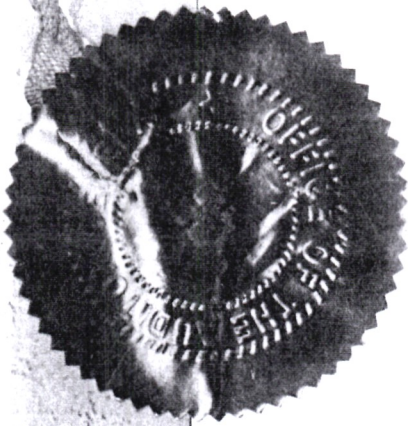


REPUBLIC OF KENYA



OFFICE OF THE AUDITOR-GENERAL

*Paper laid by
Leader of Majority
on 15/2/2018
Bambi.*

REPORT

OF

THE AUDITOR-GENERAL

ON

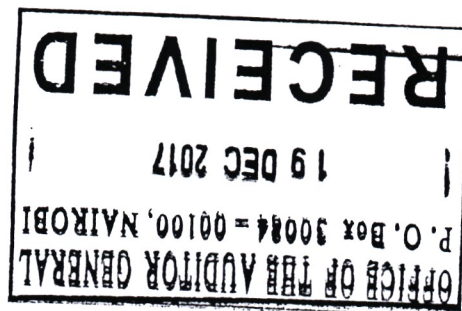
**THE FINANCIAL STATEMENTS OF
CAPITAL MARKETS AUTHORITY**

**FOR THE YEAR ENDED
30 JUNE 2017**

CAPITAL MARKETS AUTHORITY

DRAFT ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30TH JUNE 2017



*Capital Markets Authority
Annual report and financial statements
For the year ended 30th June 2017*

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Capital Markets Authority
Authority Information
For the year ended 30th June 2017

| | |
|---------------------------------------|---|
| Registered office | 3rd Floor, Embankment Plaza Longonot Road, Upper Hill P.O. Box 74,800, 00200 Nairobi, Kenya |
| Authority contacts | Telephone: (254) 2221910/ 2264900/2221869/2226225 E-mail: corporate@cma.or.ke Website: www.cma.or.ke |
| Principal bankers | Commercial Bank of Africa Limited Mara / Ragati Roads Upper Hill P.O. Box 30437, 00100 Nairobi, Kenya HFC Limited Kenyatta Avenue/Koinange Street, Rehani House P.O. Box 30088, 00100 Nairobi, Kenya KCB Mortgage Centre, Salama House Mama Ngina Street P.O. Box 45129, 00100 Nairobi, Kenya |
| Authorized independent auditor | Mbaya & Associates Certified Public Accountants 3rd Floor, Westlands Heights Karuna Road, Westlands P. O. Box 45390 - 00100 Nairobi, Kenya |
| On behalf of | The Auditor-General Kenya National Audit Office Anniversary Towers University Way P.O. Box 30084, 00100 Nairobi, Kenya |
| Principal legal adviser | The Attorney General State Law Office Harambee Avenue P.O. Box 40112, 00200 Nairobi, Kenya Archer & Wilcock Advocates Marakwet Close, Kilimani P.O. Box 10201, 00400 Nairobi, Kenya |

*Capital Markets Authority
Authority Information (continued)
For the year ended 30th June 2017*

Principal legal adviser (continued)

Hamilton Harrison & Mathews
1st Floor, Delta Office Suites
Waiyaki Way
P.O. Box 30333, 00100
Nairobi,
Kenya

Waweru Gatonye & Co. Advocates
Timau Plaza, 4th Floor, Argwings Kodhek
Timau Road Junction
P.O. Box 55207, 00200
Nairobi,
Kenya

RH Advocates
Transnational Plaza, City Hall Way, City Centre
P.O. Box 50515, 00200
Nairobi,
Kenya

**Capital Markets Authority
Authority Information
For the year ended 30th June 2017**

Background information

Capital Markets Authority (the '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.

Board Members of the Authority

| Name | Date of Birth | |
|-------------------------|----------------------|---|
| Mr James Ndegwa | 24th June, 1964 | Chairman |
| Mr Paul. M. Muthaura | 27th April, 1978 | Chief Executive |
| Dr Kamau Thugge, EBS | 1st August, 1957 | Principal Secretary to the National Treasury |
| Dr Geoffrey Mwau | 11th November, 1957 | Alternate to the Principal Secretary, The National Treasury |
| Hon. Prof. Githu Muigai | 31st January, 1960 | Attorney General |
| Mr Nevis Ombasa | 24th October, 1980 | Alternate to the Attorney General |
| Dr Patrick Njoroge | 2nd December, 1961 | Governor Central Bank of Kenya |
| Mr John Birech | 10th May, 1958 | Alternate to the Governor Central Bank of Kenya |
| Mr Paul Ngugi | 13th July, 1952 | Member |
| Ms Linda Muriuki | 29th March, 1964 | Member |
| Mr Moibi Mose | 18th June, 1974 | Member |
| Dr Thomas Kibua | 20th August, 1948 | Member |
| Ms. Christine Okoth | 26th May, 1975 | Member |
| Mr. Harry Kimtai | 13th December, 1968 | Member (Resigned from 9th May 2017) |

Capital Markets Authority
Authority Information (continued)
For the year ended 30th June 2017

Management team

Paul Muriithi Muthaura

Position Chief Executive
 Date joined the Authority September 15, 2005
 Profession Lawyer
 Key qualifications LL.M, LL.B, M.Phil, Dip Law, Dip in Financial Management.



Wyckliffe Shamiah

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



Edwin Nyaga Njamura

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



Luke Evans Ombara

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



Esther J. Maiyo

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



Daniel Ngenga Warutere

Position Manager, Market Supervision
 Date joined the Authority November 10, 2008
 Profession Lawyer,
 Key qualifications LL.B, CPS, CPA, Post Grad Cert, Capital Markets



Samuel Kamunyu Njoroge

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



Capital Markets Authority
Authority Information (continued)
For the year ended 30th June 2017

Management team

Hellen Ombati Head, Legal Affairs & Corporation Secretary
 Date joined the Authority May 6, 2016
 Profession Lawyer & Certified Secretary
 Key qualifications MBA, LLB, Dip-French, Dip in Law, CPS(K)



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



Matthew Mukisu
 Position Manager, Derivatives
 Date joined the Authority March 7, 2016
 Profession Economist
 Key qualifications MA (Economics), BSC, CPA(K)



James Kivuva
 Position Manager, Strategic Projects
 Date joined the Authority February 15, 2016
 Profession Information Technologist
 Key qualifications BSC, PRINCE 2, CBAP, Advanced Sysbase Database Administration and Performance Tuning Certification



Mary Njunguna
 Position Manager, Corporate Approvals
 Date joined the Authority December 15, 2009
 Profession Advocate of the High Court of Kenya
 Key qualifications MSC, LLB, Dip-French, CPS(K)



Abubakar Hassan
 Position Manager, Investigation and Enforcement
 Date joined the Authority April 1, 2016
 Profession Advocate of the High Court of Kenya
 Key qualifications MBA, LLB, CPA(K), CPS(K), CISA, CFE



*Capital Markets Authority
Authority Information (continued)
For the year ended 30th June 2017*

Key

| | |
|---------------|---|
| BA | Bachelor of Arts |
| BCOM | Bachelor of Commerce |
| BSC | Bachelor of Science |
| BSP | Balanced Scorecard Professional |
| CFE | Certified Fraud Examiner |
| CISA | Certified Information Systems Auditor |
| CPA | Certified Public Accountant |
| CPS | Certified Public Secretary |
| Dip | Diploma |
| EMBA | Executive Master of Business Administration |
| H. Dip | High Diploma |
| HRM | Human Resource Management |
| LLB | Bachelor of Law |
| LLM | Master of Law |
| MA | Master of Arts |
| Pg Dip | Post Graduate Diploma |

An Overview of Global Growth

According to the World Economic Outlook, April 2017, global economic activity is expected to pick up in the long term with a much awaited cyclical recovery in investment, manufacturing and trade. World growth is expected to rise from 3.1 percent in 2016 to 3.5 percent in 2017 and 3.6 percent in 2018.¹

Stronger activity and expectations of more robust global demand, coupled with agreed restrictions on oil supply by OPEC nations, have helped commodity prices recover from their troughs in early 2016. However, in the medium term, strategic efforts towards correcting structural problems such as low productivity growth, high income inequality and a shift from inward looking policies to promote global economic integration are required for the realization of a positive global outlook.

Additionally, forward looking economic policies will play an important role in staving off emerging downside risks while coordinated and renewed multilateral efforts will be critical in tackling common challenges in an integrated global economy.

The contribution of emerging markets and developing economies towards the overall growth of the global economy cannot be understated as witnessed in the recent years; they now account for more than 75 percent of global growth in output and consumption, almost double the share of just two decades ago. The external environment remains a significant enabler in the realization of these transformations as terms of trade, external demand and in particular external financial conditions remain increasingly influential determinants of medium term growth in these economies as they become more integrated into the global economy.²

Politically, the year witnessed two key global events: First the global reaction to the results of the June 23, 2016 referendum leading to the announcement of Brexit and causing the UK Government to invoke Article 50 of the Treaty on European Union, which puts the UK on a course to leave the EU by March 2019. And then the November 2016 US elections which saw Donald Trump elected as President of the United States of America raising uncertainty over the future of long established foreign treaty and trade arrangements, and indeed the USA's overall relationship with the rest of the world. The possible direction of foreign policies targeted towards developing nations and the implications of the rise of protectionism, are a key concern for Kenya, as for many African nations.

A key driver of the sustained growth observed during the year was a deliberate shift in national policy by the super economies towards infrastructure investments. Further to US President Donald Trump's pledge to close the US\$1 trillion infrastructure funding gap, the United Kingdom continued to champion infrastructure investments to mitigate the uncertainties caused by Brexit, while the Eurozone's €315 billion three-year Juncker Plan appears to be well in force. China's President Xi Jinping's New Silk Road plan to connect China with Central Asia, the Middle East and Europe through road, rail and port construction is also well underway as a further testimony to growing priority of infrastructure as a key tool of fiscal stimulus.

Regional Outlook

Africa's real GDP growth slowed down to 2.2% in 2016, mainly due to the continued decline in commodity prices and weak global economic growth. East Africa was the fastest growing region at 5.3% real GDP growth, followed by North Africa at 3%. Growth in other regions was less pronounced, ranging from a low of 0.4% in West Africa, dragged down by the recession in Nigeria, to 1.1% in Southern Africa, with South Africa, the region's largest economy, posting only 0.3% growth.³

With dynamic private sectors, entrepreneurial spirit and vast resources, Africa has the potential to grow faster and more inclusively. The continent's average growth is expected to rebound to 3.4% in 2017, assuming that the recent recovery in commodity prices is sustained, the world economy is strengthened and domestic macroeconomic reforms are entrenched. In 2018, growth is expected to consolidate, expanding by 4.3%.

The composition of total financial flows to Africa reflects the dynamism of its domestic markets. In 2017, inflows are projected at almost USD 180 billion. Remittances will reach USD 66.2 billion, up from USD 64.6 billion in 2016. Foreign direct investment inflows are expected to reach over USD 57 billion in 2017, supported mainly by greenfield investments from emerging economies, with China leading the pack. Tax revenue remains the most important source of domestic financing in African countries but has slowed with the decline in commodity prices. African countries will need to explore other options of mobilizing domestic resources to minimize vulnerability of revenues to volatility in commodity prices.⁴

1 <http://www.imf.org/-/media/Files/Publications/WEO/2017/April/pdf/c1 ashx>

2 <http://www.imf.org/en/Publications/WEO/Issues/2017/04/04/world-economic-outlook-april-2017>

3 African Economic Outlook 2017, Entrepreneurship and Industrialization

4 <http://www.et.undp.org/content/ethiopia/en/home/library/poverty/EthiopiaAfricanEconomicOutlook2017.html>

The Continent is showing signs of recovery with growth projected to reach 2.6% in 2017. However, the recovery remains inconsistent, with growth expected to rise only slightly above population growth, a pace that hampers efforts to boost employment and reduce poverty.

Nigeria, South Africa, and Angola, the continent's largest economies, are seeing a rebound from the sharp slowdown in 2016, but the recovery has been slow due to insufficient adjustment to low commodity prices and policy uncertainty. Furthermore, several oil exporters in the Central African Economic and Monetary Community (CEMAC) are facing economic difficulties.

The latest data reveals that seven countries (Côte d'Ivoire, Ethiopia, Kenya, Mali, Rwanda, Senegal and Tanzania) continue to exhibit economic resilience, supported by domestic demand, posting annual growth rates above 5.4% in 2015-2017. These countries house nearly 27% of the region's population and account for 13% of its total GDP.

The global economic outlook is improving and should support the recovery in the region. Africa's Pulse, a World Bank publication⁵ notes that the continent's aggregate growth is expected to rise to 3.2% in 2018 and 3.5% in 2019, reflecting a recovery in the largest economies. It will remain subdued for oil exporters, while metal exporters are projected to see a moderate uptick. GDP growth in countries whose economies depend less on extractive commodities should remain robust, underpinned by infrastructure investments, resilient services sectors and the recovery of agricultural production. This is especially the case for Ethiopia, Senegal, Tanzania and to some degree Kenya.

Kenya's Capital Markets Policy Issues

Capping of interest rates

A key policy change in the financial services industry in the FY 2016/17 was the passing into law of the Banking (Amendment) Act, 2016 which came into force on 14th September 2016. The law set the maximum interest rate chargeable for a credit facility in Kenya at no more than four percent above the Central Bank Rate. In addition, the Act set the minimum interest rate granted on a deposit held in an interest earning account in Kenya to at least seventy percent of the base rate. The implementation of this Act led to the growth in the average savings rates and a decrease in the average lending rates offered by commercial banks in the same period.

However, real questions and doubts remain as to whether the interest rate cap will achieve its intent of reducing the cost of accessing credit by Kenyans, with the Kenya Bankers Association (KBA) and the Nairobi Securities Exchange separately providing data that suggested a decline in lending to the private sector and a decline in the performance of listed commercial banks. In response to this, a Presidential Statement and subsequently a policy pronouncement by the Cabinet Secretary for the National Treasury at the close of this Fiscal Year indicate that the Government will work closely with the Central Bank of Kenya and the Kenya Bankers Association to conduct a more comprehensive assessment of its impact in order to inform its possible review.

