

REPUBLIC OF KENYA



KENYA NATIONAL AUDIT OFFICE

**REPORT OF
THE
AUDITOR-GENERAL**



ON

**THE FINANCIAL STATEMENTS OF
POLICYHOLDERS' COMPENSATION
FUND FOR THE YEAR ENDED
30 JUNE 2013**





POLICYHOLDERS COMPENSATION FUND

The Fund You Can Trust

ANNUAL REPORT & FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2013

POLICYHOLDERS' COMPENSATION FUND
ANNUAL REPORT & FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2012

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**POLICYHOLDERS' COMPENSATION FUND
CORPORATE INFORMATION
FOR THE YEAR ENDED 30TH JUNE 2013**

Board of Trustees

1. Abdulmalek Janmohamed -Chairman
2. Sammy Makove: Commissioner of Insurance/ CEO-IRA
3. Julius Mutua: Alt. PS Treasury
4. Mrs. Shehnaz Sumar
5. Tom Mulwa
6. Maurice Okumu - (Retired 03/09/2012)
7. Julius Manyeki
8. Douglas Mburai Alt. Commissioner of Insurance/ CEO-IRA

Chief Executive Officer / Board Secretary

Charles M. Machira
Retirement Benefits Authority
P.O. Box 57733-00200
Nairobi

Registered Office

Zep Re Place 2nd Floor
Longonot Road-Upper Hill
P.O.Box 43505-00100
Nairobi

Bankers

Commercial Bank of Africa Ltd
Standard/Wabera Streets
P.O.Box 30457-00100
Nairobi

Auditors

Auditor General
Anniversary Towers
University way
P.O. Box 30084-00100
Nairobi

**POLICYHOLDERS' COMPENSATION FUND
REPORT OF BOARD OF TRUSTEES
FOR THE YEAR ENDED 30TH JUNE 2013**

Establishment

The Policyholders' Compensation Fund was established under Section 179 of the Insurance Act by the Government of Kenya on 24th September 2004, through the Legal Notice No. 105. The operations of the Fund commenced on January 1, 2005 and are governed by the terms of that Legal Notice.

Purpose

The purpose of the Fund is to provide compensation to policyholders in the event of an insurer becoming insolvent.

Funding

The insurance policyholders, who are the beneficiaries of the Fund contribute 0.25% of the premiums payable monthly. The insurance companies also contribute 0.25% of the premiums receivable monthly, resulting in a total of 0.5% contributions from insurance companies payable within 15 days after the end of month to which they relate; payments received after 30 days attract a penalty of 2.5% per month.

Management

The Fund is run by a Board of Trustees, which is accountable to the Government through the Ministry of The National Treasury Finance. The trustees who held office during the period under review are shown on Page 1. The Retirement Benefits Authority (RBA) is the Managing Trustee.

Financial Performance

Levy Contribution

During the year under review, the Fund received contributions from 46 insurers totaling to Kshs.441,781,359 compared to Kshs.376,542,379 received in the previous year, reflecting a 17% increase which is attributable to increased business volume of the insurers. The contributions, which are a statutory levy, are invested in short term Government securities.

Investment income

Investment income of Kshs. 244,513,094 was generated compared to Kshs.217,492,274 the previous year. The increase of 12% is mainly due to volume as Treasury Bills average rate dropped from a high of 15% average in the previous year to 11 % in the year under review.

Operating Expenses

Operating expenses of Kshs15,376,479 were incurred compared to Kshs 19,915,358 the previous year.

Penalties

Penalties totaling Kshs 680,000 were paid by some insurers for breaching various sections of the Insurance Act in the year under review.

Fund Balance

The net assets of the Fund grew by 31% from Kshs 2,806,026,600 in the previous financial year to Kshs. 2,134,428,626 in the current financial year. This performance is a reflection of both non-commencement of claim settlements and prudent management of operational expenses.

By Order of the Board of Trustees


.....

For: Managing Trustee.

Date: 25-09-2013

**POLICYHOLDERS' COMPENSATION FUND
STATEMENT OF TRUSTEES' RESPONSIBILITIES
FOR THE YEAR ENDED 30TH JUNE 2013**

The Legal Notice No. 105 of 2004 requires the Trustees to prepare financial statements for each year which give a true and fair view of the state of affairs of the Fund as at the end of each financial year and of the operating results of the Fund for that year.

It also requires the Trustees to ensure the Fund keeps proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Fund. They are also responsible for safeguarding the assets of the Fund.

The Trustees accept responsibility for the financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with International Financial Reporting Standards.

