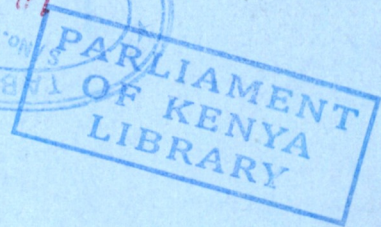
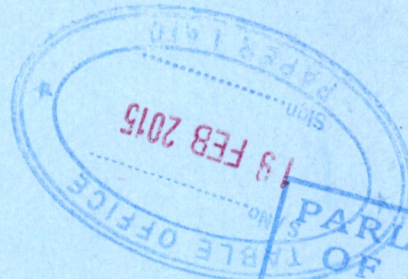


REPUBLIC OF KENYA



*Laid by the  
Hon. A. Suake (COM)  
Mw 19.2.2015*

**KENYA NATIONAL AUDIT OFFICE**



**REPORT**

**OF**

**THE AUDITOR-GENERAL**

**ON**

**THE FINANCIAL STATEMENTS OF  
CAPITAL MARKETS AUTHORITY**

**FOR THE YEAR ENDED  
30 JUNE 2014**



**CAPITAL MARKETS AUTHORITY**  
**ANNUAL REPORT AND FINANCIAL STATEMENTS**  
**FOR THE FINANCIAL YEAR ENDED 30TH JUNE 2014**

*Capital Markets Authority*  
*Annual report and financial statements*  
*For the year ended 30th June 2014*

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### Background information

Capital Markets Authority is a body corporate established under the Capital Markets Authority Act, 1989. The Act was amended in 2000 and renamed as Capital Markets Act.

### Principal activities

The Authority promotes and facilitates the development of an orderly, fair and efficient capital markets in Kenya.

### Key management

#### **Paul Muriithi Muthaura**

Position Ag. Chief Executive  
Date joined the Authority September 15, 2005  
Profession Lawyer



Key qualifications

LLM, LLB, MPhil, Dip Law, Dip in Financial Management, DBA(Candidate)

#### **Wyckliffe Shamiah**

Position Director, Market Operations  
Profession Accountant  
Date joined the Authority May 20, 1995  
Key qualifications MBA, BA, CPA (K)



#### **Rose Lumumba**

Position Director, Corporation Secretary  
and Communication  
Date joined the Authority June 2, 2008  
Profession Lawyer  
Key qualifications MBA, LLB, CPS (K), Dip In Law, PhD (Candidate)



#### **Edwin Nyaga Njamura**

Position Director, Corporate Services  
Profession Accountant  
Date joined the Authority July 17, 2012  
Key qualifications MBA, BCOM, CPA(K), BSP



#### **Esther J. Maiyo**

Position Manager, Internal Audit  
Date joined the Authority February 15, 1995  
Profession Accountant  
MBA, BCOM, CPA(K), CPS (K), CISA  
Key qualifications



#### **Luke Evans Ombara**

Position Acting Director, Regulatory  
Policy and Strategy  
Date joined the Authority February, 15 1995  
Profession Economist  
Key qualifications MA, BA, BSP



#### **Johnstone Kaila Oltetia**

Position Manager, Market Supervision  
Date joined the Authority May 20, 1997  
Profession Financial Analyst  
Key qualifications MBA, BCOM, CFE



**Capital Markets Authority**  
**Authority information (continued)**  
**For the year ended 30th June 2014**

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**Samuel Kamunyu Njoroge**

Position: Manager, Investor Education  
 Date joined the Authority: January 3, 2005  
 Profession: Economist  
 Key qualifications: MA, B.A



**Andrew Muthabuku**

Position: Manager, Human Capital & Administration  
 Date joined the Authority: July 1, 2011  
 Profession: Human Resources & Administration  
 Key qualifications: MBA, BA, H-Dip (HRM)



**Richard Chirchir**

Position: Manager, Information Communications & Technology  
 Date joined the Authority: June 22, 2009  
 Profession: Computer Science Engineering  
 Key qualifications: BSC, Pg Dip - Computer Science



**John Njoroge**

Position: Manager, Finance  
 Date joined the Authority: February 4, 2008  
 Profession: Accountant/Economist  
 Key qualifications: BA, CPA(K), CPS(K), BSP



<b>Key</b>	
<b>DBA</b>	Doctor of Business Administration
<b>PhD</b>	Doctor of Philosophy
<b>MBA</b>	Master of Business Administration
<b>MA</b>	Master of Arts
<b>LLM</b>	Master of Law
<b>BCOM</b>	Bachelor of Commerce
<b>LLB</b>	Bachelor of Law
<b>BSC</b>	Bachelor of Science
<b>BA</b>	Bachelor of Arts
<b>CPA</b>	Certified Public Accountant
<b>CPS</b>	Certified Public Secretary
<b>HRM</b>	Human Resource Management
<b>CISA</b>	Certified Information Systems Auditor
<b>CFE</b>	Certified Fraud Examiner
<b>Pg Dip</b>	Post Graduate Diploma
<b>H. Dip</b>	High Diploma
<b>Dip</b>	Diploma
<b>BSP</b>	Balanced Scorecard Professional

**Board members of the Authority**

	<b>Date of Birth</b>	
Mr Kung'u Gatabaki	1st June, 1950	- Chairman (Term ended 31st May 2014)
Mr Paul M. Muthaura	27th April, 1978	- Acting Chief Executive
Dr Kamau Thugge, EBS	1st August, 1957	- Principal Secretary to the National Treasury
Dr Geoffrey Mwau	11th November, 1957	- Alternate to the Permanent Secretary to the Treasury
Hon. Prof. Githu Muigai, MP	31st January, 1960	- Attorney General
Ms Jane Joram	1st December, 1966	- Alternate to the Attorney General
Prof. Njuguna Ndung'u, CBS	7th July, 1959	- Governor Central Bank of Kenya
Ms Rose Detho	2nd June, 1960	- Alternate to the Governor Central Bank of Kenya
Ms. Nafisa Abass	30th November 1966	- Member
Mr Humphrey Muga	1954	- Member (Term ended on 31st March, 2014)
Mr Mahmood Manji, OGW	19th December, 1953	- Member (Term ended on 31st March, 2014)
Mr Paul Ngugi, MBS	13th July, 1952	- Member
Ms Judy Thuo	30th April, 1968	- Member
Mrs Anne Schofield	1st July, 1956	- Member (Resigned on 30th June 2014)

*Capital Markets Authority*  
*Authority information (continued)*  
*For the year ended 30th June 2014*

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<b>Registered office</b>	3rd Floor, Embankment Plaza Longonot Road, Upper Hill P.O. Box 74800,00200 Nairobi
<b>Authority contacts</b>	Telephone: (254) 2221910/ 2264900/2221869/2226225 E-mail: corporate@cma.or.ke Website: www.cma.or.ke
<b>Principal bankers</b>	Commercial Bank of Africa Limited Mara / Ragati Roads Upper Hill P.O. Box 30437, 00100 Nairobi  Housing Finance Company of Kenya Limited Kenyatta Avenue/Koinange Street, Rehani House P.O. Box 30088, 00100 Nairobi  KCB Mortgage Centre, Salama House Mama Ngina Street P.O. Box 45129, 00100 Nairobi
<b>Authorized independent auditor</b>	RSM Ashvir Certified Public Accountants 1st Floor, Reliance Centre, Woodvale Grove, Westland's P.O. Box 349, 00606 Nairobi
<b>On behalf of</b>	The Auditor-General Kenya National Audit Office Anniversary Towers University Way P.O. Box 30084 - 00100 Nairobi
<b>Principal legal adviser</b>	The Attorney General State Law Office Harambee Avenue P.O. Box 40112, 00200 Nairobi  Archer & Wilcock Advocates Marakwet Close, Kilimani P.O. Box 10201, 00400 Nairobi  Hamilton Harrison & Mathews 14 ICEA Building Kenyatta Avenue P.O. Box 30333, 00100 Nairobi  Waweru Gatonye & Co. Advocates Timau Plaza, 4th Floor, Argwings Kodhek Timau Road Junction P.O. Box 55207, 00200 Nairobi  RH Advocates Transnational Plaza, City Hall Way, City Centre P.O. Box 50515, 00200 Nairobi

## **INTRODUCTION**

I am pleased to present the Authority's Annual Report for the year ended 30 June 2014.

During the year, the Country's Gross Domestic Product was estimated to have expanded by 4.1 per cent in the first quarter of 2014 compared to 5.2 per cent during the same quarter of 2013. The slowdown in GDP growth was attributable to the Agriculture sector that grew 2.7% year on year compared to 6.8% during a similar period in 2013 on account of erratic weather that suppressed vegetable and tea production coupled with lower international coffee and tea prices. Additionally, the hotels and restaurants sector contracted, driven by a decline in bed occupancy in coastal beach hotels attributable to security concerns. The growth was mainly impelled by expansion in transport and communication, manufacturing, wholesale and retail trade, mining and quarrying and electricity industries.

The World Bank's latest economic analysis for Kenya forecasts a growth rate of 4.7% in 2014, and says the economy has the potential to achieve a higher growth rate of 5% in the next two years. The report indicates that a higher growth rate will depend on macroeconomic stability and credible policies, which have underpinned Kenya's growth in the past and will be powered by aggregate demand, fuelled by strong consumption and investment.

In the most recent Global Competitiveness survey, Kenya edged up 10 slots in the rankings. We were easily the most improved African country: Our key improvement areas were: "legal rights"; 35<sup>th</sup>; "financing through the local equity market"; 44<sup>th</sup> for "ease of access to loans" and 55<sup>th</sup> for "regulation of securities exchanges". To build on that growth, and the promising performance of our financial sector, the Authority, through the Capital Markets Master Plan Steering Committee, and in consultation with stakeholders, developed the Capital Markets Master Plan 2014-2023 to guide the development of the capital markets sector in achieving our great nation's aspirations as well as consolidate Kenya's position as the 'Heart of Africa's Capital Markets' and the Financial gateway to East and Middle Africa.

## **STRATEGIC DIRECTION**

The Authority developed a new strategic plan during the year to cover the period 2013-17. The thrust of the new strategic direction is to ensure that the country's capital markets becomes more efficient, competitive, financially sound and dynamic to promote innovation and attract investments into the country. That called for deliberate focus on ensuring the country's capital markets provide access to differentiated products and services of high degree of novelty. During the year under review the Authority undertook a number of initiatives during the year which are anchored on the following strategic objectives:

- i) To establish a robust, facilitative policy, legal and regulatory framework for capital market development;
- ii) To develop and deepen the capital market products and services;
- iii) To promote investor education, awareness and interest in the capital markets;
- iv) To enhance the efficiency and integrity of the capital market infrastructure and institutional arrangements; and
- v) To strengthen the institutional capacity of the CMA to effectively and efficiently deliver on its mandate.

## **MARKET REFORMS**

In line with above strategic objectives, the Authority continued with the implementation of various activities as outlined in its strategic direction's reform agenda. The underlying principle in the reform agenda is facilitation of new products into the market to diversify and deepen the capital market in line with its critical role of mobilizing resources to meet the Vision 2030 objectives.

### **Demutualization of the Nairobi Securities Exchange (NSE)**

The Authority approved the Demutualization of the Nairobi Securities Exchange in June 2014, making it the second exchange in Africa to be demutualized. This reform will significantly address its corporate governance, ownership and operational structures in line with global trends. This is expected to increase its competitiveness through adoption of a for-profit business model supported by the introduction of clear separation of ownership from management, the institutionalization of an independent board, the removal of perceived barriers to competitive access to providing securities trading business as well as laying the ground for further work to support its recognition as a Self Regulatory Organization (SRO). The NSE plans to self-list in the first quarter of 2014/2015 financial year through an Initial Public Offering (IPO), which is expected to bring in new investors thereby further diversifying its ownership structure, in addition to allowing it to raise capital from the public markets to support infrastructure development and new business lines.

### **Capital Markets Master Plan**

During the period under review, the Authority has under the guidance of the Capital Markets Master Plan Steering Committee (CMMSC), finalized the developed a Master Plan that is expected to provide the direction for the Kenyan capital market over the next ten (10) years. The Master Plan envisions that by 2023, Kenya will be transformed into the choice market for domestic, regional and international issuers and investors looking to invest in and realize their investments in Kenya, within East Africa and across Middle Africa. This key Vision 2030 Flagship project, under the 2nd Medium Term Plan (MTP2), has not only harnessed creativity and innovation from the industry players, but has leveraged on consensus on the vision, key pillars and building blocks and execution plan necessary for capital markets to be transformative. Following its publication, key recommendations were endorsed by the Kenyan Government through policy pronouncements by the Cabinet Secretary to The National Treasury.

### **Capital Markets Corporate Governance Code**

The Authority through the Corporate Governance Committee (CGC), comprising market stakeholders, overhauled the corporate governance framework for listed companies in line with global trends to facilitate increased transparency and accountability to promote increased investment and domestic and international fund flows. The CGC oversaw during the period under review: the delivery of a robust revised corporate governance legal framework that included a Blueprint, which is a high-level summary of proposed action plans, a Code of Corporate Governance Practices for Public Listed Companies in Kenya and subsequently a Corporate Governance Code. It further reviewed of the draft Companies Bill 2012 to ensure alignment with global trends in company law and submission of detailed recommendations to the Attorney General.

