





SPECIAL AUDIT REPORT

OF THE

AUDITOR-GENERAL

ON THE PROCEEDS AND UTILIZATION OF EUROBOND

 THE NATIONAL ASSEMBLY PAPERS LAID	
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1. INTRODUCTION AND BACKGROUND

Initial Issuance

The National Treasury, was expected to raise USD2,000,000,000 through the international sovereign bond issuance as follows; (i) aggregate principal amount of USD500,000,000 at the rate of 5.875 per cent on Notes due 2019, and (ii) aggregate principal amount of USD1,500,000,000 at the rate of 6.875 per cent on Notes due 2024; all to be transacted by June 2014.

Table 1: Initial issuance

Receiving Bank	Amount USD
Gross Expected Proceeds – Initial Issuance	2,000,000,000
Less: Legal Counsel, Joint Lead Managers Fees, Road Show Expenses and Other Transaction Expenses associated with the Initial Issuance. (see table 2)	(1,002,237)
Net Proceeds – Initial Issuance	1,998,997,763

Table 2: Breakdown of the initial issuance costs

Ref	Nature of Expense	Amount USD
1	International Counsel	400,000
2	Local Counsel	16,350
3	Prospectus Printing	28,000
4	Agent Cost	8,140
5	Stock Exchange	7,380
6	Roadshow Expenses	282,267
7	Lead Managers out of pocket expenses	60,000
8	Joint Lead Managers Fees	200,000
	Total Costs	1,002,237

Tap Sale

In addition, the National Treasury engaged in a “tap sale” of Notes as follows; (i) aggregate principal amount of USD250,000,000 at a rate of 5.875 per cent on Notes due in 2019, and (ii) aggregate principal amount of USD500,000,000 at a rate of 6.875 per cent Notes due by December 2014. Collectively known as Eurobond.

Table 3: Tap Sales

Date	Receiving Bank	Amount USD
03.12.2014	Tap Sale at Par Value	750,000,000
03.12.2014	Premium from Tap Sale	65,684,271
03.12.2014	Transaction Fees and Commissions (see table 4)	(247,339)
	Net Proceeds	815,436,932

Table 4: Breakdown of the Issuance Costs

Ref	Nature of Expense	Amount USD
1	International Counsel	30,125
2	Local Counsel	95,000
3	Prospectus Printing	2,875
4	Agent Cost	6,860
5	Stock Exchange	3,979
6	Roadshow Expenses	3,500
7	Lead Managers out of pocket expenses	30,000
8	Joint Lead Managers Fees	75,000
	Total Costs	247,339

2. RECEIPTS OF THE PROCEEDS OF EUROBOND

Initial Issuance

JP Morgan Chase Bank New York and Citibank N.A New York were appointed the receiving banks of the proceeds of Eurobond during the initial issuance. The scope on verification of funds flow was to the extent that the special audit did not proceed further to ascertain the actual receipts from investors at the receiving banks. The money was collected by the receiving banks and subsequently transferred in three batches in bulk to JP Morgan Chase Bank New York - GoK/CBK Sovereign Bond Account Number 60314998 as highlighted below:

Table 5: Receipts into the JP Morgan Chase Bank New York – GOK/CBK Sovereign Bond Account Number 60314998

Date	Receiving Bank	Account Ref.	Amount USD
26.06.2014	JP Morgan Chase Bank New York	EC40 J-P	875,041,000
26.06.2014	Citibank N.A New York	10043-0001	846,721,763
26.06.2014	Citibank N.A New York	10043-0001	277,235,000
Total Net Receipts			1,998,997,763

The net receipts into the JP Morgan Chase Bank New York earned interest amounting to USD 245,956 which increased the accumulated amount in the account to USD 1,999,243,719 as shown below:

Table 6: Interest earned on the JP Morgan Chase Bank New York Account

Date	Receiving Bank	Ref	Amount USD
Net Receipts into JP Morgan Chase Bank New York (a)			1,998,997,763
Add: interest earned on deposits into JP Morgan Chase Bank New York			
30.06.2014	Interest Earned	60314998	76,541
30.07.2014	Interest Earned	60314998	169,415
Total Interest Earned (b)			245,956
Cumulative amounts in the JP Morgan Chase Bank New York (a + b)			1,999,243,719

The funds flow of the initial issuance out of the "JP Morgan Chase Bank New York - GoK/CBK Sovereign Bond Account Number 60314998 are as highlighted below:

Table 7: Fund movement out of JP Morgan Chase Bank New York - GoK/CBK Sovereign Bond Account Number 60314998

Date	Details	Reference	Amount USD
Net receipts and interest earned as per above			1,999,243,719
Withdrawals/Charges			
30.06.2014	Federal Tax on Interest Withheld	60314998	(21,431)
03.07.2014	Repayment to Standard Chartered Bank New York - Syndicate Loan	A/c. No. 3582088442001	(604,560,737)
03.07.2014	Transfer to Federal Reserve Bank of New York	A/c. No. 021084571	(395,439,262)
30.07.2014	Federal Tax on Interest Withheld	60314998	(47,436)
10.09.2014	Transfer to Federal Reserve Bank of New York	A/c. No. 021084571	(999,018,456)
Account operation charges			(156,397)
Balance at JP Morgan Chase Bank New York			-

There was no fund balance at the JP Morgan Chase Bank New York.