Consolidation of non-bank financial sector regulators

In April 2017, the Kenya Cabinet approved the draft Financial Services Authority Bill (FSA) 2016 whose aim is to merge the functions of four regulatory bodies; that is the Retirement Benefits Authority, Insurance Regulatory Authority, Capital Markets Authority and the Sacco Societies Regulatory Authority.

Through the FSA, Kenya seeks to increase efficiency and ease of doing business within the financial services industry by providing consolidated supervision of financial services to eliminate regulatory gaps and to increase protection of consumers of financial services through the introduction of a robust market conduct framework encompassing many previously unregulated financial services including non deposit taking credit providers.

However, the Bill is yet to be forwarded to the National Assembly for consideration and the Authority will continue to proactively engage on the road map for the same in the coming financial year.

⁵ <http://www.worldbank.org/en/news/press-release/2017/04/19/economic-growth-in-africa-is-on-the-upswing-following-a-sharp-slowdown>

Market Development Reforms and Innovations

During the period under review, Kenya's Capital Markets greatly benefitted from policy and regulatory support by the Government which, among other initiatives, is working steadily towards issuing its first Sukuk and other conventional sovereign debt issuances, buoyed by its consistent sovereign rating, the most recent being Standard & Poor's affirmation of the country's short and long term foreign and local currency sovereign credit ratings at "B+/B" with a stable outlook on strong external position and monetary policy flexibility. This was complemented by the tax neutrality and incentive measures pronounced during the 2017/2018 budget delivered in March 2017 by the Cabinet Secretary for the National Treasury, designed to support the introduction of Islamic finance products, Asset Backed Securities (ABS) and Real Estate Investment Trusts (REITs). It is noteworthy that Kenya's current estimated infrastructure funding gap is US\$2-3 billion per year over the next 10 years, re-emphasizing the need to fully leverage market based financing.

The pilot tranche of the M-Akiba issued in April 2017, was overwhelmingly successful with more than 100,000 registered potential investors missing out due to the small issue size and presenting a strong foundation for the further Kshs 4.85 billion tranche planned for the coming financial year. Success of this product is expected to demonstrate the true potential of this Financial Technology (FinTech) solution from the Government in mobilizing savings towards the 30% level projected in the Kenya Vision 2030.

Related to M-Akiba, the Authority further introduced a new concept of a "Regulatory Sandbox" which is a 'safe space' in which businesses are allowed to test innovative products, services, business models and delivery mechanisms without immediately incurring all the normal regulatory consequences. The aim of establishing a Sandbox is to allow firms to 'experiment' with new technology and offer innovative financial products and services subject to appropriate controls for investor protection. This is an exciting area that will be pursued further in the new financial year.

Corporate Governance and Performance Management

The Authority has, over the last couple of years, attained Global and Regional awards for its excellence in innovation, particularly in service delivery improvements. This year the Authority was once again recognized as "The most innovative capital markets regulator in Africa". These achievements come against the backdrop of deliberate reforms currently taking place in Kenya in the public sector in order to realize more effective service provision. The Mwangozo Code, issued by His Excellency, the President of the Republic of Kenya in January 2015, has been a critical document in entrenching the principles and values of public service and best practices in corporate governance. As Chairman of the Capital Markets Authority Board I am proud to note that we have complied with these principles and values fully and I believe, in so doing, we have been able to steer the capital markets to be increasingly more competitive with other emerging markets globally. I further wish to state that my Board has consistently inculcated sound corporate governance practices, which are grounded on our national values as well as global international practices, in the capital markets industry as a whole, to ensure its sustainability.

The Authority signed the 2016 -17 Performance Contract (PC) on 23rd February, 2017 following negotiations with the National Treasury, in December 2016 and subsequent vetting by the Performance Management and Coordination Office in January 2017. Cumulatively, the gross majority of the Authority's 2016/2017 PC targets were met or exceeded as at end of June 2017. Key areas where commitments were exceeded include: fees and levies collections; investor education and public awareness, stakeholder engagement, youth internship and apprenticeship, starting a business, protecting investors, research and regulatory and policy proposals. The Authority however remains committed to continuous performance improvement towards ensuring that the targets are met across all functions as prescribed by the performance contracts.

International Cooperation Agreements

Internationally, the Authority has entered into Memoranda of Understanding with two global regulators; the Australian Securities Investment Commission and the Abu Dhabi Global Market to provide a framework for co-operation and referrals between the different approaches used in the respective jurisdictions on financial markets innovations in line with the growth of fintech globally. Through the cooperation agreements, the Authority hopes to exchange lessons learned on best practices as it works towards establishing its own regulatory sandbox to support the growth of fintech companies in the country.

Appreciation and Outlook

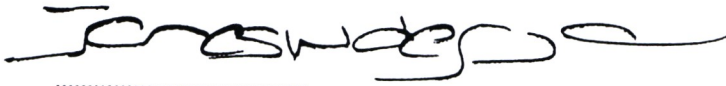
The support extended by the Government to the Authority is critical to the success we achieve in performing our duties and responsibilities. I wish to thank the National Treasury, our capital markets industry colleagues and all the other financial services regulators who have played a significant role in supporting the Authority as it executes its mandate.

The commitment and diligence of the CMA Board Members in preparing for and attending Board and Committee meetings as well as other events of the Authority has been tremendous. The excellent work of the Authority's management and staff under the able leadership of Mr. Paul Muthaura has been exemplary and the support the team as a whole provides to the Board's execution of its statutory mandate is immense.

The drive with which the Authority's staff and our industry partners have worked towards achieving the 10 Year Capital Markets Master Plan is equally impressive and very significant ground has already been covered. With this rapid progress I am confident that, while there are inevitable short term challenges to be addressed, the future looks promising as Kenya prepares to position itself as the "Heart of African Capital Markets" by the year 2023.

We therefore look forward to the exciting years ahead in the capital markets as new products and innovations are introduced to meet demands from the dynamic set of local, regional and international investors with eyes set on Kenya as an investment destination of choice.

Signed



.....
Mr. James Ndegwa
Chairman

I. Market Performance

Kenya's capital markets continued to exhibit resilience in the face of both internal and external challenges in FY 2016/17. Market capitalization for listed companies at the Nairobi Securities Exchange (NSE) grew by 11.35 percent during the period under review, rising to Kshs. 2.22 Trillion as at 30th June 2017. This was largely driven by the resilience of the NSE 20-Share Index, which experienced a significant decline of 19.90% between July 2016 and February 2017, during which time it fell below the 3000 point mark; only to resurge by 29% to 3607.18 points at the close of the Financial Year. The earlier decline in the index in the first half of the year was mainly influenced by depressed performance of listed companies as reflected in the high instances of profit warnings and the uncertainty arising from the impact of the capping of the interest rates domestically, coupled with key global events such as Britain's decision to exit the European Union and the election of Donald Trump as the President of the United States of America.

The second half recovery was driven mainly by renewed interest in the market following introduction of new products notably the listing of Kenya's first Exchange Traded Funds (ETFs), the M-Akiba bond and positive capital markets policy pronouncements by the Cabinet Secretary for the National Treasury in his delivery of the 2017/2018 Budget Statement.

Total secondary market bond turnover in FY 2016/17 amounted to Kshs. 403.29 Billion, a 6.96 percent increase from Kshs. 377.04 Billion recorded in FY 2015/16. This improved performance was driven by efforts of the Kenyan Government to bring down primary market rates by dropping high bids during its securities' auctions resulting in institutional investors such as commercial banks redeploying the funds in the secondary market. The general drop in the equities market (equity turnover recording Kshs 152.29 in FY 2016/17, a 13.19 percent decrease from total turnover recorded in FY 2015/16), further boosted performance of the secondary bond market due to their inverse correlation, leading to a shift by investors to bond investments.

Statistics indicate that the Kenyan markets remain an attractive destination for investors, particularly foreign investors, who account for more than seventy percent of the total market turnover. This was further catalysed by the policy decision to remove caps on foreign ownership of companies listed on the Nairobi Securities Exchange as the country works towards making Nairobi an international financial services centre. The market also witnessed significant growth in the private equity industry as observed by the number of deals entered into during the year. Overall, we remain optimistic and confident in Kenya's potential to withstand shocks, both local and external, and believe that we will be witnessing more favourable performance in the coming year, largely driven by innovations and favourable policy and regulatory environment.

II. Capital Markets Master Plan

The Capital Markets Master Plan identified 113 recommendations to be implemented over its 10 year (2014 – 2023) term. Key milestones achieved in the year under review included;

- i. On-boarding of a consultant to conduct a gap analysis on national and county financing through support of the Financial Sector Support Project (FSSP) expected to make policy recommendations aimed at enhancing the uptake of capital market products and services that can be leveraged towards bridging these gaps and supporting devolution;.
- ii. Stewardship Code for Institutional Investors was gazetted on June 23, 2017;
- iii Tax neutrality proposals on Real Estate Investment Trusts (REITS) and Asset Backed Securities (ABS) with respect to VAT were adopted by the National Treasury vide the Finance Act 2017;
- iv Amendments to the Capital Markets Act, the Cooperatives Societies Act and Sacco Societies Act to facilitate Shariah compliant finance products as well as tax statutes to provide for equivalent tax treatment of these alternative financial products with the conventional financial products.

Capital Markets Authority
Report of the Chief Executive Officer (continued)
For the year ended 30th June 2017

- v. The Public Finance Management Act (PFMA) was amended to provide for issuance of sovereign Sukuks (Islamic bond);
- vi. CMA staff and industry participants continued to receive level I Chartered Institute for Securities & Investment (CISI) certification and the first batch received level II certification;
- vii. Regulations to facilitate Securities Lending and Borrowing (SLB) and Short Selling were approved by the Board and submitted to National Treasury for gazettelement;
- viii. Issuance of the following policy guidance notes to facilitate roll out of new products:
 - Policy Guidance Note on Asset Backed Securities; and
 - Policy Guidance Notes on issuance of Global Depository Notes/ Receipts
- ix. Onboarding of a consultant to undertake an impact assessment of investor education by the Authority and develop a white paper to inform national consumer financial education policy and strategy;
- x. Following the issuance of policy guidance note on Exchange Traded Funds (ETFs), the Authority approved the first issue and listing of an ETF in February 2017 by New Gold ETF Issuer;
- xi. Onboarding of a consultant to support capacity building, strengthen regulatory oversight and inform product implementation for derivatives markets;
- xii. The Authority through support of Frontclear conducted an analysis of gaps in legislation hindering certainty in insolvency netting and settlement finality in REPO and Derivative transactions with the recommendations set to be implemented in FY 2017/18 following stakeholder engagement with a view to Kenya securing clean ICMA & ISDA opinions; and
- xiii. The Authority through the Financial Services Volunteer Corps (FSVC), United States Securities and Exchange Commission (US SEC) and Bloomberg LLP conducted a comprehensive capacity building initiative to supporting capital markets liquidity in Kenya through Securities Lending and Borrowing and strengthening of Collective Investment Schemes(CIS) reporting and structuring.

III. Review of the Policy Framework

To ensure policy proposals made to the National Treasury are inclusive and represent market and industry requirements, the Authority adopted an industry roundtable engagement approach that provides a platform for key stakeholders to share their views, vision and proposals on industry direction. This was implemented in the FY 2016/17 as the Authority sought to amalgamate policy proposals from industry players for consideration by the National Treasury.

FY 2016/17 was characterized by key policy wins for the capital markets and the overall financial services sector industry as convergence on efforts aimed at growing the industry and increasing product offerings was attained. These were witnessed through the Budget Statement, 2017 which entrenched key gains for the industry and are summarized as below:

Capital Markets Authority
Report of the Chief Executive Officer (continued)
For the year ended 30th June 2017

Table 1: Capital Markets Related Policy Pronouncements – Budget Statement 2017

| Issue | Policy Pronouncement | Implication | |
|-------|----------------------------------|--|---|
| 1 | Islamic Finance | <ul style="list-style-type: none"> Proposed amendments to the Capital Markets Act, the Cooperatives Societies Act and Sacco Societies Act to facilitate issuance of shariah compliant finance products. Amendment of the Public Finance Management Act to provide for issuance of Sukuk (Islamic bond). Amendment of tax statutes to provide for equivalent tax treatment of these Islamic financial products with the conventional financial products. Regulatory frameworks to facilitate development of Takaful Retirement Benefits Schemes in Kenya to be developed. | <p>This has provided a framework for introduction of Islamic products across the financial sector thereby deepening the market by providing alternative investment opportunities for investors. This further strengthens the opportunity for Kenya to position itself as a regional hub for Islamic Finance and contributes to the Vision 2030 objective of making Nairobi an International Financial Centre.</p> <p>Amendment of PFM Act paves way for issuance of Sukuks by the Government of Kenya as an alternative source of financing for development projects.</p> <p>The amendment of tax statutes on the other hand create an even playing field for Islamic products by providing for equivalent tax treatment of these alternative financial products with the conventional financial products.</p> <p>Through the Project Management Office, a review of the respective financial sector services Acts will be conducted to identify possible areas of amendment to provide a facilitative environment for the development of takaful retirement benefits schemes in Kenya.</p> |
| 2 | Tax neutrality for REITs and ABS | Amendment of the VAT Act to exempt from VAT transactions related to transfer of assets into Real Estate Investment Trusts (REITs) and Asset Backed Securities (ABS). | In conjunction with the earlier removal of income tax and stamp duty on asset transfers into REITs and ABS, this serves as the final component for providing the necessary tax neutrality to unlock the potential of these market based funding tools particularly in connection with infrastructure development. |
| 3 | NIFC Bill | Nairobi International Financial Centre (NIFC) Bill was approved by the Cabinet in December 2016, and subsequently assented to by the President in early July 2017 | The assent by the President cements certainty around the establishment of the Nairobi International Financial Centre Authority to position Nairobi as an international financial hub. The CMA and other financial services regulators will be working closely with NIFCA in reviewing and recommending review of relevant legal and regulatory framework in order to develop Kenya as an international competitive financial centre. |
| 4 | FSA Bill | The Financial Services Authority Bill was approved by the Cabinet for submission to the National Assembly for consideration. | Once the Bill is considered by the National Assembly and enacted it will set in motion the process for the consolidation of the non-bank financial sector regulators as initially announced in October 2013. |

Source: Budget Statement 2017

Moreover, the Finance Act 2016 amended the Capital Markets Act, making the Authority the primary regulator of spot commodity markets in Kenya, a critical step, in collaboration with the Ministry of Trade and other key stakeholders, in establishing a commodity exchange in the country.