### **Derivatives Market**

The Authority subjected the Derivatives Regulations relating to licensing of market intermediaries and business of futures contract to peer review and benefitted from positive feedback from regulators such as the Malaysia Securities Commission, Securities and Exchange Board of India (SEBI), Dubai Financial Services Authority (DFSA) and the China Securities Regulatory Commission. These were submitted to the Cabinet Secretary to The National Treasury on June 30, 2014. A consortium of firms has recently expressed an interest to set up a Derivatives Exchange in Kenya and is currently engaging with the Authority's technical team.

*Capital Markets Authority  
Chairman's Statement (continued)  
For the year ended 30th June 2014*

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Other developments during the period under review include; the development of a guide on Central Counter Party (CCP) Clearing Infrastructure for Derivatives Market was developed and adopted to address risk management; completion of twelve technical staff completed of a two month Futures Certification Program; development of comprehensive manuals were developed on: policies and check-lists to assist the Authority in reviewing applications, market supervision, risk management, surveillance and enforcement in Derivatives Market; development of a derivatives accounting framework ; and the approved of the Futures Unit organizational structure by the CMA Board with clear job descriptions and competencies to ensure the regulator has dedicated resources for the supervision of derivative products.

In the coming year the Authority will be addressing tax issues in relation to derivatives markets focusing on treatment of unrealized gains and losses from hedging as well as capital gains and losses by market makers in derivatives transaction.

#### **State Agency Reforms**

In July, 2013, His Excellency, The President appointed the Taskforce on Parastatal Reforms which was tasked with the responsibility of interrogating the policies on the management and governance of Kenya's parastatals with the aim of determining how best they would contribute to the pursuit of national development aspirations. In doing so, the taskforce recommended the merger of several state agencies including those in the financial services sector. In this regard, the Capital Markets Authority, Insurance Regulatory Authority, Retirement Benefits Authority and the Sacco Societies Regulatory Authority have been in frequent consultation with the Taskforce through a committee, on how best to transition smoothly into this model of financial supervision.

#### **CO-OPERATION**

The Authority continues to actively participate in the local regional and international arena. This is important to ensure that robust mutual arrangements and cooperation are promoted to assist our efforts in advancing market development. We continued working closely with organizations such as International Organization of Securities Commissions (IOSCO) and East African Securities Regulatory Authorities (EASRA) in sharing experience, knowledge and expertise. The establishment of an integrated East African market presents important opportunities for the capital markets. The integration offers opportunities for expanding the range of financial products and services and mobilization of capital from a larger market.

The Authority has been at the forefront in fast tracking the development of Nairobi as an International Financial center. To this end we are nearing the finalization of Memorandum of Understanding between Kenya and the City of London, to tap into the latter's private sector funds in excess of GBP 90 billion looking for investment opportunities globally; and will subsequently continue our engagement with the Qatar International Center to Financial Authority to enhance the current NIFC model, through technical support and international benchmarking. Further, the Authority will be seconding its staff to the Nairobi International Financial Center Authority in the near future to enhance its capacity.

In conclusion, the significant progress registered in our capital market during the year was made possible by the wise counsel and dedication of my fellow board members. I wish also to extend my gratitude to the staff of the Authority, for their dedication, commitment and continuing contribution to our reform agenda and look forward to their support in the coming years to turn our vision into reality.



.....

**Mr. Paul Ngugi, MBS  
Ag. Chairman**

#### **Board Committees**

Subject to fundamental, strategic, policy and formal matters reserved for its decision, pursuant to Section 14 of Capital Markets Act, the Board works through a number of committees which operate within defined Terms of Reference. Other committees are formed on ad-hoc basis as need arise. During the period under review, the Board constituted the following committees:

##### **The Finance and Planning Committee.**

This committee consists of five members all of whom are non-executive members of the Board. The committee was chaired by Mr Paul Ngugi. This committee has oversight on all financial issues including budgets, financial reporting process and controls and procurement. The committee met three times during the period.

##### **The Audit, Corporate Governance and Risk Management Committee.**

This committee consists of five members all of whom are non-executive members of the Board. The committee was chaired by Mr. Mahmood Manji, until the expiry of his term. It has oversight responsibility of reviewing, assessing adequacy and monitoring of internal controls, risk management and corporate governance processes; examining internal and external audit reports and recommendations; overseeing financial reporting and reviewing the accounting principles, policies and practices adopted in the preparation of financial statements. It is also charged with reviewing the risk management and corporate governance practices of licensees and listed companies. The committee met four times in the period.

##### **The Human Resource and Communication Committee.**

This committee consists of five members all whom are non-executive members of the Board. The committee was chaired by Mrs Judy Thuo. It is responsible for human resource matters including recruitment, management succession as well the corporate communication function. The committee met ten times during the year.

##### **The Technical and Policy Committee.**

The committee consists of six members all whom are non-executive members of the Board. The committee was chaired by Mr Humphrey Muga until the expiry of his term and thereafter by Ms. Nafisa Abass. It is responsible for considering technical and policy matters of the Authority, including reviewing the Authority's strategy and continuous oversight of the review of the capital market legal and regulatory frameworks. The committee met six times during the year.

##### **Ad-Hoc Board Committees.**

During the financial year, two ad-hoc committees of the board were as follows:

'-Capital Markets Master Plan Steering Committee- launched in October 2012 to spearhead the development of a capital markets master plan.

'-Capital Markets Corporate Governance Steering Committee-constituted in December 2012, to review the corporate governance guidelines.

## MARKET PERFORMANCE

The NSE 20 Share Index closed the year at 4,885 points gaining 6 percent from its opening level in July 2013 reflecting the increase in share prices and gains made by investors in our market. Market capitalization also increased by KES 489 billion during the year to close at KES 2.1 trillion, (a 30% increase). In December 2013, the index, became the highest gainer among stock exchanges in Africa, and the fourth globally<sup>[1]</sup> with a 43.58% return. Bulgaria was the best performing market with a 91.55 per cent return, followed by UAE (79.02 per cent), Argentina (68.97 per cent). Pakistan was fifth with a 27.76 per cent return<sup>[2]</sup>. Market activity during the review period was characterised by increased trading and active investor demand as the half year earnings season gathered pace. Equity turnover rose by 47% compared to a similar comparable period the previous year. In addition, there was strong foreign investor activity who accounted, on average, for 50% of total traded equity value.

In the period under review, (1) company – Home Africa Ltd, listed on the Growth Enterprise Market Segment of the Nairobi Securities Exchange. The firm, became the first publicly-traded property developer to be listed on the Nairobi Bourse as well as in the newly introduced segment. In June 2014, the Nairobi Securities Exchange (NSE) received formal approval from the Capital Markets Authority (CMA) to operate as a demutualized entity. On the same day, the CMA approved the application of the NSE to offer its shares to the public through an Initial Public Offer (IPO) and subsequently Self-list its shares on the Main Investment Market Segment (MIMS) of the NSE. Also, the Authority approved a rights issue for Diamond Trust Bank shareholders targeting to raise KES 3.6 billion. Finally, there were 2 corporate bonds issued under the review period namely I&M Bank holdings and Shelter Afrique which managed to raise KES 3.7 bn and KES 5 bn respectively. Both issues were oversubscribed. In the same vein, the Authority, in June 2014, approved the issue of a Ksh5 billion Medium Term Note Programme by British American Investment Company (Britam) to be used to fund strategic business initiatives.

## CAPITAL MARKETS MASTER PLAN

The Capital Markets Master Plan (CMMP) seeks to chart the strategic positioning and future direction of the Kenyan capital market over the next 10 years. It aims to provide market participants with strategic clarity on the vision and objectives of the capital market. It is also intended to ensure that the capital market is well positioned to play its part in supporting national growth needs and aspirations as envisioned under Vision 2030, while meeting relevant challenges such as a growing domestic marketplace, regionalization and increasing globalization of financial services.

**The Vision of the Capital Markets Master Plan; “The heart of African Capital Markets”;** envisions that the Kenyan capital markets will become sufficiently deep and dynamic to stimulate domestic development, while simultaneously providing a gateway to Middle Africa for regional and international capital flows. By 2023, it is expected that Kenya will have been transformed into the choice market for domestic, regional and international issuers and investors looking to invest in and realize their investments in Kenya, within East Africa and across Middle Africa. The market will be the **centre of excellence** for the real sectors of the economy in which Kenya already has significant capacity and potential including: agriculture, infrastructure (including real estate), and technology, while also leveraging the strength of Kenya’s financial sector to develop innovative products and services, including derivatives, asset management and Islamic finance.

Consequently, the Plan sets out the route to realize this aspiration and to ensure these critical success factors are met. The Master Plan is anchored on three key pillars that form the foundation of the transformation, from which nine core building blocks are derived as strategic imperatives of the Plan, with specific initiatives and action steps identified to ensure achievement of the envisaged outcomes:

- i) The first three building blocks focus on the role of capital markets in supporting developmental and economic transformation in the country. This support is grounded in enhancing the knowledge of domestic users of capital markets, leveraging existing strengths and developing new specialist areas of expertise.
- ii) The second three building blocks focus on developing a solid core for the market; through promoting depth and liquidity in the market, creating international standard market infrastructure, and building capacity among market participants.
- iii) The final three building blocks focus on strengthening the regulatory and legal environment that supports the capital markets, including enhancing the capacity of the regulator and on creating an open and competitive environment that enables innovation to flourish in the market.

The Government, in its FY 2014-2015 budget speech, adopted the CMMP as a masterpiece that if well implemented will be a crucial guide in the country's journey to realize the capital markets vision to become "The Heart of African Markets".

## **REVIEW OF THE POLICY FRAMEWORK**

The Authority has continued enhancing its efforts in supporting the government to develop a vibrant and globally competitive financial services sector. Promotion of high-levels of savings and financing for Kenya's investment needs remains high on our agenda. It is noted that the main financial sector flagship project under the Second Medium Plan (MTP II) is the establishment of the Nairobi International Financial Centre. International experience has proved that one of the vital prerequisite for establishing successful financial markets is to have a critical mass of financial institutions operating in a conducive business environment.

Consequently, the Authority in consultation with the industry stakeholders initiated a number of policy and regulatory measures aimed at developing the country's securities markets. Outlined below are key highlights from the CMMP as well as policy and regulatory proposals adopted by the Government.

<b>Proposal</b>	<b>Reference</b>	<b>Expected Impact</b>
1. Provisions that strengthen the Authority's investigation, intervention and licensing powers to ensure investor protection in conjunction with market growth and expansion.	The Capital Markets supervision, (Amendment) Act No. 48 of 2013,	This will boost investors' confidence by ensuring clarity and certainty in interpretation of the Capital Markets Act and the subsidiary legislation made there under. Additionally, attractiveness to a market is a function of confidence which is derived from capacity for oversight, supervision and enforcement to ensure investor protection.

**Capital Markets Authority**  
**Report of the Chief Executive Officer (continued)**  
**For the year ended 30th June 2014**

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Proposal	Reference	Expected Impact
2. Introduction of requisite anchoring provisions that introduces opportunities and products for hedging of risks, infrastructure funding, transparency and efficiency in access to capital.	The Capital Markets (Amendment) Act No. 48 of 2013,	Paves way for securitization to support the increasing budgetary demands to finance Government's developmental agenda through Public Private Partnerships (PPPs) as substitute to Government borrowing. The issuance of securitized products, such as the asset-backed securities, is expected to become even more important in the context of capital raising by County Governments and ease the pressure on sourcing for finances to support devolution. The projects that could use the securitization framework to raise the huge outlay of capital required include the LAPSSET Corridor Project, Ports, Crude Oil Pipelines, Oil Refineries, Resort and Technology Cities, Railways and Road Networks. Once private capital is availed for capital intensive development projects, the Government can channel tax revenues to fund social services. The products proposed under the Act will help meet the 70% private sector funding for Vision 2030 projects.
3. Establishment of futures/derivatives markets in Kenya	The Capital Markets (Amendment) Act No. 48 of 2013.	The amendments relating to futures markets in the Amendment Act provide the necessary provisions in the primary legislation particularly in relation to the powers of the Authority to regulate futures markets in order to ensure their integrity, orderliness and investor protection as well as anchoring provisions for the licensing futures exchanges, futures brokers and business conduct in futures markets. The operational detail will be provided for in subsidiary legislation.
4. Provide a clear guidance on the introduction of new capital markets products and services on an accelerated basis	The Capital Markets (Amendment) Act No. 48 of 2013,	Public offers of securities has been classified into general public offers targeting the wider investing public and restricted public offers tailored for sophisticated investors. The provisions seeks to protect investors from fraudulent persons making offers to the public and creates an offence of criminal liability for defective prospectuses as well as providing the right for investors to seek compensation as a result of subscribing to fraudulent offers.
5. Removal of ambiguity in the provisions relating to prohibition of insider trading and other market abuses.	The Capital Markets (Amendment) Act No. 48 of 2013,	Due to previous challenges in the prosecution of insider trading and market manipulation the relevant sections have been amended to counter the interpretation challenges especially as the market continues to evolve new products such as derivatives, SMEs trading and asset backed securities. This shall guide the courts and the investing public on the nature of these offences as well as the penalties as a result of breach.