The Trustees are of the opinion that the financial statements give a true and fair view of the financial affairs of the Fund and its operating results. The Trustees further accept responsibility for the maintenance of accounting records which may be relied upon in the preparation of the financial statements as well as adequate systems of internal financial control.

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

For the Trustees

Signed by:

Trustee

Trustee

For: Managing Trustee

Date: 25-09-2013

REPUBLIC OF KENYA

Telephone: +254-20-342330
Fax: +254-20-311482
E-Mail: cag@kenao.go.ke
Website: www.kenao.go.ke

P.O. Box 30084-00100
NAIROBI



KENYA NATIONAL AUDIT OFFICE

REPORT OF THE AUDITOR-GENERAL ON POLICYHOLDERS' COMPENSATION FUND FOR THE YEAR ENDED 30 JUNE 2013

REPORT ON THE FINANCIAL STATEMENTS

I have audited the accompanying financial statements of Policyholders' Compensation Fund set out on pages 4 to 11, which comprise the statement of financial position as at 30 June 2013, and the statement of comprehensive income, statement of changes in capital and reserves and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information in accordance with the provisions of Article 229 of the Constitution of Kenya and Section 14 of the Public Audit Act, 2003. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit.

Management's Responsibility for the Financial Statements

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

The Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 13 of the Public Audit Act, 2003.

Auditor-General's Responsibility

My responsibility is to express an opinion on these financial statements based on the audit and report in accordance with the provisions of Section 15(2) of the Public Audit Act, 2003 and submit the audit report in compliance with Article 229(7) of the Constitution of Kenya. The audit was conducted in accordance with International Standards on Auditing. Those standards require compliance with

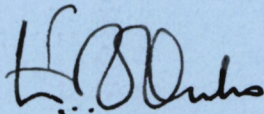
ethical requirements and that the audit be planned and performed to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the financial statements present fairly, in all material respects, the financial position of the Fund as at 30 June 2013, and of its financial performance and cash flows for the year then ended, in accordance with International Financial Reporting Standards and comply with the Insurance Act, Cap.487 of the Laws of Kenya.



Edward R.O. Ouko, CBS
AUDITOR-GENERAL

Nairobi

16 January 2014

**POLICYHOLDERS' COMPENSATION FUND
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 30TH JUNE 2013**

	Notes	2013 Kshs	2012 Kshs
Income			
Contribution Levy	2	441,781,359	376,542,379
Penalties income.	3	680,000	2,099,372
Investment income	4	244,513,094	217,492,274
Total income		<u>686,974,453</u>	<u>596,134,025</u>
Operating expenses			
Board expenses	5	(6,413,198)	(5,968,403)
Staff cost	6	(6,520,300)	(5,285,663)
Administrative expenses	7.	(2,442,981)	(8,158,849)
		-	-
Net increase in the fund during the year		<u>671,597,974</u>	<u>576,721,110</u>
Fund balance brought forward		2,099,428,626	1,522,707,516
Fund balance carried forward		<u><u>2,771,026,600</u></u>	<u><u>2,099,428,626</u></u>

**POLICYHOLDERS' COMPENSATION FUND
STATEMENT OF FINANCIAL POSITION
AS AT 30 JUNE 2013**

	Notes	2013 Kshs.	2012 Kshs.
Non-current Assets			
Property, Plant & Equipment	8	485,022	782,082
Current Assets			
Contributions receivable	9	31,360,183	25,891,612
Other Debtors	10	5,008,725	-
Government securities	11	2,748,283,989	2,095,989,701
Cash and bank deposit	12	24,278,590	17,787,188
		<u>2,808,931,487</u>	<u>2,139,668,501</u>
Less: Current Liabilities			
Payables and accruals	13	(3,389,909)	(6,021,957)
Net Current Assets		<u>2,805,541,578</u>	<u>2,133,646,544</u>
Total Net Assets		<u><u>2,806,026,600</u></u>	<u><u>2,134,428,626</u></u>
FINANCED BY:			
Capital Grant	14	35,000,000	35,000,000
Fund Balance		<u>2,771,026,600</u>	<u>2,099,428,626</u>
		<u><u>2,806,026,600</u></u>	<u><u>2,134,428,626</u></u>

The financial statements were approved by the Board of Trustees on 25-09-2013
and signed on its behalf by:

