

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 2014

PARLIAMENT  
OF KENYA  
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*Report laid  
By Hon. A. Sukahe (com)  
on Thurs. 20.08.2015  
Wmm*





POLICYHOLDERS COMPENSATION FUND

The Fund You Can Trust

KENYA NATIONAL AUDIT OFFICE  
P. O. Box 30084 - 00100, NAIROBI.

20 JAN 2015

RECEIVED

**POLICYHOLDERS COMPENSATION FUND**

**ANNUAL ACCOUNTS AND FINANCIAL STATEMENTS**

**FOR THE YEAR ENDED**

**30<sup>TH</sup> JUNE 2014**

## POLICYHOLDERS COMPENSATION FUND

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# POLICYHOLDERS COMPENSATION FUND

## I. KEY FUND INFORMATION

### (a) Establishment

The Policyholders Compensation Fund is a State corporation established under Section 179 of the Insurance Act and commenced its operations on 1st January, 2005.

### (b) Principal Activities

The principal activities of the Fund are to protect the policyholders of an insolvent insurer through provision of compensation for unpaid claims, participation in statutory management and liquidation of a wound up insurer.

### (c) Key Management

The Fund is administered by a Board of Trustees, which is accountable to Government of Kenya through the National Treasury.

### (d) Fiduciary Management

The Fund is run by a Managing Trustee. The appointed Managing Trustee is the Retirement Benefits Authority (RBA) as contained in the Kenya Gazette Notice No. 3357 of 6<sup>th</sup> May, 2005.

The key management personnel who held office during the financial year ended 30<sup>th</sup> June 2014 and who had direct fiduciary responsibility were:

No	Designation	Name
1	Representative of the Managing Trustee	Mr. Charles Machira
2	Head of Secretariat	Mr. John Keah
3	Head of Internal Audit and Risk Management	Mrs. Elizabeth Waruingi

### (e) Fiduciary Oversight Arrangements

The Audit and Risk Management Committee assists the Board of Trustees in the oversight of the integrity of the financial operations of the Fund and the performance of the Funds internal audit and external auditors and compliance by the Fund with legal and statutory requirements.

# POLICYHOLDERS COMPENSATION FUND

## I. KEY FUND INFORMATION (CONT'D)

### (f) Office

Policyholders Compensation Fund  
Zep Re Place 2<sup>nd</sup> Floor  
02 Longonot Road, Upper-Hill  
P.O. Box 24203 -00100  
Nairobi

### (g) Contact

Telephone: (254)-020-4996236/7/8  
Email: info@phcf.co.ke

### (h) Bankers

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

### (i) Independent Auditors

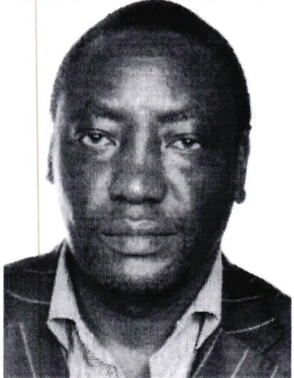
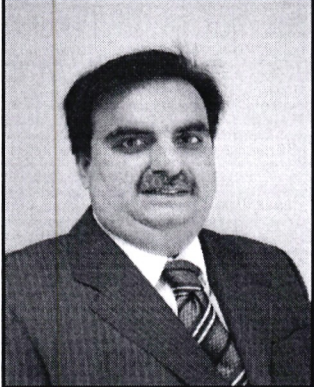

Auditor General  
Kenya National Audit Office  
Anniversary Towers University Way  
P. O. Box 30084 -00100  
Nairobi

### (j) Principal Legal Advisor

The Attorney General  
State Law Office  
Harambee Avenue  
P. O. Box 40112 - 00200  
Nairobi

## POLICYHOLDERS COMPENSATION FUND

### II. THE BOARD OF TRUSTEES

 <p><b>Mr. Gershom Otachi</b> <b>Bw'Omanwa</b> Chairman LLB(Hons.), Dip Law (KSL)</p>	<p>Mr. Otachi is the current Chairman of the Board of Trustees and was appointed on 10 January 2014. He is a practicing advocate of the High Court of Kenya, a partner in the law firm Ogetto, Otachi &amp; Company Advocates and has broad experience in civil, commercial, insurance, criminal, matrimonial and property and election petition law. Age 49.</p>
 <p><b>Mr. Abdulmalek A. Janmohamed</b> Former Chairman BSc Finance &amp; Management</p>	<p>Mr. Janmohamed is the former Chairman of the Board of Trustees, who served from 2<sup>nd</sup> July, 2012 to 9<sup>th</sup> January, 2014. He is the Managing Director of Imperial Bank Limited and has extensive experience in banking sector. Age 55.</p>
 <p><b>Mr. Sammy M. Makove</b> Trustee MBA, M.A, B.Comm, ACII, CIP, AIK, ACI Arb</p>	<p>Mr. Makove is a statutory member of the Board of Trustees in his capacity as the Commissioner of Insurance and Chief Executive Officer of the Insurance Regulatory Authority. He has over 30 years experience in insurance and management in both private and public sectors. Age 55.</p>



**Mrs. Shehnaz N. Sumar**  
Trustee  
FCCA, CPAK

Mrs. Sumar was appointed as a trustee representing insurers carrying on general business on 1<sup>st</sup> April, 2011. At the time she was the Managing Director of Fidelity Shield Insurance Company Ltd and has vast experience in Insurance, Audit and Accountancy fields. She has also served in various Boards in both private and public sectors in various capacities. Age 57



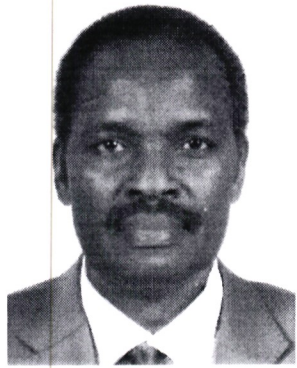
**Mr Julius Mutua**  
Trustee  
MA (Econ), BA (Econ)

Mr. Mutua is a statutory member of the Board of Trustees in his capacity as the alternate of the Principal Secretary of the National Treasury. He is a Senior Economist at the National Treasury and has over 15 years experience in Public Sector Financial Policy and Management. He also serves as an alternate director in the Boards of various State Corporations under the National Treasury. Age 43.



