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KENYA NATIONAL AUDIT OFFICE

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REPORT OF THE CONTROLLER AND AUDITOR-GENERAL

ON

THE FINANCIAL STATEMENTS OF TELKOM (K) LIMITED FOR THE YEAR ENDED 30 JUNE 2005

KENYA NATIONAL ASSEMBLY
Accession: 10013034

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MANAGEMENT REPORT AND FINANCIAL STATEMENTS

FOR THE PERIOD ENDING 30th JUNE 2005

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TELKOM KENYA LIMITED
DIRECTORS, OFFICERS AND ADMINISTRATION

Wilson N. Ayah	-	Chairman
Eng. John Waweru	-	Managing Director (Replaced 11 May 2005)
Sammy K. Kirui	-	Managing Director (Appointed 11 May 2005)
J.J Kinyua	-	PS MOF
C. Kimura	-	Alt. Director MOF (Replaced 11 March 2005)
Esther Koimett	-	Alt. Director MOF (Appointed 11 March 2005)
Eng. James Rege	-	PS MOI&C
A. Gakere	-	Alt. Director MOI&C (Replaced 15 September 2004)
Felix Mugabe	-	Alt. Director MOI&C (Appointed 15 September 2004)
Bishop Otanga	-	Director
Martin Malinda	-	Director
Nicholas Nganga	-	Director
Grace Chomba	-	Director
Father (Dr) D. Wakimani	-	Director (Appointed 6 June 2005)
John M. Makau	-	Director (Appointed 6 June 2005)
Adan A. Hassan	-	Director (Appointed 4 June 2005)

SECRETARY

P.B. Jilani

AUDITOR

Controller and Auditor General
Kencom House
P.O. Box 30084
Moi Avenue
Nairobi

REGISTERED OFFICE & PRINCIPAL PLACE OF BUSINESS

Telkom Kenya Limited
GPO/Teleposta Towers
Kenyatta Avenue
P.O. Box 30301
Nairobi

BANKERS

Kenya Commercial Bank Limited
Kencom House
Moi Avenue
P.O. Box 30081
Nairobi

National Bank of Kenya
Harambee Avenue
P.O. Box 41862
Nairobi

ADVOCATES

The company engages different advocates depending on the nature of professional services required.

TELKOM KENYA LIMITED
STATEMENT OF DIRECTORS RESPONSIBILITIES

The Companies Act requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company as at the end of each financial year and of its operating results for that year. It also requires the Directors to ensure that the Company keeps proper accounting records, which disclose with reasonable accuracy at any time the financial position of the company. They are also responsible for safeguarding the assets of the Company.

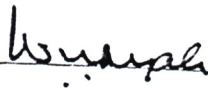
The directors accept responsibility for the annual financial statements which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with generally accepted accounting practice and the requirements of the Companies Act. The directors are of the opinion that the financial statements give a true and fair view of the state of the Company and of its operating results. The directors further accept responsibility for the maintenance of accounting records which may be relied upon in the preparation of financial statements, as well as adequate systems of internal financial control.

Nothing has come to the attention of the directors to indicate that Company will not remain a going concern for at least the next twelve months from the date of this statement.

Director



Director



Date:

29/09/05



KENYA NATIONAL AUDIT OFFICE

REPORT OF THE CONTROLLER AND AUDITOR GENERAL ON THE FINANCIAL STATEMENTS OF TELKOM (K) LIMITED FOR THE YEAR ENDED 30 JUNE 2005

The financial statements of Telkom Kenya Limited for the year ended 30 June 2005 on pages 4 to 38, which have been prepared on the basis of the accounting policies set out on pages 11 to 13, have been audited on my behalf by the authorized auditors appointed under section 39 of the Public Audit Act, 2003. The auditors have duly reported to me the results of their audit and on the basis of their report, I am satisfied that the financial statements are generally in agreement with the books of account.

Respective responsibilities of the Directors and the Controller and the Auditor General

As set out in the statement of directors' responsibilities, the directors are responsible for the preparation of financial statements which give a true and fair view of the Company's state of affairs and its operating results. My responsibility is to express an independent opinion on the financial statements based on the audit.

Basis of Opinion

The audit was conducted in accordance with International Standards on Auditing. Those standards require that the audit be planned and performed with a view to obtaining reasonable assurance that the financial statements are free from material misstatement. An audit includes an examination, on a test basis, of evidence supporting the amounts and disclosures in the financial statements. It also includes an assessment of the accounting policies used and significant estimates made by the directors, as well as an evaluation of the overall presentation of the financial statements. I believe the audit provides a reasonable basis for my opinion.

- 1. Non-compliance with International Financial Reporting Standards and International Accounting Standards**
- 1.1 Financial statements presentation and disclosure**

The accounts have not been prepared and presented according to the requirements of International Financial Reporting Standards and

International Accounting Standards as the financial statements do not have the reporting entity's name identified prominently including the notes as per the requirements of paragraph 44 IAS No.1. Further, comparative figures in the cashflow statement were missing which is a departure from paragraph 36 IAS No.1 requirements. In addition significant notes on turnover, administrative expenses, operational expenses, bank balances and capital account were missing. The date when the financial statements were authorised for issue and by whom have not been disclosed in the financial statements. Failure to adhere to the requirements of International Financial Reporting Standards and International Accounting Standards has not been explained.

1.2. International Accounting Standard No. 28

Contrary to the requirements of International Accounting Standard No. 28 on 'Accounting for Investments in Associates', the investments in Kenya Postel Directories Limited 40% and Erigtel Limited 49% as associates of the company respectively, have not been accounted for under the equity method. Management has not quantified the effect of this non-compliance on the consolidated financial statements.

1.3. International Accounting Standard No.12

As indicated in the accounting policy on taxation to the financial statements, no provision has been made for deferred tax contrary to the requirements of International Accounting Standard No. 12 on 'Income Taxes'. Management has not quantified the effect of this departure on the financial statements.

1.4. International Accounting Standard No.17

Leasehold land has not been separately accounted for as prepaid operating lease rentals as required by International Accounting Standard No.17 on 'Leases'. Management has not quantified the effect of this departure on the financial statements.

1.5. International Accounting Standard No. 24

The requirements of International Accounting Standard No.24 on 'Related Party Disclosures' have not been fully complied with as disclosures have not been made for some related party transactions and balances.

1.6. International Accounting Standard No. 19

Provision for outstanding leave and long term service dues has not been made as required by International Accounting Standard No.19 on

'Employee Benefits'. Management has not quantified the effect of this departure on the financial statements.

2. Cash and Bank Balances

The accuracy of bank balances amounting to KShs.58 million could not be verified in the absence of a reconciliation of the difference of KShs.34 million between the bank confirmations received from the bankers of the company amounting to Kshs.24 million. In addition it was not possible to verify how overdraft balances of Kshs.73 million and letters of credit and bills of acceptances drawn amounting to Kshs.432 million as confirmed by the bankers of the company, have been accounted for in the absence of adequate records and documentation. Further, the accuracy of cash in transit balance could not be confirmed in the absence of a reconciliation of the difference of Kshs.870 million between the cash in transit as per the financial statements of Kshs.241 million and cash in transit as per the accounting records of Kshs.1,111 million as at the year end. Further, no provisions have been made in the financial statements with regard to cash in transit balances which have remained long outstanding. This has resulted in the overstatement of the cash in transit balance, included under cash and cash equivalents, by Kshs.403 million at the year end.