Sufficient measures are being put in place to ensure that the policy pronouncements that have an impact in the Kenyan capital markets are highlighted through targeted investor education forums and joint public education and awareness efforts amongst the financial sector regulators to raise awareness of the evolving and more conducive environment for the use of the capital markets to fuel economic development.

IV. Newly Established Partnerships

During the financial year, the Authority was able to secure a number of MOUs with institutions of similar interest.

a. The Authority signed a Co-operation Agreement with Financial Services Regulatory Authority of the Abu Dhabi Global Market (ADGM) on Regulation of Financial Technology.

Signed on 18th June 2017, it provides a framework for co-operation and referrals between the Innovation Functions of the two Authorities. The agreement was based on the mutual desire by the Authorities to promote innovation in financial services in their respective markets. The Agreement provides for a Referral mechanism where the Authorities through their Innovation functions will refer to each other Innovator Businesses that would like to operate in the other's jurisdiction. It also caters for the Authorities to participate in joint innovation projects on the application of key technologies such as digital and mobile payments, block chain and distributed ledgers, big data, flexible platforms (API) and other areas of new technology and to share information about innovations in financial services in their respective markets.

b. Memorandum of Understanding with the Association of Chartered Certified Accounts (ACCA) to undertake joint financial literacy initiatives

In June 2017, the Authority signed a Memorandum of Understanding with the ACCA to undertake joint financial literacy initiatives for an additional period of two years. The partnership aims to enhance financial literacy in Kenya through programs targeting various stakeholders and builds on the previous joint initiatives under an earlier MOU. The joint financial literacy initiatives are aimed, in amongst other targets, at promoting excellence in financial reporting by the media, having recognized the pivotal role that the media plays in deepening financial literacy in Kenya.

c. Memorandum of Understanding with the Australian Securities Investment Commission on establishment of a Regulatory Sandbox

In October 2016, the Authority and the Australian Securities and Investment Commission (ASIC) signed a co-operation agreement which aims to promote innovation in financial services. It also sets up as framework for cooperation between the Authority and ASIC in the expanding space of innovation in financial services. This is in line with IOSCO recommendations as articulated in its Fintech report dated February 2017 where greater multilateral and bilateral collaboration and greater national regulatory coordination is encouraged to address the potential risk for regulatory arbitrage arising from the cross-cutting nature of Financial Technology (FinTech).

d. Launch of Business Incubation and Accelerator Listing Experience

The Capital Markets Authority (CMA) further partnered with industry players to engage with companies with the potential to list in March 2017 through a new initiative dubbed "the business incubator and accelerator experience." This is a continuous program intended to provide interested companies with a realistic and practical feel of the listing process.

Interested firms are given an opportunity to participate in a stage by stage, one on one, structured engagements with the CMA, NSE, Nominated Advisors (NOMADS), Transaction advisors, Lawyers, Auditors, Stockbrokers and Investment Banks, among other service providers, to allow for confidential B2B discussions on their readiness for listing.

The Authority will continue promoting this initiative in the forthcoming financial year as it works towards achieving the Capital Markets Master Plan (CMMP) goal of having at least three to four companies listed on the GEMS market segment annually.

e. Launch of an anonymous Whistleblowing Portal

As part of its mandate of ensuring fair, orderly and efficient markets, the Authority launched an anonymous reporting portal in July 2016 to enable whistle blowers to report malpractices in the capital markets. The portal which is accessible through the Authority's website, gives whistle blowers an opportunity to share anonymous but verifiable evidence with the potential to complement and support CMA's investigation and enforcement efforts. The public is encouraged to use this facility objectively and play an active role in ensuring transparency in capital markets operations.

f. CMA Resource Center Portal

During the financial year, the Authority launched its Resource Center Portal. The portal was developed based on modern information communication technologies to facilitate online access to the rich information that the Authority possesses. The Portal which was implemented in September 2016 is geared towards making more information content available online and to remove geographical barriers in accessing basic capital market information. The portal can be accessed through the link; <http://www.cmarcp.or.ke/>.

Capital Markets Authority
Report of the Chief Executive Officer (continued)
For the year ended 30th June 2017

V. Review of legal and regulatory framework

In its drive to widen the scope of available capital markets products in the Kenyan market in line with the 10-year Capital Market Master Plan, the Authority developed a number of regulations and frameworks to support the operationalization of new capital markets products. These included:

- i. Policy Guidance Note on Global Depositary Receipts/Notes, issued in June 2017;
- ii. Policy Guidance Notes on Asset Backed Securities, issued in April 2017.
- ii. Stewardship Code for institutional investors, gazetted into operation in June 2017.

The following regulations are still under development and are hoped to be finalized in the next financial year.

- i. Securities Lending and Borrowing and short selling Regulations.
- ii. Regulations on Online Forex Trading, in line with the policy pronouncement by the Cabinet Secretary, National Treasury in the 2016 budget statement.

Technical Assistance Provided by CMA Kenya

Noting the significant reforms undertaken in recent years in the areas of market supervision and regulation, market development and investor education, the Authority has stood prepared to share lessons learned with fellow regulatory authorities across the African continent. In this regard, the Authority was able to support a number of technical assistance programmes as follows:

- i. Between March 20th and 24th 2017, the Authority hosted staff from Swaziland's Financial Services Regulatory Authority (FSRA) where the participants were taken through an overview of the Kenyan capital markets, regulation procedures, legislation and guidelines, Kenya's capital markets master plan and implementation status amongst others.
- ii. In March 2017, the Authority hosted staff from Botswana's Non-Bank Financial Institutions Regulatory Authority where capacity building initiatives were offered in line with the Authority's rules and regulations governing investments, licensing policies and procedures of fund administrators, risk based supervision, inspection policies and procedures, enforcement amongst others.

VI. Market Development

FY 2016/17 marked a significant year on the market development front as the Authority made key advancements in introducing and providing a facilitative regulatory environment for the introduction of new capital markets products.

i. Exchange Traded Funds

In line with its strategic objective broadening the array of products in the Kenyan capital market, the Authority approved the secondary listing of the first Exchange Traded Fund (ETF) in Kenya in February 2017. Consequently, 400,000 gold bullion debentures issued by New Gold Issuer (RF) Limited were listed on the Main Investment Market Segment of the Nairobi Securities Exchange, commencing trading on the NSE on 27th March 2017. The ETF is expected to open the doors to local investors wishing to indirectly participate in the gold market, where they have previously had to either trade in the commodity in its physical form (bullion) or do so through offshore markets. It is also expected to provide diversification benefits from a portfolio perspective.

ii. M-Akiba Bond Issuance

FY 2016/17 saw the debut of the first mobile phone based retail bond issued by the Government of Kenya through the National Treasury. The bond was issued in two phases; a pilot phase offered in March 2017 that was 100 percent subscribed, raising Kshs. 150 Million, with a minimum investment amount of Kshs 3,000 and a maximum amount of Kshs 140,000 through Mobile Network Operators and Kshs. 999,999 through Pesalink.

The second tranche of the issue was offered on June 30 2017 following the successful pilot phase and is aimed to raise Kshs 1 billion with a green shoe option of Kshs 3.85 billion. In addition to use of Mobile Network Operators, the second tranche included subscription through Pesalink, with a maximum single transaction investment amount of Kshs 999,999. The Authority is delighted to have participated in facilitating this issue and looks forward to seeing more active trade in the secondary market. It is noted that the M-Akiba bond is a key initiative by the government to democratize access to government securities by retail investors while also leveraging Kenya's global leadership on mobile payment platforms to promote a savings culture.

iii. Islamic Finance

Following the commissioning of Islamic Finance Advisory and Assurance Services (IFAAS), in association with Simmons & Simmons to lead the Project Management Office (PMO) on Islamic Finance in the country in October 2015, the Joint Financial Sector Regulators have made notable steps towards creating an enabling environment for the growth of Islamic finance in the country.

During the financial year, the PMO team made policy proposals to the National Treasury most of which were adopted in the 2017 Budget Statement; ranging from proposed amendments to statutory provisions such as the Public Finance Management Act and amendment of the Capital Markets Act to incorporate the definition of Sukuku (Islamic bonds).

Additionally, the Islamic corporate governance structure upon which Kenya's Islamic finance industry will operate has also been established with the formation and official launch of the Islamic Finance Steering Committee (IFSC) and Islamic Finance Consultative Committee (IFCC) with the former drawing members from financial services regulatory bodies and the latter being members drawn from the industry, including Islamic scholars. The members have since been gazetted in the Kenya Gazette.

VII. Policy/Research Conducted

As one of the initiatives to deepen Kenya's capital markets, CMA initiated various studies and contributed to financial sector publications;

i. Consultative paper on policy framework for the implementation of a regulatory sandbox to support financial technology (Fintech) innovation in the Capital Markets in Kenya

The Authority developed a strategy paper outlining a proposed policy framework for the implementation of a regulatory sandbox to support financial technology (Fintech) innovation in the capital markets in Kenya that was the The consultative paper was subjected to public exposure for a 30 day period and a forum with industry players held in June 2017 aimed at receiving feedback on the Authority's approach in establishing a regulatory sandbox.

ii. A research paper on access to funding by National and County Governments

In 2010, through the promulgation of a new Constitution, Kenya adopted a devolved system of government with 47 county governments as the devolved units. To seek solutions towards infrastructural financing for both state and county development projects, the Authority, with support from the World Bank through the Financial Services Sector Project on-boarded a consultant in May 2017 who will be conducting a study aimed at proposing potential capital markets products that can be used by the institutions to raise funds. Leveraging the capital markets is expected to shift reliance on transfers from the national government in financing infrastructural and overall development projects at the county level.

iii. The Authority also provided inputs towards publications in financial services industry such as the Foreign Investment Survey 2016 and the Kenya Financial Sector Stability Report.

VIII. Financial Highlights Results

| RESULTS | 2017 | 2016 |
|---|----------------------|-----------------------|
| | Shs'000 | Shs'000 |
| The results for the year are summarised below:- | | |
| Total income for the year | 983,540 | 949,986 |
| Total operating expenditure for the year | <u>(970,011)</u> | <u>(812,206)</u> |
| Surplus for the year before tax and transfer | <u>13,529</u> | <u>137,780</u> |
| Tax expense | <u>-</u> | <u>-</u> |
| Surplus for the year | <u><u>13,529</u></u> | <u><u>137,780</u></u> |

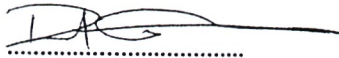
IX. Future Outlook

Throughout the FY 2016/17, the Authority is proud to have made significant steps in line with the Capital Markets 10 Year Master Plan and the Authority's Strategic Plan 2013-17 which will be entering its final year of implementation in FY 2017/18.

This has equally been supported by the Authority's internal policy on high quality performance dubbed "uwezo kipeo," that has created a spirit of excellence amongst staff as they execute their duties. Acknowledging its human capital as one of its most invaluable resources, the Authority will continue to forge ahead in confidence as it executes its dual mandate of market development and regulation.

In conclusion therefore, I wish to thank the Board for their guidance and unfailing support throughout the year. I would also like to extend my sincere appreciation to the various stakeholders both in Government and private sectors who have made the development and implementation of the Capital Markets Master Plan a reality.

My special appreciation goes to the management and staff of the Authority for their tireless commitment and willingness to drive the Authority's ambitious and multi-faceted agenda on market development and effective regulation. The teams' excellent work in fulfilment of the responsibility entrusted to us has resulted in our recognition two years in a row as "The Most Innovative Capital Markets Regulator in Africa" and moves us ever closer to facilitating the Kenyan capital markets to become the true Heart of the African Capital Markets.



.....
Mr. Paul Muthaura
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
- iii) During the period under review, the Board met thirteen times.

COMPOSITION OF THE BOARD

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

1. Mr. James Ndegwa

James Ndegwa holds a BA (Hons) and an MA degree from Oxford University. An insurer by profession, he is an Associate of the Chartered Insurance Institute (UK) and an Associate of the Insurance Institute of Kenya. He is the Chairman of First Chartered Securities Limited and a director of several companies. Prior to his present position, he was the Managing Director of Lion of Kenya Insurance Company Limited until 2003.

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 (Director General, Budget, Economics and Fiscal Affairs, 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.

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: Mr. Nevis Ombasa

Mr. Nevis Ombasa is a lawyer by profession. He holds a Bachelor of Arts (Econs) degree from D.A.V.V University India and a Bachelor of Laws (LLB) degree from Karnataka University, India. He has previously worked in the law firm of Maobe Maotsetung & Co. Advocates and Omboga & Co. Advocates. Mr. Ombasa is currently working in the Office of the Attorney General and Department of Justice as a State Counsel in the Government Transactions division.

COMPOSITION OF THE BOARD (Continued)

6 Dr. Patrick Njoroge (Governor, Central Bank of Kenya)

Dr. Njoroge is an economist by profession, and holds a PhD in Economics from the University of Yale, USA. He holds a Masters degree in Economics and a Bachelors degree in the same discipline from the University of Nairobi. He joined the Washington-based IMF in 1995 as an economist and rose through the ranks to hold the position of adviser. Prior to that, he worked briefly in the mid 1980s at the Ministry of Planning and as an economist at the Ministry of Finance in the 1990s.

7 Alternate to Governor, Central Bank of Kenya: Mr. John Birech

Mr. John Birech holds an MA (Economics); B Phil. (Economics) and BA (Economics) from the University of Nairobi. He is presently the Ag. Director, Financial Markets Department, Central Bank of Kenya.

Mr. Birech joined the Central Bank of Kenya in September, 1984 and has served in various areas of the Bank including Banking, Bank supervision and Financial Markets Department. Mr. Birech also sits in the Monetary Policy Committee of the Bank.

8 Ms. Linda Muriuki

Linda Watiri Muriuki is an Advocate of the High Court of Kenya with over Twenty-Five years' experience. Linda obtained a B.A. Economics degree from York University, Canada after which she graduated with an LLB (Honours) from the University Of Leeds, United Kingdom. Linda obtained a Masters Degree as a Graduate of the Global Executive Masters of Business Administration from United States International University, Kenya in collaboration with Columbia University New York, U.S.A. She is a Commissioner for Oaths, Notary Public, Certified Public Secretary (Kenya) and a Professional Director.