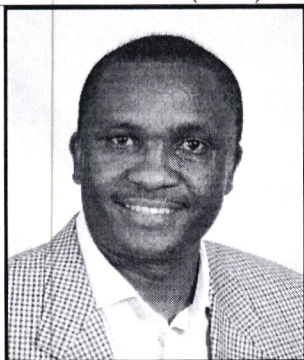
**Mr. Tom Mulwa**  
Trustee  
MBA, B.Comm

Mr. Mulwa was appointed as the trustee representing insurance brokers on 1<sup>st</sup> April, 2011. He is the Managing Director of the Liaison Group (I.B) Ltd and has over 20 years experience in the Insurance sector. He has also served in the Boards of various Insurance stakeholder and business associations in various capacities. Age 46.



**Mr. Julius Manyeki**  
Trustee  
B.Comm (B.A)

Mr. Manyeki was appointed a trustee representing special interests on 2<sup>nd</sup> July 2012. He is businessman in the oil marketing industry with over 30 years experience. He also serves in various capacities in the Boards of various entities in the water and education sectors. Age 56






**Mr. Charles M. Machira**  
Representative of the Managing  
Trustee  
and  
Secretary to the Board  
MSc, MBA, BSc

Mr. Machira is the Representative of the Managing Trustee and also serves as the Secretary to the Board. He was appointed on 15<sup>th</sup> November 2010 and has over 20 years experience in the Insurance and Pensions Regulatory sectors. Age 45.

# POLICYHOLDERS COMPENSATION FUND

## III. MANAGEMENT TEAM

 <p><b>Mr. Charles M. Machira</b> MSc, MBA, BSc</p>	<p>Representative of the Managing Trustee and Secretary to the Board</p>
 <p><b>Mr. John S. Keah</b> MBA, BSc</p>	<p>Head of Secretariat</p>
 <p><b>Mrs. Elizabeth Waruingi</b> MBA, BA, CPA, CIA, CISA, CRMA</p>	<p>Head of Internal Audit and Risk Management</p>

## **POLICYHOLDERS COMPENSATION FUND**

### **CHAIRMAN'S STATEMENT**

It is my pleasure to present the annual report and financial statements of the Policyholders Compensation Fund for the year ended 30<sup>th</sup> June 2014.

During the year under review, the Fund witnessed a growth of its asset base which is attributed to a growing insurance sector characterized by increased gross written premiums from mainly general business and increased uptake that has seen insurance penetration grow to 3.4% of Gross Domestic Product.

Taking the Fund's mandate into consideration, the growth in assets presents the Fund with an opportunity to provide adequate compensation and protection to all insurance claimants of insolvent insurers. Article 46 of the Constitution of Kenya, 2010 gives consumers the right to protection of their economic interests and to compensation for loss. The Fund is focused on upholding these rights for every insurance consumer in Kenya by working towards achievement of its key result areas which include developing a comprehensive compensation framework, financial sustainability and institutional capacity.

While the Fund works towards these goals, it is aware that there are currently four insurance companies under statutory management and which present it with potential claim liabilities. In this regard, the Fund is working closely with its stakeholders purposely to share information needed to support effective planning for possible compensation of claims. In addition, the Fund has adopted a more proactive approach by having its mandate expanded to incorporate intervention and resolution functions allowing it to contribute to the development of the industry.

I therefore take this opportunity to appreciate the continued support of the members of the Board, management, staff and stakeholder entities for their commitment towards the Fund's mandate.



**GERSHOM OTACHI**

**CHAIRMAN, BOARD OF TRUSTEES**

## **POLICYHOLDERS COMPENSATION FUND**

### **STATEMENT OF THE MANAGING TRUSTEE**

The Managing Trustee of the Policyholders Compensation Fund is the Retirement Benefits Authority which was appointed with effect from 9<sup>th</sup> December, 2004 vide Kenya Gazette Notice No. 3357 dated 6<sup>th</sup> May, 2005.

Since the commencement of its operations, the Fund has witnessed a steady growth and upward performance. This trend was maintained during the year under review and this report highlights some of the notable aspects of growth as follows:

#### **a) Mandate**

The Fund's mandate has been the payment of compensation for unsettled claims to the policyholders of an insolvent insurer. During the year under review, the Insurance (Amendment) Act, 2014 was enacted and saw the mandate of the Fund expanded to include participation in statutory management and undertaking the liquidation of a wound up insurer. In addition, the scope of coverage was extended from solely policyholders to include related claimants. These changes will empower the Fund to play a more proactive role in the protection of policyholders and promotion of stability in the insurance sector.

#### **b) Management**

The Fund is administered by the Board of Trustees which has delegated the daily operations to the Managing Trustee which in turn has seconded four staff to man the Secretariat of the Fund. In accordance with its Strategic Plan Key Result Area to build institutional capacity, the Fund undertook staff training and reviewed its processes aimed at improving its operational effectiveness and efficiency. To this end, key staff was trained in Corporate Governance and attended various insurance compensation related workshops both locally and abroad while at the same time initiated the automation of its accounting process.