**Capital Markets Authority**  
**Report of the Chief Executive Officer (continued)**  
**For the year ended 30th June 2014**

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<b>Proposal</b>	<b>Reference</b>	<b>Expected Impact</b>
6. Implementation of the East Africa Common Market Protocol:	The Capital Markets (Amendment) Act No. 48 of 2013,	To give full effect to the requirements of the East Africa Common Market Protocol and the attainment of free movement of capital and services with the EAC capital markets. The amendments facilitate the harmonization of the capital markets legal and regulatory framework by the EAC capital markets regulators which will effectively provide enterprises access to a larger market to raise more capital for growth and expansion.
7. Introduction of principle based regulation to accelerate introduction of new products and services.	Sec 12 A of The Capital Markets (Amendment) Act No. 48 of 2013	Provides that the Authority may issue such guidelines and notices as the Authority considers necessary for the better carrying out of the functions of the Authority for the regulation of capital markets activities and products subject to the assessment of the extent to which they appropriately cater for efficient, orderly and fair operation of the segment, product or intermediaries; adequate provisions for risk management and controls on market misfeasance; the proper protection of investor interests and appropriate level of disclosure; and a facilitative environment for transparent operations.
8. Operationalize the International Financial Centre	Nairobi Budget Speech 2014	Implementation of recommendations of master plan supporting establishment of an International Financial Center to be expedited.
9. Tabling of the Financial Services Authority Bill and other financial sector regulatory Bills	Budget Speech 2014	Foundations for full consolidation of the Financial services regulators set. Next steps to be determined through engagements with the Parastatal Reforms Implementation Committee.
10. Amendment to Capital Market (Demutualization of the Nairobi Market Securities Regulations) 2012 to set the minimum shareholding for Nairobi Securities Government and ICF at 5 percent.	Reg 4 (2)d Capital (Demutualization of the Nairobi Market Securities Regulations) 2012.	This will significantly address governance challenges and enhance the NSE business model (to traduce commercial and SRO role) through accelerated approval as a Demutualized Exchange and subsequent ceding of stakes by existing shareholders.
11. Enhance Depository and Settlement infrastructure through integration of the Securities Depositories for Government Securities and	CMMP	Greater economies of scale and simplify linkages with other CSDs in the region.

## REVIEW OF THE LEGAL AND REGULATORY FRAMEWORK

In the year 2012-2013 it was reported that a Capital Markets (Amendment) Bill had been submitted to the National Treasury for consideration. The Bill was enacted by the National Assembly and subsequently received Presidential Assent in December 2013. *The Capital Markets (Amendment) Act No. 48 of 2013*, has introduced reforms which include;

### a) Investment climate

The Act includes provisions that strengthen the Authority's supervision, investigation, intervention and licensing powers to ensure investor protection in conjunction with market growth and expansion. This has been done through introduction of requisite anchoring provisions that introduces opportunities and products for hedging of risks, infrastructure funding, transparency and efficiency in access to capital. Overall, the amendments are geared towards ensuring that the global competitiveness of the Kenyan capital markets is considered in line with Vision 2030. The impact is that the Act will boost investors' confidence by ensuring clarity and certainty in interpretation of the Capital Markets Act and the subsidiary legislation made there under. Additionally, attractiveness to a market is a function of confidence which is derived from capacity for oversight, supervision and enforcement to ensure investor protection.

### b) Securitization

With the increasingly budgetary demands to finance Government's developmental agenda, Public Private Partnerships (PPPs) in financing huge infrastructural projects offers an appropriate substitute to Government borrowing. *The issuance of securitized products, such as the asset-backed securities, is expected to become even more important in the context of capital raising by County Governments and ease the pressure on sourcing for finances to support devolution.* The amendments anchor the securitization regulatory framework in the primary legislation. Securitization refers to the process of structuring and converting income-producing assets to support repayments following the issuance of financial instruments that can be readily bought and sold in financial markets and also allows for the conversion of assets that are tied to long term receivables into current revenues available for immediate reinvestment. Additionally, there are critical lessons learnt from the Global Financial Crisis and the anchoring provisions provide the requisite regulatory regime with the necessary legal reinforcements. *The projects that could use the securitization framework to raise the huge outlay of capital required include the LAPSET Corridor Project, Ports, Crude Oil Pipelines, Oil Refineries, Resort and Technology Cities, Railways and Road Networks.* Once private capital is availed for capital intensive development projects, the Government can channel tax revenues to fund social services. *The products proposed under the Bill will help meet the 70% private sector funding for Vision 2030 projects.*

### c) Establishment of futures/derivatives markets in Kenya

Futures and derivatives markets differ substantially with stock markets. In the futures market, more than any other form of investment, price changes are highly leveraged, meaning a small change in a futures price can translate into a huge gain or loss. The amendments relating to futures markets in the Amendment Act provide the necessary provisions in the primary legislation particularly in relation to the powers of the Authority to regulate futures markets in order to ensure their integrity, orderliness and investor protection as well as anchoring provisions for the licensing futures exchanges, futures brokers and business conduct in futures markets. The operational detail will be provided for in subsidiary legislation.

**d) Provide a clear guidance on the introduction of new capital markets products and services on an accelerated**

Public offers of securities has been classified into general public offers targeting the wider investing public and restricted public offers tailored for sophisticated investors. Sophisticated investors are those persons and institutions deemed to appreciate the risks inherent in higher risk profile capital markets products and services. Sophisticated investors include persons licensed to operate in the financial sector; companies and high net worth individuals. Additionally, the provisions seeks to protect investors from fraudulent persons making offers to the public and creates an offence of criminal liability for defective prospectuses as well as providing the right for investors to seek compensation as a result of subscribing to fraudulent offers.

**e) Removal of ambiguity in the provisions relating to prohibition of insider trading and other market abuses**

Due to previous challenges in the prosecution of insider trading and market manipulation the relevant sections have been amended to counter the interpretation challenges especially as the market continues to evolve new products such as derivatives, SMEs trading and asset backed securities. In this regard, the offence of insider trading has been redefined as an offence of strict liability as well as identification of a range of the most common market manipulation offences to guide the courts and the investing public on the nature of these offences as well as the penalties as a result of breach.

**f) Implementation of the East Africa Common Market Protocol**

To give full effect to the requirements of the East Africa Common Market Protocol and the attainment of free movement of capital and services with the EAC capital markets. The amendments facilitate the harmonization of the capital markets legal and regulatory framework by the EAC capital markets regulators which will effectively provide enterprises access to a larger market to raise more capital for growth and expansion.

## **REGIONAL INTEGRATION AND INTERNATIONAL COOPERATION**

### **East Africa**

The Authority continued to participate in the East African Community securities markets integration agenda. In this regard, and in accordance with the EAC Common Markets Protocol, the Authority has been a key participant in the harmonization of the securities legal and regulatory framework in the region. The regulatory framework is being developed in form of Council Directives which are harmonized standards binding on all the Partner States. Council Directives are considered to be the most feasible option given the different levels of development of the regional capital markets. In the course of the year, Seven Council Directives were finalized and considered by the EAC Sectoral Council of Finance and Economic Affairs (SCFEA) and thereafter issued by the EAC Council of Ministers on 28<sup>th</sup> April 2014. Once gazette the seven Council Directives will be transposed into National Laws of each Partner State. The following are the Council Directives that have been issued;

- a) EAC Council Directive on Public Offers for Equity Securities;
- b) EAC Council Directive on Public Offers for Debt Securities;
- c) EAC Council Directive on Public Offers for Asset Backed Securities (ABS);
- d) EAC Council Directive on Collective Investment Schemes (CIS);
- e) EAC Council Directive on Corporate Governance for Securities Market Intermediaries;
- f) EAC Council Directive on Regional Listings in the Securities Market; and
- g) EAC Council Directive on Admission to a Secondary Exchange.

*Capital Markets Authority  
Report of the Chief Executive Officer (continued)  
For the year ended 30th June 2014*

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The East African Securities Regulators Association (EASRA) has also developed a Strategic Plan covering 2014 to 2018 drawing from EASRA's Memorandum of Understanding (MoU), the provisions of the EAC Treaty, the Common Market and East African Community Monetary Union protocols. The objectives of the Strategic Plan include:

- a) Development of the institutional capacity of EASRA which will be achieved by increasing the visibility of EASRA as well as enhancing its operational efficiency;
- b) Enhancement of the harmonization of the capital markets laws and market development Initiatives which will be achieved by new products, infrastructure development, increased regional intermediaries and supervision among others;
- c) Enhancement of public education and financial literacy in the EAC Capital markets;
- d) Building the capacity of EASRA members and market intermediaries by developing capacity building programs;
- e) Building Strategic Alliances to further the regional integration agenda.

Finally, EASRA is continuing with its efforts to harmonize licensing and listing requirements within the EAC securities markets. In this regard, a Risk Based Supervision consultant was engaged to undertake a study on the appropriate supervision model and how the same can be implemented in the different member countries. The recommendation of the consultant on the adoption of Risk based supervision model across the East African countries was adopted and implementation is currently ongoing. The regions is also at advanced stages of harmonizing the Risk Based Capital Adequacy requirements for regional players.

#### **International Organization of Securities Commissions (IOSCO)**

An assessment of the Central Depository and Settlement Corporation (CDSC) and the Central Bank of Kenya's Central Depository System (CDS) was conducted to establish their compliance with the clearing and settlement standards in line with the international practices' Committee on Payment and Settlement Systems (CPSS)-IOSCO principles for financial market infrastructures). IOSCO is the international standard setter for all the securities regulatory Authorities in the world. An independent assessment to establish the country's compliance with IOSCO's 9 new principles during the year was also conducted. The new principle focuses on establishing the robustness of the country's systems to address any emerging systemic risks. The assessment also focused on audit oversight standards and independence.

#### **RISK BASED SUPERVISION**

In August 2013, the Authority organized a three and a half-day workshop for all intermediaries to sensitize them on the changes in licensing requirements and the new financial resources provisions as well as the reporting obligations as automated through the Risk Based Supervision System (RBSS). Subsequently, the new RBSS which seeks to enhance efficiency in the Authority's Approval, licensing and reporting, risk assessment as well as supervision processes was publicly launched on September 26, 2013. The Authority has consequently ensured that all listed companies and intermediaries are registered and using the system which facilitates submission of all statutory returns and applications online, making internal processes more efficient and effective in the delivery of our mandate.

## **MARKET DEVELOPMENT**

During the year, the Authority completed the following research studies to inform the market development process;

- a) Concept Paper on Global Depository Receipts (GDRs) and Global Depository Notes (GDNs) and the possible establishment of a market for these products in Kenya – As one of the initiatives to deepen Kenya's capital markets, CMA initiated a seminal study on these financial instruments and the measures that will have to be put in place to have markets for the instruments established in Kenya.
- b) Linkage of Warehousing Receipt System With Futures Market In Kenya – This study sought to establish the existing state of Warehousing Receipt System in Kenya, review linkage between Warehousing Receipt System and Futures market in some jurisdiction and make research recommendations on the steps that Kenya needs to take to ensure a successful linkage and robust commodities futures markets in Kenya.

The Authority also operationalized research recommendations with regards to the following;

- a) Exchange Traded Funds (ETFs) – CMA, together with other key stakeholders has been holding consultations on using a principle-based approach to establish ETF products in Kenya, pending a comprehensive review of the regulatory framework to usher in fully collateralized ETF products in the Kenyan market. In this regard, a policy and institutional framework have been developed.
- b) Capital Markets Industry Fees and Commissions in Kenya – After a study, the Authority engaged an independent consultant to review the various fees, levies and commissions charged in the market with the aim of informing the policy framework to determine an appropriate fee structure that is consistent with the overall objective of deepening and broadening Kenya's capital markets. The consultant held comprehensive consultations with key stakeholders in the capital markets industry and published its recommended fees and commissions' structure for the Kenyan capital markets. A reviewed fee structure has been submitted to the National Treasury and is awaiting gazettelement.
- c) Islamic Capital Markets - Kenya has ambitions of becoming the Islamic finance hub of East Africa and has the first mover advantage. The Islamic capital market in Kenya albeit currently at a very nascent stage of development, has evolved tremendously, mainly in breadth rather than depth, and exhibits a broad array of Islamic financial services including banking, insurance and investment services. Consequently, the Authority has continued to engage with various stakeholders on the development of this segment. In this regard, the Authority, in partnership with Financial Sector Deepening (FSD) Africa, commissioned the Islamic Finance Council of the United Kingdom to undertake an Islamic Finance Scoping Mission in Kenya in June 2014 to inform on the development of the market segment going forward.

## **FINANCIAL HIGHLIGHTS**

The Authority's financial position will be presented in detail in the audited financial statements for the financial year ended 30 June 2014.