9. Mr. Moibi Mose

George Moibi Mose is an Advocate of the High Court of Kenya with over fifteen years experience. He is a Commissioner for Oaths and Notary Public. Mr. Moibi holds a Bachelor of Laws (LLB) degree (Honours) from the University of Nairobi and is currently pursuing a Master of Laws (LLM) from the same institution. Mr. Moibi is a Managing Partner at Ongweny & Moibi Advocates with vast experience in Conveyancing, Civil and Commercial Litigation, Company Secretarial Services, Wills and Estates, Real Estate, Family Court, Election Petitions and Immigration Law. He previously worked at Sichale & Company Advocates as well as Munoru Kagiri & Wamae Advocates.

COMPOSITION OF THE BOARD (Continued)

10. Dr. Thomas Kibua

Dr. Kibua is Director of Academic Programmes at Strathmore University Institute of Public Policy and Governance, Economic Advisor to the Governor of Makueni County and Partner and Senior Economist with African Development and Economic Consultants Ltd (ADEC), a Kenyan firm he co-founded in 1979 and which offers advisory services in economics, management, finance and development. Previously, he served as Director of Health Policy and Systems Research at the African Medical and Research Foundation (April 2008 -March 2011); the Executive Director of the Institute of Policy Analysis and Research (IPAR) a non-governmental think –tank specialising in policy analysis and research (2003-2008); and Chairman of Egerton University Council (2009-2012). He previously taught for many years at the Department of Economics, University of Nairobi. He was Deputy Governor of the Central Bank of Kenya for the statutory period of eight years (1993-2001), served as Advisor to the President of East and Southern Africa Trade and Development Bank (2001), worked on long Term Technical Assistance Programme as Economic Advisor to the Kenyan Ministry of Health (health care financing) (1991-1993) and sat on several Boards of State Corporations (Capital Markets Authority, Export Processing Zones Authority, Export Promotion Council and Deposit Protection Fund) and private companies. Dr. Kibua graduated from the University of Nairobi with a Bachelor's degree and a Master's degree in Economics in April 1974 and June 1976, respectively; a Master's degree in Economics from Yale University, USA, in 1979; and a Doctor of Philosophy degree from the University of Nairobi in 1983. He has extensive hands-on experience in: (a) the management of macro-economic affairs (especially public finance management), (b) university teaching, (c) research, research management and capacity building, (d) knowledge management and (e) and consultancy on development and economic governance and management issues. His areas of specialisation include development economics, economic governance and management (macroeconomic management and public finance management) and quantitative methods. He has written extensively on development and economic policy issues.

11. Mr. Harry Kimtai - (Resigned on May 9, 2017)

Mr. Harry Kimtai is an Economist and holds a Master of Philosophy degree in Economics specialising in Regional Planning and Economic Growth, a Master of Economics degree and a Bachelor degree in Arts from Bhopal University, India. He joined Kenya Revenue Authority as a Management Trainee in 1996 and rose to the rank of Principal Revenue Officer in charge of revenue. In 2007 he joined Branded Fine Foods as General Manager Administration, Planning and Logistics.

12. Ms. Christine Okoth

Christine is currently the Managing Director - MAL Consultancy Limited. She is an experienced Human Resource and Business Leader, with over 15 years of HR and business partnering practice. Prior to her current position, Christine worked at Safaricom Limited where she held several roles including HR Systems and Communications, Head of Talent and Resourcing and Head of HR Business Partnership. She holds a degree in International Relations and Marketing from The United States International University. She is a certified Lead and Internal Auditor, Project Manager, HR Information Systems Manager, Competency Assessor, Organization Design Expert, a Leadership Coach and Mentor. Christine is a member of the Institute of Human Resource Management (IHRM) Kenya, and Chartered Institute of Personnel Development (CIPD) in the United Kingdom.

COMPOSITION OF THE BOARD (Continued)

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). Mr. Ngugi is a Member of the Institute of Directors of Kenya. He has served as Alternate Director to Permanent Secretary, Ministry of Finance in various boards of state corporations including Kenya Roads Board, Housing Finance, Kenya Meat Commission and National Oil Corporation among others. He also served as Director in Kenya Dairy Board and Chairman of the Micro and Small Enterprises Authority (MSEA). He has attended a course in Corporate Governance for Directors and Mwangozo Induction Programme for Boards of State Corporations, among others. Mr. Ngugi was a long serving public servant and retired as Director of Budget at the National Treasury in the year 2013.

14 Mr. Paul M. Muthaura (Chief Executive)

Mr. Muthaura is the 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 and a Masters in Philosophy from the Maastricht School of Management.

CORPORATE SOCIAL RESPONSIBILITY STATEMENT

The Authority recognizes the importance of and its duty to be a responsible corporate citizen and in this context we have due regard to our responsibilities to all our stakeholders including our internal stakeholders. Through the new code of Corporate Governance for Public Issuers of securities we have championed the need for companies to have due regard to Environmental Sustainability & Governance considerations and remain committed to holding ourselves to the same standard.

The Authority undertook an Environmental Sustainability Audit in the 2016/17 Financial Year as part of the Performance Contracting requirements. The Audit noted that the Authority has been involved in tree planting programmes and automated office processes to reduced paper usage, which helped the Authority make its contribution towards reducing the depletion of the forest cover. The Authority will continue implementing the recommendations of the Audit including mainstreaming environmental issues in the coming year.

In its support to environmental and ecosystem sustainability, the Authority contributed Ksh250,000 to the NSE Charity Trading Day, whose key initiative is to support the protection of rhinos in Kenya.

In its efforts to assist Kenyans affected by the drought menace, the Authority contributed Ksh1million towards the National Famine Relief Fund initiative coordinated by the Kenya Red Cross Society and championed by Her Excellency the First Lady of the Republic of Kenya, Mrs. Margaret Kenyatta.

The Authority also continued with sponsorship for the construction of a multipurpose facility to provide students of Nthunguni Secondary School in Machakos County with a modern science laboratory; which is due for completion within 2017/18 Financial Year. During the year the Authority also participated in a Joint initiative with NSE and CDSC and donated business studies books to Shimo La Tewa Secondary School in Mombasa County.

On the internal stakeholders, the following initiatives have been taken:

The Authority remains keen on compliance with the Occupational Safety and Health Act. This is achieved through continuous sensitization on safety in addition to initiatives to optimize work place ergonomics and productivity.

The Authority has on regular basis conducted HIV Testing Services as an initiative for HIV/AIDS prevention as well as establishing access to independent counselling for staff.

The Authority has consistently ensured compliance with the 1/3 gender rule, with the current ratio of Female to Male standing at 44% : 56% respectively thereby exceeding the minimum threshold of 33%.

The Authority also takes into consideration the Face of Kenya when conducting recruitment and promotions respectively for various positions in line with the Presidential initiatives on national values.

In line with the Public Procurement and Asset Disposal Act 2015's requirement on preference and reservations, the Authority has ensured that the Access to Government Procurement Opportunities(AGPO), is maintained to above the minimum 30% threshold, and runs initiatives to empower Youth, Women and Persons with Disabilities to better leverage available opportunities.

The main entrance to the premises was fitted with ramps for ease of access by People With Disabilities(PWD), and deliberate effort is also made to attract PWDs into employment by sharing information with the National Council of Persons with Disability.

**Capital Markets Authority
Report of the board members of the Authority
For the year ended 30th June 2017**

The Board Members of the Authority submit their Report together with the audited financial statements for the year ended 30th June 2017, 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 2017 are set out on page 29.

Board Members of the Authority

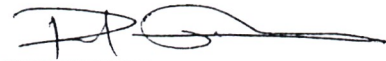
The Board Members of the Authority who held office during the year and to the date of this report are set out on page 3.

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.

Mbaya & Associates Certified Public Accountants were nominated by the Auditor General to carry out the audit of the Authority for the year ended 30th June 2017.

By order of the Board



.....
Chief Executive

Nairobi 14th September..... 2017

*Capital Markets Authority
Statement of the Board Members responsibilities
For the year ended 30th June 2017*

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 four 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 four times during the year and had five special meetings.

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 Dr. Thomas Kibua. 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. The committee met five times in the year.

The Human Resource and Communication Committee

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

The Technical and Policy Committee

The committee consists of five members all of whom are non-executive members of the Board. The committee was chaired by Mr. John Birech. 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

The following were the Ad hoc Committees in the financial year:

- i) The Implementation Committee for the Capital Markets Master Plan- Launched in 2015.
- ii) The Board established the ICT Adhoc Committee in February 2017. It consists of two non executive members of the Board, and three external experts from ICT industry. It is a dedicated ICT Committee to assist in providing Strategic Oversight of ICT at the Authority.

*Capital Markets Authority
Statement of the Board Members responsibilities (Continued)
For the year ended 30th June 2017*

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 2017. 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 Public Finance Management 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 2017, 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 September 14 2017 and signed on its behalf by:



.....
Chairman



.....
Chief Executive

SECTION A

Operational and Financial performance

The Authority promotes and facilitates the development of an ordinary, fair, and efficient Capital Market in Kenya. This mandate has continued to be delivered in the year. Revenue earned was 17% higher than last financial year driven mainly by the market activity. The results in the quarter are a recurrent surplus of 14million, which is 90% drop from previous year.

The Authority is in a strong cashflow position capable of meeting obligations as they fall due. The performance at hand has a bearing on the future market activities. It is of importance to note that any changes affecting investors in the economic, social and political environment, has a significant impact on the capital markets industry.

SECTION B

Compliance with statutory requirements

The Authority is in compliance with all statutory obligations including but not limited to: remittances of PAYE, NHIF, NSSF, VAT, HELB, Withholding tax etc within the stipulated deadlines.

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 of its provisions periodically against case developments and related legal costs. A full provision has been made in the books, and CMA has a prequalified list of legal consultants, from which services are sourced competitively from time to time.

SECTION C

Key projects and investment decisions being implemented

The following is the major project being implemented at CMA.

| Project | Brief description | Viability | Funding | Sustainability |
|---------------------------------|---|--|--------------|---------------------------------|
| Change Management (Uwezo Kipeo) | Cultivating a culture of excellence driven by outcomes, staff empowerment and a globally benchmarked code of conduct and ethics. This involves complete review of how we manage and motivate staff, the single most important resource in achieving the mandate of Authority. | More skills, systems, agility, and raising the capability of CMA to regulate the capital markets, and being ready to take on new challenges in making Kenya a great place to invest. | Donor Funded | The project is fully successful |

SECTION D

Major risks identified in the ERM

The Authority updated its Enterprise Risk Management Framework in 2017, on the basis of which Risk Management has been mainstreamed within the Authority to allow for structured risk assessments on a continuous basis.

The Board is responsible for the Authority's risk management and at least once every quarter receives reports to enable the review, monitoring and evaluation of the implementation and effectiveness of the ERM framework. The Authority in the course of its mandate identified key corporate risks, the associated risk levels, and their mitigation strategies as defined below:

1. Trading, clearing and settlement systems failure

The Authority will mitigate the risk by:

- a). Ensuring implementation of the Principles for Financial Markets Infrastructure and effective business plan by the market players.
- b). Taking enforcement action against violations
- c). Strengthening supervision of the ATS system at NSE and the CDS systems
- d). Carrying out the system audits and ensure strengthening the weaknesses noted.

2. Sub-optimal level of uptake of new and/or existing capital markets products and services

The Authority shall collaborate with relevant stakeholders on investor education and awareness programmes on new products and services to support and successful implementation and maintain an updated database on necessary reforms and continuously review the market to provide guidance to the relevant stakeholders.

3. Negative perception of capital markets by Investors

The Authority shall continuously engage the stakeholders on matters relating to capital markets research initiatives and sensitization forums on capital market products and services. The Authority shall further put in place a robust complaints handling and effective enforcement framework to strengthen investor confidence and promote participation in the markets.

4. Sub-optimal staff capacity

The Authority shall effectively train the staff and align the departmental activities to the corporate activities and projects, while optimizing vacancy ratios and supporting effective learning and development programs.

5. Unfavourable changes in the macro economic environment

The Authority shall monitor the trends on macro economic factors and monitor the policy changes that have an impact on capital markets and execute its mandate as the lead proactivity advisor to government on matters relating to the capital markets.

6. Judicial misapplication of the law

The Authority shall collaborate and partner with relevant bodies to facilitate training on dynamics and regulations, prosecution and continuous legal education involving capital markets.

The Authority will build internal capacity of internal counsel especially on development law to enable proper representation.

SECTION E

Material arrears in statutory/financial obligations

The Authority has no statutory arrears and has been prompt to remit all pension deductions to an independent administrator appointed competitively by the Trustees. The defined contribution Scheme operated has been in Surplus.

There is an existing engagement with KRA for the latter to grant waiver of penalties and interest in line with prior confirmations being pursued in conjunction with the Authority's tax consultants.

SECTION F

Financial probity and serious governance issues

There are no issues of financial improbity reported by any board committee or by external auditors. There are no governance issues and no conflicts of interest at the Board or top management of the Authority.



REPUBLIC OF KENYA

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NAIROBI

OFFICE OF THE AUDITOR-GENERAL

REPORT OF THE AUDITOR-GENERAL ON CAPITAL MARKETS AUTHORITY FOR THE YEAR ENDED 30 JUNE 2017

REPORT ON THE FINANCIAL STATEMENTS

Opinion

The accompanying financial statements of Capital Markets Authority set out on pages 29 to 54, which comprise the statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, statement of cash flows and statement of comparison of budget and actual amounts for the year then ended, and a summary of significant accounting policies and other explanatory information, have been audited on my behalf by Mbaya & Associates, auditors appointed under Section 23 of the Public Audit Act, 2015. 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.

In my opinion, the financial statements present fairly, in all material respects, the financial position of Capital Market Authority as at 30 June 2017, and of its financial performance and its cash flows for the year then ended, in accordance with International Public Sector Accounting Standards (Accrual Basis) and comply with the Capital Market Authority Act, Cap 485A of the Laws of Kenya.

Further, as required by Article 229(6) of the Constitution, based on the procedures performed, I confirm that, nothing has come to my attention to cause me to believe that public money has not been applied lawfully and in an effective way.

