Liberty Kenya Holdings Limited
(Formerly CfC Insurance Holdings Limited)

Annual Report

& financial statements

2012

LIBERTY KENYA HOLDINGS LIMITED

Our vision, purpose and values

Our Vision

To become the market leading investment and insurance provider in Africa

We will make a difference to people's lives by being the group most trusted to make financial freedom possible

Our Purpose

It is our **passion** to make a **difference** to people's lives by making **financial freedom** possible

We aspire to be the guiding light in the industry, trusted as the company that knows how to always find a way of delivering excellence.

Our Values

- Always passionate, positive, professional and having fun
- Maintaining open channels of communication that encourage freedom of expression
- Interacting with rspect and integrity, by being honest, trustworthy and transparent
- Taking responsibility for our attitudes, actions and development
- Providing excellent customer service, from end to end, all the time
- Creating a culture of sharing, knowledge and expertise

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1 | Notice of Annual General Meeting

Notice is hereby given that the Eighth Annual General Meeting of the members of Liberty Kenya Holdings Limited will be held on Wednesday 22 May 2013, at The Sarova Stanley Hotel, Nairobi, at 11.00 in the forenoon to transact the following business:

1. The Secretary to read the notice convening the meeting and confirm the presence of a quorum.
2. To receive, consider and if thought fit, adopt the Annual Report and the Audited Financial Statements for the year ended 31 December 2012 and the Directors' and Auditors' Report thereon.
3. To declare a dividend.
4. To elect Directors:
   i) In accordance with Article 88 of the Company's Articles of Association, Ms S Kilonzo, a director appointed to fill a casual vacancy, retires at the dissolution of the meeting and, being eligible, offers herself for re-election.
5. To approve the Directors' remuneration for the year ended 31 December 2012 as provided in the Financial Statements.
6. To note that Messrs PricewaterhouseCoopers continue in office as the auditor under Section 159(2) of the Companies Act and to authorise the Directors to fix their remuneration.
7. Special Business:

   To consider and if thought fit, to pass the following resolution as a Special Resolution:

   "THAT Mr Gayling R May having attained the age of 70 on 2 March 2013 be approved to continue to serve as a director of the Company".
8. Any other business of the Company of which due notice has been given.

By order of the Board

Caroline Kioni

Company Secretary

Date14 March 2013

NOTE:

In accordance with section 136(2) of the Companies Act every member entitled to attend and vote at the above meeting and any adjournment thereof is entitled to appoint a proxy to attend and vote on his/her behalf. A proxy need not be a Member of the Company. A form of proxy is enclosed and should be returned to the Company Secretary, P.O. Box 30390-00100 Nairobi, to arrive not later than 48 hours before the meeting.

2 | Group Information

Directors

S A Mboya	-	Chairman
M L du Toit *		
P N Gethi		
G R May **		
S Kilonzo	-	(Appointed on 3 December 2012)
M Mittal**	-	(Appointed on 28 March 2012)
S Wenman *	-	(Alternate to M Mittal)
B Katompa *	-	(Resigned on 31 July 2012)
J G Kiereini	-	(Retired on 3 August 2012)

*** South African** **** British**

Secretary

C Kioni
CfC House
Mamlaka Road
P O Box 30390, 00100
Nairobi

Registered office

LR No 209/8592/2
CfC House
Mamlaka Road
P O Box 30390, 00100
Nairobi

Subsidiaries

CfC Life Assurance Ltd (100%)
The Heritage Insurance Company Kenya Ltd (100%)
Azali Limited (100%)
CfC Investments Ltd (100%)
The Heritage Insurance Tanzania Ltd (60%)

Associate

Strategis Insurance (Tanzania) Ltd

Bankers

CfC Stanbic Bank Ltd
NIC Bank Ltd

Auditor

PricewaterhouseCoopers
The PwC Tower
Waiyaki way
P O Box 43963, 00100
Nairobi

Share registrar

Comprite Kenya Limited
Crescent Business Centre
Off Parklands Road, Parklands
P O Box 63428, 00619
Nairobi

3 | Chairman's Statement

It is my pleasure to present the annual report and financial statements for Liberty Kenya Holdings Limited ("LKHL") for the year ended 31 December 2012.

Overview

The Company is the holding Company of two operating entities, CfC Life Assurance Company Limited (CfC Life) and Heritage Insurance Company Kenya Limited (Heritage), formerly known as CfC Insurance Holdings Limited. In 2012 the Company changed its name to Liberty Kenya Holdings Limited as an initial step of aligning the group to the Liberty Group corporate brand, with the subsidiaries adopting the use of 'A member of the Liberty Group' endorsement tag on their logos. This is part of the process of simplification, differentiation and economies of scale in the Group's brand building strategy.

Economic Environment and outlook for 2013

Compared to 2011 which was a challenging year for the economies within the East African region, the impact of some of the negative factors (interest rates, inflation and the equity market) were less severe in 2012 and this had a positive effect on the Group's performance.

Equities staged a broad rally in the year buoyed by a blend of domestic and global factors. On the economic front, monetary policy easing in response to lowering inflationary pressures, stable exchange rates and gradually declining interest rates offered the stock market support. Relatively attractive valuation metrics helped pull back investment capital into the equity market.

The Central Bank of Kenya (CBK) undertook measures to address inflation. Tightening of monetary policy positively shaped inflation and inflation expectations. As part of the strategy for managing inflation, the CBK hiked the Central Bank Rate (CBR) by 11% in the fourth quarter of 2011 to 18%. This was primarily to curb demand driven inflationary pressures through reducing the rate of credit growth to the private sector. Domestic demand had remained resilient and inflation was still elevated and facing upside risks. CBK held the CBR constant at 18% for first six months of 2012 and gradually eased to 11% in December. The annual headline inflation rate decelerated for most of 2012. Annual inflation stood at 3.2% in December down from 18.3% at the start of the year. I believe that inflationary pressures have largely abated and that inflation seems to have bottomed out at current levels. Upside risks to inflation in 2013 are present but probably limited.

Key indicative market rates gradually declined in the year 2012. Key in interest rates such as Repo rate, Inter-bank rate and the 91-day Treasury bill almost converged. Falling inflation and improved liquidity firmly established the trend towards lower interest rates. In the second half of the year, the CBK commenced a monetary easing cycle. I believe that going forward, monetary policy can durably keep rates in check. Inflation expectations are likely to remain relatively well anchored. Heavy liquidity from Government securities maturities expected in the first half of 2013 are likely to maintain rates at high single digit levels.

Financial highlights

The Group was able to achieve some key milestones. We continued to show strong performance as a consequence of sound underwriting and claims management, improvements to distribution channels, introduction of differentiated products, identification of new alternative distribution channels, process re-engineering, management of costs and use of new technology to enhance service delivery to our customers and intermediaries. The improved economic climate, particularly in the second half of the year, contributed positively to the Group's performance. The following is a synopsis of the financial performance for the year under review:

- Profit before tax at Kshs 1.2 billion improved by 19% from Kshs 1 billion.
- Gross earned premium revenue at Kshs 6.9 billion is up 9% from Kshs 6.3 billion.
- Total income at Kshs 7.5 billion up 16% from Kshs 6.4 billion.
- Net insurance benefits and claims increased to Kshs 3.1 billion from Kshs 2.5 billion.
- The Group's share of profit from Associates was significantly higher than in 2011.
- Chairman's Statement (continued)
- Completed the separation and transfer of the Short and Long Term businesses between Heritage Kenya and CfC Life respectively.
- The overall total asset base of the Group has grown by 12.8% from Kshs 24.3 Billion to Kshs 27.4 Billion.