3. Turnover

The completeness of income from public payphones could not be verified in the absence of a reconciliation of the difference of Kshs.1,560 million between the revenue as per the billing system of Kshs.2,078 million and the actual revenue reported of Kshs.518 million. Further the Integrated Services Digital Network (ISDN) credit adjustments amounting to Kshs.5 million during the year could not be verified in the absence of adequate supporting documentation. In addition telephone credit adjustments amounting to Kshs.459 million during the year and completeness of 'Other Income' received amounting to Kshs.176 million could not be confirmed due to absence of supporting documents. In addition, contrary to the company's accounting policy, revenue from prepaid telephone services has been recognised as income based on sale of prepaid cards rather than on utilisation of airtime by the customer. Consequently unused airtime is not recognised as deferred income. Management has not quantified the effect of this departure from the accounting policy on the financial statements. Further, total income from various sources is understated by Kshs.64 million.

4. Creditors

- 4.1 The accuracy, validity and completeness of other staff advances, included under 'creditors' could not be confirmed in the absence of a reconciliation of the difference of Kshs.45 million between the staff advances as included in the accounting records of a credit balance of Kshs.27 million and as indicated by the payroll department of Kshs.18 million as amounts

due from employees. Further, the validity and completeness of amounts payable to local and overseas suppliers amounting to Kshs.1,851 million included under 'Creditors' could not be confirmed due to absence of reconciliations between balances as per the financial records of the company and suppliers statements. In addition, the validity and completeness of revenue creditors amounting to Kshs.309 million and sundry creditors of Kshs.113 million included under 'creditors' could not be verified as a result of inadequate supporting records and documentation.

- 4.2 The validity, existence and valuation of other creditors described as 'reversal from bank adjustments – creditors', included under 'Creditors' amounting to KShs.160 million could not be confirmed due to absence of adequate supporting records and documentation. Furthermore the completeness of Kenya Postel Directories (KPD) net creditor's balance of KShs.45 million, made up of KShs.1,262 million in revenue and below the line creditors and KShs.1,217 million in non-operational revenue debtors, could not be confirmed in the absence of a reconciliation of a difference of Kshs.108 million arising from KPD's direct confirmation showing Kshs.153 million. In addition, the difference of KShs.638 million in the absence of a reconciliation between the balances in subsidiaries as included in the accounting records of the company of Kshs.3,563 million and as disclosed in the accounting records of the subsidiaries of Kshs.2,925 million could not be verified.
- 4.3 The completeness, validity and existence of other creditors described as institutions – insurance companies and co-operatives, included under 'Creditors' could not be confirmed in the absence of a reconciliation for the difference of Kshs.187 million between the balance included in the accounting records of the company of Kshs.210 million and the underlying records provided by the salaries department of Kshs.23 million.
- 4.4 The other creditors difference of Kshs.30 million could also not be verified in the absence of reconciliation between the balances as disclosed in the accounting records of the company of Kshs.30 million and a nil balance in the supporting schedules records. Additionally, the completeness, validity and existence of other creditors (described as suspense) included under 'Creditors' amounting to Kshs.684 million could not be confirmed as at 30 June 2005.
- 4.5. Other sundry creditors, included in 'Creditors' as at 30 June 2005 were overstated by Kshs.16 million as these relate to accounts long outstanding for over four years and which should have been settled or written back to the accounts.

5. Property, Plant and Equipment

- 5.1** The additions to property, plant and equipment during the year amounting to Kshs.1,550 million, their existence and the accounting treatment of plant and machinery, acquired through credit notes issued to customers amounting to KShs.59 million could not be verified in the absence of adequate supporting documentation. Further, the difference of Kshs.39 million could not be verified in the absence of reconciliation between additions to land and buildings as per schedules provided by the engineering department of Kshs.63 million and costs as per the financial statements of Kshs.102 million. It was also not possible to verify the validity of additional indirect overhead costs amounting to Kshs.39 million incurred on capital projects executed during the year in the absence of adequate supporting records and documentation.
- 5.2** The completeness of plant and machinery and motor vehicles, included in the balance sheet as at 30 June 2005, could not be verified due to lack of a reconciliation of a difference of Kshs.533 million between the fixed assets listed in the fixed assets register of Kshs. 26,840 million and the fixed assets as per the financial statements of Kshs.26,307 million. Further, the completeness, valuation and existence of furniture and equipment, included under property, plant and equipment as at 30 June 2005, at net book value of Kshs.408 million could not be confirmed as these were not included in the fixed assets register.
- 5.3** The completeness of motor vehicles, included under property, plant and equipment as at 30 June 2005 and their ownership could not be verified in the absence of a complete motor vehicles register. In addition, included under property, plant and equipment as at 30 June 2005 is Kshs.496 million worth of properties which were vested in Telkom Kenya Limited on 1 July 1999, but which could not be verified as the company does not have the original titles for the properties.

6. Debtors

The existence and valuation of current debtors included in 'Debtors', could not be verified in the absence of a reconciliation of the difference amounting to Kshs.2,693 million between the trade debtors balance as per the financial statements of Kshs.9,462 million and the underlying records balance of Kshs.6,769 million. Further the adequacy of provisions for bad and doubtful debts amounting to Kshs.13,445 million could not be confirmed in the absence of listings of related debtors supporting this amount. Moreover the existence of sundry debtors and prepayments amounting to Kshs.1,110 million, included in 'Debtors', could not also be confirmed due to lack of adequate supporting records and documentation. It was also not possible to confirm whether all goods or services were subsequently received for the advance payments of Kshs.1,110

million. Additionally, it was not possible to confirm the existence of staff loans of Kshs.32 million due to absence of adequate supporting documentation. Further, provision for bad and doubtful debts, included under trade debtors is understated by Kshs.677 million which is the amount of long outstanding debts due to the company from various debtors including government institutions and other privileged institutions that are not provided for. This has had the effect of overstating debtors and understating the loss for the year by a similar amount. In addition, provision for staff advances, included under other debtors, is also understated by Kshs.11 million. This has the effect of overstating other debtors and understating the loss for the year by a similar amount.

7. Pensions

The completeness and validity of the balance payable on account of the pension and provident fund schemes could not be verified, in the absence of a reconciliation of the difference of Kshs.2,304 million between the actual pension and provident fund balances reported in the financial statements of Kshs.4,258 million and the balance as confirmed by Teleposta Pension Scheme of Kshs.1,954 million and also in the absence of an updated actuarial valuation, the last one being for Kshs.6,044 million as at 30 June 2004. The validity of payments made to Teleposta Pension Fund for employee contributions amounting to Kshs.563 million and other pensions accounts (BTL creditors), included under 'Creditors', with a net credit balance of KShs.22 million could also not be verified due to absence of adequate supporting evidence and documentation.

8. Loans

The completeness and valuation of two loan balances as at the year end could not be verified in the absence of a reconciliation of the difference of Kshs.115 million between the actual loan balances reported in the financial statements of Kshs.706 million and the balances as confirmed by the financiers of the company of Kshs.591 million. In addition, loans outstanding as at 30 June 2005 are understated by Kshs.40 million being the difference between the loan schedule showing Kshs.123 million while accounts reflect Kshs.83 million as a result of using incorrect foreign currency translations.

9. Stocks

The physical quantities of stocks amounting to Kshs.1,410 million as at 30 June 2005 could not be verified as the company did not carry out a physical count of stocks at the year-end. In the absence of adequate stock records, there were no alternative audit procedures that could be relied upon. Further, the basis of valuation and adequacy of the provisions for stock obsolescence at the year end could also not be verified in the absence of adequate supporting documentation and stock listings.

10. Other investments

The ownership and valuation of 'Other Investments' amounting to Kshs.132million including appropriateness of the accounting treatment of these investments could not be verified in the absence of adequate supporting documentation. In addition, it was not possible to verify the difference of Kshs.510 million in the absence of a reconciliation between the investments in subsidiaries included in the accounting records of the company of Kshs.2,149 million and disclosed in the accounting records of the subsidiaries of Kshs.2,658 million.

