and performed to express a conclusion about whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities that 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 controls would not necessarily disclose all matters in the internal controls that 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 that 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 controls 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 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 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 controls.

- 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 that 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 controls that 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 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.

CPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

23 September, 2022