Short Term Business

The Group's short term business is managed through Heritage Kenya ("Heritage") and its subsidiary in Tanzania, the Heritage Insurance Company Tanzania Limited. 2012 saw continued improvement in Heritage's underwriting performance, particularly in the medical and motor classes of business. This is as a result of the Company maintaining strict discipline in its ratings, notwithstanding fierce competition and rate cutting prevailing in the market. Claims ratios have been managed downward in all classes of business.

Heritage completed the transfer of its Long Term Business to CfC Life during the year, in accordance with the requirements of the Insurance Regulatory Authority that long term and short-term- businesses should be separated – the impact of this was that profitability of the Long Term portfolio was significantly reduced but this was compensated by the much improved performance of the Short Term business, most notably the medical portfolio.

In 2013 the Company expects to implement new IT systems which should lead to greater efficiencies, improved customer experience and management information for the years to come.

Long Term Business

The Long Term business of CfC Life performed satisfactorily, returning a profit after tax of Kshs 331 million compared to Kshs 315 million for the prior year. Despite the challenging business environment, the company registered a 13.6% growth in life premiums while pension contributions remained level at Kshs 1.6 billion.

The Company's assets increased by 35% to Kshs 18 billion as a result of good investment performance and the transfer of Long Term business from Heritage.

In the first half of 2013 the Company will introduce a number of innovative and relevant products to its current and new target markets and will embark on technology initiatives that will enhance efficiencies and reduce costs.

Performance of Associates

Earnings from Associates are up significantly in line with their performance during the year. The Group is currently in the process of restructuring its operations in Tanzania to ensure increased efficiencies and maximization of shareholder value.

Compliance

Compliance with best practice and regulatory requirements is enshrined within our Values and governance structures in all the subsidiaries.

The following are our key regulators:

- The Capital Markets Authority in Kenya (CMA).
- The Insurance Regulatory Authority of Kenya (IRA) – the primary regulator of insurance businesses in Kenya.
- The Tanzanian Insurance Regulatory Authority (TIRA) – the primary regulator of insurance businesses in Tanzania.
- The Retirement Benefits Authority (RBA).
- The Nairobi Securities Exchange (NSE).

We have a cordial relationship with our key regulators as well as the respective Revenue Authorities. This is founded on our endeavor to strictly comply with the guidelines of our industry and ensure that we maintain channels of regular open communication.

Directorate

The directors who were in office in 2012 are listed on page 2 of this report. I am delighted to welcome Ms. Stella Kilonzo and Mr. Mukesh Mittal who joined the Board in 2012. Mr. Jeremiah Kiereini, the Group's long serving Chairman, retired from the Board after many years of dedicated service and outstanding leadership. His invaluable vision was instrumental in transforming the Group into an industry leader and eventual listing at the Nairobi Securities Exchange. Similarly Mr. Bernard Katompa resigned from the Board during the year. I take this opportunity to thank them for their service and commitment to the Company's and Group's growth.

Human resources

These results are a reflection of a committed team of staff who believe that in delivering value to our stakeholders, we will continue to build on the legacy of our Group. We shall continue to raise the skills of our human capital to empower them and improve customer service standards across the Group. The Group's total staff complement as at 31 December 2012 was 342 compared to 366 in 2011.

Outlook

The Group has made some significant investments in making its existing business more sustainable over the past three years. In particular the rationalisation of our life and short term business across CfC and Heritage will ensure that we achieve better scale in each business line and that the right focus and expertise is being applied to each entity. In addition we are implementing a number of cost management initiatives, including system rationalisation, that we expect to have a positive effect on the overall cost base both in the short and longer terms.

Whilst we continue to focus in the traditional areas of our business, we shall innovate to attract customers by way of new product development, improved service offering and expanded distribution channels. Furthermore, we shall target appropriate growing alternative distribution channels using technology availed from the Liberty Group, building partnerships and investing in appropriate resources.

We shall continue to review our regional structure in order to align with the parent Group whilst also being open to the opportunities that may present themselves.

Dividend

The Directors propose a first and final dividend of Kshs 0.40 per share totaling Kshs 206,108,146 which will be subjected to the relevant taxes. The dividend represents a distribution of 23% of the profit after tax. The balance of the profits will be retained to maintain sufficient capitalization required to drive diversification and create long-term growth.

Appreciation

I take this opportunity to express my sincere appreciation to our customers, shareholders, the Governments of Kenya and Tanzania, management, staff, suppliers and fellow board members for their dedicated contribution to the growth of the Group.

S A Mboya - Chairman
14 March 2013

4 | Members of the Board

Susan Mboya

Susan Mboya is the Chairman of Liberty Kenya Holdings Limited and the Group Director, Eurasia, Africa Group (EAG) for Women's Economic Empowerment at Coca Cola. In this role, Susan is leading the Groups deployment of an initiative undertaken by The Coca-Cola Company in September 2010 to empower five million women entrepreneurs across the Coca-Cola System by 2020.

In May 2009, Dr Mboya was awarded a honorary Doctorate in Humanities from Lakeland College in Wisconsin, for her work on the Zawadi Africa Educational Fund. In December 2010 she was awarded the Elder of the Burning Spear (EBS) the highest civilian award from the Kenya Government, in recognition of her dedication and service to the country's youth through the Zawadi Africa Educational Fund. She Joined Liberty Kenya Board in 2012.

Mike du Toit

Mr. Mike du Toit is the Company's Managing Director and Liberty Africa Regional Managing Director for East Africa responsible primarily for Strategic Growth initiatives. He joined Liberty in 2010, prior to this he was Managing Director of CfC Stanbic Bank having led the merger of the Stanbic and CfC Groups.

As a career banker, he has extensive experience in the financial services field across sub-Sahara Africa having worked and lived in, amongst others, Botswana, Mozambique, South Africa and Uganda

Gayling May

Mr. Gayling R. May was appointed to the Board in December 2009. He has an extensive accounting background and is a member of the Institute of Certified Public Accountants of Kenya (ICPAK) and a fellow of the Institute of Chartered Accounts in England and Wales (FCPA).

He has worked in the UK, USA and for the most part, Kenya, and has a history of 37 years with PricewaterhouseCoopers, 32 of which as a Partner/Regional Senior Partner.

He is currently the Regional Representative of the Eastern Africa Association, a business information service based in Nairobi, but operating throughout East Africa.

He holds various directorships in banks, insurance companies, manufacturing entities and an aircraft ground handling company.

Mukesh Mittal

Mr. Mukesh Mittal is Liberty Group Chief Executive- Business Development Cluster and Group Strategy. He holds a BSc (Hons) (Imperial London), FIA

Mukesh has significant international insurance experience having held the position of Group Chief Actuary at Old Mutual plc (London) and leading Old Mutual's strategy and business development for the Asia Pacific region, Deputy Group Chief Actuary of Allianz (SE) and a director of PricewaterhouseCoopers UK. Mukesh also served on the board for Actuarial Standards in the UK. He joined the group in 2011.