11. Expenses

The difference of Kshs.15 million between the salaries and wages expense as per financial statements of Kshs.6,161 million and salaries and wages expense as per payroll of Kshs.6,176 million could not be verified in the absence of a reconciliation. Further, it was not possible to verify other expenses amounting to Kshs.2,395 million due to lack of adequate supporting documentation. In addition it was noted that total interest expense on loans is understated by Kshs.447 million, and similarly borrowings are understated by a similar amount.

12. Corporation Tax Liability

It was not possible to verify corporate tax figure, to the profit and loss account, for the year amounting to Kshs.784 million and the corresponding amount included in the balance sheet, due to the absence of adequate supporting documentation.

13. Procurement procedures

13.1 The Company did not produce for audit review tender documents for construction of office extensions amounting to Kshs.29 million and for supply and delivery of access network repair tools and test gears amounting to Kshs.27 million, awarded during the year. Consequently it was not possible to comment on the adequacy of the procurement procedures and controls in relation to this specific tender.

13.2 The laid down procedures that require competitive bidding for the supply of goods or provision of services were not complied with in acquiring equipment and support services amounting to Kshs.1,024 million. Although it was explained that these specific items in question were only available from single suppliers, it was not possible to confirm that this was the case in the absence of adequate supporting documentation.

13.3 The total payments made on award of contracts by the company amounting to Kshs.38 million and US \$ 1.17 million (approximately Kshs.90 million) could not be verified and traced to the accounting

records. In addition, it was not possible to confirm that total contracts payments did not exceed the contracted amounts, as a result of inadequate supporting records and documentation.

- 13.4** Donation of equipment received amounting to Kshs.21 million and relevant taxes paid on the same amounting to Kshs.7 million could not be traced and verified in the absence of adequate supporting documentation.

14. Investment in Subsidiaries

14.1 Gilgil Telecommunications Industries Limited

Investment in subsidiaries as at 30 June 2005 amounting to Kshs.4,610 million includes an amount of Kshs.880 million being 100% ownership of Gilgil Telecommunications Industries Limited. The financial statements of Gilgil Telecommunications Industries Limited indicate that the company has consistently registered significant losses for the last six years since 1999. The value of the investment is therefore doubtful and may not be recoverable. No provision has been made for the diminution in value in the financial statements.

14.2 Kenya College of Telecommunications Technology Limited

Investment in subsidiaries, as at 30 June 2005, amounting to Kshs.4,610 million includes an amount of Kshs.1,269 million being 100% ownership in Kenya College of Telecommunications Technology Limited. The financial statements of Kenya College of Telecommunications Technology Limited indicate that the company has consistently registered significant losses, is unable to pay its creditors and its continued existence as a going concern is dependent upon the support of the parent company and its creditors. The value of the investment is therefore doubtful and may not be recoverable. No provision has been made for the diminution in value in the financial statements.

14.3 Loan to the subsidiary

Included under the company's investment in subsidiaries is an amount of Kshs.2,541 million which is a loan to Safaricom Ltd which ought to have been disclosed separately as other non-current receivables rather than investments.

15. Contingent liabilities

Based on representations by some of the company's legal advisors, an amount of Kshs.599 million of possible litigation claims and charges payable exist,

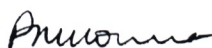
although these have not been disclosed as contingent liabilities. In addition, management has not assessed the financial impact of the same.

Emphasis of matter

Without qualifying my opinion I draw attention to Note no. 21 to the financial statements which indicates that the Government disbursed a loan of Kshs.2,609 million (US\$ 33,000,000) to Telkom Kenya Limited in 2001 that was repayable fully within two weeks of completion of the intended sale of the Safaricom shares to a strategic partner. The loan carried interest at the rate of 7.5% per annum with additional interest of 9.5% being chargeable on payments delayed based on the agreed repayment plan. Having defaulted on the repayment of this loan, the company has entered into negotiation with the Government to vary the terms of the loan and have, therefore, not provided for the penal interest since 2001 estimated at Kshs.1,069 million. Negotiations are in progress and, I understand the government has to date not enforced the repayment clause. Resolution of this matter could have an effect on the results and financial position of the company and the group.

Opinion

Except for the effect of any adjustments that may be necessary to the company and group financial statements on the matters referred to in the preceding paragraphs, in my opinion the financial statements present fairly, the financial position of the company and the group as at 30 June 2005 and of their losses and cash flows for the year then ended in accordance with International Financial Reporting Standards, except as reported under paragraph 1, and comply with the Companies Act (Cap. 486 of the Laws of Kenya).



**P.N. KOMORA
CONTROLLER AND AUDITOR GENERAL**

Nairobi

07 December 2006

TELKOM KENYA LIMITED
COMPANY PROFIT AND LOSS ACCOUNT
FOR THE PERIOD ENDING 30TH JUNE 2005

	Notes	JUNE 2004	JUNE 2005
		Kshs Million	Kshs. Million
Turnover		20,063	17,657
Administration expenses		(2,921)	(2,978)
Operational expenses		(2,384)	(3,948)
Other operating expenses	2(b)	<u>(16,925)</u>	<u>(14,135)</u>
		<u>(22,230)</u>	<u>(21,061)</u>
Profit/(Loss) from operations		(2,167)	(3,404)
Net finance cost	3(b)	(577)	(696)
Loss before tax		<u>(2,744)</u>	<u>(4,100)</u>
Other income	4(b)	516	602
Profit/(Loss) before tax		(2,228)	(3,498)
Tax	6(b)	(257)	764
Net profit/(loss) after tax		<u>(2485)</u>	<u>(2,733)</u>

The company profit and loss account is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

TELKOM KENYA LIMITED
CONSOLIDATED PROFIT AND LOSS ACCOUNT
FOR THE PERIOD ENDING 30TH JUNE 2005

	Notes	JUNE 2004	JUNE 2005
		Kshs Million	Kshs. Million
Turnover		36,841	47,180
Administration expenses		(4,794)	(4,476)
Operational expenses		(6,220)	(10,815)
Other operating expenses	2(a)	<u>(21,966)</u>	<u>(25,158)</u>
		<u>(32,979)</u>	<u>(40,450)</u>
Profit from operations		3,862	6,730
Net finance cost	3(a)	(899)	(2,232)
Profit before tax		2,963	4,498
Other income	4(a)	534	1,074
Profit before tax		3,497	5,573
Tax	6(a)	<u>(2,083)</u>	<u>(2,260)</u>
Net profit/(Loss) tax		1,414	3,312
Minority interest	20	<u>(1,597)</u>	<u>(2,511)</u>
Net profit /(loss) for the year after tax and minority interest		<u>(183)</u>	<u>801</u>

The consolidated profit and loss account is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

TELKOM KENYA LIMITED
COMPANY BALANCE SHEET AS AT 30TH JUNE 2005

ASSETS	NOTES	JUNE 2004 Kshs. Million	JUNE 2005 Kshs. Million
Non current assets			
Property, plant and equipment	7(b)	33,499	32,359
Investment in subsidiary	8	5,879	5,879
Investment in associate	10	9	9
Other investments	11	906	132
Other assets	12	<u>1,453</u>	<u>1,285</u>
Current Assets			
Stocks	13(b)	<u>41,746</u>	<u>39,664</u>
Debtors	14(b)	1,400	1,464
Bank deposits	15	21,266	22,367
Bank balances and cash		331	251
Current A/C GTI		824	739
TOTAL ASSETS		<u>964</u>	<u>1,066</u>
		<u>24,785</u>	<u>25,887</u>
		<u>66,531</u>	<u>65,551</u>
EQUITY AND LIABILITIES			
Capital and reserves			
Government interest	17	21,075	21,075
Reserves	19(b)	12,575	9,841
		<u>33,650</u>	<u>30,916</u>
Non current liabilities			
Government loan	21	2,609	2,609
Long term loans	22	3,180	530
Pensions	23	<u>1,641</u>	1,384
		<u>7,430</u>	<u>4,523</u>
Current liabilities			
Creditors	24(b)	18,133	23,750
Corporation tax	25	4,405	3,640
KPTC Corporation tax	26	1,648	1,648
Bank overdraft	27	<u>1,265</u>	<u>1,073</u>
		<u>25,451</u>	<u>30,111</u>
TOTAL EQUITY AND LIABILITIES		<u>66,531</u>	<u>65,551</u>

The company balance sheet is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.