Basis for Opinion

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Capital Market Authority in accordance with ISSAI 30 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with ISSAI and accordance with other ethical requirements applicable to performing audits of financial statements in Kenya. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Key Audit Matters

Key audit matters are those matters that, in my professional judgment, are of most significance in the audit of the financial statements. These matters were addressed in

Report of the Auditor-General on the Financial Statements of Capital Markets Authority for the year ended 30 June 2017

the context of the audit of the financial statements, and in forming my opinion thereon, and I do not provide a separate opinion on these matters. For each matter below, a description of how the audit addressed the matter is provided in that context. I have fulfilled the responsibilities described in the Auditor's Responsibilities for the Audit of the Financial Statements section of the report, including in relation to these matters. Accordingly, the audit included the performance of procedures designed to respond to the assessment of the risks of material misstatement of the financial statements. The results of the audit procedures, including the procedures performed to address the matters below, provide the basis for my audit opinion on the accompanying financial statements.

| | Key Audit Matters | How the Audit Addressed the Key Audit Matter |
|----|--|--|
| 1. | <p>Revenue Revenue primarily include; capitalization, rights and new issue fees, NSE – transaction fees, application and licensing fees and market development fees. I treated this as a key audit matter due to its materiality and its status as the main income stream of the organization. The risk for interest income from Investor Compensation Fund (ICF) being recognized as revenue for the authority presents a key audit matter due to the financial significance it has in the financial statements.</p> | <p>I addressed the key audit matter by performing the following procedures:-</p> <ul style="list-style-type: none"> ▪ I evaluated internal control activities, and supporting documentation on revenue recognition, and also performed walkthrough procedures of key controls and confirmed that they were adequate and sufficient. ▪ I inspected significant investment securities and investments instructions and verified the ownership. ▪ I tested revenue recognition by comparing individual income items to the related investment security and verified their accuracy and completeness. |
| 2. | <p>Investments of Investors Compensation Fund As outlined in the financial statements, the Authority holds financial investments worth Kshs.1.88 billion which are valued at their fair value. These included marketable securities, and share investments. I consider that valuing financial assets and financial liabilities at their fair value is a key audit matter, given their significance in the financial statements.</p> | <p>I addressed this key audit matter by performing the following:-</p> <ul style="list-style-type: none"> ▪ I obtained the valuation reports of the quoted equities and verified to the prevailing market values as 30th June 2017. ▪ I reviewed transaction reports of the financial investments during the year with the investors compensation fund account to confirm the investment movements |

| | | |
|----|--|---|
| 3. | <p>Employees Costs</p> <p>I considered this a key audit matter due to the following:-</p> <ul style="list-style-type: none"> ▪ The employee costs absorb 44% of the total income earned by the Authority. ▪ In comparison to the previous year, the employee costs have increased by 22%. ▪ The core mandate of the Authority, as the regulator of the Capital Markets, is personnel driven. | <p>My audit procedures covered assessment of the payroll's internal control environment as well as testing of the operating effectiveness of the related financial controls for accuracy and completeness.</p> <p>I also assessed the recruitment process of the Authority, as well as its staff appraisal process to ensure that the capacity of the Human Resource is sufficient and adequate.</p> |
| 4. | <p>Procurement</p> <p>I considered this a key audit matter due to the materiality of the expenses incurred by the organizations as well as its responsibility as a public entity to ensure compliance with the Public Procurement and Disposal Act and value for money principals were met.</p> | <p>I addressed this key audit matter by inspecting procurement documentation and:-</p> <ul style="list-style-type: none"> ▪ I verified that there was an appropriate level of segregation of duties. ▪ I verified that tender invitation and quotation evaluation processes were performed in a transparent and objective manner. ▪ I analyzed the resultant tender award and noted that the selection process ensured value for money in terms of cost and quality. |

Responsibilities of Management and Those Charged with Governance 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 (Accrual Basis) and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the corporation's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the applicable basis of accounting unless the management either intends to liquidate the Authority or to cease operations, or have no realistic alternative but to do so.

Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 47 of the Public Audit Act, 2015.

Those charged with governance are responsible for overseeing the corporation's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that include my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances and for the purpose of giving an assurance on the effectiveness of the Corporation's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Authority's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up

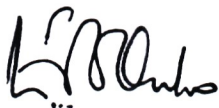
to the date of my audit report. However, future events or conditions may cause the Authority's to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Authority's to express an opinion on the financial statements.
- Perform such other procedures as I consider necessary in the circumstances.

I communicate with the management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

I also provide management with a statement that I have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.

From the matters communicated with management, I determine those matters that were of most significance in the audit of the financial statements and internal control of the current period and are therefore the key audit matters. These matters are described in my auditor's report unless law or regulation precludes public disclosure about the matters or when, in extremely rare circumstances, I determine that a matter should not be communicated in my report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.



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

Nairobi

08 January 2018



Capital Markets Authority
 Financial statements
 For the year ended 30th June 2017

STATEMENT OF FINANCIAL PERFORMANCE FOR THE YEAR ENDED 30TH JUNE 2017

| | Note | 2017 Shs'000 | 2016 Shs'000 |
|---|------|-----------------|-----------------|
| Revenue from non-exchange transactions | | | |
| Capitalization, rights and new issue fees | 6 | 759,059 | 749,682 |
| Donor fund income | 7 | 109,246 | 91,140 |
| | | <u>868,304</u> | <u>840,822</u> |
| Revenue from exchange transactions | | | |
| Other income | 8 | 115,457 | 108,510 |
| Total revenue | | <u>983,761</u> | <u>949,332</u> |
| Expenses | | | |
| Operating expenditure | 30 | (970,011) | (812,206) |
| Total expenses | | (970,011) | (812,206) |
| Other gains/ (losses) | | | |
| (Loss)/Gain on disposal of property and equipment | 9 | (221) | 654 |
| Surplus before tax | 10 | 13,529 | 137,780 |
| Tax expense | 11 | - | - |
| Surplus for the year | | <u>13,529</u> | <u>137,780</u> |

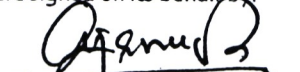
Capital Markets Authority
Financial statements
For the year ended 30th June 2017

STATEMENT OF FINANCIAL POSITION AS AT 30TH JUNE 2017

| | Note | 2017 Shs'000 | 2016 Shs'000 |
|--|-------|-------------------------|-------------------------|
| ASSETS | | | |
| Current assets | | | |
| Inventories | 12 | 1,102 | 1,591 |
| Trade and other receivables from non exchange transactions | 13(a) | 47,639 | 52,154 |
| Trade and other receivables from exchange transactions | 13(b) | 22,134 | 24,780 |
| Staff loans and advances/guarantee fund | 14 | 47,095 | 34,759 |
| Held-to-maturity investments | 15 | 626,967 | 370,934 |
| Cash at bank and in hand | 16 | 64,350 | 269,384 |
| Investors' Compensation Fund | 17 | 689,791 | 512,558 |
| | | <u>1,499,078</u> | <u>1,266,160</u> |
| Non-current assets | | | |
| Property and equipment | 18 | 56,314 | 82,657 |
| Intangible assets | 19 | 6,019 | 4,702 |
| Staff loans and advances/guarantee fund | 14 | 324,292 | 249,175 |
| Held-to-maturity investments | 15 | 260,999 | 341,118 |
| Investors' Compensation Fund's investments | 17 | 1,193,520 | 992,448 |
| | | <u>1,841,144</u> | <u>1,670,100</u> |
| Total Assets | | <u><u>3,340,222</u></u> | <u><u>2,936,260</u></u> |
| Liabilities | | | |
| Current liabilities | | | |
| Trade and other payables | 20 | 168,639 | 139,246 |
| Provision for liabilities and charges | 21 | 85,842 | 95,906 |
| Current tax payable | 22 | - | - |
| Deferred income | 23 | - | 7,200 |
| Investors' Compensation Fund | 17 | 689,790 | 512,558 |
| | | <u>944,271</u> | <u>754,910</u> |
| Non-current liabilities | | | |
| Investors' Compensation Fund liabilities | 17 | 1,193,520 | 992,448 |
| Total liabilities | | <u><u>2,137,791</u></u> | <u><u>1,747,358</u></u> |
| Net assets | | | |
| Funds | | | |
| Capital fund | | 1,202,431 | 1,188,902 |
| General fund | 24 | 27,886 | 27,886 |
| Building fund | 25 | 698,582 | 931,016 |
| | 26 | 475,963 | 230,000 |
| Total Funds | | <u><u>1,202,431</u></u> | <u><u>1,188,902</u></u> |
| Total Funds and Liabilities | | <u><u>3,340,222</u></u> | <u><u>2,936,260</u></u> |

The financial statements set out on pages 29 to 58 were approved for issue by the Board Members of the Authority on 14th September, 2017 and were signed on its behalf by:


Chief Executive


Director, Corporate Services
TCMAK 10 1849


Chairman of the Board

Date: 14th September, 2017

Date: 14th September, 2017

Date: 14th September, 2017

Capital Markets Authority
 Financial statements
 For the year ended 30th June 2016

STATEMENT OF CHANGES IN NET ASSETS FOR THE YEAR ENDED 30TH JUNE 2017

| | Capital fund Shs'000 | General fund Shs'000 | Building fund Shs'000 | Total Shs'000 |
|---------------------------|----------------------------|----------------------------|-----------------------------|------------------|
| At 1st July 2015 | 27,886 | 923,236 | 100,000 | 1,051,122 |
| Surplus for the year | - | 137,780 | - | 137,780 |
| Transfer to building fund | - | (130,000) | 130,000 | - |
| At 30th June 2016 | <u>27,886</u> | <u>931,016</u> | <u>230,000</u> | <u>1,188,902</u> |
| At 1st July 2016 | 27,886 | 931,016 | 230,000 | 1,188,902 |
| Surplus for the year | - | 13,529 | - | 13,529 |
| Transfer to building fund | - | (245,963) | 245,963 | - |
| At 30th June 2017 | <u>27,886</u> | <u>698,582</u> | <u>475,963</u> | <u>1,202,431</u> |

*Capital Markets Authority
Financial statements
For the year ended 30th June 2017*

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 30TH JUNE 2017

| | Note | 2017 Shs'000 | 2016 Shs'000 |
|---|------|------------------|------------------|
| Cash flows from operating activities | | | |
| Surplus for the year | | 13,529 | 137,780 |
| Adjustments for: | | | |
| Tax expense | 11 | - | - |
| Depreciation of property and equipment | 18 | 51,791 | 34,835 |
| Amortisation of intangible assets | 19 | 3,785 | 38,801 |
| Deferred donor funded income | | (7,200) | (34,862) |
| Gain on disposal of property and equipment | 9 | 221 | (654) |
| Interest income | 8 | (100,569) | (101,282) |
| Operating profit before working capital changes | | <u>(38,442)</u> | <u>74,618</u> |
| Decrease/(increase) in: | | | |
| Inventories | | 489 | 449 |
| Trade and other receivables | | 7,161 | 27,119 |
| Staff loans and advances | | (87,453) | (17,709) |
| Increase/(decrease) in: | | | |
| Trade and other payables | | 29,393 | (7,520) |
| Provision for liabilities and charges | | (10,064) | 7,166 |
| Investors' Compensation Fund | | 378,306 | 202,308 |
| Staff benevolent fund | | - | - |
| Cash generated from operations | | <u>279,391</u> | <u>286,431</u> |
| Interest received | 8 | 100,569 | 101,282 |
| Income tax paid | | | <u>(18,007)</u> |
| Net cash generated from operating activities | | <u>379,959</u> | <u>369,706</u> |
| Cash flows from investing activities | | | |
| Purchase of property and equipment | 18 | (26,046) | (12,656) |
| Purchase of intangible assets | 19 | (5,102) | (1,216) |
| Proceeds from disposal of property and equipment | | 376 | 654 |
| Purchase of treasury bonds from the Investors' Compensation Fund | | (194,311) | (177,620) |
| (Purchase)/sale of treasury bills from the Investors' Compensation Fund | | (157,818) | (107,156) |
| (Purchase)/sale of treasury bonds | | 24,716 | 51,681 |
| (Purchase)/sale of treasury bills | | (200,631) | (113,579) |
| Net cash used in from investing activities | | <u>(558,816)</u> | <u>(359,892)</u> |
| Net increase/(decrease) in cash and cash equivalents | | <u>(178,857)</u> | <u>9,814</u> |
| Cash and cash equivalents at start of the year | | <u>338,839</u> | <u>329,025</u> |
| Cash and cash equivalents at end of the year | 16 | <u>159,982</u> | <u>338,839</u> |