Stella Kilonzo

Mrs Stella Kilonzo MBS is the Founder of Astute Capital, an advisory company specializing on Africa in capital markets, strategic policy, research & regulatory space, infrastructure finance, acquisitions strategies and matching investment opportunities with funding partners. Stella also serves on World Economic Forum (WEF) Global Agenda Council on Global Financial System. She is a Non Executive Director at Athi River Cement Ltd, Liberty Holdings Kenya Ltd and UBA Capital Plc. Stella served as Chief Executive, Capital Markets Authority Kenya (2008 to 2012) overseeing development and regulation of capital markets.

She also served as Chairperson, East African Securities Regulatory Authorities (EASRA) from 2008 to 2010. Previously she worked for FINRA, USA's largest independent securities regulator, and PwC Kenya. Stella is a 2010 Fellow of Africa Leadership Initiative East Africa and Aspen Global Leadership Network, USA. She holds an MBA, Corporate Finance, Loyola University Chicago and a First Class Honours Bachelor of Commerce, Catholic University of Eastern Africa, and is a CPA (USA). She joined the Liberty Holdings Board in 2012.

Peter Gethi

Peter Nderitu Gethi (47yrs) was appointed to the Board of Directors of LHKL on 17th December 2009. He holds a BSc (Hons) degree in Agricultural Economics and has expansive managerial experience in Agricultural Business Management. He has been a General Manager with Kilimanjaro Plantations Ltd (TZ) and Senior Group Manager with SCEM Ltd (formerly Standard Chartered Estate Management). He currently works both as a an Agricultural Consultant and is involved with Real Estate Development as Managing Director of Nebange Ltd.

He is also the Chairman of Heritage Insurance (K) Ltd; Chairman of CfC Life Assurance Ltd; Director Heritage Insurance (T); Director CfC Stanbic Holdings; Director CfC Stanbic Bank. He serves in the Audit & Risk Committees of LHKL and Heritage Insurance (T).

5 | Corporate Governance Report

Introduction

The directors are committed to the principles of good governance and appreciate the importance of governing the business with integrity and accountability to all the stakeholders. The Board prescribes to the Commonwealth Association of Corporate Governance principles and has adopted the recommended guidelines and associated principles of best practice.

Through its subsidiaries, CfC Life Assurance Company Ltd, The Heritage Insurance Company Kenya Ltd and CfC Investments Ltd, the Board of Liberty Kenya Holdings Ltd follows principles of openness, integrity and accountability in its stewardship of the organisation's affairs. It recognises the dynamic nature of corporate governance and continuously assesses the Group's compliance with generally accepted corporate practices on a regular basis. The role of the Board is to ensure conformance by focusing on and providing the Group's overall strategic direction and policy-making as well as performance review through accountability and ensuring appropriate monitoring and supervision.

The Board is responsible for maintaining a system of internal control and for reviewing its effectiveness regularly to ensure that the assets of the Group are safeguarded while maintaining a reliable system of managing financial information, so that the Group's objectives of increased growth in profitability and shareholder value are realised.

Board of Directors

The Board of Directors consists of one executive Director and five non-executive directors who have been chosen for their business acumen and wide range of skills and experience. The Board meets quarterly as a minimum. During the year five meetings were held and the attendance by the Directors was as follows:

Directors	Meeting on 28/03/2012	Meeting on 25/06/2012	Meeting on 28/08/2012	Meeting on 8/10/2012	Meeting on 3/12/2012"
Ms S.A Mboya	✓	✓	✓	✓	✓
Mr J. G Kiereini	✓	✓	N/A	N/A	N/A
Mr M. L du Toit	✓	✓	✓	✓	✓
Mr M. Mittal	N/A	N/A	✓	✓	✓
Mr G. R. May	✓	✓	✓	✓	✓
Mr P. Gethi	✓	✓	✓	✓	✓
Ms S. Kilonzo	N/A	N/A	N/A	N/A	✓
Mr B. Katompa	✓	✓	N/A	N/A	N/A
Mr S. Wenman *	N/A	N/A	✓	✓	✓

✓: Attended AP: Absent with Apology N/A: Not a member *: Alternate to M. Mittal

The Board is responsible for setting the direction of the Group through the establishment of strategic objectives, key policies and decision making processes to achieve the objectives of the organisation.

It monitors the implementation of strategies and policies through a structured approach of reporting by executive management and consequent accountability against approved strategies and budgets.

Board Committees

The Group is headed by the Board of Directors, which has ultimate responsibility for the management and strategic guidance and assumes the primary responsibility of fostering the sustainability of the Group's business. The Board has the overall responsibility for the establishment and oversight of the Group's risk management framework. The performance against financial and corporate governance objectives is monitored by the Board through managements' quarterly reporting.

The implementation of the Group's strategic objectives is done at the individual subsidiary companies, through various established Board and management committees including Board Audit and Risk Committee ('BARC'). The BARC meets at least twice a year in accordance with the half yearly financial reporting period adopted by the Group. All members attended the meetings as shown below:

Directors	Meeting on 24/02/2012	Meeting on 28/08/2012
Mr G. R. May	✓	✓
Mr M. Mittal	N/A	✓
Mr P. Gethi	✓	✓

Board effectiveness and evaluation

The Board is focused on continued improvements to its effectiveness and corporate governance performance.

In 2012 the Board of Directors conducted a self assessment evaluation, which was divided into structure, process and effectiveness. The Board continued to use the results of the self assessment evaluation conducted in 2011 to further improve Board functioning. In particular, during the year the Board appointed one additional director to address the skills mix that was deemed necessary and also to reflect gender parity.

Sustainability

Social and environmental responsibility remains an important part of Liberty Kenya Group culture. The monitoring and reporting of sustainability issues is still an evolving discipline within the organisation. However the Board, through its subsidiaries, is conscious of the fact that as a Group our sustainability and success is dependent upon the environment and the community within which we operate. Through the subsidiaries it is our Group policy to ensure that our activities meet the social, economic and environmental expectations of all our stakeholders.

Social responsibility

As a Kenyan business, the Group understands the challenges and benefits of doing business in Kenya, and owes its existence to the people and societies within which it operates. The Group is committed therefore not only to the promotion of the economic development but also to the strengthening of civil society and human well-being. The Group concentrates its social investment expenditure in defined focus areas in order to make the greatest impact. These areas of focus are subject to annual revision as the country's socio-economic needs change. The Group focus was mainly in the area of education, health and environment with a long term view of sustaining the projects at hand.

Growing Concern

The Board has reviewed the facts and assumptions, on which it relied and, based on these, will continue to view the Group as a going concern for the foreseeable future.

Remuneration

Liberty Kenya Holdings Limited has a clear policy on remuneration of executive and non-executive directors at levels that are fair and reasonable in a competitive market for the skills, knowledge, experience required, nature and size of the Board.

The amounts paid to directors are included in note 34 which represents the total remuneration paid to executive and non-executive directors for the year under review.