DIRECTOR

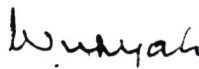

DIRECTOR

TELKOM KENYA LIMITED
CONSOLIDATED BALANCE SHEET AS AT 30TH JUNE 2005

ASSETS	NOTES	JUNE 2004 Kshs Million	JUNE 2005 Kshs. Million
Non current assets			
Property, plant and equipment	7(a)	56,359	64,427
Intangible assets	9	3,249	2,923
Investment in associate	10	9	9
Other investments	11	906	132
Other assets	12	<u>1,800</u>	1,285
Current Assets		<u>62,323</u>	<u>68,776</u>
Stocks	13(a)	2,152	2,318
Debtors	14(a)	22,415	23,610
Bank deposits	15	332	252
Bank balances and cash		1,815	2,139
Escrow Account	16	<u>431</u>	<u>25</u>
TOTAL ASSETS		<u>27,145</u>	<u>28,344</u>
		<u>89,468</u>	<u>97,120</u>
EQUITY AND LIABILITIES			
Capital and reserves			
Government interest	17	21,075	21,075
Grants	18	2	2
Reserves	19(a)	11,973	12,774
Minority interest	20	6,011	9,483
Capital Account		<u>3,850</u>	<u>3,850</u>
		<u>42,911</u>	<u>47,184</u>
Non current liabilities			
Government loan	21	2,609	2,609
Long term loans	22	3,180	530
Pensions	23	1,839	1,601
Commercial Paper	16	<u>7,495</u>	<u>5,726</u>
		<u>15,123</u>	<u>10,466</u>
Current liabilities			
Creditors	24(a)	24,095	33,091
Corporation tax	25	4,405	3,640
KPTC Corporation tax	26	1,648	1,648
Bank overdraft	27	<u>1,287</u>	<u>1,091</u>
		<u>31,435</u>	<u>39,470</u>
TOTAL EQUITY AND LIABILITIES		<u>89,468</u>	<u>97,120</u>

The consolidated balance sheet is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.


DIRECTOR


DIRECTOR

**TELKOM KENYA LIMITED
CONSOLIDATED CASH FLOW STATEMENT
FOR THE PERIOD ENDING 30TH JUNE 2005**

	NOTES	JUNE 2005 Kshs. Million
Cash inflow from operating activities	29(b)	19,075
Corporation tax paid		(765)
Investing activities		
Purchase of fixed assets		(18,748)
Disposal of investments		774
Cash outflow from investing activities		<u>(17,974)</u>
Financing activities		
Interest paid		(367)
Interest received		64
Cash outflow from financing activities		<u>(303)</u>
Net decreases in cash and cash equivalents		<u>(33)</u>
Cash and cash equivalent – 30.6.2004		<u>1,291</u>
Cash and cash equivalent – 30.6.2005		<u>1,325</u>

The consolidated cash flow statement is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

**TELKOM KENYA LIMITED
COMPANY CASH FLOW STATEMENT
FOR THE PERIOD ENDING 30TH JUNE 2005**

	NOTES	JUNE 2005 Kshs. Million
Cash inflow from operating activities	28(a)	1,162
Corporation tax paid		-
Investing activities		
Purchase of fixed assets		1,605
Disposal of investments		774
Cash outflow from investing activities		<u>(831)</u>
Financing activities		
Interest paid		(367)
Interest received		64
Cash outflow from financing activities		<u>(303)</u>
Net decreases in cash and cash equivalents		<u>(41)</u>
Cash and cash equivalent – 30.6.2004		<u>(110)</u>
Cash and cash equivalent – 30.6.2005		<u>(83)</u>

The company cash flow statement is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

TELKOM KENYA LIMITED
STATEMENT OF CHANGES IN EQUITY
FOR THE PERIOD ENDING 30TH JUNE 2005

(a) **Company**

	Government Interest	Retained surplus	Revaluation Reserve	Total
	Kshs. Million	Kshs. Million	Kshs. Million	Kshs. Million
Balance as at 1 st July 2004	21,075	11,641	933	33,649
Retained profit/(loss) for the year	-	(2,733)	-	(2,733)
At 30th June 2005	<u>21,075</u>	<u>8,908</u>	<u>933</u>	<u>30,916</u>

(b) **Group**

	Government Interest	Retained surplus	Revaluation Reserve	Total
	Kshs. Million	Kshs. Million	Kshs. Million	Kshs. Million
Balance as at 1 st July 2004	21,075	11,040	933	33,048
Retained profit/(loss) for the year	-	801	-	801
At 30th June 2005	<u>21,075</u>	<u>11,841</u>	<u>933</u>	<u>33,849</u>

The statement of changes in equity is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 11 to 38.

TELKOM KENYA LIMITED
NOTES TO THE FINANCIAL STATEMENT
FOR THE PERIOD ENDING 30th JUNE 2005

1. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements are set out below:-

a) Basis of Preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards under the historical cost convention modified by the revaluation of Plant, Property and Equipment.

b) Consolidation Principles

The financial statements include those of the company, the Kenya College of Communication Technology Ltd. (KCCT), Gilgil Telecomms Industries Limited (GTI) and Safaricom Limited (SCL).

The financial year end of Safaricom Limited is 31st March and the financial statements as at 31st March 2005 have been incorporated into these accounts. Also consolidated are its unaudited Management financial statements for the three month period ending 30th June , 2005 which is the financial year end of the parent company. The results of the following associated companies have not been consolidated:-

- ◆ Eritel Limited in which TKL's shareholding amounts to 49%. The value of TKL's investment in this company, Kshs.60 million, is deemed to be irrecoverable and has therefore been fully provided in these accounts.
- ◆ Kenya Postel Directories Limited (KPD) in which TKL has a 40% shareholding and whose accounting date is 31st December. Management believes that the operating results of the company are not material and will not have a significant effect on these financial statements.

c) Turnover

Turnover represents revenue accruing upon billings from the major services, namely domestic and international telephone, telex, interconnect services, Kenpac, Kenline, Jambonet and Kenstream, exclusive of value added tax and is recognised at the time of billing.

It does not include the value of TKL's own use of telephone and other related services. Airtime revenue from the prepaid services is recognised when used by the customer.

d) Foreign Currency Transactions

All assets and liabilities expressed in foreign currencies are translated into Kenya Shillings at the exchange rate ruling at the balance sheet date. Foreign currency transactions conducted during the year in foreign currencies are converted at the rates ruling at the date of transaction. The resulting differences are dealt with in the profit and loss account.

e) Property, Plant and Equipment

Items of property, plant and equipment are stated at cost or valuation less accumulated depreciation and impairment. Cost comprises purchase price, including import duties and non-refundable purchase taxes and directly attributable costs of bringing an asset to working condition for its intended use. Depreciation is calculated to write off the cost or valuation of fixed assets on a straight-line basis over the expected remaining useful lives of the specific assets. Indicative rates are as follows:-

	Useful lives (in years)
Freehold land	No depreciation
Leasehold land	Over the period of the lease
Buildings	1 -50 years
Motor vehicles	2 -10 years
Furniture and fixtures	1 -11 years
Computers	5 years
Plant and machinery	1 -25 years

f) Impairment of Property, Plant and Equipment

The carrying amounts of assets mentioned in Note (e) above are reviewed at each balance sheet date to determine whether these exceed the recoverable amounts in which case an impairment loss is recognised.

g) Investments

Investments are stated at the following values:

- ◆ Satellite and cable investments are stated at cost and depreciated over the useful life of the cable, appropriate provisions and write-offs are made where necessary.
- ◆ Other unquoted investments are stated at the lower of cost and management's opinion of net realisable value
- ◆ Quoted investments are stated at closing market value on the balance sheet date.

h) Stocks

Stocks are valued at the lower of cost and net realisable value. Cost is determined on a weighted average basis or where this is not available, depreciated replacement cost.