Tap Sale

JP Morgan Chase Bank London and Citibank N.A London were appointed the receiving banks of the proceeds of Eurobond during the "Tap sale". The scope on verification of funds flow was also limited to the extent that the special audit was not able to ascertain the actual receipts from investors at the receiving banks. The money was collected by the receiving banks and subsequently transferred in three batches to CitiBank N.A. New York - GoK/CBK Sovereign Bond Tap Proceeds Account Number 36341018 as highlighted below:

Table 8: Receipts in the CitiBank N.A. New York - GoK/CBK Sovereign Bond Tap Proceeds Account Number 36341018

Date	Bank	Account Ref.	Amount USD
03.12.2014	JP Morgan Chase Bank London	021000021	238,483,308
03.12.2014	Citibank N.A London	10990765	382,551,426
03.12.2014	Citibank N.A London	10990765	194,402,198
Total Receipts			815,436,932

Funds flow of the "tap sale" out of the CitiBank N.A. New York - GoK/CBK Sovereign Bond Tap Proceeds Account Number 36341018 are as highlighted below:

Table 9 : Funds movement out of CitiBank N.A. New York - GoK/CBK Sovereign Bond Tap Proceeds Account Number 36341018

Date	Details	Reference	Amount USD
Opening Balance			815,436,932
18.12.2014	Transfer to Federal Reserve Bank of New York	A/c. No. 021084571	(815,436,932)
Closing Balance			-

Receipts into the National Exchequer Accounts

A portion of the proceeds of Eurobond totaling USD 604,560,737 (Kshs.53,201,344,900) was utilized overseas as repayment of a syndicate loan. The balance of the proceeds of Eurobond from both the original issuance and the "tap sale" were received into the country as follows:

Table 10: Receipts of the initial issuance in the Receipts into the National Exchequer Accounts

Date	Remitting institution	Receiving institution	Amount USD	Amount Kshs.
03.07.2014	Federal Reserve Bank of New York A/c. No. 021084571	Central Bank of Kenya National Exchequer A/c. No. 100003987	395,439,262	34,648,388,180
10.09.2014	Federal Reserve Bank of New York A/c. No. 021084571	Central Bank of Kenya Proceeds of Sovereign Bond A/c. No. 8000212764	999,018,701	88,463,084,420
Received balance			1,394,457,963	123,111,472,600

Table 11: Receipts of tap sale in the Receipts into the National Exchequer Accounts

Date	Remitting institution	Receiving institution	Amount USD	Amount Kshs.
18.12.2014	Federal Reserve Bank of New York A/c. No. 021084571	Central Bank of Kenya Proceeds of Sovereign Bond A/c. No. 10000212764	815,436,932	73,805,196,715
Received balance			815,436,932	73,805,196,715
Total receipt of the proceeds of Eurobond (table 10 + table 11)				196,916,669,315

The special audit therefore confirmed that the Eurobond proceeds were received, and were fungible (came into one pot), at the National Exchequer Accounts in Central Bank of Kenya and therefore not identifiable to any particular infrastructure project. Consequently, the proof in total for the fiscal year 2014/2015 was necessary and thus required a delay to allow for an audit trail through to utilization in order to be conclusive. The transfers into the National Exchequer Accounts at Central Bank of Kenya were as detailed below:

Table 12: Original Issuance transfers

Date	Transfer	Amounts Kshs.
03.07.2014	CBK National Exchequer A/c. No. 100003987	34,648,388,180
15.09.2014	CBK National Exchequer A/c. No. 100003987	25,000,000,000
19.09.2014	CBK National Exchequer A/c. No. 100003987	25,000,000,000
30.09.2014	CBK National Exchequer A/c. No. 100003987	15,000,000,000
15.09.2014	CBK National Exchequer A/c. No. 100003987	23,463,084,420

Table 13: Tap sale transfers

21.01.2015	CBK National Exchequer A/c. No. 100003987	1,536,915,580
17.03.2015	CBK National Exchequer A/c. No. 100003987	25,000,000,000
02.06.2015	CBK National Exchequer A/c. No. 100003987	30,000,000,000
01.07.2015	CBK National Exchequer A/c. No. 100003987	17,268,281,135
Total (table 12 + table13)		196,916,669,315

3. EXCHEQUER RELEASES

The special audit further noted that at a global level, the records of government receipts at CBK reconciled with the records of the National Exchequer Accounts at the National Treasury.