S Mboya
Chairman
14 March 2013

M L du Toit
Managing Director

6 | Director's Report

The directors submit their report together with the audited financial statements for the year ended 31 December 2012, in accordance with Section 157 of the Kenyan Companies Act, which discloses the state of affairs of Liberty Kenya Holdings Limited and its subsidiaries (together the "Group") and of Liberty Kenya Holdings Limited (the "Company").

Incorporation

The Company was incorporated on 6 July 2004 under the name of Quadco One Limited. On 12 August 2004, the shareholders unanimously resolved to change the name of the Company from Quadco One Limited to CfC Holdings Limited. The Company was subsequently renamed CfC Insurance Holding Limited in preparation for the demerger from CfC Stanbic Holdings Limited which occurred in April 2011. On 22 October 2012 the Company, through a special resolution and with the approval of the Registrar of Companies, changed its name to Liberty Kenya Holdings Limited. This was to align itself with the brand of the holding company, Liberty Holdings Limited, South Africa.

Principal activities

The Group is engaged in the business of insurance and wealth management through its subsidiaries namely CfC Life Assurance Limited, CfC Investments Limited, and The Heritage Insurance Company Kenya Limited. The Group underwrites all classes of long term and general insurance as defined in the Kenyan Insurance Act. It also issues investment contracts to provide customers with asset management solutions for their savings and retirement needs.

Results and dividend

Profit for the year ended 31 December 2012 is Shs 886,671,000 (2011: Shs 950,418,000) has been added to retained earnings. During the year, no interim dividend was paid (2011: Nil). The directors have resolved to recommend to the shareholders at the forth coming Annual General Meeting the payment of a first and final dividend for the year of Shs 0.40 per share (2011: Nil).

Directors

The names of the directors who held office during the year and to the date of this report are set out on page 2.

Auditor

The Company's auditor, PricewaterhouseCoopers, continue in office in accordance with Section 159(2) of the Companies Act.

Approval of Financial Statements

The financial statements were approved and authorised for issue by the Board of Directors on 14 March 2013.

By order of the Board
C. Kioni - Company Secretary
14 March 2013

7 | Statement of Directors' Responsibilities

The Companies Act requires the directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Group and Company as at the end of the financial year and of its profit or loss. It also requires the directors to ensure that the Company and its subsidiaries keep proper accounting records that disclose, with reasonable accuracy, the financial position of the Company and its subsidiaries. They are also responsible for safeguarding the assets of the Company and its subsidiaries.

The directors accept responsibility for the annual financial statements, which have been prepared using appropriate accounting policies supported by reasonable estimates, in conformity with International Financial Reporting Standards and the requirements of the Companies Act. The directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the Company and its subsidiaries and of its profit or loss in accordance with International Financial Reporting Standards. The directors further accept responsibility for the maintenance of accounting records that may be relied upon in the preparation of financial statements, as well as designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement.

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

S Mboya
Chairman
Director

M L du Toit
Director

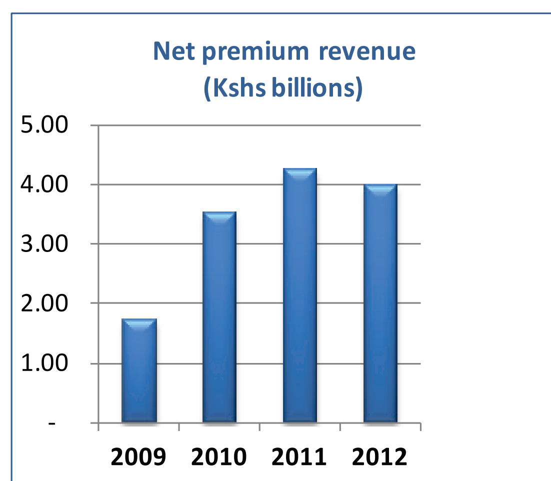
14 March 2013

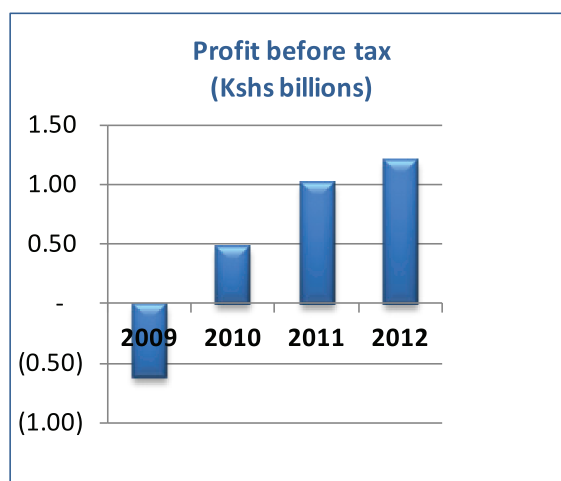
8 | Financial Highlights

Four year review

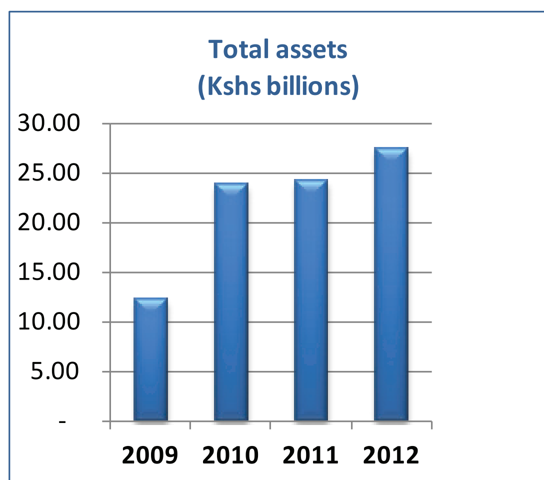
	31/12/2009 Shs'000	31/12/2010 Shs'000	31/12/2011 Shs'000	31/12/2012 Shs'000
Net premium revenue	1,733,280	3,531,909	4,237,933	3,982,386
Investment and other income	354,937	1,842,744	2,195,322	3,478,478
Total income	**2,088,217**	**5,374,653**	**6,433,255**	**7,460,864**
Net insurance benefits and claims	(1,471,322)	(2,714,472)	(2,482,494)	(3,108,922)
Operating expenses and commissions	(1,237,745)	(2,214,028)	(2,940,927)	(3,172,745)
Result of operating activities	(620,850)	446,153	1,009,834	1,179,197
Earnings from associates	-	36,782	2,381	23,704
Profit before taxation	(620,850)	482,935	1,012,215	1,202,901
Income tax expense	(77,965)	(222,921)	(61,797)	(316,230)
Profit for the year	**(698,815)**	**260,014**	**950,418**	**886,671**
Cost to income (%)	59%	41%	46%	43%
Earnings per share (Shs)	(1.72)	0.54	1.84	1.72

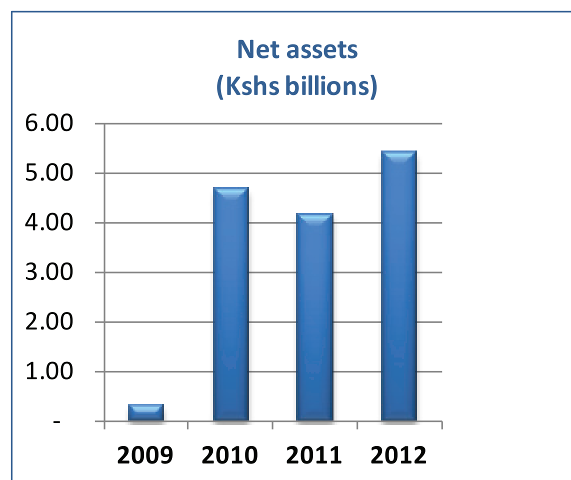
Figures included in the four year review have been re-stated where necessary to provide a meaningful comparison of performance over the period.