The Authority experienced an increase of 31% in total revenue in the year to Shs 881 million from Shs 672 million last year. The increase is largely attributed to the improved market activities experienced in the year, caused by improved investor confidence, increase in investor education activities and stable macroeconomic environment. Fee income went up by 30% to Shs 766 million this year from Shs 588 million in 2013.

**Capital Markets Authority**  
**Report of the Chief Executive Officer (continued)**  
**For the year ended 30th June 2014**

A surplus of Shs 153.6 million after tax is reported compared to a surplus of Shs 116.1 million realized last year.

The total expenditure incurred is Shs 660.6 million which is higher than the previous year's amount by Shs 141.9 million.

<b>Income &amp; expenditure summary:</b>	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
<b>Income</b>		
Government bonds and capitalization fees	285,486	246,756
NSE transaction fees	452,242	316,169
Others	<u>99,131</u>	<u>84,735</u>
Total operating income	836,859	647,660
Donor funding	<u>44,102</u>	<u>24,659</u>
<b>Total income</b>	<b><u>880,961</u></b>	<b><u>672,319</u></b>
<b>Expenditure</b>		
Salaries and staff costs	294,195	280,934
Rent and maintenance	43,885	27,592
Trainings and conferences	38,160	27,134
Investor education	27,464	18,538
Authority members' allowances	23,614	22,015
Professional and market development	86,333	52,424
Depreciation on property, plant and equipment	32,022	24,037
Others	<u>114,936</u>	<u>66,064</u>
<b>Total expenditure</b>	<b><u>660,609</u></b>	<b><u>518,738</u></b>

**Capital Markets Authority**  
**Report of the Chief Executive Officer (continued)**  
**For the year ended 30th June 2014**

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<b>3. RESULTS</b>	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
The results for the year are summarised below;		
Total income for the year	880,961	672,319
Total operating expenditure for the year	<u>(660,609)</u>	<u>(518,738)</u>
Surplus for the year before tax and transfer	<u>220,352</u>	<u>153,581</u>
Tax expense	<u>(66,690)</u>	<u>(37,450)</u>
Surplus after tax	<u><u>153,662</u></u>	<u><u>116,131</u></u>

### **FUTURE OUTLOOK**

The capital market in Kenya has evolved as a viable and critical component of the financial system, complementing the conventional money markets as a driver for economic growth and development. We must therefore position ourselves to take advantage of the opportunities the market presents. In this regard, while a great deal has been achieved, I believe that the years ahead call for much more work and cooperative effort. We must continue to be proactive in further developing our market. We must strive to look and act beyond our frontier. With Kenya assuming an increasingly prominent role as a regional financial hub, the capital market is poised to play an increasingly important role in supporting national socio-economic goals and aspirations.

In conclusion, I want to thank the Board for their guidance and unfailing support throughout the year. The considerable achievements the capital market has witnessed in recent years is due in no small measure to their outstanding contribution, commitment and selfless service to the ideal of developing a world class capital market in Kenya. My appreciation also goes to the management and staff who have put in tremendous efforts and showed great commitment, enthusiasm and high standards in carrying out their work in fulfillment of the responsibility entrusted to us. I'm confident that with everyone's continued support and teamwork the capital market in Kenya is poised to scale even greater heights in the years ahead.



.....  
**Mr. Paul Muthaura**  
**Ag. Chief Executive**

## **CORPORATE GOVERNANCE STATEMENT**

The Board of the Authority (the Board) is responsible and accountable to the Government of Kenya, through The National Treasury, in ensuring that the Authority complies with the law and the highest standards of corporate governance.

- i) There are eleven members of the Board all of whom, save for the Chief Executive, are non-executive directors.
- ii) The Members possess a broad range of skills and competencies, including legal, finance, banking, economics and management.
- iii) During the period under review, the Board met twelve times.

## **COMPOSITION OF THE BOARD**

**During the period under review, the Board was composed as follows:**

### **1 Mr. Kung'u Gatabaki**

Mr. Gatabaki, the Chairman of the Board is an Economist and holds a Bachelor of Science Degree in Economics from Legon University, Ghana and a Diploma in Project Planning and Management from the Bradford University, UK. He has acquired wide experience in project finance, portfolio management and corporate board business. He started his working career with Firestone Africa (1969) Limited in 1972, briefly moving to Nation Media Group, where he served as Marketing Assistant before joining CDC Group, Plc (formerly Commonwealth Development Corporation) in 1974 where he worked until 2004. He currently serves as the Chairman of Micro-Africa Limited (Micro Kenya/Micro Africa). He is also a Non-executive Director of Development Bank of Kenya, Grain Bulk Handlers Limited, Jacaranda Hotels, Kenya Safari Lodges & Hotels, Uganda Micro Finance, among others. He previously served as a Director of Housing Finance Company of Kenya Limited and Shelter Afrique Limited.

### **2 Dr. Kamau Thugge (Principal Secretary, The National Treasury)**

Dr. Kamau Thugge holds a doctorate in Economics from the Johns Hopkins University. He was appointed an Economic Advisor to the Treasury in December 2005 after serving as an Economic Affairs Director, Treasury since July 29, 2004. Prior to joining Treasury, he worked at the International Monetary Fund from 1985 to 2004.

### **3 Alternate to Principal Secretary, The National Treasury: Dr. Geoffrey Mwau (Economic Secretary at The National Treasury)**

Dr. Mwau graduated from McGill University in Canada with a PhD in Economics in 1994. He worked as a Senior Advisor to the Executive Director representing Kenya and 21 other African countries at the Executive Board of World Bank. Prior to joining the World Bank, he was a Senior Regional Advisor on Economic Policy Analysis with the United Nations Economic Commission for Africa. Previously, Dr. Mwau also worked for the International Monetary Fund (IMF) as an economist for Rwanda, Malawi, Botswana, and Uganda.

### **4 Hon. Prof Githu Muigai**

Professor Muigai is the Attorney General of the Republic of Kenya. He holds a Bachelor's Degree in Law and was called to the bar in 1985. He also holds a Master's Degree in International Law from Columbia University School of Law, New York and a PhD in Constitutional Law from the University of Nairobi.

**4 Hon. Prof Githu Muigai (continued)**

He is a Fellow of the Chartered Institute of Arbitrators (UK) and a member of the American Association of Trial Lawyers. In addition to Law practice, he is an Associate Professor of Public Law in the School of Law of the University of Nairobi. He specialises in Public Law, Human Rights and trans-national legal practice.

**5 Alternate to Hon. Attorney General: Ms. Jane Joram**

Ms. Jane Joram is an Advocate of the High Court of Kenya, holder of a Bachelors of Laws Degree from the University of Nairobi and currently undertaking a Master's Degree in International Studies at the University of Nairobi.

She is a Senior Deputy Registrar in the Department of the Registrar General, Attorney General's Chambers. She is the head of the Companies Registry and spearheaded major reforms that have taken place in the Registry, including modernization of the Registry and computerization.

**6 Prof. Njuguna S. Ndung'u (Governor, Central Bank of Kenya)**

An Economist by profession, Prof. Ndung'u holds a PhD in Economics from the University of Gothenburg, Sweden, and Masters and Bachelor's degrees in Economics from the University of Nairobi. He's an Associate Professor of Economics at the University of Nairobi, and has worked in various capacities with the International Development Research Centre (IDRC) Canada, and the Kenya Institute of Public Policy Research and Analysis (KIPPRA), among other Institutions.

**7 Alternate to Governor, Central Bank of Kenya: Ms. Rose Detho**

Ms. Detho holds Master of Business Administration and Bachelor of Commerce degrees from the University of Nairobi. She is the Director of the Deposit Protection Fund Board. Ms Detho joined Central Bank of Kenya on August 10, 1988 and has served the bank in various capacities. She has served on several occasions as Statutory Manager, appointed by the Bank, to manage financially distressed institutions.

**8 Mr. Mahmood Manji**

Mr. Manji is a Non-Executive Director of TPS Eastern Africa (Serena) Limited. He is also a fellow of the Institute of Chartered Accountants in England and Wales and the Kenya Institute of Bankers. He is the Chairman of Air Uganda Limited and the Property Development and Management Group of Companies amongst others. Mr. Manji is a member of the International Who's Who of professionals and previously served as the Chairman of Diamond Trust Bank (East Africa).

**9 Mr. Humphrey Muga**

Mr. Muga holds a Masters of Arts in Economics degree from the McGill University, Canada and has previously worked in various capacities at the Central Bank of Kenya.

**10 Ms. Nafisa Abass**

Ms. Abass holds a Bachelor of Business Administration degree from the American University in Cairo, and an MBA from the United States International University Nairobi. She has diverse experience in the business sector where she holds directorship roles, and has some non-executive responsibilities in non-profit organizations.

**11 Mrs. Judy Thuo**

Mrs. Judy Thuo holds a Bachelor of Arts Communications (major) Community Development (minor) from Daystar University College (Messiah University). She is currently a director in City Hopper Limited and Kwani Trust. She has extensive experience in Transport Sector, IT and Telecommunications, Leading Advertising Agency, Integrated Communications Agency among other sectors.

**12 Mrs. Anne Schofield**

Mrs. Anne Schofield holds a Bachelor degree in Law (LLB Hons Degree) from the University of Nairobi. She has extensive legal professional experience in Kenya, the Caribbean, the Mediterranean and the United Kingdom particularly in the Banking and Trust sector in the Cayman Islands.

**13 Mr. Paul Ngugi**

Mr. Paul Ngugi holds a Masters of Social Science (M.Soc.SC) in Development Administration from the University of Birmingham (UK), a Bachelor of Arts from the University of Nairobi and a Diploma of Professional Development in Management with Specialization in Budgeting and Financial Management from the University of Connecticut (USA). He has served as Alternate Director to Permanent Secretary, Ministry of Finance and also in various boards of state corporations including Kenya Roads Board, Housing Finance, Kenya Meat Commission, National Oil Corporation,

**14 Mr. Paul M Muthaura (Acting Chief Executive)**

Mr. Muthaura is the Acting Chief Executive, Capital Markets Authority. In his time with the Authority he has held positions as the Director, Regulatory Policy and Strategy; Head of Legal Framework and Head of Enforcement.

Mr. Muthaura is a member of the Board of the International Organization of Securities Commissions (IOSCO), the Steering Committee of the Growth and Emerging Markets Committee of IOSCO, the Financial Stability Board (FSB) Regional Consultative Group for Sub-Saharan Africa and the Consultative Committee of the East African Securities Regulatory Authorities (EASRA). Mr. Muthaura is also an ex officio member of the Boards of Directors of the Retirement Benefits Authority, the Insurance Regulatory Authority and the Vision 2030 Delivery Secretariat.

He has previously worked as an Emerging Markets Advisor with the General Secretariat of the International Organization of Securities Commissions (IOSCO). Before moving into the regulatory industry Mr. Muthaura was a senior commercial associate with the law firm of Daly and Figgis Advocates.

Mr. Muthaura is an Advocate of the High Court of Kenya and is the holder of a Bachelor of Laws degree from the University of Warwick, a Masters in Banking and Finance Law from the London School of Economics and Political Science, a Masters in Philosophy from the Maastricht School of Management and is currently undertaking a Doctorate in Business Administration at the Maastricht School of Management.

**CORPORATE SOCIAL RESPONSIBILITY STATEMENT**

The Authority participated in three Corporate Social Responsibility activities that included a tree planting activity in collaboration with financial sector regulators at Ngong Forest's Kuwinda Grounds; donation of books to five secondary schools in Mombasa together with the financial sector regulators; and donation of books to Wema Centre in Mombasa in collaboration with the Central Depository and Settlement Corporation and the Nairobi Securities Exchange.

The Authority will continue to endeavour to improve the welfare of the less fortunate in the society, as well as corporate communications functions within the Authority with a strategic focus to enhancing media relations.

*Capital Markets Authority  
Report of the board members of the Authority  
For the year ended 30th June 2014*

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The board members of the Authority submit their report together with the audited financial statements for the year ended 30th June 2014, which show the state of the affairs of the Authority.

**Principal activities**

The Authority promotes and facilitates the development of an orderly, fair and efficient capital market in Kenya.

**Results**

The results of the Authority for the year ended 30th June 2014 are set out on page 24.

**Board members of the Authority**

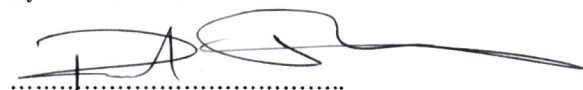
The board members of the Authority who held office during the year and to the date of this report are set out on page 1.

**Auditor**

The Auditor-General is responsible for the statutory audit of the Authority in accordance with Article 229 of the Constitution of Kenya. Section 39 (1) of the Public Audit Act 2012 , empowers the Auditor General to nominate other auditors to carry out the audit on his behalf.

RSM Ashvir Certified Public Accountants were nominated by the Auditor General to carry out the audit of the Authority for the year ended 30th June 2014.