Table 14: Reconciliation of receipts and issuance

	30 June 2015	30 June 2014
	Kshs.	Kshs.
Receipts		
Tax Income	1,001,245,431,206	893,547,719,445
Non-tax Income	40,804,376,558	42,790,876,550
Proceeds from domestic borrowing	292,680,000,000	267,360,000,000
Grants	10,473,510,502	11,126,034,282
Proceeds from external borrowings – Euro Bond	162,268,281,136	34,648,388,180
Proceeds from external borrowings - Others	86,965,501,361	28,432,304,539
Total Receipts	1,594,437,100,763	1,277,905,322,996
Issues from the Exchequer		
National Government for recurrent expenditure	640,352,208,883	601,745,585,436
National Government for development expenditure	270,240,838,230	224,355,607,699
Consolidated fund services	454,466,411,172	258,792,271,715
Sub-total: Issues to National Government	1,365,059,458,285	1,084,893,464,850
Issues to County Governments	229,336,237,197	193,345,947,825
Total Issues	1,594,395,695,482	1,278,239,412,675
Excess\ (Deficit) of Receipts over issues during the year	41,405,281	(334,089,679)
Balance brought forward	162,277,138	496,366,817
Balance carried forward	203,682,419	162,277,138

4. UTILIZATION OF THE EUROBOND

The special audit compared expenditure as disclosed in the annual consolidated financial statements to development and recurrent expenditure from the IFMIS Vote Book for the financial year 2014/2015 and noted the following differences which were reconciled with the appropriation accounts as below:

Table 15: Reconciliation between IFMIS AND Consolidated Financial Statements

DESCRIPTION	Amount Kshs.
Development Expenditure as per IFMIS vote Book	268,553,690,241
Recurrent Expenditure as per IFMIS vote Book	383,087,510,768
Reconciling items Between IFMIS and the National Treasury Appropriation	
Total probable expenditure financed through AIA revenue (table 16)	179,193,452,944
Total expenditure of entities not in IFMIS Vote Book (table 17)	725,318,230,052
Other timing variance between IFMIS Vote Book and Appropriation	(7,914,324,604)
Total expenditure expected in the Consolidated Financial Statement	1,548,238,559,401
Total expenditure as per the Consolidated Financial Statement	1,548,238,559,401
Difference	-

Expenses incurred through AIA

- i. The special audit noted that additional expenses being incurred through Appropriation-in-Aid and these funds were outlined in the consolidated receipts and payments of annual consolidated financial statement as summarized below:

Table 16 : Total probable expenditure financed through AIA revenue

Description	Amount Kshs.
Tax revenues	5,014,849,318
Proceeds from foreign and domestic grants	17,503,053,693
Transfers from other government grants	37,377,485,253
Proceed from borrowing	72,707,591,959
Proceeds from sale of assets	25,795,982,225
Refunds and reimbursements	4,458,659,802
Other revenues	16,335,830,694
Total AIA	179,193,452,944

Expenditures of entities not in the IFMIS in 2014/2015

The special audit noted differences between the National Exchequer Accounts for the year ended 30 June 2015, and the records of all payments through the IFMIS, for recurrent and development for six MDAs that did not process their transactions through IFMIS in the financial year 2014/15. These entities accounted for the expenditures difference of Kshs.725,318,230,052 are as shown below:

Table 17: Expenditures of entities not in the IFMIS in 2014/2015

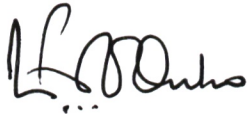
Vote	Entity	Expenditure incurred in 2014/2015 Kshs.
1041	Ministry of Defense	80,116,250,000
1281	National Intelligence Service	19,241,237,217
2019	Teachers Service Commission	170,984,437,579
R50	Public Debt-National Treasury	416,272,302,525
R51	Pension-National Treasury	35,270,693,993
R52	Salaries and Allowances- National Treasury	3,433,308,738
	Total	725,318,230,052

Based on the understanding that expenditure is initiated by the user through the budgetary and appropriation process, the special audit noted that these expenditures especially for the Ministry of Defense and the National Intelligence Service were under the rubric of confidential expenditure as they were disbursed and utilized outside of the Government Integrated Financial Management Information System (IFMIS).

5. CONCLUSION AND RECOMMENDATION

Based on foregoing, the special audit:

- i. Confirmed receipt of the Eurobond proceeds into the National Exchequer Accounts of the Country as per the preceding paragraphs;
- ii. Noted that utilization of the proceeds of the Eurobond could not be traced to specific development projects. The National Treasury explained that these funds were fungible. Furthermore, as identified in the report, some of the funds were expended outside of the Government Integrated Financial Management Information System; and
- iii. Therefore, recommends that subsequent issuance of international sovereign bonds should be earmarked and be identifiable to specific development projects.



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Nairobi

15 April 2019