	31/12/2009 Shs'000	31/12/2010 Shs'000	31/12/2011 Shs'000	31/12/2012 Shs'000
Total equity	**329,307**	**4,676,659**	**4,174,597**	**5,421,591**
Assets				
Property, equipment and intangible assets	844,721	1,260,013	1,176,517	1,165,093
Investment property	354,000	545,000	623,553	710,449
Goodwill	1,084,649	1,254,995	1,254,995	1,254,995
Investment in associates	-	313,180	355,400	61,948
Financial investments	9,329,227	15,084,710	14,510,876	14,833,362
Other assets	73,879	2,539,229	3,672,586	3,886,160
Cash and cash equivalents	654,445	2,830,202	2,699,606	5,478,339
Total assets	**12,340,921**	**23,827,329**	**24,293,533**	**27,390,346**
Liabilities				
Insurance contract liabilities	3,484,257	6,027,195	6,689,310	7,538,857
Deposit administration liabilities	6,160,510	8,703,273	9,237,856	10,104,276
Other liabilities	1,866,847	3,811,391	3,617,058	3,845,826
Borrowings and bank overdraft	500,000	608,811	574,712	479,796
Total liabilities	**12,011,614**	**19,150,670**	**20,118,936**	**21,968,755**
Net assets	**329,307**	**4,676,659**	**4,174,597**	**5,421,591**





Figures included in the four year review have been re-stated where necessary to provide a meaningful comparison of performance over the period.

9 | Report of the Indepedent auditor
to the Members of Liberty Kenya Holdings Ltd

Report on the financial statements

We have audited the accompanying consolidated financial statements of Liberty Kenya Holdings Limited (the "Company") and its subsidiaries (together, the "Group"), as set out on pages 16 to 86. These financial statements comprise the consolidated statement of financial position at 31 December 2012 and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and the consolidated statement of cash flow for the year then ended, together with the statement of financial position of the Company standing alone as at 31 December 2012, the income statement, statement of comprehensive income and the statement of changes in equity of the Company for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

The directors are responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards and with the requirements of the Kenyan Companies Act and for such internal control, as the directors determine necessary to enable the preparation of consolidated financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's responsibility

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

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

In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion the accompanying financial statements give a true and fair view of the state of the financial affairs of the Group and of the Company at 31 December 2012 and of the profit and cash flows of the Group for the year then ended in accordance with International Financial Reporting Standards and the Kenyan Companies Act.

Report on other legal requirements

The Kenyan Companies Act requires that in carrying out our audit we consider and report to you on the following matters. We confirm that:

i) we have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit;

ii) in our opinion proper books of account have been kept by the Company, so far as appears from our examination of those books;

iii) the Company's statement of financial position is in agreement with the books of account.

Certified Public Accountants | _____ March 2013

Nairobi

10 | Statement of Financial Position

	Notes	Group 31/12/2012 Shs'000	31/12/2011 Shs'000	Company 31/12/2012 Shs'000	31/12/2011 Shs'000
Ordinary share capital	16	515,270	515,270	515,270	515,270
Share premium	16	1,701,239	1,701,239	1,701,239	1,701,239
Revenue reserve	17	1,759,864	1,134,938	696,911	513,917
Proposed dividend	17	206,108	-	206,108	-
Other reserves	17	917,309	522,369	-	-
Equity attributable to equity holders		5,099,790	3,873,816	3,119,528	2,730,426
Non-controlling interest		321,801	300,781	-	-
Total equity		**5,421,591**	**4,174,597**	**3,119,528**	**2,730,426**
REPRESENTED BY:					
Assets					
Property and equipment	20	1,097,599	1,056,551	-	-
Intangible assets	22	67,494	119,966	-	-
Goodwill	18	1,254,995	1,254,995	-	-
Investment property	21	710,449	623,553	-	-
Investment in associates	13	61,948	355,400	-	-
Investment in subsidiaries	13	-	-	3,202,333	3,202,333
Financial investments	19	14,833,362	14,510,876	-	-
Receivable arising from reinsurance		224,848	216,266	-	-
Receivable arising from direct insurance		662,212	740,559	-	-
Reinsurers' share of insurance liabilities	23	2,040,892	2,117,135	-	-
Deferred acquisition costs		95,219	137,510	-	-
Other receivables		784,869	300,121	500,000	-

	Notes	Group 31/12/2012 Shs'000	Group 31/12/2011 Shs'000	Company 31/12/2012 Shs'000	Company 31/12/2011 Shs'000
Deferred income tax	30	49,235	57,548	-	-
Tax recoverable		28,885	103,447	-	-
Cash and cash equivalents	24	5,478,339	2,699,606	54,638	188,218
Total assets		**27,390,346**	**24,293,533**	**3,756,971**	**3,390,551**
Liabilities					
Insurance contract liabilities	25	7,538,857	6,689,310	-	-
Deposit administration liabilities	26	10,104,276	9,237,856	-	-
Unearned premium reserve	27	2,325,287	2,242,031	-	-
Creditors arising from direct insurance		45,411	72,731	-	-
Creditors arising from reinsurance		353,787	475,480	-	-
Deferred acquisition income		82,829	77,867	-	-
Other liabilities	28	910,435	715,969	157,647	155,504
Current income tax payable		128,077	32,980	-	-
Bank overdraft		-	70,091	-	-
Borrowings	32	479,796	504,621	479,796	504,621
Total liabilities		**21,968,755**	**20,118,936**	**637,443**	**660,125**
Net assets		**5,421,591**	**4,174,597**	**3,119,528**	**2,730,426**

The notes on pages 23 to 86 are an integral part of these financial statements.