#### **c) Levy collection**

The Fund's primary mandate is the payment of compensation. The funds for this purpose collected from a statutory levy which is calculated at 0.5% of the insurance premiums paid to an insurer. In addition, the Fund also collects penalties charged either by itself or the Insurance Regulatory Authority (IRA) on insurers defaulting on specific sections of the Insurance Act. During the

## **POLICYHOLDERS COMPENSATION FUND**

### **STATEMENT OF THE MANAGING TRUSTEE (CONT'D)**

year there was a growth in the collection of levy by 22% to Kshs 539,596,662 from Kshs 441,781,359 in the previous year while penalties paid amounted to Kshs. 716,526. The growth on levy collection was largely due to the increased volume of insurance premiums as a result of industry growth but also due to correct computation of payable levy by insurers, timely payments and improved levy management. With increased enforcement of the law and close cooperation with the IRA, this trend is expected to increase in the next financial year.

#### **d) Investments**

The Fund invests its surplus assets primarily in Government securities. During the year the Fund generated an investment return of Kshs. 300,184,584 by investing in Treasury Bills which represents a 23% growth from the previous year. In addition, the Fund improved its cash management processes by reviewing its banking terms to ensure that funds awaiting investments are held in competitive interest bearing instruments.

#### **e) Administration Expenses**

During the year, the Fund continued to maintain low administration expenses due to the fact that it has not been required to exercise mandate its primary mandate of compensation payments. Overall administration expenses comprising of Board, Staff and Operational costs amounted to Kshs. 19,847,900 compared to Kshs. 15,376,479 during the previous year with the increase relating to development related activities necessary for capacity building.

#### **f) Net Asset Value**

The upshot in the improved performance in levy collection, investment returns, low administration costs and improved governance is a notable 29% growth in the net asset value of the Fund translating to KShs. 3,626,676,472 from Kshs. 2,806,026,600 in the previous year. The Fund is keen on maintaining this performance in order to be able to offer to fulfil its mandate of paying claimants effectively.

## POLICYHOLDERS COMPENSATION FUND

### STATEMENT OF THE MANAGING TRUSTEE (CONT'D)

#### g) Research

In order to effectively deliver on its mandate, the Fund undertakes research to inform policy recommendations. During the year under review, the Fund concluded an Actuarial Study on its compensation and contribution rates. This represents a step closer to attaining our strategic objective of paying an appropriate compensation as its findings will inform the review of the current compensation amount of KShs 100,000.

#### h) Strategic Partnerships

Fostering strategic partnerships is one of the Fund's strategic objectives. In this regard, the Fund became a member of the International Forum for Insurance Guarantee Schemes (IFIGS) in November 2013 and also appointed as an observer to its Executive Committee in recognition of its existence as the only entity of its kind in the region. The purpose of the Forum is to facilitate and promote international cooperation between insurance guarantee schemes and other stakeholder organizations in the development of policyholder protection. The Fund will therefore be able to share ideas, experiences and discussing issues of mutual interest and concern.

#### Conclusion

The Fund has not been required to pay out compensation. However, four insurers are currently under statutory management and the Fund may, in the near future, be called upon to pay compensation to policyholders as required by law should the courts declare any of the insurers insolvent. Until such a time, the focus of the Fund is to grow its assets and capacity to ensure it has the required structures in place to fulfil its mandate.



**CHARLES MACHIRA**  
**REPRESENTATIVE OF MANAGING TRUSTEE**

## POLICYHOLDERS COMPENSATION FUND

### CORPORATE GOVERNANCE STATEMENT

The Policyholders Compensation Fund is a State Corporation established in 2004 under section 179 of the Insurance Act.

#### Board Composition

The management of the Fund is vested in the Board of Trustees. The composition of the Board in the year under review was as follows:

Name	Membership	Representation
Mr. Gershom Otachi	Chairman	Independent
Mr. Abdulmalek Janmohamed	Former Chairman	Independent
Mr. Sammy M. Makove	Chief Executive Office Insurance Regulatory Authority	Commissioner of Insurance
Mrs. Shehnaz N. Sumar	Trustee	Representative of Insurers carrying on general business
Mr. Julius Mutua	Trustee	Alternate to Principal Secretary, The National Treasury
Mr. Tom Mulwa	Trustee	Nominee of Insurance brokers
Mr. Julius Manyeki	Trustee	Independent

During the period under review, the following changes took place:

1. Mrs. Shehnaz Sumar retired from the Board of Trustees on 10<sup>th</sup> September, 2013
2. Mr. Abdulmalek Janmohamed retired as the Board chairman on 10<sup>th</sup> January 2014.
3. Mr. Gershom Otachi was appointed Chairman on 10<sup>th</sup> January 2014 for a period of three years.
4. Mr. Tom Mulwa's term as a member of the Board expired on 31<sup>st</sup> March 2014.

## **POLICYHOLDERS COMPENSATION FUND**

### **CORPORATE GOVERNANCE STATEMENT (CON'D)**

Members of the board other than statutory members hold office for a period of three years and are eligible for re-appointment for a further one term. The Board is currently not fully constituted as the seats of the representative of insurers carrying on long term business and the nominee of persons carrying on the business of insurance loss assessment remain vacant. However, the Fund continues to engage with the National Treasury on the appointment of these Trustees.

Trustees are required to disclose any conflict of interest in relation to matters that are brought before them for deliberation as stipulated in the Board Charter.

#### **Board Committees**

The Board has delegated its authority to the standing committees to enable it effectively carry out its mandate. These Committees are described below and each has its own Terms of reference setting forth the purposes, goals and responsibilities as well as qualifications for membership and operational procedures.

During the period under review, the Board Committee membership was reconstituted by resolution of the Board. The committees meet at least four times in a year or at such times the Chairman of the committee shall require.