Capital Markets Authority
Financial statements
For the year ended 30th June 2017

STATEMENT OF COMPARISON OF BUDGET AND ACTUAL AMOUNTS

| | Approved | | | Actual on | |
|--|--------------------------------|---|--------------------------------------|-------------------------------|---|
| | budget 2016-2017 Shs'000 | Adjustments | Final budget 2016-2017 Shs'000 | basis 2016-2017 Shs'000 | Performance difference 2016-2017 Shs'000 |
| | | (Reallocations) 2016-2017 Shs'000 | | | |
| Revenue | | | | | |
| Fee income from NSE | 561,279 | 0 | 561,279 | 385,547 | (175,732) |
| Licenses and permits | 21,600 | 0 | 21,600 | 19,789 | (1,811) |
| Market development Fees | 13,391 | 0 | 13,391 | 13,023 | (368) |
| Capitalisation and bond approvals | 388,900 | 0 | 388,900 | 340,699 | (48,201) |
| Fee based income | 985,170 | 0 | 985,170 | 759,059 | (226,112) |
| Donor Funding- gifts and services-in-kind | 323,912 | 0 | 323,912 | 109,246 | (214,666) |
| Finance income - external investments | 52,371 | 0 | 52,371 | 100,569 | 48,197 |
| Gains on disposal, rental income and agency fees | - | - | - | (221) | (221) |
| Other income | 3,330 | 0 | 3,330 | 14,888 | 11,558 |
| Total income | 1,364,784 | 0 | 1,364,784 | 983,540 | (381,244) |
| Expenses | | | | | |
| Personnel cost | 482,958 | 0 | 482,958 | 429,889 | 53,069 |
| Rent and maintenance | 54,162 | 0 | 54,162 | 53,365 | 797 |
| Equipment maintenance and stationery | 31,912 | 0 | 31,912 | 29,501 | 2,411 |
| Telephone, postage and utilities | 16,910 | 0 | 16,910 | 14,327 | 2,583 |
| Entertainment and public relations | 40,000 | (3,930) | 36,070 | 33,183 | 2,887 |
| Medical scheme and insurance expenses | 27,975 | 0 | 27,975 | 26,365 | 1,610 |
| Training and conferences | 72,000 | (4,000) | 68,000 | 62,047 | 5,953 |
| Motor vehicle running expenses | 7,600 | 0 | 7,600 | 6,113 | 1,487 |
| Subscriptions and IOSCO membership Authority board members' emoluments and allowance | 14,875 | - | 14,875 | 11,946 | 2,929 |
| Professional & consultancy services | 36,949 | 0 | 36,949 | 36,968 | (19) |
| Litigation/legal expenses | 22,190 | 20,465 | 42,655 | 31,148 | 11,507 |
| Market Development & Islamic Finance | 24,000 | (12,595) | 11,405 | (346) | 11,751 |
| Capital Markets Masterplan | 55,344 | 10,817 | 66,161 | 39,893 | 26,268 |
| Donor Funded Projects | 20,000 | (11,700) | 8,300 | 4,891 | 3,409 |
| Depreciation of property, plant and equipment | 287,667 | 0 | 287,667 | 102,521 | 185,146 |
| Amortisation of intangible assets | 55,927 | 0 | 55,927 | 51,791 | 4,136 |
| Auditor's remuneration | 62,294 | 0 | 62,294 | 3,785 | 58,509 |
| Investors' education and awareness programme | 817 | 943 | 1,760 | 1,760 | 0 |
| Tribunal expenses | 35,000 | 0 | 35,000 | 26,767 | 8,233 |
| | 5,194 | 0 | 5,194 | 4,097 | 1,097 |
| Total expenditure | 1,353,774 | 0 | 1,353,774 | 970,011 | 383,762 |
| Surplus for the period | 11,010 | 0 | 11,010 | 13,529 | 2,519 |

The Authority has not recognized in the financial statements items for which commitments in the budget had been made amounting to Ksh29.5million(2016:Ksh7.8million).This in compliance to IPSAS19.The procurement of the same had been completed in 2016/17 but the delivery was made in 2017/18.(Note 28b)

In its 279th meeting held on 28th April 2017, the Board approved reallocation of budget to market intervention and professional and consultancy votes respectively; from training & development, market development, Capital Markets Master-Plan and legal /litigation votes respectively, totalling to Ksh30million. This was to facilitate forensic audit/investigations of operations of past Management and Board of Mumias Sugar Company Ltd; conducted through the firm of M/S J. Miles Limited.

*Capital Markets Authority
Financial statements
For the year ended 30th June 2017*

STATEMENT OF COMPARISON OF BUDGET AND ACTUAL AMOUNTS (CONTINUED)

Notes on Significant variances (10% and above) between actual and budget.

REVENUE

- a) Finance income from NSE was affected by the low market trading volumes in the year .
- b) The performance of the Capitalization and bond approvals fees was lower than budget arising from low market activity from mainly institutions(borrowers), than anticipated in the year.
- c) Donor Funding- gifts and services-in-kind was low, since substantial portions of the Projects being supported by donor funding have been extended for delivery in 2017/18 FY.
- d) Finance income from external investments was above the budget as the Authority continued investing excess cash per policy.
- e) Other income line was above budget arising from partnering support for investor education activities, coupled with refund for legal costs incurred in prior years.

EXPENDITURE

- a) The Authority's staff complement was gradually filled in the year, and the Personnel cost was well within the budget.
- b) Telephone, postage and utilities was below budget due to cost control strategies that the Authority continued to implement in the year .
- c) Motor vehicle running expenses was within the budget as cost control strategies (e.g. use of fuel cards, negotiated transport rates, pooling of taxi cabs) contributed to the low costs.
- d) Subscriptions and IOSCO membership expenses was within the budget and all programmed IOSCO engagements in the year were undertaken , well within the allocated budget.
- e) Professional & consultancy services expenses were spent below budget, as there were some carry over of activities into next year.
- f) Litigation/legal costs was lower than budget as the number of prior year provisions were reversed, due to several respondents to some cases negotiating for out of court settlement. This is in line with enhancement of alternative resolution mechanisms.
- g) Market Development & Islamic Finance expenses were lower than budget due to support of programmes by donor funding .
- h) Capital Markets Masterplan expenses was below budget as the main activities in the implementation road maps still under working group review and development.
- i) Donor Funded Projects cost was lower than budget as some of the donor funded projects targeted to be started and completed in the year didn't kick off in time due to lengthy kick off logistical reasons.
- j) Amortisation of intangible assets was well within the budget level as few intangible assets were acquired.
- k) Investors' education and awareness programme expenses was below budget as partnering(cost sharing) with other stakeholders was improvised for some of the activities undertaken.
- l) Although substantial number of meetings were held, the Tribunal's other activities (like training) were minimal hence the cost was well within the budget.

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). 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 indirect method. The financial statements are prepared on accrual basis.

The Authority adopted IPSAS in the year 2014 following the gazette of the Public Sector Accounting Standards Board (PSASB) which was established by the Public Financial Management Act (PFM) No.18 of 24th July 2012. PSASB issued financial reporting standards and guidelines to be adopted by all state organs and public sector entities, which the Authority complies with.

2. ADOPTION OF NEW AND REVISED STANDARDS

New and amended standards and interpretations in issue but not yet effective in the year ended 30 June 2017

| Standard | Impact |
|--------------------------------------|--|
| IPSAS 39: Employee Benefits | <p>Applicable: 1st January 2018</p> <p>The objective to issue IPSAS 39 was to create convergence to changes in IAS 19 Employee benefits. The IPSASB needed to create convergence of IPSAS 25 to the amendments done to IAS 19. The main objective is to ensure accurate information relating to pension liabilities arising from the defined benefit scheme by doing away with the corridor approach.</p> |
| IPSAS 40: Public Sector Combinations | <p>Applicable: 1st January 2019:</p> <p>The standard covers public sector combinations arising from exchange transactions in which case they are treated similarly with IFRS 3 (applicable to acquisitions only) Business combinations and combinations arising from non exchange transactions which are covered purely under Public Sector combinations as amalgamations.</p> |

3. 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.

Donor Income

Donor funds are received through Government supported programmes and other development Agencies. These funds are recognised at fair value when there is reasonable assurance that the Authority will comply with the conditions attaching to them and the funds will be received. Donor funds 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 as it is earned over the life of the investments held .

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)

3. Summary of significant accounting policies (continued)

c) Taxes

Current income tax

The Authority is exempt from income tax vide PFMA regulation no.34 of 2015.

On 20th March 2015, The National Treasury issued PFMA Regulation No. 34 which under Section 219 exempts the Authority from paying taxes in the future. The Authority will however be required to submit 90% of its surplus to the National Treasury.

d) Property and equipment

All property 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 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.

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 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.

NOTES (CONTINUED)

3. Summary of significant accounting policies (continued)

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.

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 an entity 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.
- iv) 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.

NOTES (CONTINUED)

3. Summary of significant accounting policies (continued)

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 not remote.

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 various commercial banks at the end of the financial year.

The Authority manages the Investor Compensation Fund (ICF) and reports the funds held in the bank, call accounts on behalf of ICF as part of cash and cash equivalents.

NOTES (CONTINUED)

3. Summary of significant accounting policies (continued)

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.

4. 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:

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

The pensions contributions into the Defined Contribution (DC) Scheme are expensed as incurred in the year

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.

NOTES (CONTINUED)

5. 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.

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 institute

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.

| | Fully performing Shs'000 | Past due but not impaired Shs'000 | Impaired Shs'000 | Total Shs'000 |
|------------------------------------|-----------------------------|--------------------------------------|---------------------|------------------|
| At 30th June 2017 | | | | |
| Held-to-maturity investments | 887,966 | - | - | 887,966 |
| Staff loans and advances/ fund | 367,208 | - | 4,179 | 371,387 |
| Trade receivables | 48,089 | - | - | 48,089 |
| Other receivables | 13,219 | - | - | 13,219 |
| Cash at bank, in hand and deposits | 64,210 | - | - | 64,210 |
| Maximum exposure to credit risk | <u>1,380,691</u> | <u>-</u> | <u>-</u> | <u>1,384,870</u> |
| At 30th June 2016 | | | | |
| Held-to-maturity investments | 712,052 | - | - | 712,052 |
| Staff loans and advances/ fund | 279,755 | - | 4,179 | 283,934 |
| Trade receivables | 53,120 | - | - | 53,120 |
| Other receivables | 6,812 | - | - | 6,812 |
| Cash at bank, in hand and deposits | 269,244 | - | - | 269,244 |
| Maximum exposure to credit risk | <u>1,320,983</u> | <u>-</u> | <u>4,179</u> | <u>1,325,162</u> |

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

| | 2017 Shs'000 | 2016 Shs'000 |
|---------------|-----------------|-----------------|
| Over 6 months | <u>4,179</u> | <u>4,179</u> |
| | <u>4,179</u> | <u>4,179</u> |

The past due debtors are nil. An impairment provision of Shs 4,104,000 (2016: Shs 57,866,000) 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.

5. Risk management objectives and policies (continued)

a) Financial risk management (continued)

ii) Liquidity risk (continued)

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 |
|---------------------------------------|-----------------------------------|----------------------------------|-----------------------------------|---------------------------|------------------|
| Year ended 30th June 2017 | | | | | |
| Trade and other payables | 41,443 | | 196 | | 41,639 |
| Accruals | 31,079 | | 3,144 | 9,110 | 43,333 |
| Provision for liabilities and charges | 42,338 | | 28,060 | | 70,398 |
| Gratuity obligations | 13,269 | | | | 13,269 |
| | <u>128,129</u> | <u>0</u> | <u>31,400</u> | <u>9,110</u> | <u>168,639</u> |
| Year ended 30th June 2016 | | | | | |
| Trade and other payables | 19,766 | 1,290 | | | 21,056 |
| Accruals | 32,029 | | 19,005 | | 51,034 |
| Provision | 25,074 | 3,813 | 27,654 | | 56,541 |
| Gratuity obligations | 10,615 | | | | 10,615 |
| | <u>87,484</u> | <u>5,103</u> | <u>46,659</u> | | <u>139,246</u> |

iii) Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market price and comprises three types of risks: interest rate risk, price risk and foreign exchange risk.

Interest rate risk

Interest rate risk is the risk that the interest rate movement may have a significant impact on Authority's value of investments.

The Authority's investments in fixed rate bonds expose it to fair value interest rate risk. The Authority has no interest bearing liabilities. The Authority considers that a change in interest rates of 2 percentage points in the year ending 30th June 2017 is reasonably possible. If the interest rates on the Authority's held-to-maturity investments at the year-end were to decrease/increase by this number of percentage points, with all other factors remaining constant, the surplus would be lower/higher by KShs13million (2016: Shs 14,241,000).

Price risk

Marketable instruments held by the Authority include Treasury Bonds and Treasury Bills whose market prices are subject to change. The Authority review the portfolio, set exposure limits and respond to market price changes and conditions to secure both fair values and cash flow from such instruments.

Foreign exchange risk

Foreign exchange risk would arise where transactions or bank balances are denominated in foreign currency. The Authority's transactions and bank balances are denominated in Kenya Shillings. Hence the exposure to foreign exchange risk does not exist.

NOTES (CONTINUED)

6. Revenue from non - exchange transactions

| | 2017 Shs'000 | 2016 Shs'000 |
|---|-----------------|-----------------|
| Fees income | | |
| Capitalization, rights and new issue fees | | |
| NSE - transaction fees | 340,699 | 268,194 |
| Application and licensing fees | 385,547 | 434,945 |
| Market development fees | 19,789 | 33,404 |
| | <u>13,023</u> | <u>13,139</u> |
| | <u>759,059</u> | <u>749,682</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.

7. Donor fund income

| | 2017 Shs'000 | 2016 Shs'000 |
|-------------------|-----------------|-----------------|
| Donor fund income | <u>109,246</u> | <u>91,140</u> |

The Authority received support worth Shs69.7 million (2015:Shs56.4 million) in the year to support institutional capacity for Islamic Finance deepening study and for the change management support initiative "Uwezo Kipeo". A further Shs 7.2 million (2015: Shs34.9million) was recognized from deferred income related purchase of Enterprise Resource Planning(ERP) software, Risk Based Supervision System (RBSS) and related Information Technology (ICT systems).

8. Revenue from exchange transactions - other income

| | 2017 Shs'000 | 2016 Shs'000 |
|----------------------|-----------------|-----------------|
| Interest income | 100,569 | 101,282 |
| Miscellaneous income | <u>14,888</u> | <u>7,228</u> |
| | <u>115,457</u> | <u>108,510</u> |

9. (Loss)/Gain on disposal of property and equipment

| | | |
|---|--------------|------------|
| Gain or (loss) on disposal of obsolete and retired Property and Equipment | <u>(221)</u> | <u>654</u> |
|---|--------------|------------|

10. Surplus before tax

| a) Items charged | Note | 2017 Shs'000 | 2016 Shs'000 |
|------------------|------|-----------------|-----------------|
|------------------|------|-----------------|-----------------|

The following items have been charged in arriving at net surplus for the year

| | | | |
|---|-------|--------|--------|
| Depreciation of property and equipment | 17 | 51,791 | 34,835 |
| Amortisation of intangible assets | 18 | 3,785 | 38,801 |
| Authority board members' emoluments, allowances and other Board | 27 | 36,968 | 26,974 |
| Post employment benefits expense (Note 9(b)) | 10(b) | 31,763 | 23,137 |
| Provision for impairment of financial assets | | | |
| Trade and other receivables | | | |

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NOTES (CONTINUED)

10. Net surplus for the year (continued)

| b) Employee benefits expense | 2017 Shs'000 | 2016 Shs'000 |
|--|-----------------|-----------------|
| The following items are included in employee benefits expense: | | |
| Retirement benefit costs | | |
| Defined contribution scheme | 31,451 | 22,870 |
| National Social Security Fund | <u>312</u> | <u>267</u> |
| | <u>31,763</u> | <u>23,137</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.