The financial statements on pages 16 to 86 were approved for issue by the board of Directors on 14 March 2013 and signed on its behalf by:

S A Mboya M L du Toit G R May C Kioni

Income statement

	Notes	Group 31/12/2012 Shs'000	Group 31/12/2011 Shs'000	Company 31/12/2012 Shs'000	Company 31/12/2011 Shs'000
Gross earned premium revenue	6	6,953,842	6,389,035	-	-
Less: Outward reinsurance		(2,971,456)	(2,151,102)	-	-
Net insurance premium revenue		**3,982,386**	**4,237,933**	**-**	**-**
		3,478,478	**2,195,322**	**500,000**	**615,000**
Commissions earned		660,441	513,025	-	-
Investment income	7	2,591,896	1,640,630	500,000	615,000
Administration fees		13,292	13,937	-	-
Other income	8	212,849	27,730	-	-
Total income		**7,460,864**	**6,433,255**	**500,000**	**615,000**
Claims and policyholder benefits payable	9	(3,337,436)	(3,379,417)	-	-
Change in insurance contract liabilities		(480,031)	(39,214)	-	-
Amounts recoverable from reinsurers		708,545	936,137	-	-
Net insurance benefits and claims		**(3,108,922)**	**(2,482,494)**	**-**	**-**
Total expenses and commissions		**(3,172,745)**	**(2,940,927)**	**(110,898)**	**(89,200)**
Commissions payable		(892,089)	(1,003,068)	-	-
Finance costs	10	(95,179)	(74,233)	(97,254)	(78,534)
Other operating expenses	11	(2,185,477)	(1,863,626)	(13,644)	(10,666)
Result of operating activities		**1,179,197**	**1,009,834**	**389,102**	**525,800**

	Notes	Group 31/12/2012 Shs'000	Group 31/12/2011 Shs'000	Company 31/12/2012 Shs'000	Company 31/12/2011 Shs'000
Earnings from associates	13	23,704	2,381	-	-
Profit before taxation		**1,202,901**	**1,012,215**	**389,102**	**525,800**
Income tax expense	14	(316,230)	(61,797)	-	-
Profit for the year		**886,671**	**950,418**	**389,102**	**525,800**
Attributable to :					
Owners of the parent		819,615	919,334	389,102	525,800
Non-controlling interest		67,056	31,084	-	-
		886,671	**950,418**	**389,102**	**525,800**
Basic and diluted earnings per share (Shs)	**15**	**1.72**	**1.84**	**0.76**	**1.02**

The notes on pages 23 to 86 are an integral part of these financial statements.

Statement of comprehensive income

	Group		Company	
	31/12/2012 Shs'000	31/12/2011 Shs'000	31/12/2012 Shs'000	31/12/2011 Shs'000
Profit for the year	**886,671**	**950,418**	**389,102**	**525,800**
Other comprehensive income/(loss) for the year net of tax	**397,231**	**(1,434,738)**	**-**	**-**
Foreign currency translation operations	18,951	(38,782)	-	-
Gain/(loss) on fair valuation of available-for-sale financial assets (Note 19)	305,495	(1,508,151)	-	-
Impairment loss on available-for-sale equity securities charged through the income statement (Note 7)	18,259	94,348	-	-
Gains on property revaluations (Note 20)	54,209	-	-	-
Share of associate's fair value reserve (Note 13)	317	17,847	-	-
Total comprehensive income/(loss) for the year	**1,283,902**	**(484,320)**	**389,102**	**525,800**
Total comprehensive income attributable to:				
Equity holders of parent	1,226,402	(513,652)	389,102	525,800
Non-controlling interest	57,500	29,332	-	-
Total comprehensive income/(loss) for the year	**1,283,902**	**(484,320)**	**389,102**	**525,800**

The notes on pages 23 to 86 are an integral part of these financial statements.

Consolidated statement of changes in equity

	Share capital	Share premium	Statutory reserve	Fair value reserve	Revaluation reserve	Currency translation and reserve	Revenue reserve	Proposed dividend	Non controlling interest	Total equity
	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000	Shs'000
At 1 January 2012	**515,270**	**1,701,239**	**263,246**	**92,636**	**225,471**	**(58,984)**	**1,134,938**	**-**	**300,781**	**4,174,597**
Total comprehensive income for the year	**-**	**-**	**(37,180)**	**340,666**	**54,209**	**37,245**	**831,034**	**-**	**57,928**	**1,283,902**
Profit for the year	-	-	-	-	-	-	819,615	-	67,056	886,671
Other comprehensive income:										
Transfers to statutory reserve (Note 17)	-	-	(37,180)	-	-	-	21,946	-	15,234	-
Gains/(loss) on fair valuation of available-for-sale investments net of tax	-	-	-	322,217	-	-	-	-	(16,722)	305,495
Impairment recognised in income statement	-	-	-	18,259	-	-	-	-	-	18,259
Foreign currency translation differences	-	-	-	-	-	37,245	(10,527)	-	(7,767)	18,951
Gain on revaluation of owner-occupied property	-	-	-	-	54,209	-	-	-	-	54,209
Share of associate's fair value reserve	-	-	-	190	-	-	-	-	127	317
Total other comprehensive income	**-**	**-**	**(37,180)**	**340,666**	**54,209**	**37,245**	**11,419**	**-**	**(9,128)**	**397,231**
Distributions to owners										
Dividend paid to non-controlling interests	-	-	-	-	-	-	-	-	(36,908)	(36,908)
Proposed dividend of Shs 0.40 per share	-	-	-	-	-	-	(206,108)	206,108	-	-
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**-**	**-**	**(206,108)**	**206,108**	**(36,908)**	**(36,908)**
At 31 December 2012	**515,270**	**1,701,239**	**226,066**	**433,302**	**279,680**	**(21,739)**	**1,759,864**	**206,108**	**321,801**	**5,421,591**

STATEMENT OF FINANCIAL POSITION

	Share capital Shs'ooo	Share premium Shs'ooo	Statutory reserve Shs'ooo	Fair value reserve Shs'ooo	Revaluation reserve Shs'ooo	Currency translation and reserve Shs'ooo	Revenue reserve Shs'ooo	Proposed dividend Shs'ooo	Non controlling interest Shs'ooo	Total equity Shs'ooo
At 1 January 2011		**515,270**	**1,701,239**	**524,805**	**1,498,986**	**225,471**	**(32,348)**	**(45,955)**	**289,191**	**4,676,659**
Total comprehensive income for the year		**-**	**-**	**(261,559)**	**(1,406,350)**	**-**	**(26,636)**	**1,180,893**	**29,332**	**(484,320)**
Profit for the year		-	-	-	-	-	-	919,334	31,084	950,418
Other comprehensive income:										
Transfers to statutory reserve (Note 17)		-	-	(261,559)	-	-	-	261,559	-	-
Gains/(loss) on fair valuation of		-	-	-	(1,503,577)	-	-	-	(4,574)	(1,508,151)
Impairment recognised in income statement		-	-	-	86,519	-	-	-	7,829	94,348
available-for-sale investments net of tax										
Foreign currency translation differences		-	-	-	-	-	(26,636)	-	(12,146)	(38,782)
Share of associate's fair value reserve		-	-	-	10,708	-	-	-	7,139	17,847
Total other comprehensive income		**-**	**-**	**(261,559)**	**(1,406,350)**	**-**	**(26,636)**	**261,559**	**(1,752)**	**(1,434,738)**
Distributions to owners										
Dividend paid to non-controlling interests		-	-	-	-	-	-	-	(17,742)	(17,742)
Total contributions by and distributions to owners		-	-	-	-	-	-	-	(17,742)	(17,742)
At 31 December 2011		**515,270**	**1,701,239**	**263,246**	**92,636**	**225,471**	**(58,984)**	**1,134,938**	**300,781**	**4,174,597**

The notes on pages 23 to 86 are an integral part of these financial statements.