The Committees had nine (9) meetings in the financial year 2013/2014 as follows:

#### **i) Finance and Management Committee**

The terms of reference of the committee are to review and make recommendations to the Board on financials, operations, budget and the annual accounts.

In the year under review the members of the committee were;

1. Shehnaz Sumar - Chairman (Until 10<sup>th</sup> September 2013)
2. Tom Mulwa - Chairman (From 10<sup>th</sup> September 2013)
3. Commissioner of Insurance
4. Julius Mutua

The committee held four (4) meetings.

## **POLICYHOLDERS COMPENSATION FUND**

### **CORPORATE GOVERNANCE STATEMENT (CON'D)**

#### **ii) Technical and Public Policy Committee**

The Technical and Public Policy committee responsibility is to review the technical and policy related aspects of the Fund to ensure it operates within statutory and best practice requirements.

The membership to this committee was as follows:

1. Mr. Julius Manyeki - Chairman
2. Commissioner of Insurance
3. Julius Mutua - Alternate to the PS, The National Treasury

The committee held two (2) meetings.

#### **iii) Audit and Risk Committee**

The role of the committee is oversight of integrity of the financial statements of the Fund, performance of internal and external auditors and compliance with legal and regulatory requirements.

Members of the committee were:

1. Mr. Julius Manyeki - Chairman
2. Mr. Tom Mulwa
3. Mr. Julius Mutua

The committee held three (3) meetings.

#### **Board Attendance**

During the financial year 2013/2014 four (4) Board meetings and nine (9) committee meetings were held. Attendance by individual members for the period is as tabulated below:

## POLICYHOLDERS COMPENSATION FUND

### CORPORATE GOVERNANCE STATEMENT (CON'D)

Trustee	Board meetings		Committee Meetings	
	Held	Attended	Eligible	Attended
Gershon Otachi	4	2	N/a	N/a
Abdulmalek Janmohamed	4	2	N/a	N/a
Shehnaz N. Sumar	N/a	N/a	N/a	N/a
Julius Manyeki	4	4	5	8*
Commissioner of Insurance	4	4	6	9*
Tom Mulwa	4	3	7	4
Julius Mutua	4	1	9	7

\*Trustee invited to form quorum

#### Statement of Compliance

The Funds operations are legally guided by the Constitution of Kenya - 2010, the provisions of the Insurance Act Chapter 487 of the Laws of Kenya, the State Corporation Act, Chapter 446 of the Laws of Kenya and by the principles of good corporate governance.

The Fund continues to comply with all statutory requirements relevant to its operations as a body corporate and complies with relevant Government circulars issued from time to time.

#### Board Oversight

The Board is responsible for the formulation, implementation and monitoring of the fund's Strategic Plan therefore providing appropriate strategic direction for the Fund. In addition, the Board defines the Vision, Mission and Core Values that enable the realization of the set Strategic Plan. During the period under review, the Board oversaw the implementation of its Strategic Plan for the period 2012-2017.

The day to day operations of the Fund have been delegated to the Management which is headed by the Managing Trustee through its representative. Periodically, the Board monitors and evaluates the implementation of its plans and strategies through reports received from Management through its Committees.

#### Board Remuneration

The Board is remunerated in accordance to the approved terms and conditions of service prescribed under Government circular Number OP/CAB.2/12A (9) of 29<sup>th</sup> August 2003.

## **POLICYHOLDERS COMPENSATION FUND**

### **CORPORATE GOVERNANCE STATEMENT (CON'D)**

#### **Secretary to the Board**

The Secretary to the Board co-ordinates the Boards activities and ensures, in conjunction with the Chairman, that the Board meetings are held procedurally. In addition, the Secretary links the flow of information between the Board and management as well as ensuring the Board receives adequate and timely information.

All Trustees have direct access to the Secretary who is also responsible for implementing and monitoring good corporate governance practices, ensuring that Board business meets all statutory requirements, keeps all legal and regulatory requirements under review and briefs the Board accordingly about these developments.

## **POLICYHOLDERS COMPENSATION FUND**

### **CORPORATE SOCIAL RESPONSIBILY STATEMENT**

The Fund, owing to its mandate and nature of operations, partners and supports other State Corporations in undertaking Corporate Social Responsibility activities. In the year under review, the Fund undertook the following activities:

#### **a) Tree Planting**

The Fund partnered with other financial sector regulators in a tree planting exercise at Ngong forest. The Fund, through its staff participated to help plant over five hundred trees. The aim of the activity is the reforestation and preservation of Ngong Forest which is an important natural resource.

#### **b) Supporting the Cerebral Palsy Society of Kenya**

The Fund supported the Cerebral Palsy Society of Kenya in its efforts to raise awareness required to help alleviate stigma and challenges associated with the condition and to provide continued support to the individuals afflicted by Cerebral Palsy by donating funds and participating in its Annual Charity Walk held on 21<sup>st</sup> June, 2014.

## **POLICYHOLDERS COMPENSATION FUND**

### **REPORT OF THE BOARD OF TRUSTEES**

The Trustees submit their report together with Financial Statements of the Policyholders Compensation Fund for the period ending 30<sup>th</sup> June 2014.

### **ESTABLISHMENT**

The Policyholders Compensation Fund is a State corporation established under Section 179 of the Insurance Act and commenced its operations on 1st January, 2005.

### **PRINCIPAL ACTIVITIES**

The principal activities of the Fund are to protect the policyholders of an insolvent insurer through provision of compensation for unpaid claims, participation in statutory management and liquidation of a wound up insurer.