If the purchase or production cost is higher than net realisable value, stocks are written down to net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less estimated cost of completion and selling expenses.

i) Trade and Other Debtors

Trade and other receivables are stated at nominal value, less provision for any amounts expected to be irrecoverable.

j) Taxation

The tax charge for the year has been estimated on the adjusted group accounting profit in accordance with tax legislation. Deferred tax has not been computed.

k) Net Financial Costs

Finance costs incurred on the issue of Commercial Paper (medium Term floating rate secured notes) in June 2001 and July 2002 by Safaricom Ltd have been capitalised and are being amortised over the 5 year term of the paper. Net financial costs include interest payable on borrowings as well as interest receivable on funds invested outside the group.

l) Amortisation of Licence Fee

The cellular phone licence fee in SCL is being amortised over 15 years (the term of the licence), proportionate to the number of projected subscribers on the network in each year.

The projected subscribers for the first years are taken from the Business Plan with full network maturity being reached in Year 5 (i.e. year 5 to 15 will incur the same charge).

m) Cash and Cash Equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise cash in hand, bank balances, and deposits held at call with the banks net of bank overdrafts.

2. OTHER OPERATING EXPENSES

(a) Group

	June 2004	June 2005
	Kshs' Million	Kshs' Million
Depreciation charge	6,146	8,197
Maintenance	3,200	2,375
Interconnect charges	4,384	6,815
International services	1,443	1,670
Bad debts provisions	2,507	552
Pension scheme and provident fund cost	832	1,774
Licences	741	1,472
Utilities	574	321
Sales and marketing	706	768
Rentals	299	767
Training	76	209
Amortisation of mobile phone licence fee	311	146
Miscellaneous	747	150
Investment write-back	-	(58)
Total	<u>21,966</u>	<u>25,158</u>

(b) Company

	June 2004	June 2005
	Kshs' Million	Kshs' Million
Depreciation charge	2,787	2,745
Maintenance	2,740	2,232
Interconnect charges	5,052	4,300
International services	1,354	1,667
Bad debts provisions	2,492	548
Pension scheme and provident fund cost	742	860
Licences	668	606
Utilities	261	265
Sales and marketing	241	455
Rentals	273	240
Training	122	161
Investment write-back		(58)
Miscellaneous	193	114
Total	<u>16,925</u>	<u>14,135</u>

3. NET FINANCE COSTS

(a) Group

	June 2004	June 2005
	Kshs' Million	Kshs' Million
Interest payable	303	1,492
Foreign exchange loss	596	(114)
Financing costs		854
Interest income	—	—
Total	<u>899</u>	<u>2,232</u>

(b) Company

Interest expense	303	814
Foreign exchange loss	274	(119)
Interest income	—	—
Total	<u>577</u>	<u>696</u>

4. OTHER INCOME
(a) Group

	June 2004	June 2005
	Kshs' Million	Kshs' Million
Services to PCK	7	8
Services to SCL	44	37
Maintenance revenue	146	105
Sale of sundry equipment and stores	35	62
Interest on staff loans	67	64
Application, licensing and approval fees	2	2
KPD retention	188	57
Insurance GPA claims receipts	2	16
Safaricom other income	17	472
Miscellaneous	<u>26</u>	<u>252</u>
Total	<u>534</u>	<u>1074</u>

(b) Company

	June 2004	June 2005
	Kshs' Million	Kshs' Million
Services to PCK	7	8
Services to SCL	44	37
Maintenance revenue	46	105
Sale of sundry equipment and stores	19	62
Interest on staff loans	65	64
Application, licensing and approval fees	1	2
KPD retention	188	57
Insurance GPA claims receipts	3	16
Miscellaneous	<u>143</u>	<u>251</u>
Total	<u>516</u>	<u>602</u>

5. PROFIT BEFORE TAX

	June 2004 Kshs' Million	June 2005 Kshs' Million
Profit before tax is arrived at after charging:		
Staff costs	7,251	5,875
Depreciation	6,146	11,006
Director emoluments		
- Fees	3	3
- Other	1	2
Auditors remuneration		
- Current year	5	11

The number of employees engaged by the group as at 30th June 2005 was 18,892 analysed as follows:-

	June 2004 No. of Employees	June 2005 No. of Employees
Telkom Kenya Ltd (TKL)	17,959	17,328
Kenya College of Communication Technology	581	529
Gilgil Telecomms Industries Ltd	364	339
Safaricom	595	696
Total	<u>19,499</u>	<u>18,892</u>

6. INCOME TAX EXPENSE

(a) Group

	June 2004 Kshs' Million	June 2005 Kshs' Million
Current tax charge/(credit)	2,083	2,260

(b) Company

	June 2004 Kshs' Million	June 2005 Kshs' Million
Current tax charge/(credit)	(257)	764

The tax charge for the year has been estimated on the adjusted taxable profits. No provision has been made for interest and penalties amounting to Kshs 13 Billion due to late payments on the 1998/1999, 1999/2000, 2001/2002 and 2003/2004 tax liabilities as the same are expected to be waived by the Government as part of the restructuring of the company.

7. PROPERTY, PLANT AND EQUIPMENT

(a) Group

	Land and Buildings Kshs' Million	Plant & Machinery Kshs' Million	Motor Vehicle Kshs' million	Furniture & Office Equipment Kshs' million	Total Kshs' million
At 1 st July 2004	8,095	70,976	948	1,807	81,826
Adjustments	(49)	(42)			(91)
Additions	275	10,520	85	813	11,693
Disposals	-	-	(2)	-	(2)
At 30th June 2005	8,321	81,454	1,031	2,620	93,426
Depreciation					
At 1 st July 2004	832	18,742	590	717	20,881
Adjustments		(2,882)	(4)		(2,886)
Charge for the year	335	9,726	128	817	11,006
Disposals		-	(2)	-	(2)
At 30th June 2005	1,167	25,586	712	1,534	28,999
Asset in operation					
At 30 th June 2005	7,154	55,868	319	1,086	64,427

(b) Company

	Land and Buildings Kshs' Million	Plant & Machinery Kshs' Million	Motor Vehicle Kshs' million	Furniture & Office Equipment Kshs' million	Total Kshs' million
At 1 st July 2004	5,824	39,524	723	768	46,839
Other Adjustments	(49)	(42)			(91)
Additions	155	1,287	69	94	1,605
Disposals					
At 30th June 2005	5,930	40,769	792	862	48,353
Depreciation					
At 1 st July 2004	449	12,080	455	357	13,341
Adjustments		(88)	(4)		(92)
Charge for the year	89	2,470	89	97	2,745
Disposals					
At 30th June 2005	538	14,462	540	454	15,994
Asset in operation At 30th June 2005	5,392	26,307	252	408	32,359

Property titles

The group does not have titles for some of its properties, as summarised below

	Number of Properties	Professional Valuation Kshs.million
Registered	181	
Unregistered: - In Nairobi	-	
- Outside Nairobi	171	
Total properties valued as at 30th June 2005	352	6,147
Total properties owned	352	

Property valuation of **Ksh. 6,147 Million** does not include any capital cost incurred on the properties or depreciation since 1st July, 1999 the due date the properties were transferred to TKL.