Trustee

Trustee

For: Managing Trustee

**POLICYHOLDERS' COMPENSATION FUND
STATEMENT OF CHANGES IN FUND BALANCE
FOR THE YEAR ENDED 30TH JUNE 2013**

	Fund Balance Kshs	Capital Grant Kshs	Total Kshs
As at 01/07/11	1,522,707,516	35,000,000	1,557,707,516
Surplus for the year	576,721,110	-	576,721,110
As at 30/06/12	<u>2,099,428,626</u>	<u>35,000,000</u>	<u>2,134,428,626</u>
As at 01/07/12	2,099,428,626	35,000,000	2,134,428,626
Surplus for the year	671,597,974	-	671,597,974
As at 30/06/13	<u>2,771,026,600</u>	<u>35,000,000</u>	<u>2,806,026,600</u>

**POLICYHOLDERS' COMPENSATION FUND
STATEMENT OF CASHFLOWS
FOR THE YEAR ENDED 30TH JUNE 2013**

	2013 Kshs	2012 Kshs
Cash flow from operations		
Surplus for the year	671,597,974	576,721,110
Adjustments for:		
Depreciation	323,896	260,161
Investment income	(244,513,094)	(217,492,274)
Net cash inflow from operating activities	427,408,776	359,488,997
Movement of changes in working capital		
Increase in other debtors	(5,008,725)	-
Increase in levy contribution receivable	(5,468,571)	(2,408,277)
Decrease in payables	(2,632,048)	5,371,887
Net working capital change	(13,109,344)	2,963,610
Net cash flow from operating activities	414,299,432	362,452,607
Cash flow from investing activities		
Purchase of office furniture	(26,836)	(838,305)
Investment income	244,513,094	217,492,274
Net cash flow from investing activities	244,486,258	216,653,969
Net increase in cash and cash equivalent	658,785,690	579,106,576
Cash and Cash equivalents at the beginning of y	2,113,776,889	1,534,670,313
Cash and Cash equivalents at the end of year	2,772,562,579	2,113,776,889

**POLICYHOLDERS' COMPENSATION FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2013**

1. Accounting Policies

The principal accounting policies applied in the preparation of the financial statements are set out below:

(a) Basis of preparation

The financial statements are prepared in accordance with and comply with International Financial Reporting Standards. The financial statements are presented in Kenya shillings (Kshs) and are prepared under the historical cost convention.

(b) Property and Equipment

Property and Equipment are stated historical cost less accumulated depreciation. The depreciated rate is calculated on straight line method for non-current assets over useful lives as follows:

Computers	33.3%
Office furniture & equipment	12.5%

(c) Revenue recognition

Contribution levy income is accounted for in the period it relates to. Interest on treasury bills is accounted for in the period it is earned. Interest on savings account is recognized when earned. Government grant is recognized when received.

(d) Fund Balance

This represents the Government grant to the Fund at inception and contribution levy.

(e) Stationery

The Fund procures stationery as and when need arises and the amounts are expensed in the period it relates.

2. Contributions Levy

46 Insurance companies paid levy contributions during the year under review. Each insurance company pays 0.25% and its policyholders contribute 0.25% making a total of 0.5% of monthly premiums as levy contributions. These contributions are payable by the 15th day of the following month to which they relate.

3. Penalties

These are penalties paid by some insurers for non compliance with various provisions of the Insurance Act.

4. Investment Income

	2013 Kshs	2012 Kshs
Government securities	243,718,627	215,814,137
Current accounts	794,467	1,678,137
	<u>244,513,094</u>	<u>217,492,274</u>

The treasury bill rate declined in 2011/12 from an average of 15% to 11% in 2012/13, a trend which was also witnessed on the current accounts interest.

POLICYHOLDERS' COMPENSATION FUND
NOTES TO THE FINANCIAL STATEMENTS (Continued)
FOR THE YEAR ENDED 30TH JUNE 2013
Total Operating Expenditure