**By order of the board**



.....  
Ag. Chief Executive

Nairobi ..... 25<sup>th</sup> Sept. .... 2014

*Capital Markets Authority  
Statement of board members of the Authority's' responsibilities  
For the year ended 30th June 2014*

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Section 68 of the Public Finance Management Act, No. 18 of 2012, requires the board members to prepare financial statements in respect of the Authority, which give a true and fair view of the state of affairs of the Authority at the end of the financial year and the operating results of the Authority for that year. The board members are also required to ensure that the Authority keeps proper accounting records which disclose with reasonable accuracy the financial position of the Authority. The board members are also responsible for safeguarding the assets of the Authority.

The board members are responsible for the preparation and presentation of the Authority's financial statements, which give a true and fair view of the state of affairs of the Authority for and as at the end of the financial year ended on 30th June 2014. This responsibility includes: (i) maintaining adequate financial management arrangements and ensuring that these continue to be effective throughout the reporting period; (ii) maintaining proper accounting records, which disclose with reasonable accuracy at any time the financial position of the entity; (iii) designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of the financial statements, and ensuring that they are free from material misstatements, whether due to error or fraud; (iv) safeguarding the assets of the authority; (v) selecting and applying appropriate accounting policies; and (vi) making accounting estimates that are reasonable in the circumstances.

The board members accept responsibility for the Authority's financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with International Public Sector Accounting Standards (IPSAS), and in the manner required by the PFM Act and the State Corporations Act. The board members are of the opinion that the Authority's financial statements give a true and fair view of the state of Authority transactions during the financial year ended 30th June 2014, and of the Authority's financial position as at that date. The board members further confirm the completeness of the accounting records maintained for the Authority, which have been relied upon in the preparation of the Authority's financial statements as well as the adequacy of the systems of internal financial control.

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

**Approval of the financial statements**

The Authority's financial statements were approved by the board on 25<sup>th</sup> Sept.....2014 and signed on its behalf by:



.....  
**Chairman**



.....  
**Ag. Chief Executive**

## **REPORT OF THE INDEPENDENT AUDITORS ON CAPITAL MARKETS AUTHORITY**

We have audited the accompanying financial statements of Capital Markets Authority for the year ended 30th June 2014, which comprise: (i) a statement of financial performance; (ii) a statement of financial position; (iii) a statement of changes in net assets; (iv) a statement of cash flows; (v) a statement of comparison of budget and actual amounts and (v) a summary of significant accounting policies and other explanatory information.

### **Management's responsibility for the financial statements**

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

### **Auditors' responsibility**

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with the International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Authority as at 30th June 2014, and its financial performance and cash flows for the year then ended in accordance with International Public Sector Accounting Standards.

.....  
**Auditor General**  
**Nairobi**

.....  
**Date**

# REPUBLIC OF KENYA

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P.O. Box 30084-00100  
NAIROBI

## KENYA NATIONAL AUDIT OFFICE

### **REPORT OF THE AUDITOR-GENERAL ON CAPITAL MARKETS AUTHORITY FOR THE YEAR ENDED 30 JUNE 2014**

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#### REPORT ON THE FINANCIAL STATEMENTS

The accompanying financial statements of Capital Markets Authority set out on pages 25 to 50 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 comparison of budget and actual amounts, and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information have been audited on my behalf by RSM Ashvir, 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 all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit were obtained.

#### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Public Sector Accounting Standards (Accruals Basis) 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 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**

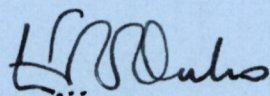
My responsibility is to express an opinion on the financial statements based on the audit and report in accordance with the provisions of Section 15(2) of the Public Audit Act, 2003 and submit the audit report in compliance with Article 229(7) of the Constitution of Kenya. The audit was conducted in 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 Authority'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 Authority 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 (Accruals Basis) and comply with the Capital Markets Authority Act, Cap 485A of the Laws of Kenya.



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

**Nairobi**

**19 December 2014**

*Capital Markets Authority*  
*Financial statements*  
*For the year ended 30th June 2014*

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

	Note	2014 Shs'000	2013 Shs'000
<b>Revenue from non-exchange transactions</b>			
Capitalization, rights and new issue fees	5	<u>809,848</u>	<u>612,667</u>
		<u>809,848</u>	<u>612,667</u>
<b>Revenue from exchange transactions</b>			
Other income	6	<u>70,955</u>	<u>58,633</u>
<b>Total revenue</b>		<u>880,803</u>	<u>671,300</u>
<b>Expenses</b>			
Operating expenditure	30	<u>(660,609)</u>	<u>(518,738)</u>
<b>Total expenses</b>		<u>(660,609)</u>	<u>(518,738)</u>
<b>Other gains/ (losses)</b>			
Gain on disposal of property, plant and equipment	8	<u>158</u>	<u>1,019</u>
<b>Surplus before tax</b>	9	220,352	153,581
Tax expense	10	<u>(66,690)</u>	<u>(37,450)</u>
<b>Surplus for the year</b>		<u><u>153,662</u></u>	<u><u>116,131</u></u>

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**STATEMENT OF FINANCIAL POSITION AS AT 30TH JUNE 2014**

<b>ASSETS</b>	<b>Note</b>	<b>2014 Shs'000</b>	<b>2013 Shs'000</b>
<b>Current assets</b>			
Inventories	11	1,573	1,133
Trade and other receivables from non exchange transactions	12(a)	75,853	69,445
Trade and other receivables from exchange transactions	12(b)	15,631	17,573
Staff loans and advances/guarantee fund	13	26,132	20,382
Held-to-maturity investments	14	295,386	266,168
Staff benevolent fund	15	7,882	7,231
Cash at bank and in hand	16	125,193	94,085
Investors' Compensation Fund	17	<u>518,140</u>	<u>281,049</u>
		<u>1,065,790</u>	<u>757,066</u>
<b>Non-current assets</b>			
Property, plant and equipment	18	101,341	117,573
Intangible assets	19	85,788	126,828
Staff loans and advances/guarantee fund	13	200,408	146,624
Held-to-maturity investments	14	245,045	245,096
Investors' Compensation Fund's investments	17	358,532	446,705
Deferred tax asset	20	<u>28,619</u>	<u>17,154</u>
		<u>1,019,733</u>	<u>1,099,980</u>
<b>Total Assets</b>		<u><u>2,085,523</u></u>	<u><u>1,857,046</u></u>
<b>Liabilities</b>			
<b>Current liabilities</b>			
Staff benevolent fund	15	7,882	7,231
Trade and other payables	21	138,778	118,615
Provision for liabilities and charges	22	46,483	43,555
Current tax payable	23	25,325	47,821
Deferred income	24	83,513	126,862
Investors' Compensation Fund	17	<u>518,140</u>	<u>281,049</u>
		<u>820,121</u>	<u>625,133</u>
<b>Non-current liabilities</b>			
Investors' Compensation Fund liabilities	17	<u>358,532</u>	<u>446,705</u>
<b>Total liabilities</b>		<u><u>1,178,653</u></u>	<u><u>1,071,838</u></u>
<b>Net assets</b>			
Capital fund	25	906,870	785,208
General fund	26	<u>27,886</u>	<u>27,886</u>
		<u>878,984</u>	<u>757,322</u>
<b>Total net assets and liabilities</b>		<u><u>2,085,523</u></u>	<u><u>1,857,046</u></u>

The financial statements set out on pages 25 to 50 were approved for issue by the board members of the Authority on .....2014 and were signed on its behalf by:

  
**Ag. Chief Executive**

  
**Chairman of the board**

Date: 25-09-2014

Date: 25th Sept. 2014

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**STATEMENT OF CHANGES IN NET ASSETS FOR THE YEAR ENDED 30TH JUNE 2014**

	Note	Capital fund Shs'000	General fund Shs'000	Total Shs'000
<b>At 1st July 2012</b>		27,886	641,191	669,077
Surplus for the year		-	116,131	116,131
<b>At 30th June 2013</b>		<u>27,886</u>	<u>757,322</u>	<u>785,208</u>
<b>At 1st July 2013</b>		27,886	757,322	785,208
Surplus for the year		-	153,662	153,662
Dividend paid to National Treasury		-	(32,000)	(32,000)
<b>At 30th June 2014</b>		<u>27,886</u>	<u>878,984</u>	<u>906,870</u>

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**STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 30TH JUNE 2014**

	Note	2014 Shs'000	2013 Shs'000
<b>Cash flows from operating activities</b>			
<b>Surplus/(deficit) for the year</b>		153,662	116,131
<b>Adjustments for:</b>			
Tax expense	10	66,690	37,450
Depreciation of property, plant and equipment	18	32,022	24,037
Amortisation of intangible assets	19	49,411	12,245
Deferred donor funded income		(43,349)	119,000
Gain on disposal of property, plant and equipment	7	(158)	(1,019)
Interest income	6	(62,645)	(57,939)
<b>Operating profit before working capital changes</b>		<u>195,633</u>	<u>249,905</u>
Decrease/(increase) in:			
Inventories	11	(440)	866
Trade and other receivables	12	(4,466)	(45,574)
Staff loans and advances	13	(59,534)	(86,926)
Increase/(decrease) in:			
Trade and other payables	21	20,163	(12,948)
Provision for liabilities and charges	22	2,928	1,855
Investors' Compensation Fund	17	148,918	305,435
Staff benevolent fund	15	651	1,138
<b>Cash generated from operations</b>		<u>303,854</u>	<u>413,751</u>
Interest received	6	62,645	57,939
Income tax paid		<u>(100,650)</u>	<u>(9,862)</u>
<b>Net cash generated from operating activities</b>		<u>265,849</u>	<u>461,828</u>
<b>Cash flows from investing activities</b>			
Purchase of property, plant and equipment	19	(16,059)	(53,018)
Purchase of intangible assets	20	(8,371)	(113,698)
Proceeds from disposal of property, plant and equipment		427	3,275
Purchase of treasury bonds from the Investors' Compensation Fund		(117,000)	(256,500)
(Purchase)/sale of treasury bills from the Investors' Compensation Fund		(11,145)	(115,487)
(Purchase)/sale of treasury bonds		35,000	70,000
(Purchase)/sale of treasury bills		(64,168)	(113,744)
Purchase of treasury bills from the Benevolent fund		(75)	(654)
Surplus payment to National Treasury	26	<u>(32,000)</u>	<u>-</u>
<b>Net cash (used in) from investing activities</b>		<u>(213,391)</u>	<u>(579,826)</u>
<b>Net increase/(decrease) in cash and cash equivalents</b>		52,458	(117,998)
<b>Cash and cash equivalents at start of the year</b>		<u>151,538</u>	<u>269,536</u>
<b>Cash and cash equivalents at end of the year</b>	16	<u><u>203,996</u></u>	<u><u>151,538</u></u>

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

	<b>Original budget 2013-2014 Shs'000</b>	<b>Adjustments 2013-2014 Shs'000</b>	<b>Final budget 2013-2014 Shs'000</b>	<b>Actual on comparable basis 2013-2014 Shs'000</b>	<b>Performance difference 2013-2014 Shs'000</b>
<b>Revenue</b>					
Fee income from NSE	264,361	68,054	332,415	452,242	119,827 a)
Licenses and permits	14,195	(79)	14,116	16,645	2,529 b)
Market development Fees	11,045	404	11,449	11,373	(76) c)
Capitalisation and bond approvals	237,750	110,828	348,578	285,487	(63,091) d)
Donor Funding- gifts and services-in-kind	30,000	17,587	47,587	44,101	(3,486) e)
Finance income - external investments	28,980	29,647	58,627	62,644	4,017 f)
Gains on disposal, rental income and agency fees	1,000	-	1,000	1,000	-
Other income	-	7,000	7,000	7,469	469
<b>Total income</b>	<b>587,331</b>	<b>233,441</b>	<b>820,772</b>	<b>880,961</b>	<b>60,189</b>
<b>Expenses</b>					
Personnel cost	298,262	11,930	310,192	294,194	15,998 g)
Rent and maintenance	29,400	14,198	43,598	43,885	(287) h)
Equipment maintenance and stationery	14,864	-	14,864	13,383	1,481 i)
Telephone, postage and utilities	15,335	4,227	19,562	14,780	4,782 j)
Entertainment and public relations	10,561	5,000	15,561	11,060	4,501 k)
Medical scheme and insurance expenses	16,477	1,618	18,095	17,548	547 l)
Training and conferences	25,771	14,229	40,000	38,158	1,842 m)
Motor vehicle running expenses	9,000	475	9,475	6,612	2,863 n)
Subscriptions and IOSCO membership	4,380	-	4,380	4,211	169
Authority board members' emoluments and allowances	35,030	2,075	37,105	23,614	13,491 o)
Professional and market development services	103,541	4,550	108,091	82,800	25,291 p)
Depreciation of property, plant and equipment	27,907	6,101	34,008	32,022	1,986 q)
Amortisation of intangible assets	43,057	9,418	52,475	49,411	3,064 r)
Auditor's remuneration	539	-	539	539	-
Investors' education and awareness programme	71,550	(23,050)	48,500	27,464	21,036 s)
Tribunal expenses	5,502	(1,522)	3,980	720	3,260 t)
Increase in provision for doubtful debts	-	-	-	208	(208) u)
<b>Total expenditure</b>	<b>711,176</b>	<b>49,249</b>	<b>760,425</b>	<b>660,609</b>	<b>99,816</b>
<b>Surplus for the period</b>	<b>(123,845)</b>	<b>184,192</b>	<b>60,347</b>	<b>220,352</b>	<b>160,005</b>

Notes on the significant variances

- a) The vibrant market activities in the year resulted in the positive performance.  
b) Licences of new market products like REITS resulting in a higher income.  
c) This revenue source was within the budgeted level.