8. INVESTMENT IN SUBSIDIARIES

These are stated at cost and include

Company	Key activity	Beneficial ownership	Company Kshs.million
KCCT Ltd	Manpower Training	100%	1,269
Gilgil Industries Ltd	Telecomms Assembly of Telecomms equipment	100%	880
Safaricom Ltd (SCL)	Cellular phone operator	60%	<u>3,730</u>
			<u>5,879</u>

The investment in SCL comprises

Transfer of mobile phone assets at Net value	1,189
Shareholders loan (US \$33 million)– acquisition of licence	2,541
	<u>3,730</u>

INVESTMENT IN SUBSIDIARY

No provision has been made in the accounts for the precarious financial position of GTI and KCCT, as their status is being addressed in the Corporate restructuring of Telkom Kenya limited.

9. INTANGIBLE ASSET

The intangible asset comprises the cost of the mobile phone licence issued to SCL by the Communications Commission of Kenya. The term of the licence is 15 years effective 1st July 1999. The cost of the licence is being amortised with effect from the date SCL commenced trading, 26th May 2000. A reconciliation of the balance is as follows:-

Group	2004 Kshs' Million	2005 Kshs' Million
Cost of the licence (US\$ 55 million)	4,235	4235
Deduct amortisation	<u>(986)</u>	<u>(1,312)</u>
	<u>3,249</u>	<u>2,923</u>

During the year, the company disposed of its investment in Intelsat and New Sky Satellite.

10. INVESTMENT IN ASSOCIATE

Group & Company

	2004	2005
	Kshs' Million	Kshs' Million
Kenya Postel Directories Limited 40%.	9	9

The investment in the associated company is carried at cost.

11. OTHER INVESTMENTS

International cable and satellite organisations

Group and Company

	June 2004	June 2005
	Kshs' Million	Kshs' Million
Gross value	1,233	906
LESS:		
Provisions	(267)	(105)
Disposals	(60)	(669)
Net	<u>906</u>	<u>132</u>

12. OTHER ASSETS

Other assets comprise the long-term portion of staff loans, as follows:-

	GROUP		COMPANY	
	June 2004	June 2005	June 2004	June 2005
	Kshs.million	Kshs.million	Kshs.million	Kshs.million
Total staff loans	2,003	1,603	1,647	1,458
Deduct current	(35)	(27)	(35)	(27)
Non current	1,968	1,576	1,612	1,431
Less: provisions	(168)	(291)	(159)	(146)
Net staff loans	<u>1,800</u>	<u>1,285</u>	<u>1,453</u>	<u>1,285</u>

13. STOCKS
(a) Group

	June 2004 Kshs.Million	June 2005 Kshs.Million
Engineering parts	1,478	2,194
Furniture and equipment	410	34
Consumables and miscellaneous	<u>264</u>	<u>90</u>
	<u>2,152</u>	<u>2,318</u>

(b) Company

	June 2004 Kshs.Million	June 2005 Kshs.Million
Engineering parts	1,308	1,351
Furniture and equipment	16	34
Consumables and miscellaneous	<u>76</u>	<u>79</u>
	<u>1,400</u>	<u>1,464</u>

14. DEBTORS
(a) Group

	June 2004 Kshs' Million	June 2005 Kshs' Million
Local debtors	25,197	28,040
Deduct provisions	<u>(12,764)</u>	<u>(14,069)</u>
Net	<u>12,433</u>	<u>13,971</u>
International debtors	5,625	5,522
Deduct provisions	(649)	(721)
Net	<u>4,976</u>	<u>4,801</u>
Total service	<u>17,409</u>	<u>18,772</u>
Non operational debtors	2,202	3,080
Sundry debtors and prepayments	2,759	1,731
Staff Loans and advances	45	27
	<u>5,006</u>	<u>4,838</u>
Total	<u>22,415</u>	<u>23,610</u>

Company

	June 2004	June 2005
	Kshs' Million	Kshs' Million
Local debtors	24,398	27,042
Add adjustments	1,572	-
Deduct provisions	<u>(13,517)</u>	<u>(14,069)</u>
Net	12,453	12,973
International debtors	5,625	5,522
Deduct provisions	<u>(689)</u>	<u>(721)</u>
Net	<u>4,936</u>	<u>4,801</u>
Total service	<u>17,389</u>	<u>17,774</u>
Non operational debtors	1,834	2,834
Sundry debtors and prepayments	1,997	1,731
Staff Loans and advances	<u>46</u>	<u>27</u>
	<u>3,877</u>	<u>4,592</u>
Total	<u>21,266</u>	<u>22,366</u>

The Company policy is not to provide for Bad and Doubtful debts relating to Government and Parastatals' accounts. This policy is supported by previous debt swap arrangements with Government as follows;

- April 1999, Kshs 4.9 billion government debt offset against Government on lent loans of Kshs 26 billion.
- Ongoing debts swap arrangement where already Kshs 3.2 billion has been agreed for accounts outstanding as at June 2003.
- Government is also considering effecting debt swap in the ongoing restructuring of Telkom Kenya limited.

The Government as the sole shareholder of Telkom Kenya Limited has given an undertaking in certain circumstances to settle some of the parastatal debts in the event of default. Consequently, Government and parastatal debtors are deemed secured and not provided for in the accounts.

15. BANK DEPOSITS

Group and Company	June 2004	June 2005
	Kshs' Million	Kshs' Million
Deposits in failed financial institutions	220	487
Deduct provision	(220)	(487)
Other fixed deposits	<u>331</u>	<u>251</u>
Total	<u>331</u>	<u>251</u>

The bank deposits, other than those in failed financial institutions, have been provided to secure specific letters of credit. The weighted average effective interest rate on these deposits at year-end was 8.5%.

16. ESCROW ACCOUNT/COMMERCIAL PAPER

In June 2001 SCL borrowed Kshs 4,000 million from the public and institutional investors through the issue of commercial paper, a medium term floating rate secured note. This facility was drawn in the year ended 30th June 2003. Further, on July 24th 2002, Safaricom obtained a Ksh 2,500 million term loan from a syndicate of local banks.

The amount is shown as due on an escrow account, the debtor being the bank which facilitated the issue of the paper.

The medium term note and the bank borrowings all have a tenor of five years. They are secured by a fixed and floating charge over Safaricom's assets, undertaking and property, both present and future, including a charge over the Euro Escrow bank account and a charge over all the issued shares of the company. The interest on the Euro term loan is payable semi annually at a margin of 1.5% over the reference European Inter Bank Offer Rate. Interest on the shilling term loan and the medium note is paid quarterly in arrears based on a mark up of 1% above the prevailing Treasury bill rate. Finance costs incurred on the issue is amortised over the term of the paper.

The notes will be redeemed in six semi-annual instalments as shown below.

Date	Repayments %
30 th September 2003	10
31 st March 2004	10
30 th September 2004	19
31 st March 2005	19
30 TH September 2005	21
31 st March 2006	<u>21</u>
	<u>100</u>

17. GOVERNMENT INTEREST

The **Kshs 21.1 billion** represents the Government of Kenya's interest resulting from the conversion to equity of GOK on-lent loans to KPTC of **Kshs 26 billion**, inclusive of interest, this amount being reduced by **Kshs 4.9 billion** for service debt owed to KPTC by Government ministries and departments at the time of conversion.

Government interest has not been translated to share capital. The share capital of the company is as follows:-

	June 2004 Kshs	June 2005 Kshs
Authorised		
5,000 ordinary shares of Kshs 20 each	100,000	100,000
Issued and fully paid		
100 ordinary shares of Kshs 20 each	2,000	2,000

18. GRANTS

	June 2004 Kshs' Million	June 2005 Kshs' Million
KCCT hostel	2	2

The grants comprises a donation for hostel construction of shillings 3 million. It is amortised annually at the rate of 2% and charged to accumulated depreciation.