### **RESULTS**

The results for the year ended 30<sup>th</sup> June, 2014 are set out on page 21 of this report

### **BOARD OF TRUSTEES**

The Trustees who served during the current year are as follows:

Mr. Gershom Otachi	Chairman (appointed 10 <sup>th</sup> January 2014)
Mr. Abdulmalek Janmohamed	Chairman (up to 10 <sup>th</sup> January 2014)
Mr. Sammy Makove	Commissioner of Insurance
Mrs. Shehnaz Sumar	Trustee - Representative of Insurers conducting General Business
Mr. Julius Mutua	Trustee - Alternate to Principal Secretary, The National Treasury
Mr. Tom Mulwa	Trustee - Nominee of Insurance Brokers (upto 31 <sup>st</sup> March 2014)
Mr. Julius Manyeki	Trustee

### **AUDITORS**

The Auditor General is responsible for the statutory audit of the Policyholders Compensation Fund in accordance with Section 12 of the Public Audit Act 2003 (Cap.12)

**By Order of the Board**



**Charles Machira**

**Representative of the Managing Trustee and Secretary to the Board**

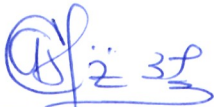
## POLICYHOLDERS COMPENSATION FUND

### STATEMENT OF THE BOARD OF TRUSTEES RESPONSIBILITIES

The Public Financial Management Act section 68 requires the Fund to prepare financial statements for each financial year. Financial statements include a statement of financial position showing in detail the assets and liabilities of the Fund, a statement of financial performance, a statement of cash flows and any other statements and accounts that may be necessary to fully disclose the financial position of the Fund. The State Corporations Act (Cap 446) requires the Fund to keep or cause to be kept proper books recording all the property, undertakings, funds, activities, contracts, transactions and other business of the Fund. Under the State Corporations Act, the Board of Trustees is responsible for the proper management of the affairs of a state corporation.

The Board of Trustees accepts responsibility for the annual financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgments and estimates, in conformity with generally accepted accounting principles and in the manner required by the State Corporations Act. The Trustees are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the Fund and of its operating results. The Board of Trustees further accepts 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 control.

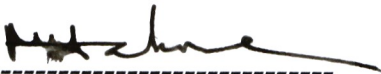
Nothing has come to the attention of the Board of Trustees to indicate that the Fund will not continue to operate as a "going concern" for at least the next twelve months from the date of this statement.



-----  
**Managing Trustee**



-----  
**Chairman**



-----  
**Trustee**

Date \_\_\_\_\_

# REPUBLIC OF KENYA



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NAIROBI

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## OFFICE OF THE AUDITOR-GENERAL

### REPORT OF THE AUDITOR-GENERAL ON POLICYHOLDERS' COMPENSATION FUND FOR THE YEAR ENDED 30 JUNE 2014

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#### REPORT ON THE FINANCIAL STATEMENTS

I have audited the accompanying financial statements of Policyholders' Compensation Fund set out on pages 21 to 37, which comprise the statement of financial position as at 30 June 2014, and the statement of financial performance, statement of changes in net assets, statement of cash flows and statement of comparison of budget and actual amounts 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**

The Board of Trustees is responsible for the preparation and fair presentation of these financial statements in accordance with International Public Sector Accounting Standards and for such internal control as the Board determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

The Board 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) and (3) 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.

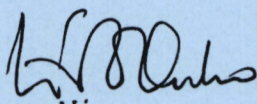
An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial

statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls 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 Board, 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 2014, and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards and comply with the Insurance Act, Cap 487 of the Laws of Kenya.



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

**Nairobi**

**20 April 2015**

**POLICYHOLDERS COMPENSATION FUND**

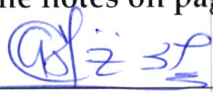
**STATEMENT OF FINANCIAL PERFORMANCE  
FOR THE YEAR ENDED 30 JUNE 2014**

		<b>2014</b>	<b>2013</b>
	<b>Notes</b>	<b>KSHS</b>	<b>KSHS.</b>
<b>Revenue from non-exchange transactions</b>			
Contribution levy	3	539,596,662	441,781,359
Penalties	4	716,526	680,000
		<u>540,313,188</u>	<u>442,461,359</u>
<b>Revenue from exchange transactions</b>			
Interest income	5	300,184,584	244,513,094
		<u>300,184,584</u>	<u>244,513,094</u>
<b>Total Revenue</b>		<u>840,497,772</u>	<u>686,974,453</u>
<b>EXPENDITURE</b>			
Board expenses	6	9,022,887	6,413,198
Personnel emoluments	7	8,008,100	6,520,300
Administrative expenses	8	2,816,913	2,442,981
Total expenses		<u>19,847,900</u>	<u>15,376,479</u>
<b>SURPLUS FOR THE YEAR</b>		<u>820,649,872</u>	<u>671,597,974</u>

**POLICYHOLDERS COMPENSATION FUND  
STATEMENT OF FINANCIAL POSITION  
AS AT 30 JUNE 2014**

		2014	2013
	Notes	KSHS	KSHS
<b>ASSETS</b>			
CURRENT ASSETS			
Receivable from non exchange transaction	9	44,873,757	31,360,183
Receivable from exchange transactions	10	60,986,	-
Other debtors		-	5,008,725
Investments	11	3,502,291,888	2,748,283,989
Cash and bank balances	12	<u>79,916,787</u>	<u>24,278,590</u>
		<u>3,627,143,418</u>	<u>2,808,931,487</u>
NON CURRENT ASSETS			
Property, plant and equipment	13	451,178	485,022
		<u>451,178</u>	<u>485,022</u>
<b>TOTAL ASSETS</b>		<b><u>3,627,594,596</u></b>	<b><u>2,809,416,509</u></b>
<b>CURRENT LIABILITIES</b>			
Payables from exchange transactions	14	570,124	3,041,909
Provisions	15	<u>348,000</u>	<u>348,000</u>
		<u>918,124</u>	<u>3,389,909</u>
<b>NET ASSETS</b>		<b><u>3,626,676,472</u></b>	<b><u>2,806,026,600</u></b>
<b>RESERVES</b>			
Government Grant	19	35,000,000	35,000,000
Accumulated surplus		<u>3,591,676,472</u>	<u>2,771,026,600</u>
		<u>3,626,676,472</u>	<u>2,806,026,600</u>