	2013 Kshs.	2012 Kshs.	
5 Board expenses			
Honoraria	960,000	-	
Sitting allowances	3,020,000	2,185,000	
Lunch allowances and snacks	241,750	895,933	
Training -Local	227,915	2,417,311	
Training -International	1,671,214	-	
Mileage claims	-	114,586	
Medical cover	292,339	355,573	
	<u>6,413,198</u>	<u>5,968,403</u>	
6 Staff cost			
Representative of Managing Trustee	727,900	600,000	
Secretariat	5,792,400	4,685,663	
	<u>6,520,300</u>	<u>5,285,663</u>	
7 Administrative expenses			
Insurance expense	8,980	29,118	
Repairs & maintenance equipment	28,700	500	
Travelling expenses (Local)	804,670	512,000	
Information Technology	3,000	750,537	
General office expenses	90,481	131,495	
Official entertainment	32,700	-	
Printing & stationery	229,081	540,329	
Library expenses	55,470	51,870	
Telephone & postage	102,000	91,000	
Public education & publicity	236,200	464,632	
Professional fees	401,000	5,790,200	
Bank charges	43,635	39,450	
Training & development	83,168	-	
Depreciation	323,896	260,161	
	<u>2,442,981</u>	<u>8,661,292</u>	
8 Property, Plant & Equipments			
	Computer Equipment	Office Furniture & Equipment	Total
	33.3%	12.5%	
	Kshs.	Kshs.	Kshs.
Cost			
At 01 July 2012	1,868,107	357,307	2,225,414
Additions	-	26,836	26,836
Disposal	(689,832)	-	(689,832)
At 30 June 2013	<u>1,178,275</u>	<u>384,143</u>	<u>1,562,418</u>
Depreciation			
At 01 July 2012	1,150,829	292,503	1,443,332
Charge for the year	279,254	44,642	323,896
Disposal	(689,832)	-	(689,832)
At 30 June 2013	<u>740,251</u>	<u>337,145</u>	<u>1,077,396</u>
Net book value			
At 30 June 2013	<u>438,024</u>	<u>46,998</u>	<u>485,022</u>
At 30 June 2012	<u>446,953</u>	<u>64,804</u>	<u>511,757</u>
Property, Plant & Equipments			
	Computer Equipment	Office Furniture & Equipment	Total
	33.3%	12.5%	
	Kshs.	Kshs.	Kshs.
Cost			
At 1 July 2011	1,029,802	357,307	1,387,109
Additions	838,305	-	838,305
At 30 June 2012	<u>1,868,107</u>	<u>357,307</u>	<u>2,225,414</u>
Depreciation			
At 1 July 2011	935,340	247,831	1,183,171
Charge for the year	215,489	44,672	260,161
At 30 June 2012	<u>1,150,829</u>	<u>292,503</u>	<u>1,443,332</u>
Net Book Value			
At 30 June 2012	<u>717,278</u>	<u>64,804</u>	<u>782,082</u>
At 30 June 2011	<u>94,462</u>	<u>109,476</u>	<u>203,938</u>

POLICYHOLDERS' COMPENSATION FUND
NOTES TO THE FINANCIAL STATEMENTS (Continued)
FOR THE YEAR ENDED 30TH JUNE 2013

9. Contributions Outstanding	2013 Kshs	2012 Kshs
Within 30 days	31,360,183	25,757,963
Between 30-90 days	-	133,649
Total	31,360,183	25,891,612

10. Other Debtors

The amount of Kshs 5,008,725 relates to levy paid by two insurers to Insurance Regulatory Authority.

11. Government Securities

Treasury bills are stated at cost plus accrued interest.

12. Cash and Bank	2013 Kshs	2012 Kshs
Commercial Bank of Africa Ltd		
Operational account	654,559	630,091
Collection account	23,621,966	17,151,717
Cash on hand	2,065	5,380
	24,278,590	17,787,188

13. Payables and accruals	2013 Kshs	2012 Kshs
	3,389,909	6,254,075

14. Capital grant

The capital grant was seed capital provided by the Government of Kenya to the Fund in two financial years, Kshs.15,000,000.00 in 2005/2006 and Kshs.20,000,000.00 in 2006/2007. This grant was not refundable and the amounts were immediately invested upon receipt.

15. Related party transactions

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making the financial or operational decisions.

The Managing Trustee of the Fund is Retirement Benefits Authority(RBA) and Insurance Regulatory Authority(IRA), the industry regulator have both seconded staff on reimbursement basis to the Fund.

POLICYHOLDERS' COMPENSATION FUND
NOTES TO THE FINANCIAL STATEMENTS (Continued)
FOR THE YEAR ENDED 30TH JUNE 2013

16. Financial Risk Management

The Fund's activities expose it to a variety of financial risks, including interest rate risk, liquidity risk and credit risk.

The Fund's overall risk management focuses on unpredictability of interest rates on Treasury bills but does not diversify investments to minimise interest rate risk.

Credit risk

Credit risk is limited to the outstanding contributions from insurers as all the investments are in risk-free government stock.

Liquidity risk

Prudent liquidity risk management includes maintaining sufficient cash balances to cover anticipated expenditures. The secretariat identifies anticipated expenditures and sets aside sufficient funds before the surplus is invested.

17. Currency

The financial statements are presented in Kenya Shillings (Kshs) and are rounded to the nearest Kshs 1.