19. RESERVES

(a) Group

	2004	2005
	Kshs' Million	Kshs' Million
Balance as at 1 st July 2004	14,436	11,973
Adjustments	(2,280)	
Retained profit for the year	<u>(183)</u>	<u>801</u>
At 30 th June 2005	<u>11,973</u>	<u>12,774</u>

(b) Company

	2004	2005
	Kshs' Million	Kshs' Million
Balance brought forward	16,430	12,574
Adjustments	(1,157)	-
Prior year adjustments	(47)	-
Retained profit for the year	<u>(2,652)</u>	<u>(2,733)</u>
Balance carried forward	<u>12,574</u>	<u>9,841</u>

20 MINORITY INTEREST

Minority interest comprises:

	2004	2005
	Kshs' Million	Kshs' Million
Shareholders loan	1,694	1,694
Reserves	2,719	5,278
Profit & Loss	<u>1,597</u>	<u>2,511</u>
	<u>6,011</u>	<u>9,483</u>

21 GOVERNMENT LOAN

In 2000 the Government of Kenya (GOK) lent TKL US \$ 33 million. At 30 June 2000, the loan was represented by a Gok promissory note and was subsequently disbursed to TKL on 29 June 2001. TKL on –lent the entire amount to SCL to pay for its mobile phone licence.

In the books of TKL, the loan amount is included in the cost of investment in SCL, per Note 9. In SCL's books, this loan ranks *pari passu* with a similar shareholders loan of US\$22 million received from Vodafone Kenya Ltd for the purpose. The loan to SCL is interest free and subordinated to all other loan obligations of the company.

The agreement between TKL and GoK in respect of this loan was signed in July 2001. The agreement provides that interest will be payable at 7.5% per annum with effect from the disbursement date and that the principal amount and accrued interest would be repaid in one instalment within two weeks of completion of the intended sale of the new TKL shares to a strategic partner.

The agreement further stipulates that, in the event the sale was not concluded by 30 September 2001, the terms of repayment would be renegotiated immediately and, unless otherwise agreed in writing, the full amount of the loan was to be considered due and payable as of that date.

However GOK has not enforced this repayment clause and has requested the company to make repayment proposals. The company has done so, and the key proposals made are as follows:

- ◆ The principal amount and any accrued interest be converted to government equity. This amount will be recouped from the proceeds of any future sale to either a strategic investor or from an Initial Public Offer (IPO) should the privatisation process take this form.
- ◆ That if TKL is not privatized, the principal amount of Kshs 2,608,881,000.00 be repaid over a ten (10) years period beginning 1st July,2007.

Negotiations with the Government on the repayment of this loan have not been concluded. However it is expected that the status of this loan will be addressed by the Government restructuring of the company.

22 LONG TERM LOANS

Company and Group	2004	2005
	Kshs' Million	Kshs' Million
Safaricom Loan	2,609	2,609
Commercial loans		-
GOK guaranteed loans	<u>3,180</u>	<u>530</u>
Total loans	<u>5,789</u>	<u>3,139</u>

(a) Amounts falling due within one year

	Commercial loans (Ksh Million)	Safaricom Loan (Ksh Million)	GOK Guaranteed loans (Ksh Million)	Total (Ksh Million)
Principal due	400		504	904
Interest		782	675	1,457
Redemption Arrears			2,768	2,768
Management Charges			5	5
Total	400	782	3,952	5,134

(b) Amounts falling due after one year Kshs' million

Details	2005			Total
	Commercial loans	GOK Loans	Guaranteed	
1-2 years	100		2,666	2,766
2-5 years	-		114	114
Over 5 years	-		259	259
Total	100		3,039	3,139

These loans are unsecured and will be payable under terms to be agreed with Government. Included in this category is the Safaricom loan amounting to Ksh 2.61 billion.

23 PENSIONS

(a) National social security fund

This is a statutory defined contribution pension scheme in which both the employer and employee contribute equal amounts. The amount contributed during the period has been charged to the profit and loss account.

(b) Telposta Pension Fund and Teleposta Provident Fund

Two new retirement benefit plans were established on 1st July 1999 as part of the restructuring of the defunct KPTC. These are the Telposta Pension Scheme (TPS) and the Telposta Provident Fund (TPF). The Scheme and the Fund operate retrospectively and supersede the former KPTC pension and provident fund regulations, which have been revoked.

Current membership comprises of employees of TKL, GTI, and KCCT and retired KPTC pensioners.

Certain assets of Telkom division of KPTC were transferred to TPS and TPF on 30th June 1999 to cover the accumulated liability of TKL arising in respect of past service. However, the assets did not fully fund the liability, hence the deficit of **Kshs 6.044 billion**, based on the valuation as at 30th June 2004.

Current contributions to the Fund and the Scheme are based on salary, as follows:-

	Pension Scheme	Provident Fund
Employee contribution	7.5%	7.5%
Employer contribution	26.8%	10.6% - 18.1%

The total amount charged to the profit and loss account is **Kshs 860 million**.

24 CREDITORS

(a) Group

	2004	2005
	Kshs' Million	Kshs' Million
Trade creditors	9,816	14,919
Taxes	1,990	2,392
Stores and expense creditors	2,727	1,851
Loans due within one year - Note 23	895	5,137
Pensions	1,839	2,658
Sundry creditors	6,828	6,134
Total	<u>24,095</u>	<u>33,091</u>

(b) Company

	2004	2005
	Kshs' Million	Kshs' Million
Trade creditors	5,484	5,709
Taxes	1,990	2,392
Stores and expense creditors	1,138	1,851
Loans due within one year - Note 23	895	5,137
Pensions	2,416	2,658
Payable to subsidiary	1,041	1,859
Sundry creditors	5,169	4,144
Total	<u>18,133</u>	<u>23,750</u>

25 TKL CORPORATION TAX

Company	2004	2005
	Kshs' Million	Kshs' Million
Opening balance 1.7.2004	4,078	4,405
Adjustment to opening balance	70	0
Charge/Credit for the period	257	(764)
Less: payments made	<u>0</u>	<u>0</u>
Balance at 30.6.2005	<u>4,405</u>	<u>3,640</u>

The tax charge for the year has been estimated on the adjusted group taxable profit.

26. KPTC CORPORATION TAX

	2004	2005
	Kshs' Million	Kshs' Million
Opening Balance	1,648	1,648
Less payments during the year	-	-
Closing Balance	1,648	1,648

27. BANK OVERDRAFT

Bank overdraft facilities are secured by a legal charge over several of the company's properties.

28. FINANCIAL INSTRUMENTS.

Exposure to credit, rate and currency risk arise in the normal course of the group's business.

Credit risk

Management has a credit policy in place and the exposure to credit is monitored on an ongoing basis. All subscribers are required to place cash deposit with the group before credit facilities are granted. Prepaid telephone services have also been introduced to further minimise credit risk.

Investments are allowed only in liquid securities with reputable financial institutions.

At the balance sheet date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset.

Interest rate risk

The following table indicates applicable interest rates in respect of the group's income -earning financial assets and interest bearing liabilities at the balance sheet date.

	Note	Interest rate
Bank deposit	16	7% - 9%
Bank balances and cash	-	Nil
Commercial paper	17	1% above treasury bills rate
Government loan	22	7.5%
Long term loans	23	0% to 9.2% (details on Note 24)
Bank overdraft	28	Base rate (10 % at 30 th June 2005).

The principal terms applicable for the financial assets and interest bearing liabilities are disclosed in the respective notes in these financial statements.