The notes on page 26 to 34 form an integral part of these financial statements



Managing Trustee



Trustee



Chairman

**POLICYHOLDERS COMPENSATION FUND  
STATEMENT OF CHANGES IN NET ASSETS  
FOR THE YEAR ENDED 30 JUNE 2014**

<b>FUND RESERVE</b>	<b>Notes</b>	<b>KSHS</b>
1 July, 2012		2,134,428,626
<b>Changes in reserves for 2013</b>		
Surplus for the year		<u>671,597,974</u>
<b>Balance at 30 June, 2013</b>		<u><b>2,806,026,600</b></u>
1 July, 2013		2,806,026,600
<b>Changes in reserves for 2014</b>		
Surplus for the year		<u>820,649,872</u>
<b>Balance at 30 June, 2014</b>		<u><b>3,626,676,472</b></u>

## POLICYHOLDERS COMPENSATION FUND

### STATEMENT OF CASHFLOWS FOR THE YEAR ENDED 30 JUNE 2014

	Notes	2014 KSHS	2013 KSHS
<b>Cash flow from operating activities</b>			
Surplus for the year		820,649,872	671,597,974
<b>Adjustments for:</b>			
Depreciation on property, plant & equipment	13	373,144	323,896
Interest income		<u>(300,184,584)</u>	<u>(244,513,094)</u>
Surplus before working capital changes		520,838,432	427,408,776
Decrease in other receivables		5,008,725	(5,008,725)
Increase in withholding tax	10	(60,986)	-
Increase in Levy receivable	9	(13,513,574)	(5,468,571)
(Decrease)/ Increase in payables	14,15	<u>(2,471,785)</u>	<u>(2,632,048)</u>
<b>Net Cash from Operating Activities</b>		<b>509,800,812</b>	<b>414,299,432</b>
<b>Cash flow from investing activities</b>			
Purchase of property, plant and equipment	13	(339,300)	(26,836)
Investment income		300,184,584	244,513,094
Net cash used in investing Activities		<u>299,845,284</u>	<u>244,486,258)</u>
Net increase in cash & cash equivalents		809,646,096	658,785,690
Cash & cash equivalent at the beginning	17	<u>2,772,562,579</u>	<u>2,113,776,889</u>
Cash & cash equivalent at the end	17	<u><b>3,582,208,675</b></u>	<u><b>2,772,562,579</b></u>

**POLICYHOLDERS COMPENSATION FUND**

**STATEMENT OF COMPARISON OF ACTUAL AND BUDGET AMOUNTS**

	NOTES	2014 KSHS BUDGET	2014 KSHS ACTUAL	KSHS VARIANCE
<b>INCOME</b>				
Contribution levy		477,219,000	539,596,662	62,377,662
Interest Income		268,860,000	300,901,110	32,041,110
		<b>746,079,000</b>	<b>840,497,772</b>	<b>94,418,772</b>
<b>OPERATING EXPENDITURE</b>				
Board expenses		13,204,800	9,022,887	4,181,913
Managing Trustee		7,895,800	8,008,100	(112,300)
Insurance expenses		100,000	-	(100,000)
Repairs & maintenance		155,000	25,346	129,654
Official entertainment		300,000	55,800	244,200
Travel and accommodation		1,670,000	1,132,021	537,979
Office expenses		135,000	15,268	119,732
Printing & stationery		795,450	261,612	533,838
Public Education & Publicity		1,000,000	16,300	983,700
Training & Development		550,000	218,080	331,920
Library expenses		79,200	65,490	13,710
Post & telephone		186,500	99,500	87,000
Professional charges		1,000,000	487,200	512,800
Information technology		500,000	6,100	493,900
Bank Charges		100,000	61,052	38,949
Depreciation		<u>234,000</u>	<u>373,144</u>	<u>(139,144)</u>
<b>TOTAL EXPENDITURE</b>		<b>27,905,750</b>	<b>19,847,900</b>	<b>8,057,850</b>
<b>SURPLUS FOR THE YEAR</b>	<b>18</b>	<b>718,173,250</b>	<b>820,649,872</b>	<b>102,242,622</b>

**POLICYHOLDERS COMPENSATION FUND  
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR  
ENDED 30 JUNE, 2014**

**1. Statement of compliance and basis of preparation**

The financial statements are prepared in accordance and comply with International Public Sector Accounting Standards (IPSAS). The financial statements have been prepared on a going concern basis and the accounting policies have been applied consistently throughout the period. The financial statements have been prepared on the basis of historical cost. The cashflow is prepared using the indirect method.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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

**(a) Income recognition**

**i) Revenue from non-exchange transactions**

**Contribution Levy and Penalties**

The Fund recognizes revenues from levies and penalties when the event occurs and the asset recognition criteria are met. Other non-exchange revenues are recognized when it is probable that the future economic benefits or service potential associated with the asset will flow to the Fund and the fair value of the asset can be measured reliably.

**ii) Revenue from exchange transactions**

**Interest income**

Interest income is accrued using the effective yield method. The effective yield discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. The method applies this yield to the principal outstanding to determine interest income each period.