Though the scheme is subjected to triennial valuations by independent actuaries to fulfil the statutory requirements under the Income Tax (Retirement Benefits) Rules 1994 and the Retirement Benefits Rules 2000, the scheme is in the process of purchasing annuities for the 3 pensioners, and the winding up cause will begin. Hence the valuation will not be necessary once it becomes due. All active members already transferred to DC scheme, and all the pensioners will have an annuity in force.

The scheme has sufficient funding for the annuity arrangement, and for the winding up process.

11. Tax expense

| | 2017 Shs'000 | 2016 Shs'000 |
|---|-------------------|-------------------|
| Current income tax | - | - |
| Deferred income tax (Note 19) | <u>-</u> | <u>-</u> |
| Income tax expense | <u>-</u> | <u>-</u> |
| Surplus before income tax | <u> </u> | <u> </u> |
| Tax calculated at the statutory tax rate of 30% | 0 | 0 |
| Tax effect of: | | |
| Deferred tax asset not recognised | - | - |
| Income not subject to tax | 0 | 0 |
| Expenses not deductible for tax purposes | <u>-</u> | <u>-</u> |
| Income tax expense | <u>-</u> | <u>-</u> |

On 20th March 2015, The National Treasury issued PFMA Regulation No.34 which under section 219 exempts the Authority from paying taxes in the future. The regulation requires corporations exempted from income tax to remit 90% of surplus to National Treasury. No remission was done in the year.

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NOTES (CONTINUED)

| | 2017 Shs'000 | 2016 Shs'000 | | | | |
|--|----------------------------|----------------------------|---------------------------------|------------------------------------|--------------------------|--------------------------|
| 12. Inventories | | | | | | |
| Consumables | 1,102 | 1,591 | | | | |
| Inventories consist of stationery and computer consumables required for day to day use by the Authority. | | | | | | |
| 13a. Trade and other receivables from non exchange transactions | | | | | | |
| Trade receivables | 47,382 | 53,923 | | | | |
| Statutory management expenses receivable | - | 49,286 | | | | |
| Less: Provision for impairment losses | (4,104) | (57,866) | | | | |
| Net trade receivables | 43,278 | 45,343 | | | | |
| Other receivables | 4,361 | 6,811 | | | | |
| Trade and other receivables from non exchange transactions | 47,639 | 52,154 | | | | |
| 13b. Trade and other receivables from exchange transactions | | | | | | |
| Trade receivables | 4,811 | 7,985 | | | | |
| Less: Provision for impairment losses | - | (208) | | | | |
| Net trade receivables | 4,811 | 7,777 | | | | |
| Prepayments | 17,323 | 17,003 | | | | |
| Trade and other receivables from exchange transactions | 22,134 | 24,780 | | | | |
| Total trade and other receivables from non exchange and exchange transactions | 69,773 | 76,934 | | | | |
| The movement on the provision for impairment losses for non exchange transactions is as follows: | | | | | | |
| At 1st July | 57,866 | 57,616 | | | | |
| Less: Provision utilised as debts written off | (53,762) | 250 | | | | |
| Less: Provision reversed on debt collection | - | - | | | | |
| At 30th June | 4,104 | 57,866 | | | | |
| The movement on the provision for impairment losses for exchange transactions is as follows: | | | | | | |
| At 1st July | 208 | 208 | | | | |
| Add: Additional provision | (208) | - | | | | |
| At 30th June | 0 | 208 | | | | |
| 14. Staff loans and advances | | | | | | |
| | Current 2017 Shs'000 | Current 2016 Shs'000 | Non- current 2017 Shs'000 | Non- current 2016 Shs'000 | Total 2017 Shs'000 | Total 2016 Shs'000 |
| Car loans | 10,177 | 10,032 | 23,455 | 19,968 | 33,632 | 30,000 |
| Other loans and advances | 4,921 | 1,103 | - | - | 4,921 | 1,103 |
| Provision for impairment losses | - | - | (1,922) | (1,922) | (1,922) | (1,922) |
| Miscellaneous advances | - | - | 4,179 | 4,179 | 4,179 | 4,179 |
| Staff mortgage back up funds* | 31,996 | 23,624 | 298,580 | 226,950 | 330,577 | 250,574 |
| | 47,094 | 34,759 | 324,292 | 249,175 | 371,386 | 283,934 |

* These funds are deposited with the bank to support concessionary interest rate facilities to staff.

Mortgage back up accounts are:

HFC: Mortgage 3000013543 and Mortgage 2000094161

KCB Mortgage MM1509100194

Total

Shs'000
140,872
189,705
330,577

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NOTES (CONTINUED)

| 15. Held-to-maturity investments - government securities | 2017 Shs'000 | 2016 Shs'000 |
|--|-----------------|-----------------|
| Non-current | | |
| Treasury bonds | | |
| Maturing after four years | 155,375 | 155,375 |
| Unamortised premium | <u>(11,525)</u> | <u>(13,055)</u> |
| | <u>143,850</u> | <u>142,320</u> |
| | | |
| Treasury bonds | | |
| Maturing after one year | 117,153 | 197,976 |
| Unamortised (discount)/premium | <u>(4)</u> | <u>822</u> |
| | <u>117,149</u> | <u>198,798</u> |
| | <u>260,999</u> | <u>341,118</u> |
| | | |
| Current | | |
| Treasury bonds | | |
| Maturing within one year | 75,000 | 20,000 |
| Unamortised premium | <u>403</u> | <u>-</u> |
| | <u>75,403</u> | <u>20,000</u> |
| | | |
| Treasury bills | 581,600 | 362,000 |
| Unamortised discount | <u>(30,036)</u> | <u>(11,066)</u> |
| | <u>551,564</u> | <u>350,934</u> |
| | <u>626,967</u> | <u>370,934</u> |
| | <u>887,966</u> | <u>712,052</u> |

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

| | | |
|------------------------------|----------------|----------------|
| Non- current | | |
| Held-to-maturity investments | <u>260,999</u> | <u>341,118</u> |
| | | |
| Current | | |
| Held-to-maturity investments | <u>626,967</u> | <u>370,934</u> |

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NOTES (CONTINUED)

| | | | | 2017 | 2016 |
|------------------------------------|-----------------------------------|-------------------------|-------------------------|----------------------|-----------------------|
| | | | | Shs'000 | Shs'000 |
| 16a. Banks | | | | | |
| | Name of the Bank | Bank account no. | Account currency | | |
| | Commercial Bank of Africa Limited | 6580810018 | Shs | 5,520 | 20,487 |
| 16b. Cash in hand | | | | | |
| | Cash in hand | | Shs | 140 | 140 |
| 16c. Short term deposits | | | | | |
| | Commercial Bank of Africa Limited | MM1718100068 | Shs | 20,000 | 25,374 |
| | Commercial Bank of Africa Limited | MM1718100101 | Shs | 7,000 | 137,946 |
| | HFC Bank | A/c 1345823403-0 | Shs | 31,690 | 85,437 |
| | | | | <u>58,690</u> | <u>248,757</u> |
| Total cash in hand and bank | | | | <u><u>64,350</u></u> | <u><u>269,384</u></u> |

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

| | | |
|--|----------------|----------------|
| Short-term bank deposits | 58,690 | 248,757 |
| Cash at bank and in hand | 5,660 | 20,627 |
| Investors Compensation Fund bank balance (Note 16) - (KCB) | 3,632 | 15,455 |
| Investors Compensation Fund bank balance (Note 16) - (Call accounts - KCB) | 92,000 | 54,000 |
| | <u>159,982</u> | <u>338,839</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:

- Interest accruing on funds received from subscribers to public issues, between the day of closing the issue and making the refunds.
- 0.01% of the consideration from sale and purchase of shares through the Nairobi Securities Exchange.
- 0.004% of the consideration from sale and purchase of bonds traded through the Nairobi Securities Exchange.
- Interest earned from investment of the funds held in this account.
- 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:

| | 2017 | 2016 |
|--|-------------------------|-------------------------|
| | Shs'000 | Shs'000 |
| At beginning of the year | | |
| Nairobi Securities Exchange transactions fees | 1,505,006 | 1,298,437 |
| Interest on investments | 63,819 | 65,621 |
| Financial penalties | 169,773 | 148,578 |
| Management fees | 162,284 | 784 |
| Gain/(loss) in Investment in NSE | (500) | (500) |
| Compensation to Discount Securities/Nyaga Stockbrokers Ltd investors | (17,754) | 4,261 |
| | 683 | (12,175) |
| At end of the year | <u><u>1,883,311</u></u> | <u><u>1,505,006</u></u> |

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NOTES (CONTINUED)

17. Investors' Compensation Fund (continued)

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

| | 2017 Shs'000 | 2016 Shs'000 |
|--|------------------|------------------|
| Non-current | | |
| Equity investment in the Central Depository and Settlement | 7,000 | 7,000 |
| Equity investment in the NSE | <u>109,594</u> | <u>130,922</u> |
| | 116,594 | 137,922 |
| Treasury bonds | | |
| Maturing after five years | 737,000 | 685,550 |
| Unamortised discount (premium) | <u>(9,977)</u> | <u>(13,662)</u> |
| | <u>727,023</u> | <u>671,888</u> |
| Maturing after one year | 348,250 | 182,100 |
| Unamortised discount | <u>1,654</u> | <u>538</u> |
| | <u>349,904</u> | <u>182,638</u> |
| | <u>1,076,926</u> | <u>854,526</u> |
| | <u>1,193,520</u> | <u>992,448</u> |
| Current | | |
| Treasury bonds | 35,000 | 42,000 |
| Unamortised discount | <u>231</u> | <u>(8)</u> |
| | <u>35,231</u> | <u>41,992</u> |
| Treasury bills | 554,950 | 391,500 |
| Unamortised discount | <u>(29,729)</u> | <u>(13,840)</u> |
| | <u>525,221</u> | <u>377,660</u> |
| Fees receivable | 33,707 | 23,451 |
| Bank balance | 3,632 | 15,455 |
| Call account | <u>92,000</u> | <u>54,000</u> |
| | <u>129,339</u> | <u>92,906</u> |
| | <u>689,791</u> | <u>512,558</u> |
| | <u>1,883,311</u> | <u>1,505,006</u> |

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NOTES (CONTINUED)

| 18. Property 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 |
|---|---------------------------|---------------------------------------|-----------------------------|---------------------------------|-------------------------------------|------------------|
| Cost | | | | | | |
| At 1st July 2015 | 24,188 | 108,420 | 21,542 | 84,976 | 74 | 239,200 |
| Additions | - | 6,868 | 2,582 | 3,206 | - | 12,656 |
| | -- | (157) | 0 | 0 | - | (2,253) |
| Disposals | 0 | 0 | 0 | 0 | (74) | (74) |
| At 30th June 2016 | 22,092 | 115,131 | 24,124 | 88,182 | 0 | 249,529 |
| Additions | 7,726 | 7,309 | 3,934 | 3,039 | 4,037 | 26,045 |
| Disposals | | (9,365) | (3,639) | (3,254) | | (16,258) |
| Reversal | | | | | | 0 |
| At 30th June 2017 | 29,818 | 113,075 | 24,419 | 87,968 | 4,037 | 259,317 |
| Depreciation | | | | | | |
| At 1st July 2015 | (15,994) | (70,148) | (15,308) | (32,840) | - | (134,290) |
| Depreciation | (3,631) | (18,787) | (1,966) | (10,451) | - | (34,835) |
| Accumulated depreciation reversed on disposal | 2,096 | 157 | 0 | 0 | - | 2,253 |
| At 30th June 2016 | (17,529) | (88,778) | (17,274) | (43,291) | - | (166,872) |
| Depreciation | (4,028) | (17,864) | (2,416) | (27,484) | | (51,791) |
| Accumulated depreciation reversed on disposal | | 9,365 | 3,639 | 2,656 | | 15,660 |
| At 30th June 2017 | (21,557) | (97,276) | (16,052) | (68,119) | - | (203,003) |
| Net carrying amount | | | | | | |
| At 30th June 2017 | 8,261 | 15,798 | 8,368 | 19,849 | 4,037 | 56,314 |
| At 30th June 2016 | 4,563 | 26,353 | 6,850 | 44,891 | 0 | 82,657 |

Included above in the items of property and equipment is the cost of fully depreciated assets of Shs 136,126,943(2016: Shs 65,296,641) which are still in use and have not been impaired. Work in progress was carried at cost.

Work in progress relates to the refurbishment works that are progressing of the 6th floor space that the Authority has newly occupied. The commissioning and office utilization is in the month of July 2017. The detailed works are as follows:

| Description | Cost Ksh'000 |
|--|-----------------|
| i.) Tiling & Wood skirting for the 6th floor | 990.00 |
| ii.) Cabling works for the 6th floor | 2,187.00 |
| iii.) Ceiling repairs for the 6th floor | 39.00 |
| iv.) Electrical cabling for the 6th floor | 382.00 |
| v.) Biometric Access Control for the 6th Floor | 439.00 |
| Total | 4,037.00 |

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NOTES (CONTINUED)

| | Intangible assets Shs'000 |
|-----------------------------------|---------------------------------|
| 19. Intangible assets | |
| Software costs | |
| Cost | |
| At 1st July 2015 | 159,862 |
| Additions | 1,216 |
| Derecognition of intangible asset | |
| At 30th June 2016 | <u>161,078</u> |
| Additions | 5,102 |
| | <u>166,180</u> |
| At 30th June 2017 | <u><u>166,180</u></u> |
| Amortisation | |
| At 1st July 2015 | 117,575 |
| Amortisation | 38,801 |
| At 30th June 2016 | <u>156,376</u> |
| Amortisation | 3,785 |
| | <u>160,161</u> |
| At 30th June 2017 | <u><u>160,161</u></u> |
| Net book value | |
| At 30th June 2017 | <u><u>6,019</u></u> |
| At 30th June 2016 | <u><u>4,702</u></u> |

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NOTES (CONTINUED)

| | 2017 Shs'000 | 2016 Shs'000 |
|-------------------------------------|-----------------|-----------------|
| 20. Trade and other payables | | |
| Trade payables | 41,639 | 21,056 |
| Provisions | 70,398 | 56,541 |
| Gratuity obligations | 13,269 | 10,615 |
| Accruals | 43,333 | 51,034 |
| | <u>168,640</u> | <u>139,246</u> |

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

| Provisions | Leave benefits Shs'000 | Performance Shs'000 | Total Shs'000 |
|------------------------------|---------------------------|------------------------|------------------|
| | At 1st July 2016 | 12,864 | 43,677 |
| Additional provisions raised | 16,505 | 25,833 | 42,338 |
| Provision utilized/reversed | (12,864) | (15,617) | (28,481) |
| At 30th June 2017 | <u>16,505</u> | <u>53,893</u> | <u>70,398</u> |

| Accruals | Consultancies Shs'000 | Other Provisions Shs'000 | Total Shs'000 |
|---------------------|--------------------------|--------------------------------|------------------|
| | At 1st July 2016 | 8,956 | 42,078 |
| Additional accruals | 1,726 | 19,434 | 21,160 |
| Accruals realized | (742) | (27,977) | (28,719) |
| At 30th June 2017 | <u>9,940</u> | <u>33,535</u> | <u>43,475</u> |

21. Provision for liabilities and charges

| | | |
|------------------------------|---------------|---------------|
| At 1st July 2016 | 95,906 | 88,740 |
| Add: Additional provision | 6,672 | 8,044 |
| Less: Provision written back | (16,736) | (878) |
| At 30th June 2017 | <u>85,842</u> | <u>95,906</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 of its provisions periodically against case developments and related legal costs.