Foreign currency risk

The group incurs foreign currency risk on sales, purchase and borrowings that are denominated in a currency other than the Kenya shilling. The currencies giving rise to this risk are primarily US dollars, Euros, Dutch Guilders and Japanese Yen. In respect of assets and liabilities denominated in foreign currency, receipts act as a hedge against liabilities.

Fair values

The fair value of the group's financial assets and liabilities is estimated at the respective carrying amounts.

29. NOTES TO CASH FLOW STATEMENT

Reconciliation of net profit before tax to net cash flows from operating activities.

(a) Group	2005
	Kshs. Million
Profit before tax	4,273
Adjustments for:-	
Depreciation charges	11,006
Interest paid	367
Interest received	(64)
Provision for bad & doubtful debts	545
Realised Exchange loss/ Gain	-
Gain/loss on disposal	
Operating profit before working capital changes	16,127
Changes in stock	(166)
Changes in debtors	(1,225)
Change in creditors	4,339
Operating profit after working capital changes	19,075

(b) Company	2005
	Kshs. NOTES Million
Profit before tax	(3,498)
Adjustments for:-	
Depreciation charges	2,745
Interest paid	367
Interest received	(64)
Provision for bad & doubtful debts	545
Net Exchange loss/ Gain	-
Gain/loss on disposal	-
Operating profit before working capital changes	98
Changes in stock	(64)
Changes in debtors	(1,582)
Change in creditors	2,710
Operating profit after working capital changes	1,162

30. **TERMINATION BENEFITS**

These accounts do not incorporate any costs that may arise from a future redundancy programme. The company is currently negotiating with the Government on a formal detailed plan to terminate the employment of 11,873 employees.

31. **CAPITAL COMMITMENTS (TKL)**

Company and Group	2004	2005
	Kshs' Million	Kshs' Million
Contracted but not provided for		
Authorised but not contracted	-	-
SCL		
- TKL	-	-
Authorised and contracted	8,496	699
SCL		
- TKL	<u>677</u>	<u>1,454</u>
Total	<u>9,173</u>	<u>2,153</u>

32. RELATED PARTY TRANSACTIONS

The company controls the following organizations

- 1) K.C.C.T - 100%
- 2) G.T.I - 100%
- 3) Safaricom - 60%
- 4)

The following transactions were carried out with related parties:-

(a) Remuneration

The total remuneration of directors and senior management of the group is as follows:

Company	2004	2005
	Kshs' Million	Kshs' Million
Directors	4	5
Senior management	<u>86</u>	<u>89</u>
	<u>90</u>	<u>94</u>

(b) Loans

Company	2004	2005
	Kshs' Million	Kshs' Million
Directors	-	-
Senior management	<u>25</u>	<u>26</u>
	<u>25</u>	<u>26</u>

The loans have been granted on normal staff loan conditions.

(c) Sale of goods and services

	2004	2005
	Kshs' Million	Kshs' Million
K.C.C.T	6	7
G.T.I	2	1
Safaricom	845	1,038

Telephone billing done by TKL to its subsidiaries is through the normal course of business and there are no special intergroup concessions on the members of the group.

(d) Purchase of goods and services

	2004	2005
	Kshs' Million	Kshs' Million
K.C.C.T	42	53
G.T.I	190	-
Safaricom Ltd	3,125	3,230

(e) Current Account Transactions

	2004	2005
	Kshs' Million	Kshs' Million
K.C.C.T	4	49
G.T.I	45	82

33. OPERATING LEASES.

The group has leased office space at Telposta Towers and Safaricom House under operating leases. Leases for both premises run for an initial period of 6 years. Lease payments for Telposta Towers are increased every 2 years to reflect market rentals while rentals for Safaricom House are constant. None of the leases include contingent rentals.

Non cancellable operating leases rentals are payable as follows:

Company and Group	2004	2005
	Kshs' Million	Kshs' Million
Less than one year	185	210
Between one and five years	<u>621</u>	<u>489</u>
	<u>806</u>	<u>699</u>

34. POST BALANCE SHEET EVENTS.

(a) PENSION LIABILITY ACTUARIAL VALUATION

Alexander Forbes Actuarial Services Ltd was commissioned to carry out a revaluation of TKL's Pension liability on 2005. The liability as at 30th June 2004 stood at **Kshs 6.044 billion** has been approved for incorporation in 2005/2006 Accounts Report.

(b) CORPORATE RESTRUCTURING

PKF Consulting was commissioned to carry out an independent detailed assessment of Telkom Kenya Ltd operations and recommend ways to revert the company to profitability. The consultancy report has now been finalised and presented to the Inter-Ministerial Steering Committee for deliberation and direction.

(c) JAMBO TELKOM LIMITED (JTL)

Telkom Kenya is preparing to commence provision of internet services through its subsidiary company Jambo Telkom Limited which was registered under the laws of Kenya as a wholly owned subsidiary of TKL in August 2001 and was issued with an Operating Licence by the Communications Commission of Kenya (CCK) in April 2002.

The JTL Board of Directors has already been constituted and an inaugural meeting was held on 15th July, 2005. The company is set to start operations in October 2005 subject to Telkom Kenya Ltd Board approval.

35. CONTINGENT LIABILITIES

Contingent liabilities comprise the following:-

(a) Investments vested to the pension scheme

- (i) A bank deposit at National Bank of Kenya, Kenya stock investments and treasury bonds amounting to **Kshs. 492 million** was vested to Teleposta Pension Scheme under the Vesting Order but title has not yet passed.

In addition, there is a lien on the deposit on account of loans given to TKL by a third party. The lender, Treasury and Telkom Kenya Ltd are finalising the legal formalities that will facilitate cancellation of the lien and release of the deposits to Telposta pension scheme.

(b) Tax matters

- ◆ Telkom Kenya Limited has engaged the services of Ernst and Young, Certified Public Accountants to act as its advisers in all tax matters. The firm is currently reviewing past tax liabilities indicated below with KRA with a view to agreeing on mitigation's and final amounts payable by the company.

- ◆ Corporation tax matters of the former KPTC as at 30th June 1999 were agreed at **Kshs 3,673 million** with the KRA but currently amount to **Kshs1,648 Million as at 30th June 2004**. TKL is liable to pay penalties and interest on this amount principally due to delayed payments.
- ◆ KRA has issued a demand for import duties amounting to **Kshs.104 million** in respect of equipment imported by KPTC and now vested in and used by TKL. Receipts for duty payments were issued to KPTC through third party clearing agents but KRA is unable to trace the receipt of such duty in its account. TKL and KRA are co-operating to resolve this matter.
- ◆ KRA has also issued additional assessments in respect of VAT and PAYE amounting to **Kshs' 2.6 billion** and **kshs' 105 Million** respectively. TKL has through Ernst & Young appealed for waiver of the total amount on VAT including any related accrued interest and penalties.
- ◆ Following an audit, KRA has issued a VAT notice of assessment for **Kshs.392 million** to GTI. Included therein are penalties and interest of **Kshs.355 million** of which application for remission will be made to the Minister for Finance upon full payment of the principal amount. GTI was yet to finalise payment of the outstanding amount as at 30th June 2005.
- ◆ No VAT is declared on training courses offered at KCCT but is declared on all other services rendered by KCCT.

(c) **Litigation**

There are potential liabilities in respect of various pending court cases arising in the normal course of business. The majority of these cases were taken over from the defunct KPTC. Management is of the opinion that these claims would not give rise to material liabilities.

36. INCORPORATION

The Company is incorporated in Kenya under the Companies Act.

37. CURRENCY

These accounts are presented in Kenya shillings million (Kshs.million).

38. LIST OF SIGNIFICANT SUBSIDIARIES

Name	Country of Incorporation	Ownership interest
KCCT Ltd	Kenya	100%
Gilgil Telecomms Ltd	Kenya	100%
Safaricom Ltd	Kenya	60%