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014 (CONT'D)**

**(b) Budget information**

The annual budget is prepared on accrual basis, that is, all planned costs and income are presented in a single statement to determine the needs of the Fund.

As a result of the adoption of the accrual basis for budgeting purposes, there is no basis that would require reconciliation between the actual comparable amounts and the amounts presented as a separate additional financial statement in the statement of comparison of budget and actual amounts.

**(c) Property, plant, equipment and depreciation**

All property and equipment is initially recorded at cost and thereafter stated at historical cost less accumulated depreciation. Historical cost comprises expenditure initially incurred to bring the asset to its location and condition ready for its intended use.

Depreciation is calculated on the cost of each asset on a straight-line basis at annual rates estimated to write off the cost of the asset over its estimated useful life.

The Depreciation rates used are as follows.

Computers	33.3%
Office furniture & Equipment	12.5%

**(d) Related parties**

The Fund regards a related party as a person or an entity with the ability to exert control individually or jointly, or to exercise significant influence over the Fund, or vice versa. The Board of Trustees and members of key management, Retirement Benefits Authority and Insurance Regulatory Authority are regarded as related parties.

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014 (CONT'D)**

Entity	Relationship	Transaction	Justification
Retirement Benefits Authority	Managing Trustee	Operational - Secondment of staff Financial - Salary reimbursement	Gazette notice 3357 of 6 <sup>th</sup> May 2005 Seconded staff
Insurance Regulatory Authority	Industry Regulator	Operational - supervision	Insurance Act section 179
Board members	Trustees	Operational - oversight Financial - allowances	Section 179 2B of the Insurance Act Based on existing laws

**(e) Financial instruments**

Financial assets and financial liabilities are recognised in the Fund's statement of financial position when the Fund becomes a party to the contractual provisions of the instrument.

**Financial Assets**

*Receivables*

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Fund provides money, goods or services directly to a debtor with no intention of trading the receivable.

*Government securities*

Government securities comprise treasury bills and treasury bonds which debt securities are issued by the Government of Kenya. Government securities are classified as held to maturity and are stated at amortised cost.

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014 (CONT'D)**

*Short term deposits*

Short term deposits are classified as held to maturity and are stated at amortised cost.

**Financial liabilities**

*Trade payables*

Trade payables are current and are stated at their nominal value.

**(f) Financial Risk Management**

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

*Interest Rate Risk*

The Funds overall risk management focuses on unpredictability of interest rate on Treasury bills.

*Credit Risk*

Credit risk is limited to the outstanding contribution from insures as all the investments are in risk free Government securities.

*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.

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014 (CONT'D)**

**(g) Inventories**

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

**(h) Provisions**

Provisions are recognized when the Fund has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

**(i) Nature and Fund reserve**

The Fund maintains a general reserve to be utilized for the payment of compensation to claimants of an insolvent insurer in accordance to its mandate.

The reserve is held in Government securities.

**(j) Cash and cash equivalents.**

For the purposes of the statement of cash flows, cash and cash equivalents comprise cash in hand, current account bank balances, short term fixed deposits and Treasury Bills.

**(k) Comparatives**

Comparative figures have, where applicable, been adjusted to conform to changes in the current presentation.

**(l) Provisions**

Provisions are measured at the management's best estimate of the expenditure required to settle the obligation at the reporting date

**POLICYHOLDERS COMPENSATION FUND  
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR  
ENDED 30<sup>TH</sup> JUNE 2014 (CONT'D)**

**(m) Currency**

The financial statements are prepared in Kenya Shillings (KShs.), rounded to the nearest shilling

**(n) Subsequent events**

There have been no events subsequent to the financial year end with a significant impact on the financial statements for the year ended June 30, 2014.

**3. CONTRIBUTION LEVY**

	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Contribution Levy	<u>539,596,662</u>	<u>441,781,359</u>
	<u><b>539,596,662</b></u>	<u><b>441,781,359</b></u>

As per section 179 (2) of the Insurance Act, Insurers are required to pay a levy on gross direct premiums written at a rate prescribed by the Cabinet Secretary. The rate is currently at 0.5%.

**4. PENALTIES**

	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Penalties	<u>716,526</u>	<u>680,000</u>
	<u><b>716,526</b></u>	<u><b>680,000</b></u>

The Insurance Act Section 179 requires insurers to pay a penalty of 2.5% of any overdue levy amount. Additionally, late submissions of return to the Insurance Regulatory Authority also attract a penalty payable into the Fund.

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014 (CONT'D)**

**5. INTEREST INCOME**

	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Treasury Bills	297,222,787	243,718,627
Deposit accounts	<u>2,962,787</u>	<u>794,466</u>
	<u>300,184,584</u>	<u>244,513,094</u>

**6. BOARD EXPENSES**

	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Honoraria	960,000	960,000
Sitting allowances	3,220,000	3,020,000
Lunch allowances and snacks	106,387	241,730
Seminars, travel and accommodation	3,665,075	1,899,129
Bonus	1,071,425	-
Medical	<u>-</u>	<u>292,339</u>
	<u>9,022,887</u>	<u>6,413,198</u>

**7. PERSONNEL EMMOLUMENTS**

Representative of Managing Trustee	600,000	727,900
Secretariat	6,872,386	5,792,400
Bonus	<u>535,714</u>	<u>-</u>
	<u>8,008,100</u>	<u>6,520,300</u>

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014 (CONT'D)**

**8. ADMINISTRATIVE EXPENSES**

Insurance	-	8,980
Repairs and maintenance	25,346	28,700
Travel and accommodation	1,132,021	804,670
Information technology	6,100	3,000
Office expenses	15,268	90,481
Official entertainment	55,800	32,700
Printing and stationery	261,612	229,081
Library	65,490	55,470
Postage and telephone	99,500	102,000
Public education and publicity	16,300	236,200
Professional fees	487,200	401,000
Bank charges	61,052	43,635
Training and development	218,080	83,168
Depreciation	373,144	323,896
	<u>2,816,913</u>	<u>2,442,981</u>

**9. RECEIVABLES FROM NON EXCHANGE TRANSACTIONS**

	2014 KShs	2013 KShs
Contribution levy	<u>44,873,757</u>	<u>31,360,183</u>
	<u>44,873,757</u>	<u>31,360,183</u>

This is contribution levy for June 2014 receivable in July 2014.