**STATEMENT OF COMPARISON OF BUDGET AND ACTUAL AMOUNTS (CONTINUED)**

- d) The performance on this fee is below the budgeted level in the year, attributed to low uptakes of capital raising vehicles by the market. The "appetite" was lower than budgeted level.
- e) The budget level was not achieved due to minimal donor funding in the year.
- f) The income level was slightly above budget as the Authority continued investing excess cash in the government securities.
- g) The Authority's staff complement was not filled due to the ongoing financial sector regulators merger process.
- h) To a minimal level, this cost is above budget due to increased service charges in the year.
- i) Cost control strategies improvised by management contributed to the low costs.
- j) Cost control strategies improvised by management contributed to the low costs.
- k) Activities were completed in line with anticipated targets, as others stretched to the following financial year.
- l) The medical costs were well within the budget allocation.
- m) Some of the programmes were scheduled for the first month of the new financial year.
- n) Cost control strategies improvised (e.g. use of fuel cards, negotiated transport rates) by management contributed to the low costs.
- o) The Authority undertook its activities as per annual time table, but with controlled costs. Coupled with reduced number of board members, the cost was kept to a minimum.
- p) Activities were completed in line with anticipated targets, as others stretched to the following financial year.
- q) The depreciation charge was within the budget level, but actual lower due to the low capital expenditure due to the ongoing merger process.
- r) The amortisation charge was within the budget level, but actual lower due to the low capital expenditure due to the ongoing merger process.
- s) Activities were completed in line with anticipated targets, as others stretched to the following financial year.
- t) Minimal meetings were undertaken as the Tribunal was not fully constituted for the best part of the year.
- u) Two licensees showed unwillingness to continue trading, and the Authority withdrew their licenses as per the law. The had not paid renewal fees for past years, resulting in the bad debts being written off.

**NOTES**

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

The Authority's financial statements have been prepared in accordance with and comply with International Public Sector Accounting Standards (IPSAS). In absence of an IPSAS that specifically applies to a transaction, other event or condition, the IFRS has been applied in selecting the accounting policy for that specific transaction, event or circumstance. The financial statements are presented in Kenya Shillings, which is the functional and reporting currency of the authority and all values are rounded to the nearest thousand (Shs '000'). The accounting policies have been consistently applied to all the years presented.

The financial statements have been prepared on the basis of historical cost, unless stated otherwise. The cash flow statement is prepared using the direct method. The financial statements are prepared on accrual basis.

**2. Summary of significant accounting policies**

**a) Revenue recognition**

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

**Fees**

The Authority recognizes revenues from fees when the event occurs and the asset recognition criteria are met. To the extent that there is a related condition attached that would give rise to a liability to repay the amount, deferred income is recognized instead of revenue. 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 Authority and the fair value of the asset can be measured reliably.

**Government grants**

Government grants are recognised at fair value when there is reasonable assurance that the Authority will comply with the conditions attaching to them and the grants will be received. Grants related to purchase of assets are treated as deferred income and allocated to statement of financial performance income over the useful lives of the related assets while grants related to expenses are treated as donor fund income in the income statement.

**ii) Revenue from exchange transactions**

The Authority recognizes revenue from rendering of services by reference to the stage of completion when the outcome of the transaction can be estimated reliably.

Where the contract outcome cannot be measured reliably, revenue is recognized only to the extent that the expenses incurred are recoverable.

**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.

**b) Budget information**

The annual budget is prepared on the accrual basis, that is, all planned costs and income are presented in a single statement to determine the needs of the entity. As a result of the adoption of the accrual basis for budgeting purposes, there are no basis, timing or entity differences 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.

**NOTES (CONTINUED)**

**c) Taxes**

**Current income tax**

Current income tax assets and liabilities for the current year are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date in the area where the Authority operates and generates taxable income.

Current income tax relating to items recognized directly in net assets is recognized in net assets and not in the statement of financial performance. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

**Deferred tax**

Deferred tax is provided using the liability method on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date.

Deferred tax liabilities are recognized for all taxable temporary differences, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences, the carry forward of unused tax credits and any unused tax losses. Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilized.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are re-assessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax relating to items recognized outside surplus or deficit is recognized outside surplus or deficit.

Deferred tax items are recognized in correlation to the underlying transaction in net assets.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

**d) Property, plant and equipment**

All property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the items. When significant parts of property, plant and equipment are required to be replaced at intervals, the entity recognizes such parts as individual assets with specific useful lives and depreciates them accordingly. Where an asset is acquired in a non-exchange transaction for nil or nominal consideration the asset is initially measured at its fair value.

NOTES (CONTINUED)

**d) Property, plant and equipment (continued)**

Depreciation is calculated using the straight line method to write down the cost of each asset to its residual value over its estimated useful life using the following annual rates:

	<u>Rate</u>
Motor vehicles	25%
Furniture & fittings	12.5%
Office equipment	20%
Computers, copiers & faxes	25%

Gains and losses on disposal of property, plant and equipment are determined by reference to their carrying amount and are taken into account in determining surplus for the year.

**e) Leases**

**Operating leases**

Operating leases are leases that do not transfer substantially all the risks and benefits incidental to ownership of the leased item to the Authority. Operating lease payments are recognized as an operating expense in surplus or deficit on a straight-line basis over the lease term.

**f) Intangible assets**

Intangible assets acquired separately are initially recognized at cost. The cost of intangible assets acquired in a non-exchange transaction is their fair value at the date of the exchange. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditure is reflected in surplus or deficit in the period in which the expenditure is incurred. Amortisation is calculated using the straight line method to write down the cost of each licence or item of software to its residual value over its estimated useful life of three years.

The useful life of the intangible assets is assessed as finite.

**g) Financial instruments**

**Financial assets**

**Initial recognition and measurement**

Financial assets within the scope of IPSAS 29 Financial Instruments: Recognition and Measurement are classified as financial assets at fair value through surplus or deficit, loans and receivables, held-to-maturity investments or available-for-sale financial assets, as appropriate. The Authority determines the classification of its financial assets at initial recognition.

**Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such financial assets are subsequently measured at amortized cost using the effective interest method, less impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. Losses arising from impairment are recognized in the surplus or deficit.

NOTES (CONTINUED)

**g) Financial instruments (continued)**

**Held-to-maturity**

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held to maturity when the Authority has the positive intention and ability to hold it to maturity. After initial measurement, held-to-maturity investments are measured at amortized cost using the effective interest method, less impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. The losses arising from impairment are recognized in surplus or deficit.

**Impairment of financial assets**

The Authority assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include the following indicators:

- i)** The debtors or a group of debtors are experiencing significant financial difficulty.
- ii)** Default or delinquency in interest or principal payments.
- iii)** The probability that debtors will enter bankruptcy or other financial reorganization.

Observable data indicates a measurable decrease in estimated future cash flows (e.g. changes in arrears or economic conditions that correlate with defaults)

**Financial liabilities**

**Initial recognition and measurement**

Financial liabilities within the scope of IPSAS 29 are classified as financial liabilities at fair value through surplus or deficit or loans and borrowings, as appropriate. The Authority determines the classification of its financial liabilities at initial recognition.

All financial liabilities are recognized initially at fair value and, in the case of loans and borrowings, plus directly attributable transaction costs.

**h) Provisions**

Provisions are recognized when the Authority 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.

Where the Authority expects some or all of a provision to be reimbursed, for example, under an insurance contract, the reimbursement is recognized as a separate asset only when the reimbursement is virtually certain.

The expense relating to any provision is presented in the statement of financial performance net of any reimbursement.

**Contingent liabilities**

The Authority does not recognize a contingent liability, but discloses details of any contingencies in the notes to the financial statements, unless the possibility of an outflow of resources embodying economic benefits or service potential is remote.

**NOTES (CONTINUED)**

**i) Employee benefits**

**Retirement benefit plans**

The Authority provides retirement benefits for its employees. Defined contribution plans are post employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund), and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. The contributions to fund obligations for the payment of retirement benefits are charged against income in the year in which they become payable.

The Authority and its employees also contribute to the National Social Security Fund (NSSF), a national defined contribution scheme. Contributions are determined by local statute and the Authority's contributions are charged to the statement of comprehensive income in the year to which they relate.

**j) Gratuity obligations**

The Authority pays service gratuity to staff on contract under their terms of employment. Employee entitlements to gratuity are recognized when they accrue to employees. A provision for gratuity payable is made in the statement of financial position. The gratuity is not subject to actuarial valuation.

**k) Foreign currency transactions**

Transactions in foreign currencies are initially accounted for at the ruling rate of exchange on the date of the transaction. Trade creditors or debtors denominated in foreign currency are reported at the statement of financial position reporting date by applying the exchange rate on that date. Exchange differences arising from the settlement of creditors, or from the reporting of creditors at rates different from those at which they were initially recorded during the period, are recognized as income or expenses in the period in which they arise.

**l) Cash and cash equivalents**

Cash and cash equivalents comprise cash on hand and cash at bank, short-term deposits on call and highly liquid investments with an original maturity of three months or less, which are readily convertible to known amounts of cash and are subject to insignificant risk of changes in value. Bank account balances include amounts held at the Central Bank of Kenya and at various commercial banks at the end of the financial year.

**m) Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first-in first-out (FIFO) method. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

**n) Related party**

The Authority 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 Authority, or vice versa. Members of key management are regarded as related parties.

**o) Comparative figures**

Where necessary comparative figures for the previous financial year have been amended or reconfigured to conform to the required changes in presentation.

NOTES (CONTINUED)

**3. Significant judgments and sources of estimation uncertainty**

The preparation of the Authority's financial statements in conformity with IPSAS requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

**a) Significant judgements made in applying the Authority's accounting policies**

The judgements made by the board members of the Authority in the process of applying the Authority's accounting policies that have the most significant effect on the amounts recognised in the financial statements include:

- i) Whether the Authority has the ability to hold 'held-to maturity' investments until they mature. If the Authority were to sell other than an insignificant amount of such investments before maturity, it would be required to classify the entire class as 'available-for-sale' and measure them at fair value.

**b) Key sources of estimation uncertainty**

Key assumptions made about the future and other sources of estimation uncertainty that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year include:

**i) Retirement benefit obligations**

Assumptions made by the actuary in determining the present value of retirement benefit obligations. The carrying amount of the provision and the key assumptions made in estimating the provision are set out in Note 9.

**ii) Impairment losses**

Estimates made in determining the impairment losses on receivables. Such estimates include the determination of the net realisable value or the recoverable amount of the asset. The movement on the impairment provision is set out in Note 12.

**4. Risk management objectives and policies**

**a) Financial risk management**

The Authority's activities expose it to a variety of financial risks including credit, liquidity and market risks. The Authority's overall risk management policies are set out by the board and implemented by the management, and focus on the unpredictability of changes in the business environment and seek to minimise the potential adverse effects of such risks on the Authority's performance by setting acceptable levels of risk. The Authority does not hedge against any risks.

**i) Credit risk**

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Credit risk mainly arises from financial assets, and is managed on a Authority-wide basis. The Authority does not grade the credit quality of financial assets that are neither past due nor impaired.

NOTES (CONTINUED)

4. Risk management objectives and policies (continued)

i) Credit risk (continued)

Credit risk on financial assets with banking institutions is managed by dealing with institutions with good credit ratings and placing limits on deposits that can be held with each institution.

Credit risk on trade receivables is managed by ensuring that credit is extended to customers with an established credit history. The credit history is determined by taking into account the financial position, past experience and other relevant factors. Credit is managed by setting the credit limit and the credit period for each customer. The utilisation of the credit limits and the credit period is monitored by management on a monthly basis.