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NOTES (CONTINUED)

| | | |
|--|------------------|------------------|
| 22. Current tax payable | 2017 Shs'000 | 2016 Shs'000 |
| Current year tax | <u>-</u> | <u>-</u> |
| 23. Deferred income | | |
| In line with the Authority's accounting policy, Nil (2016: Shs 7,200,000) of the donor funded income has been deferred for future periods. | | |
| | 2017 Shs'000 | 2016 Shs'000 |
| At 1 July | 7,200 | 42,062 |
| Recognised in the year | <u>(7,200)</u> | <u>(34,862)</u> |
| At 30 June | <u>-</u> | <u>7,200</u> |
| 24. Capital fund | | |
| At 1st July 2016 and at 30th June 2017 | <u>27,886</u> | <u>27,886</u> |
| Capital fund represents the initial contribution by the Government of Kenya towards the establishment of the Capital Markets Authority. | | |
| 25. General fund | 2017 Shs'000 | 2016 Shs'000 |
| At 1 July | 931,016 | 923,236 |
| Surplus for the year | 13,529 | 137,780 |
| Transfer to building fund (Note 26) | <u>(245,963)</u> | <u>(130,000)</u> |
| At 30 June | <u>698,582</u> | <u>931,016</u> |
| General fund represents accumulated surpluses over the years. | | |
| 26. Building fund | 2017 Shs'000 | 2016 Shs'000 |
| At 1 July | 230,000 | 100,000 |
| Appropriation from general fund (Note 25) | <u>245,963</u> | <u>130,000</u> |
| At 30 June | <u>475,963</u> | <u>230,000</u> |
| Building fund represents an appropriation from the general fund towards the construction of the Authority's future building. The appropriations are in line with the approved budget for the year. | | |
| 27. Related party transactions | 2017 Shs'000 | 2016 Shs'000 |
| i) Board members of the Authority' remuneration | | |
| Honoraria | 1,044 | 1,044 |
| Retainer | 8,498 | 6,926 |
| Sitting allowances | 8,140 | 5,567 |
| Training expenses | 7,622 | 3,648 |
| Others (medical, mileage, bonus) | <u>11,664</u> | <u>9,789</u> |
| | <u>36,968</u> | <u>26,974</u> |
| There were 10 board members during the year (2016:10) | | |
| ii) Key management compensation | | |
| Gross salaries | 36,958 | 35,600 |
| Pension | 313 | 680 |
| Gratuity | <u>8,252</u> | <u>6,684</u> |
| | <u>45,523</u> | <u>42,964</u> |
| There were 4 members of senior management who served during the year (2016:5) | | |

NOTES (CONTINUED)

28. Commitments

a. Contracted for but not recognised

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

| | 2017 Shs'000 | 2016 Shs'000 |
|--------------------------------------|-----------------|-----------------|
| Capital expenditure contracted for | 10,000 | 8,049 |
| Recurrent expenditure contracted for | 19,505 | 7,826 |
| | <u>29,505</u> | <u>15,875</u> |

b. Item description

| | Capital Shs'000 | Recurrent Shs'000 | Total Shs'000 |
|---|--------------------|----------------------|------------------|
| Consultancy to review & design the securities market surveillance system at CMA | | 7,900 | 7,900 |
| Consultancy to develop specifications for E-learning system | | 4,000 | 4,000 |
| Consultancy to develop specifications for advanced financial analysis system | | 4,000 | 4,000 |
| Consultancy for Value for Money; with a view to adopt best practice policy | - | 3,605 | 3,605 |
| Business Intelligence system | 10,000 | - | 10,000 |
| Total | <u>10,000</u> | <u>19,505</u> | <u>29,505</u> |

Operating lease commitments

Operating lease commitments represent rentals payable by the Authority for rented office space. Rental expenses during the year amounted to Shs 45,783,000 (2016: Shs42,915,000).

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

| | 2017 Shs'000 | 2016 Shs'000 |
|--|-----------------|-----------------|
| Not later than 1 year | 45,783 | 42,915 |
| Later than 1 year and not later than 5 years | 165,510 | 128,745 |
| | <u>211,293</u> | <u>171,660</u> |

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

NOTES (CONTINUED)

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 46 million. The cost has not been recognised in the books, since based on professional advice, it is likely that the outcome of the suit will be in favour of the Authority and will not materially impact on these financial statements.

- b) In the normal course of operation, Kenya Revenue Authority (KRA) had completed a tax audit for the period 2007 to 2012 and had issued an assessment notice. The total tax liability arising from the year 2012 assessment was Shs 46 million. The Authority in conjunction with its tax agents has been following up on the outstanding tax issues raised. Principal tax arrears amounting to Shs 12 million were paid in the previous years 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. The KRA has in the course of the financial year 2015/16 granted full waiver of interest and penalties for the years 2003-2009 estimated at Shs9.5million. The balance on the Statement of Account (comprising of penalties and interest for the years 2010-2012), for which waiver was applied for is being addressed by KRA. Based on the professional advice received and the mitigating grounds 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
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NOTES (CONTINUED)

| | 2017 Kshs'000 | 2016 Kshs'000 |
|--|-----------------------|-----------------------|
| 30. Operating expenditure | | |
| 30.1 Employment expense | | |
| Consolidated pay, leave pay and passages | 377,940 | 312,946 |
| Staff uniform expenses | 85 | 228 |
| Staff welfare and other costs | 10,560 | 9,428 |
| Staff retirement benefits | 31,451 | 22,870 |
| Staff gratuity | 9,541 | 6,684 |
| National Social Security Fund (NSSF) | <u>312</u> | <u>267</u> |
| | <u>429,889</u> | <u>352,423</u> |
| 30.2 Other administrative expenses | | |
| Rent and maintenance | 53,365 | 47,818 |
| Equipment maintenance and stationery | 29,501 | 30,099 |
| Telephone, postage and utilities | 14,327 | 12,337 |
| Entertainment and public relations | 33,183 | 32,835 |
| Medical scheme and insurance expenses | 26,365 | 23,444 |
| Training and conferences | 62,047 | 68,705 |
| Motor vehicle running expenses | 6,113 | 4,898 |
| Subscriptions and IOSCO membership | 11,946 | 9,825 |
| Authority board members' emoluments and allowances | 36,968 | 26,974 |
| Professional and market development services | 178,106 | 92,246 |
| Depreciation of property and equipment | 51,791 | 34,835 |
| Amortisation of intangible assets | 3,785 | 38,801 |
| Auditor's remuneration | 1,760 | 823 |
| Investors' education and awareness programme | 26,767 | 32,998 |
| Tribunal expenses | 4,097 | 3,145 |
| Provision for impairment losses | <u> </u> | <u> </u> |
| | <u>540,122</u> | <u>459,783</u> |
| Total expenditure | <u><u>970,011</u></u> | <u><u>812,206</u></u> |

Appendix I: PROGRESS ON FOLLOW UP OF AUDITOR RECOMMENDATIONS

| Reference No. on the external audit Report | Issue/Observations from Auditor | Management Comments | Focal Point person to resolve the issue (Name and Designation) | Status: (Resolved/ Not Resolved) | Timeframe: (Put a date when you expect the issue to be resolved) |
|---|---------------------------------|---------------------|--|----------------------------------|--|
| All observations made in the Management Letter were resolved in the financial statements of FY 2015/16. | | | | | |
| | | | | | |


 Chief Executive


 Chairman of the Board

Date: 14th September 2017

Date: 14th September 2017

Capital Markets Authority
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Appendix 1: Projects Implemented by the Entity

Projects implemented by the State Corporation Funded by development partners (Financial Sector Deepening Africa)

| Project title | Project Number | Donor | Period/ duration | Donor commitment | Separate donor reporting required as per the donor agreement (Yes/No) |
|--|----------------|------------|------------------|------------------|---|
| 1 CMA- Change Management Project Uwezo Kipeo | | FSD-Africa | 2 years | YES | NO |
| 2 Islamic Finance Project | | FSD-Africa | 2 years | YES | NO |
| 3 Chartered Institute for Securities & Investment (CISI) Pilot programme | | FSD-Africa | 2 years | YES | NO |

Status of Projects completion

(Summarise the status of project completion at the end of each quarter, ie total costs incurred, stage which the project is etc)

| Project | Total project Cost | Total expended to date | Completion % to date | Budget | Sources of Funds |
|--|--------------------|------------------------|----------------------|------------|---|
| 1 CMA- Change Management Project (Uwezo Kipeo) Phase I | 35,823,091.20 | 35,823,091.20 | 100% | £ 34,5,000 | Donor Funded and CMA Internal resources |
| 2 Islamic Finance Project | 33,890,694.20 | 33,890,694.20 | 45% | £ 659,953 | Donor Funded and Joint Financial Regulators resources |
| 3 Chartered Institute for Securities & Investment (CISI) Pilot programme | 18,684,493.30 | 18,684,493.30 | 100% | £ 75,000 | Donor Funded |

As per note 7 - Donor Fund income : The Authority received support from FSDA, FSSP, and the funds were paid directly to the consultants.

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Appendix 2- Inter Entity Transfers

| Name of the MDA/Donor Transferring the funds | Date received as per bank statement | Nature: Recurrent/Development/ Others | Total Amount - KES | Where Recorded/recognized | | | | Total Transfers during the Year |
|--|-------------------------------------|---------------------------------------|--------------------|------------------------------------|--------------|-----------------|-------------|---------------------------------|
| | | | | Statement of Financial Performance | Capital Fund | Deferred Income | Receivables | |
| FSSP | See Appendix 3 | Recurrent | 8,914,874 | 8,914,874 | - | - | - | 8,914,874 |
| FLSTAP | See Appendix 3 | Direct Payments | 7,199,479 | 7,199,479 | - | - | - | 7,199,479 |
| FSSP | See Appendix 3 | Direct Payments | 4,733,195 | 4,733,195 | - | - | - | 4,733,195 |
| FSDA | See Appendix 3 | Direct Payments | 88,398,279 | 88,398,279 | - | - | - | 88,398,279 |
| Total | | | 109,245,826 | 109,245,826 | - | - | - | 109,245,826 |

As per note 7 - Donor Fund income : The Authority received support from FSDA, FSSP, and the funds were paid directly to the consultants.

The above amounts have been communicated to and reconciled with FSSP-Project implementation Unit of the National Treasury

Finance Manager
Capital Markets Authority

Signature: 

KEY:

FSSP : Financial Sector Support Project : This is a World Bank funded project that strengthens the legal regulatory and institutional environment for improved financial stability.

FLSTAP : Financial and Legal Sector Technical Assistance Project : This was a four year World Bank project in Kenya from FY2009 whose objective was to create a sound financial system and strengthen legal framework ensuring broad access to financial and other services. The project's term ended in June 201

FSDA : Financial Sector Deepening Africa ; This is a project funded by the United Kingdom's Department for International Development which promotes financial sector Development.

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Appendix 3: Recording of Transfers from other Government Entities

| ENTITY NAME: CAPITAL MARKETS AUTHORITY | Bank Statement Date | Amount (KShs) | Indicate the FY to which the amounts relate |
|--|--|----------------|---|
| Break down of Transfers from the National Treasury | | | |
| FY 2016/2017 | | | |
| a. Reimbursements for Capacity building Technical Costs. | | | |
| Financial Sector Support Project (FSSP) | Between 28/8/2016 and 22/6/2017 | 8,914,873.70 | 2016/17 |
| Reimbursement for Staff training and Development for Various Capital Markets technical skills | Sub Total | 8,914,873.70 | |
| b. Direct Payments | | | |
| Details of the Payment | Transaction Description | Amount (KShs) | |
| b(i) Capital expenditure-Acquired in FY2013 | | | |
| Enterprise Resource Planning (ERP) & Risk Based Supervision System(RBSS) Servers paid for by Financial and Legal Sector Technical Programme (FLSTAP) | Deferred Income | 7,199,479.43 | 2016/17 |
| | Sub Total | 7,199,479.43 | |
| b(ii) Capacity Building | | | |
| Capacity building of Staff Payment to Nasdaq Technology Stockholm, by FSSP | Contra-Staff Training and Donor Funding income | 4,733,194.55 | 2016/17 |
| | Sub Total | 4,733,194.55 | |
| b(iii) Donor funded Consultancies . | | | |
| Consultancy for Islamic Finance paid to Islamic Finance Advisory & Assurance Services (I.F.A.A.S) | Contra-Donor Funded Consultancies and Donor Funding income | 33,890,694.20 | 2016/17 |
| Consultancy for Uwezo Kipeo paid to Promontory Group by the Financial Sector Deepening Africa(FSDA) | Contra-Donor Funded Consultancies and Donor Funding income | 35,823,091.20 | 2016/17 |
| Donor Funded CISI Trainings Paid to Chartered Institute for Securities & Investment (CISI) by FSDA | Contra-Donor Funded Consultancies and Donor Funding income | 18,684,493.30 | 2016/17 |
| | Total | 88,398,278.70 | |
| | GRAND TOTAL | 109,245,826.38 | |

As per note 7 - Donor Fund income : The Authority received support from FSDA, FSSP, and the funds were paid directly to the consultants.