**10. WITHHOLDING TAX**

	2014 KShs	2013 KShs
Withholding tax	<u>60,986</u>	-
	<u>60,986</u>	-

This relates to investment interest and was erroneously withheld by Cooperative Bank since the Fund's income is tax exempt as per Legal Notice No.68 of 15<sup>th</sup> June 2006

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014**

<b>11. INVESTMENTS</b>	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Treasury bills	<u>3,502,291,888</u>	<u>2,748,283,989</u>
	<b><u>3,502,291,888</u></b>	<b><u>2,748,283,989</u></b>

The effective rate of interest rate was 10.230% as at 30<sup>th</sup> June 2014.

<b>12. CASH AND BANK BALANCES</b>	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Commercial Bank of Africa		
Operational	604,130	654,559
Fund	24,898,424	23,621,966
Kenya Commercial Bank	488,282	-
Cooperative Bank of Kenya	53,913,101	-
Cash on Hand	<u>12,850</u>	<u>2,065</u>
	<b><u>79,916,787</u></b>	<b><u>24,278,590</u></b>

**POLICYHOLDERS COMPENSATION FUNDNOTES TO THE  
FINANCIAL STATEMENTS FOR THE YEAR  
ENDED 30 JUNE, 2014**

**13.PROPERTY, PLANT & EQUIPMENT**

	Computer Equipment 33.3% Kshs.	Office Furniture & Equipment 12.5% Kshs.	Total Kshs.
<u>Cost</u>			
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	1,178,275	384,143	1,562,418
<u>Depreciation</u>			
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	740,251	337,145	1,077,396
<u>Net book value</u>			
At 30 June 2013	438,024	46,998	485,022
At 30 June 2012	446,953	64,804	511,757
<u>Cost</u>			
At 01 July 2013	1,178,275	384,143	1,562,418
Additions	339,300	-	339,300
Disposal	-	-	-
At 30 June 2014	1,517,575	384,143	1,901,718
<u>Depreciation</u>			
At 01 July 2013	740,251	337,145	1,077,396
Charge for the year	363,897	9,247	373,144
Disposal	-	-	-
At 30 June 2014	1,104,148	346,392	1,450,540
<u>Net book value</u>			
At 30 June 2014	413,427	37,751	451,178
At 30 June 2013	438,024	46,998	485,022

**POLICYHOLDERS COMPENSATION FUND**  
**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR**  
**ENDED 30 JUNE, 2014**

**14. PAYABLES FROM EXCHANGE TRANSACTIONS**

	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Sundry creditors	<u>570,124</u>	<u>3,041,909</u>
	<b><u>570,124</u></b>	<b><u>3,041,909</u></b>

**15. PROVISIONS**

	<b>2014</b>	<b>2013</b>
	<b>KShs</b>	<b>KShs</b>
Audit fees	<u>348,000</u>	<u>348,000</u>
	<b><u>348,000</u></b>	<b><u>348,000</u></b>

**16. GOVERNMENT GRANT**

The Government grant was seed capital provided to the Fund by Government of Kenya in two financial years, Kshs. 15 million in 2005/2006 and Kshs 20 million in 2006/2007. The grant was not refundable and was immediately invested.

**17. CASH AND CASH EQUIVALENT**

This includes cash in hand, current account balances and treasury bills.

		<b>2014</b>	<b>2013</b>
		<b>KShs</b>	<b>KShs</b>
Investments	11	3,502,291,888	2,748,283,989
Cash and bank balance	12	<u>79,916,787</u>	<u>24,278,590</u>
		<b><u>3,582,208,675</u></b>	<b><u>2,772,562,779</u></b>

**POLICYHOLDERS COMPENSATION FUNDNOTES TO THE  
FINANCIAL STATEMENTS FOR THE YEAR  
ENDED 30 JUNE, 2014**

**18. STATEMENT OF ACTUAL AND BUDGET AMOUNTS**

Vote	Variance Kshs	Variance %	Remarks
<b>Income</b>			
Contribution Levy	62,377,662	13	Increase in business volumes by insurers
Interest income	32,041,110	12	Increased in surplus funds invested
<b>Operating expenditure</b>			
Board	4,181,913	32	Board not fully constituted
Insurance	100,000	100	Due to Scaled down operations resulting from Government directive (OP/CAB 9/1/5)
Repairs & maintainance	129,654	84	Due to Scaled down operations resulting from Government directive (OP/CAB 9/1/5)
Official entertainment	244,200	81	Scaled down activities
Travel & accomodation	537,979	32	Limited activities
Office expenses	119,732	87	Due to Scaled down operations resulting from Government directive (OP/CAB 9/1/5)
Printing & stationery	533,838	67	Due to Scaled down operations resulting from Government directive (OP/CAB 9/1/5)
Public education & publicity	983,700	98	Postponement of International Conference - the International Forum of Insurance Guarantee Schemes (IFIGS)
Training & development	331,920	60	Due to Scaled down operations resulting from Government directive (OP/CAB 9/1/5)
Postage & telephone	87,000	47	Scaled down activities
Professional	512,800	51	Due to Scaled down operations resulting from Government directive (OP/CAB 9/1/5)