The maximum exposure of the Authority to credit risk as at the balance sheet date is as follows:

	<b>Fully performing</b>	<b>Past due but not impaired</b>	<b>Past due and impaired</b>	<b>Total</b>
	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>
<b>30th June 2014</b>				
Held-to-maturity investments	540,431	-	-	540,431
Staff loans and advances/ fund	222,361	2,257	-	224,618
Trade receivables	58,572	-	-	58,572
Other receivables	32,912	-	-	32,912
Cash at bank	125,193	-	-	125,193
	<u>979,469</u>	<u>2,257</u>	<u>-</u>	<u>981,726</u>
Gross financial assets				
	<u>979,469</u>	<u>2,257</u>	<u>-</u>	<u>981,726</u>
	<b>Fully performing</b>	<b>Past due but not impaired</b>	<b>Past due and impaired</b>	<b>Total</b>
	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>
<b>30th June 2013</b>				
Held-to-maturity investments	511,264	-	-	511,264
Staff loans and advances/ fund	164,749	2,257	-	167,006
Trade receivables	39,580	5,635	-	45,215
Other receivables	33,762	8,041	-	41,803
Cash at bank	94,085	-	-	94,085
	<u>843,440</u>	<u>15,933</u>	<u>-</u>	<u>859,373</u>
Gross financial assets				
	<u>843,440</u>	<u>15,933</u>	<u>-</u>	<u>859,373</u>

NOTES (CONTINUED)

4. Risk management objectives and policies (continued)

a) Financial risk management (continued)

i) Credit risk (continued)

The ageing analysis of past due but not impaired trade receivables is

	2014 Shs'000	2013 Shs'000
Over 6 months	2,257	15,933
	<u>2,257</u>	<u>15,933</u>

The past due debtors are not impaired and continue to be paid. An impairment provision of Shs 59,954, 000 (2013: Shs 60,412,000) is held against the impaired receivables. The Authority does not hold any collateral against the past due or impaired receivables. The management continues to actively follow up past due and impaired receivables.

ii) Liquidity risk

Liquidity risk is the risk that the Authority will encounter difficulty in meeting obligations associated with financial liabilities. The board has developed a risk management framework for the management of the Authority's short, medium and long-term liquidity requirements thereby ensuring that all financial liabilities are settled as they fall due. The Authority manages liquidity risk by continuously reviewing forecasts and actual cash flows, and maintaining banking facilities to cover any shortfalls.

The table below summarises the maturity analysis for financial liabilities to their remaining contractual maturities. The amounts disclosed are the contractual undiscounted cash flows.

	Less than one month Shs'000	Between 1-3 months Shs'000	Between 3-12 months Shs'000	Over 1 year Shs'000	Total Shs'000
<b>Year ended 30th June 2014</b>					
Trade and other payables	19,692	1,326	792	584	22,394
Accruals	51,619	2,252	10,122	52,391	116,384
Provision for liabilities and charges	2,928	-	-	43,555	46,483
	<u>74,239</u>	<u>3,578</u>	<u>10,914</u>	<u>96,530</u>	<u>185,261</u>
<b>Year ended 30th June 2013</b>					
Trade and other payables	14,630	1,092	597	-	16,319
Accruals	51,849	11,320	21,640	17,487	102,296
Provision for liabilities and charges	1,855	-	-	41,700	43,555
	<u>68,334</u>	<u>12,412</u>	<u>22,237</u>	<u>59,187</u>	<u>162,170</u>

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<b>5. Revenue from non - exchange transactions</b>	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
<b>Fees income</b>		
Capitalization, rights and new issue fees	285,486	246,756
NSE - transaction fees	452,242	316,169
Application and licensing fees	16,645	14,116
Market development fees	11,373	10,967
Donor fund income	44,102	24,659
	<u>809,848</u>	<u>612,667</u>

The Authority charges fees on the following basis :

Capitalization / rights issues at a rate of 0.25% of the value of the issue.

Approval for listing of Government securities is charged at a rate of 0.075% of the amount raised.

New issues / IPOs at a rate of 0.15% of the value of the issue.

NSE Transaction fees at a rate of 0.12% of the value of the equities traded and 0.0015% of the value of bonds traded.

Application for license at Kshs 2,500 while annual licensing fees are up to a maximum of Shs 250,000.

Market development fees are charged to listed companies at a rate of 0.01% subject to a minimum of Shs 50,000 and a maximum of Shs 100,000 per annum.

<b>6. Revenue from exchange transactions - other income</b>	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
Interest income	62,645	57,939
Miscellaneous income	8,310	694
	<u>70,955</u>	<u>58,633</u>
<b>7. Gain on disposal on property, plant and equipment</b>		
Gain on disposal on property, plant and equipment	<u>158</u>	<u>1,019</u>

**8. Donor funding**

From the total income, the Authority received support worth Shs 0.75 million (2013: Shs 180.371 million) in the year. Of the total donor funding, income worth Shs 83.5 million (2012: Shs 126.862 million) has been deferred in line with the Authority's accounting policy.

<b>9. Net surplus for the year</b>	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
<b>(a) Items charged</b>		
The following items have been charged in arriving at net		
Depreciation of property, plant and equipment	32,022	24,037
Amortisation of intangible assets	49,411	12,245
Authority board members' emoluments, allowances and other Board related expenses	23,614	22,015
Post employment benefits expense (Note 8(b))	19,176	18,034
Provision for impairment of financial assets		
Trade and other receivables	208	1,534
	<u>208</u>	<u>1,534</u>

**NOTES (CONTINUED)**

**9. Net surplus for the year (continued)**

<b>(b) Employee benefits expense</b>	<b>2014 Shs'000</b>	<b>2013 Shs'000</b>
The following items are included in employee benefits expense:		
Retirement benefit costs		
Defined contribution scheme	18,953	17,836
National Social Security Fund	<u>223</u>	<u>198</u>

The Authority operated an in-house defined benefits pension scheme for its employees and made contributions up to 31 December 2011. The investment of the scheme's assets is managed by an independent fund manager, Genesis Kenya Investment Management Limited, on behalf of the Trustees.

The scheme is subjected to triennial valuations by independent actuaries to fulfill the statutory requirements under the Income Tax (Retirement Benefits) Rules 1994 and the Retirement Benefits Rules 2000. The latest actuarial valuation was carried out as at 31 December 2011. The actuarial valuation method adopted, 'Attained Age Method', entailed the comparison of the scheme's assets at the valuation date with its liabilities and an assessment of the ability of the scheme to meet its obligations to members. The deficit was paid for in July 2012.

The principal actuarial assumptions applied in the valuation are:

Investment returns	9% per annum
Rates of salary escalation	7% per annum
Rate of pension increases	3% per annum

Based on the actuarial report, the actuaries estimated that the present value of past service actuarial liabilities amounted to Shs 149,616,000 at 31 December 2011, and that the value of scheme's liabilities exceeded the assets by Shs 18,400,000 at that date. The deficit was provided for in the year ended 30th June 2012 and paid in July 2012.

<b>10. Tax expense</b>	<b>2014 Shs'000</b>	<b>2013 Shs'000</b>
Current income tax	78,154	47,871
Deferred income tax (Note 20)	(11,464)	(17,154)
Prior year tax arrears	<u>-</u>	<u>6,733</u>
Income tax expense	<u>66,690</u>	<u>37,450</u>

The tax on the Authority's surplus before income tax differs from the theoretical amount that would arise using the statutory income tax rate as follows:

<b>Surplus before income tax</b>	<u>220,352</u>	<u>153,581</u>
Tax calculated at the statutory tax rate of 30%		
Tax effect of:	66,105	46,074
Deferred tax recognised	-	(16,183)
Income not subject to tax	(4,761)	(4,749)
Expenses not deductible for tax purposes	5,346	5,575
Prior year tax arrears	<u>-</u>	<u>6,733</u>
Income tax expense	<u>66,690</u>	<u>37,450</u>

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	2014 Shs'000	2013 Shs'000
<b>11. Inventories</b>		
Consumables	<u>1,573</u>	<u>1,133</u>

Inventories consist of stationery and computer consumables required for day to day use by the Authority.

	2014 Shs'000	2013 Shs'000
<b>12a. Trade and other receivables from non exchange transactions</b>		
Trade receivables	58,783	54,419
Statutory management expenses receivable	49,286	49,286
Less: Provision for impairment losses	<u>(57,616)</u>	<u>(58,490)</u>
Net trade receivables	50,453	45,215
Other receivables	<u>25,400</u>	<u>24,230</u>
Trade and other receivables from non exchange transactions	<u>75,853</u>	<u>69,445</u>

**12b. Trade and other receivables from exchange transactions**

Trade receivables	8,327	16,202
Less: Provision for impairment losses	<u>(208)</u>	<u>-</u>
Net trade receivables	8,119	16,202
Prepayments	<u>7,512</u>	<u>1,371</u>
Trade and other receivables from exchange transactions	<u>15,631</u>	<u>17,573</u>
Total trade and other receivables from non exchange and exchange transactions	<u>91,484</u>	<u>87,018</u>

The movement on the provision for impairment losses for non exchange transactions is as follows:

At 1st July	58,490	56,956
Less: Provision utilised as debts written off	(200)	1,534
Less: Provision reversed on debt collection	<u>(674)</u>	<u>-</u>
At 30th June	<u>57,616</u>	<u>58,490</u>

The movement on the provision for impairment losses for exchange transactions is as follows:

At 1st July	-	-
Add: Additional provision	<u>208</u>	<u>-</u>
At 30th June	<u>208</u>	<u>-</u>

13. Staff loans and advances	Current 2014 Shs'000	Current 2013 Shs'000	Non- current 2014 Shs'000	Non- current 2013 Shs'000	Total 2014 Shs'000	Total 2013 Shs'000
	Car loans	6,490	3,644	16,261	13,324	22,751
Other loans and advances	305	2,473	69	155	374	2,628
Provision for impairment losses	-	-	(1,922)	(1,922)	(1,922)	(1,922)
Miscellaneous advances	-	-	4,179	4,179	4,179	4,179
House loans/staff mortgage guarantee fund	19,337	14,265	181,821	130,888	201,158	145,153
	<u>26,132</u>	<u>20,382</u>	<u>200,408</u>	<u>146,624</u>	<u>226,540</u>	<u>167,006</u>

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**14. Held-to-maturity investments - government securities**

	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
<b>Non-current</b>		
Treasury bonds		
Maturing after four years	165,000	145,000
Unamortised premium	45	-
	<u>165,045</u>	<u>145,000</u>
Treasury bonds		
Maturing after one year	80,000	100,000
Unamortised premium/(discount)	-	96
	<u>80,000</u>	<u>100,096</u>
	<u>245,045</u>	<u>245,096</u>
<b>Current</b>		
Treasury bonds		
Maturing within one year	100,000	135,000
Unamortised premium	45	(228)
	<u>100,045</u>	<u>134,772</u>
Treasury bills	203,300	139,500
Unamortised discount	(7,959)	(8,104)
	<u>195,341</u>	<u>131,396</u>
	<u>295,386</u>	<u>266,168</u>
	<u>540,431</u>	<u>511,264</u>

The fair value of the held to maturity assets -treasury bonds at the reporting date were:

**Non- current**

Held-to-maturity investments 240,223

**Current**

Held-to-maturity investments 98,591

**15. Staff benevolent funds**

	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
Investment in government securities	7,200	7,000
Unamortised discount on T-bills	(100)	(46)
Contributions receivable	713	159
Cash and cash equivalents (Note 16)	69	118
	<u>7,882</u>	<u>7,231</u>

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	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
<b>16. Cash in hand and bank</b>		
Cash in hand and cash at bank	37,071	70,303
Short term deposits	<u>88,122</u>	<u>23,782</u>
	<u><u>125,193</u></u>	<u><u>94,085</u></u>

For the purpose of the cash flow statement, cash and cash equivalents comprise the following:

Cash and current account balances		
Short-term bank deposits	88,122	23,782
Cash at bank and in hand	37,071	70,303
Benevolent bank balance (Note 15)	69	118
Investors Compensation Fund bank balance (Note 17)	<u>78,734</u>	<u>57,335</u>
	<u><u>203,996</u></u>	<u><u>151,538</u></u>

**17. Investors' Compensation Fund**

In accordance with Section 18 of Capital Markets Act, Cap 485A, the Authority is required to maintain a fund to be known as the Investors' Compensation Fund for the purpose of granting compensation to investors who may suffer pecuniary loss resulting from the failure of a licensed broker or dealer to meet its contractual obligations. This requirement was implemented in July 1995.

The fund derives its income from the following sources:

- i) Interest accruing on funds received from subscribers to public issues, between the day of closing the issue and making the refunds.
- ii) 0.01% of the consideration from sale and purchase of shares through the Nairobi Securities Exchange.
- iii) 0.004% of the consideration from sale and purchase of bonds traded through the Nairobi Securities Exchange.
- iv) Interest earned from investment of the funds held in this account.
- v) Financial penalties imposed on operators for non-compliance with Capital Markets Authority Rules and Regulations.

The movement in the fund balance during the year is as shown below:

	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
At beginning of the year	727,753	422,318
Nairobi Securities Exchange transactions fees	70,271	74,377
Interest on investments	82,633	58,142
Unamortised discounts on investments	-	1,356
Financial penalties	6,028	446
Management fees	(500)	(500)
Public issue fees	-	238,486
Compensation to Discount Securities/Nyaga Stockbrokers Ltd investors	<u>(9,523)</u>	<u>(66,872)</u>
At end of the year	<u><u>876,662</u></u>	<u><u>727,753</u></u>

**NOTES (CONTINUED)**

**17. Investors' Compensation Fund (continued)**

Included in the Investor Compensation Fund is Shs 4,044,268 (2013: Shs 4,169,674) worth of claims payable. The amount relates to claims by investors of Nyaga Stock Brokers (Under Statutory Management) which are due for payment.

The Investors' Compensation Fund balance is represented by the following assets:

<b>Non-current</b>	<b>2014 Shs'000</b>	<b>2013 Shs'000</b>
Equity investment in the Central Depository and Settlement	<u>7,000</u>	<u>7,000</u>
Treasury bonds		
Maturing after five years	275,150	182,150
Unamortised discount	<u>2,316</u>	<u>4,334</u>
	<u>277,466</u>	<u>186,484</u>
Maturing after one year	74,000	250,000
Unamortised discount	<u>66</u>	<u>3,220</u>
	<u>74,066</u>	<u>253,220</u>
	<u>351,532</u>	<u>439,705</u>
	<u>358,532</u>	<u>446,705</u>
<b>Current</b>		
Treasury bonds	250,000	16,300
Unamortised discount	<u>965</u>	<u>(10)</u>
	<u>250,965</u>	<u>16,290</u>
Treasury bills	177,300	200,900
Unamortised discount	<u>(7,015)</u>	<u>(8,901)</u>
	<u>170,285</u>	<u>191,999</u>
Fees receivable	18,155	10,988
Bank balance	1,711	1,721
Call account	77,024	55,614
Interest income receivable	<u>-</u>	<u>4,437</u>
	<u>96,890</u>	<u>72,760</u>
	<u>518,140</u>	<u>281,049</u>
	<u>876,672</u>	<u>727,754</u>

The Authority is mandated to manage the assets of the Investor Compensation Fund until such a time that the latter will have a functional independent Board. The assets of ICF of Shs 877 million (2013: Shs 728 million) are invested in both long term and short term investments. The matching liabilities have been stated to reflect appropriate portions in current and noncurrent liabilities.

The fair value of Investor Compensation Fund in nature of treasury bonds at the balance sheet date were Shs 595 million.

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18. Property, plant and equipment	Motor vehicles Shs'000	Computers, copiers & faxes Shs'000	Office equipment Shs'000	Furniture & fittings Shs'000	Capital work-in- progress Shs'000	Total Shs'000
<b>At 1st July 2012</b>						
Cost	17,876	48,010	16,383	67,492	13,334	163,095
Accumulated depreciation	(12,516)	(28,035)	(9,046)	(10,923)	-	(60,520)
Net carrying amount	5,360	19,975	7,337	56,569	13,334	102,575
<b>Year ended 30th June 2013</b>						
Opening carrying amount	5,360	19,975	7,337	56,569	13,334	102,575
Additions	4,145	47,806	802	265	-	53,018
Reclassified to intangible assets	-	-	-	-	(11,547)	(11,547)
Reclassified to expenses	-	-	-	-	(180)	(180)
Work-in-progress capitalised	-	-	-	472	(472)	-
Disposals	(6,013)	(2,201)	(461)	(3,258)	-	(11,933)
Accumulated depreciation reversed on disposal	4,510	1,897	390	2,880	-	9,677
Depreciation charge	(2,730)	(10,905)	(2,382)	(8,020)	-	(24,037)
Closing carrying amount	5,272	56,572	5,686	48,908	1,135	117,573
<b>At 30th June 2013</b>						
Cost	16,008	93,615	16,724	64,971	1,135	192,453
Accumulated depreciation	(10,736)	(37,043)	(11,038)	(16,063)	-	(74,880)
Net carrying amount	5,272	56,572	5,686	48,908	1,135	117,573
<b>Year ended 30th June 2014</b>						
Opening carrying amount	5,272	56,572	5,686	48,908	1,135	117,573
Additions	10,380	4,768	130	35	746	16,059
Disposals	-	(449)	-	(69)	-	(518)
Accumulated depreciation reversed on disposal	-	197	-	52	-	249
Depreciation charge	(3,826)	(18,098)	(2,266)	(7,832)	-	(32,022)
Closing carrying amount	11,826	42,990	3,550	41,094	1,881	101,341
<b>At 30th June 2014</b>						
Cost	26,388	97,934	16,854	64,937	1,881	207,994
Accumulated depreciation	(14,562)	(54,944)	(13,304)	(23,843)	-	(106,653)
Net carrying amount	11,826	42,990	3,550	41,094	1,881	101,341

Work in progress balance relate to the relocations works at the Authority offices at Embankment Plaza.

NOTES (CONTINUED)

	<b>Intangible assets Shs'000</b>	<b>Work in progress Shs'000</b>	<b>Total Shs'000</b>
<b>19. Intangible assets</b>			
<b>Software costs</b>			
<b>Cost</b>			
At 1st July 2012	25,852	238	26,090
Reclassification from work-in-progress	238	(238)	-
Additions	113,698	-	113,698
Reclassification from property, plant and equipment	11,547	-	11,547
	<u>151,335</u>	<u>-</u>	<u>151,335</u>
At 30th June 2013	<u>151,335</u>	<u>-</u>	<u>151,335</u>
<b>Amortisation</b>			
At 1st July 2012	12,262	-	12,262
Amortisation	12,245	-	12,245
	<u>24,507</u>	<u>-</u>	<u>24,507</u>
At 30th June 2013	<u>24,507</u>	<u>-</u>	<u>24,507</u>
<b>Net book value</b>			
At 30th June 2013	<u>126,828</u>	<u>-</u>	<u>126,828</u>
<b>Cost</b>			
At 1st July 2013	151,335	-	151,335
Additions	8,371	-	8,371
	<u>159,706</u>	<u>-</u>	<u>159,706</u>
At 30th June 2014	<u>159,706</u>	<u>-</u>	<u>159,706</u>
<b>Amortisation</b>			
At 1st July 2013	24,507	-	24,507
Amortisation	49,411	-	49,411
	<u>73,918</u>	<u>-</u>	<u>73,918</u>
At 30th June 2014	<u>73,918</u>	<u>-</u>	<u>73,918</u>
<b>Net book value</b>			
At 30th June 2014	<u>85,788</u>	<u>-</u>	<u>85,788</u>

**NOTES (CONTINUED)**

**20. Deferred income tax**

Deferred tax assets and liabilities, and the deferred tax charge/(credit) in the profit and loss account and in other comprehensive income are attributable to the following items:

<b>Year ended 30th June 2014</b>	<b>At 1st July 2013</b>	<b>Credited/(charged) to profit or loss</b>	<b>At 30th June 2014</b>
	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>
<b>Deferred income tax asset</b>			
Accrued leave	3,178	(313)	2,865
Provision for pending law suits	13,067	878	13,945
Staff gratuity provision	3,250	2,227	5,477
Provision for bonus - staff and board members	5,574	1,599	7,173
Provision for impairment losses	460	(398)	62
Provision for investor education	332	(332)	-
	<u>25,861</u>	<u>3,661</u>	<u>29,522</u>
<b>Deferred income tax liability</b>			
Property, plant and equipment	(3,895)	2,081	(1,814)
Intangible assets	(4,811)	5,722	911
	<u>(8,706)</u>	<u>7,803</u>	<u>(903)</u>
<b>Net deferred tax asset</b>	<u>17,155</u>	<u>11,464</u>	<u>28,619</u>

<b>21. Trade and other payables</b>	<b>2014</b>	<b>2013</b>
	<b>Shs'000</b>	<b>Shs'000</b>
Trade payables	22,394	16,319
Accruals	116,384	102,296
	<u>138,778</u>	<u>118,615</u>

Included under accruals are the provisions for various services whose movement has been presented below:

	<b>Leave benefits</b>	<b>Performance bonus</b>	<b>Consultancies</b>	<b>Other provisions</b>	<b>Total</b>
	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>	<b>Shs'000</b>
At 1 July 2013	10,781	18,581	5,244	67,690	102,296
Additional provisions raised	9,550	23,910	14,248	68,676	116,384
Provision utilized/reversed	(10,781)	(18,581)	(5,244)	(67,690)	(102,296)
At 30 June 2014	<u>9,550</u>	<u>23,910</u>	<u>14,248</u>	<u>68,676</u>	<u>116,384</u>

**22. Provision for liabilities and charges**

At 1st July	43,555	41,700
Add: Additional provision	5,133	1,855
Less: Provision written back	(2,205)	-
At 30th June	<u>46,483</u>	<u>43,555</u>

The Authority being the Capital Markets regulator in Kenya, is subject to legal proceedings in the normal course of business. While it is not possible to forecast or determine the final results of all pending legal proceedings, the Authority assesses the adequacy its provisions periodically against case developments and related legal costs.

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**23. Current tax payable**

	<b>2014</b> <b>Shs'000</b>	<b>2013</b> <b>Shs'000</b>
Current year tax	<u>25,325</u>	<u>47,821</u>

**24. Deferred income**

In line with the Authority's accounting policy, Shs 83,513,463 of the donor funded income has been deferred for future periods as follows:

Within one year	27,838	47,587
Within two years	<u>55,675</u>	<u>79,275</u>
Total	<u>83,513</u>	<u>126,862</u>

**25. Capital fund**

At 1st July 2013 and at 30th June 2014

<u>27,886</u>	<u>27,886</u>
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Capital fund represents the initial contribution by the government of Kenya towards the establishment of the Capital Markets Authority.

**26. General fund**

	<b>2014</b> <b>Shs'000</b>	<b>2013</b> <b>Shs'000</b>
At 1 July	757,322	641,191
Surplus for the year	153,662	116,131
Dividend paid to National Treasury	<u>(32,000)</u>	<u>-</u>
At 30 June	<u>878,984</u>	<u>757,322</u>

General fund represents accumulated surpluses over the years.

**27. Related party transactions**

**i) Board members of the Authority' remuneration**

Authority Board members remuneration and allowances	<u>23,614</u>	<u>22,015</u>
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**ii) Key management compensation**

Salaries and other employment benefits	<u>91,790</u>	<u>89,100</u>
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**28. Commitments**

**Contracted for but not recognised**

Capital expenditure contracted for at the balance sheet date but not recognised in the financial statements is as follows:

Capital expenditure contracted for	<u>28,000</u>	<u>28,000</u>
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The Authority embarked on the partitioning and refurbishment of the 5th floor. The structural plan has been drawn and the actual work will be accomplished in the following financial year at a cost of Shs 28 million.

**NOTES (CONTINUED)**

**28. Commitments (continued)**

**Operating lease commitments**

Operating lease commitments represent rentals payable by the Authority for rented office space. Rental expenses during the year amounted to Shs 43,884,833 (2013: Shs 27,592,204).

The future minimum lease payments under operating leases are as follows:

	<b>2014 Shs'000</b>	<b>2013 Shs'000</b>
Not later than 1 year	42,074	27,592
Later than 1 year and not later than 5 years	<u>77,491</u>	<u>119,072</u>
	<u><u>119,565</u></u>	<u><u>146,664</u></u>

The board members of the Authority are of the view that future net revenues and funding will be sufficient to cover these commitments.

**29. Contingent liabilities**

- a) A former employee of the Authority had filed a suit against the Authority for wrongful dismissal and is seeking damages amounting to Shs 16 million and the Authority has counterclaimed for a sum of Shs 42 Million. Based on professional advice, the Authority has estimated liability of Shs 6 million. The estimated liability has been recognised in these financial statements (Note 22). Based on the advice of the internal legal counsel, the Authority is of the opinion that no material liability is expected to arise to have an impact on these financial statements.
- b) In the normal course of operation, Kenya Revenue Authority had completed a tax audit for the period 2007 to 2012 and had issued an assessment notice. The Authority is currently in process of addressing and concluding the issues raised. Principal tax arrears amounting to Shs 12 million were paid in the previous year and the Authority had applied for set-off of tax paid in error in previous years amounting to Shs 14.8 million. The Authority had also applied for waiver of interest and penalties amounting to Shs 19 million providing mitigating grounds in support of the waiver. Based on the professional advice received and the mitigating ground provided, the Authority is of the opinion that no material liability is expected to arise to have an impact on these financial statements.

*Capital Markets Authority*  
*Financial statements*  
*For the year ended 30th June 2014*

NOTES (CONTINUED)

	2014 Kshs'000	2013 Kshs'000
<b>30. Operating expenditures</b>		
<b>30.1 Employment expense</b>		
Consolidated pay, leave pay and passages	261,639	251,535
Staff uniform expenses	223	297
Staff welfare and other costs	5,447	3,676
Staff retirement benefits	19,180	25,960
Staff gratuity	7,482	(863)
Benevolent fund contributions	-	131
National Social Security Fund (NSSF)	223	198
	<u>294,194</u>	<u>280,934</u>
<b>30.2 Other administrative expenses</b>		
Rent and maintenance	43,885	27,592
Equipment maintenance and stationery	13,383	8,009
Telephone, postage and utilities	14,780	9,454
Entertainment and public relations	11,060	8,638
Medical scheme and insurance expenses	17,548	13,882
Training and conferences	38,158	27,134
Motor vehicle running expenses	6,612	5,641
Subscriptions and IOSCO membership	4,211	2,897
Authority board members' emoluments and allowances	23,614	22,015
Professional and market development services	82,800	52,424
Depreciation of property, plant and equipment	32,022	24,037
Amortisation of intangible assets	49,411	12,245
Auditor's remuneration	539	539
Investors' education and awareness programme	27,464	18,538
Tribunal expenses	720	3,225
Provision for impairment losses	208	1,534
	<u>366,415</u>	<u>237,804</u>
<b>Total expenditure</b>	<u><u>660,609</u></u>	<u><u>518,738</u></u>