Company statement of changes in equity

Year ended 31 December 2012	Share capital Shs' 000	Share premium Shs' 000	Revenue reserve Shs' 000	Proposed dividend Shs' 000	Total Shs' 000
As at 01 January 2012	**515,270**	**1,701,239**	**513,917**	**-**	**2,730,426**
Total comprehensive income for the year					
Profit for the year	-	-	389,102	-	389,102
Proposed dividend of Shs 0.40 per share	-	-	(206,108)	206,108	(206,108)
As at 31 December 2012	**515,270**	**1,701,239**	**696,911**	**206,108**	**3,119,528**
As at 01 January 2011	515,270	1,701,239	(11,883)	-	2,204,626
Total comprehensive income for the year					
Profit for the year	-	-	525,800	-	525,800
As at 31 December 2011	**515,270**	**1,701,239**	**513,917**	**-**	**2,730,426**

The notes on pages 23 to 86 are an integral part of these financial statements.

11 | Notes

Consolidated statement of cash flows

	Notes	31/12/2012 Shs' 000	31/12/ 2011 Shs' 000
Cash generated from/(used in) operations	31	223,272	(615,002)
Net interest received		1,692,278	1,228,388
Income tax paid		(178,541)	(197,803)
Net cash generated from operating activities		**1,737,009**	**415,583**
Investment in associate	13	-	(41,659)
Additions to investment property	21	(4,468)	(553)
Additions to property and equipment	20	(99,984)	(77,367)
Additions to intangible assets	22	(15,937)	(11,600)
Proceeds from the sale of equipment		26,093	14,676
Net investment in quoted shares		1,907,713	785,057
Net investment in unquoted shares		12,066	97,763
Net investment in government securities and corporate bonds		(1,323,623)	(1,460,566)
Net investment in loans and receivables		(30,212)	220,474
Proceeds from disposal of investments in Alliance Insurance Corporation Ltd		440,508	-
Dividend, rental and other income received		335,641	213,443
Cash flows from/(used in) investing activities		**1,247,797**	**(260,332)**
Cash flows used in financing activities		**(131,824)**	**(248,776)**
Dividends paid		(36,908)	(248,776)
Change in borrowings and overdrafts		(94,916)	-
Net increase/(decrease) in cash and cash equivalents		2,852,982	(93,525)
Currency translation differences		(4,158)	1,649
Cash and cash equivalents at 1 January		**2,629,515**	**2,721,391**
Cash and cash equivalents at 31 December	**24**	**5,478,339**	**2,629,515**

The notes on pages 23 to 86 are an integral part of these financial statements.

1. General information

Liberty Kenya Holdings Limited (formerly CfC Insurance Holdings Limited) is incorporated in Kenya under the Companies Act as a limited liability Company, and is domiciled in Kenya. The address of its registered office is:

LR No 209/8592/2
CfC House, Mamlaka Road
P.O. Box 30390-00100 Nairobi

The Company was listed on the Nairobi Securities Exchange by way of introduction on 21 April 2011. For Kenyan Companies Act reporting purposes, the balance sheet is represented by the statement of financial position and the profit and loss account by the income statement in these financial statements.

2. Summary of significant accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all periods presented, unless otherwise stated.

a) Basis of preparation

The financial statements are prepared in compliance with International Financial Reporting Standards (IFRS). The financial statements have been prepared under the historical cost convention, as modified by the revaluation of land and buildings, available for sale financial assets and derivative instruments at fair value through profit or loss. The financial statements are presented in Kenyan Shillings (Shs), rounded to the nearest thousand.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or where assumptions and estimates are significant to the financial statements, are disclosed in Note 3.

Changes in accounting policy and disclosures

(i) New and amended standards adopted by the Company and the Group

There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning on 1 January 2012 that would be expected to have a material impact on the Group and the Company.

(ii) New standards and interpretations that are not yet effective and have not been early adopted

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 January 2012, and have not been applied in preparing these financial statements. None of these is expected to have a significant effect on the financial statements of the Company and the Group, except the following:

Amendment to IAS 1, 'Presentation of Financial Statements' regarding other comprehensive income. The main change resulting from these amendments is a requirement for entities to group items presented in 'other comprehensive income' (OCI) on the basis of whether they are potentially reclassifiable to profit or loss subsequently (reclassification adjustments). The amendments do not address which items are presented in OCI.

IFRS 13, 'Fair value measurement', aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The requirements, which are largely aligned between IFRSs and US GAAP, do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs or US GAAP.

IAS 19, 'Employee benefits', was amended in June 2011. The impact on the Company and the Group will be as follows: to immediately recognise all past service costs; and to replace interest cost and expected return on plan assets with a net interest amount that is calculated by applying the discount rate to the net defined benefit liability (asset). The amendment will not have a significant impact to the Group.

IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 was issued in November 2009 and October 2010.

It replaces the parts of IAS 39 that relate to the classification and measurement of financial instruments. IFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortised cost. The determination is made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For financial liabilities, the standard retains most of the IAS 39 requirements.

The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch. The directors are yet to assess IFRS 9's full impact and intends to adopt IFRS 9 no later than the accounting period beginning on or after 1 January 2015. The directors will also consider the impact of the remaining phases of IFRS 9 when completed by the IASB.

IFRS 10, Consolidated financial statements', builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. The directors are yet to assess IFRS 10's full impact and intends to adopt IFRS 10 no later than the accounting period beginning on or after 1 January 2013.

IFRS 12, 'Disclosures of interests in other entities', includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles.

The directors are yet to assess IFRS 12's full impact and intends to adopt IFRS 12 no later than the accounting period beginning on or after 1 January 2013.

There are no other IFRSs or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Group or Company.

b) **Basis of consolidation**

The consolidated financial statements incorporate the financial statements of Liberty Kenya Holdings Limited and its subsidiaries; CfC Life Assurance Limited, CfC Investments Limited, The Heritage Insurance Company (Kenya) Limited, The Heritage Insurance Company (Tanzania) Limited and Azali Limited. The financial statements have been made up to 31 December 2012.

Subsidiaries

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date the control ceases.

The Group uses the acquisition method of accounting to account for business combinations. The consideration transferred for the acquisition of

a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

Investments in subsidiaries are accounted for at cost less impairment. Cost is adjusted to reflect changes in consideration arising from contingent consideration amendments. Cost also includes direct attributable costs of investment.

The excess of the consideration transferred the amount of any non-controlling interest in the acquiree and the acquisition-date fair value over any previous equity interest in the acquiree over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in profit or loss.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies.

Significant influence generally accompanies, but is not limited to, a shareholding of between 20% and 50% of the voting rights. Investments in mutual funds over whose financial and operating policies the Group is able to exercise significant influence (including those in which the Group has between 20% and 50% economic interest) are also classified as associates.

Interest in associates is accounted for using the equity method and are measured in the consolidated statement of financial position at an amount that reflects the Group's share of the net assets of the associate (including goodwill). Equity accounting involves recognising the investment initially at cost, including goodwill, and subsequently adjusting the carrying value for the Group's share of the associates' income and expenses and other comprehensive income.

Equity accounting of losses in associates is restricted to the interests in these entities, including unsecured receivables or other commitments, unless the Group has an obligation or has made payments on behalf of the associate. Unrealised intra-Group profits are eliminated in determining the Group's share of equity accounted profits.

Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Equity accounting is applied from the date on which the entity becomes an associate, up to the date on which it ceases to be an associate. The accounting policies of associates have been changed where necessary to ensure consistency with the policies of the Group. Investment in associates is accounted for at cost less impairment losses in the Company financial statements.

c) Functional currency and translation of foreign currencies

i. Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (functional currency). The consolidated and Company financial statements are presented in Kenya Shillings, which is the Group's presentation currency.

ii. Consolidation of Group entities

The results and financial position of all foreign operations that have a functional currency different from the Group's presentation currency are translated into the presentation currency as follows:

- assets and liabilities (including goodwill and fair value adjustments arising on acquisition) are translated at the closing rate on the reporting date;
- income and expenses are translated at average exchange rates for the year, to the extent that such average rates approximate actual rates; and
- all resulting foreign exchange differences are accounted for directly in a separate component of other comprehensive income, being the foreign currency translation reserve.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities are taken to shareholders' equity. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate. The exchange differences arising are recognised in equity.

iii. Transactions and balances

Foreign currency transactions are translated into the respective functional currencies of Group entities at exchange rates prevailing at the date of the transactions.

Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at year-end exchange rates are recognised in the income statement.

Translation differences on non-monetary financial assets and liabilities, such as equities held at fair value through profit or loss, are recognised in the income statement as part of the fair value gain or loss. Translation differences on non-monetary financial assets, such as equities classified as available-for-sale financial assets, are included in the available-for-sale reserve in equity.

d) Insurance contracts

Classification

The Group issues contracts that transfer insurance risk or financial risk or both. Insurance contracts are those contracts that transfer significant insurance risk. Such contracts may also transfer financial risk.

As a general guideline, the Group defines as significant insurance risk, the possibility of having to pay benefits on the occurrence of an insured event that are at least 10% more than the benefits payable if the insured event did not occur.

Investment contracts are those contracts that transfer financial risk with no significant insurance risk. See accounting policy for these contracts under 2(f).

A number of insurance and investment contracts contain a discretionary participation feature (DPF). This feature entitles the holder to receive, as a supplement to guaranteed benefits, additional benefits or bonuses:

(a) that are likely to be a significant portion of the total contractual benefits;

(b) whose amount or timing is contractually at the discretion of the Group; and

(c) that are contractually based on:

- the performance of a specified pool of contracts or a specified type of contract;
- realised and/or unrealised investment returns on a specified pool of assets held by the Group; or
- the profit or loss of the Company, fund or other entity that issues the contract.

Insurance contracts and investment contracts are classified into two main categories, depending on the duration of risk and as per the provisions of the Insurance Act.

i) Long term insurance business

Includes insurance business of all or any of the following classes, namely, life assurance business, superannuation business and bond investment business and business incidental to any such class of business;

Life assurance business means the business of, or in relation to, the issuing of, or the undertaking of liability to pay money on death (not being death by accident or in specified sickness only) or on the happening of any contingency dependent on the termination or continuance of human life (either with or without provision for a benefit under a continuous disability insurance contract), and include a contract which is subject to the payment of premiums for term dependent on the termination or continuance of human life and any contract securing the grant of an annuity for a term dependent upon human life;

Superannuation business means life assurance business, being business of, or in relation to, the issuing of or the undertaking of liability under superannuation, Group life and permanent health insurance policy.

ii) General insurance business

Means insurance business of any class or classes not being long term insurance business.

Classes of General Insurance include Aviation insurance, Engineering insurance, Fire insurance - domestic risks, Fire insurance - industrial and commercial risks, Liability insurance, Marine Insurance, Motor insurance - private vehicles , Motor insurance - commercial vehicles, Personal accident insurance, Theft insurance ,Workmen's Compensation and Employer's Liability insurance and Miscellaneous insurance (i.e. class of business not included under those listed above)

Motor insurance business means the business of affecting and carrying out contracts of insurance against loss of, or damage to, or arising out of or in connection with the use of, motor vehicles, inclusive of third party risks but exclusive of transit risks.

Personal accident and medical insurance business means the business of affecting and carrying out contracts of insurance against risks of the persons insured sustaining injury as the result of an accident or of an accident of a specified class or dying as the result of an accident or of an accident of a specified class or becoming incapacitated in consequence of disease or of disease of a specified class.

Fire insurance business means the business of affecting and carrying out contracts of insurance, otherwise than incidental to some other class of insurance business against loss or damage to property due to fire, explosion, storm and other occurrences customarily included among the risks insured against in the fire insurance business.

Recognition and measurement

i) Premium income

For long term insurance business, premiums are recognised as revenue when they become payable by the contract holder. Premiums are shown before deduction of commission.

For general insurance business, premium income is recognised on assumption of risks, and includes estimates of premiums due but not yet received, less an allowance for cancellations, and less unearned premium. Unearned premiums represent the proportion of the premiums written in periods up to the accounting date that relates to the unexpired terms of policies in force at the financial reporting date, and is computed using the 1/24th method.

Premiums are shown before deduction of commission and are gross of any taxes or duties levied on premiums.

ii) Claims

For long term insurance business, benefits are recorded as an expense when they are incurred. Claims arising on maturing policies are recognised when the claim becomes due for payment. Death claims are accounted for on notification. Surrenders are accounted for on payment.

A liability for contractual benefits that are expected to be incurred in the future is recorded when the premiums are recognised. The liability is determined as the sum of the expected discounted value of the benefit payments and the future administration expenses that are directly related to the contract, less the expected discounted value of the theoretical premiums that would be required to meet the benefits and administration expenses based on the valuation assumptions used (the valuation premiums). The liability is based on assumptions as to mortality, persistency, maintenance expenses and investment income that are established at the time the contract is issued. A margin for adverse deviations is included in the assumptions.

Where insurance contracts have a single premium or a limited number of premium payments due over a significantly shorter period than the period during which benefits are provided, the excess of the premiums payable over the valuation premiums is deferred and recognised as income in line with the decrease of unexpired insurance risk of the contracts in-force or, for annuities in force, in line with the decrease of the amount of future benefits expected to be paid.

The liabilities are recalculated at each financial reporting date using the assumptions established at inception of the contracts.

For general insurance business, claims incurred comprise claims paid in the year and changes in the provision for outstanding claims.

Claims paid represent all payments made during the year, whether arising from events during that or earlier years. Outstanding claims represent the estimated ultimate cost of settling all claims arising from incidents occurring prior to the financial reporting date, but not settled at that date.

Outstanding claims are computed on the basis of the best information available at the time the records for the year are closed, and include provisions for claims incurred but not reported ("IBNR"). Outstanding claims are not discounted.

iii) Commissions payable and deferred acquisition costs ("DAC")

A proportion of commission payable is deferred and amortised over the period in which the related premium is earned. Deferred acquisition costs represent a proportion of acquisition costs that relate to policies that are in force at the year end.

iv) Liability adequacy test

At each financial reporting date, liability adequacy tests are performed to ensure the adequacy of the contract liabilities net of related DAC. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from the assets backing such liabilities, are used. Any deficiency is immediately charged to profit or loss initially by writing off DAC and by subsequently establishing a provision for losses arising from liability adequacy tests (the unexpired risk provision).

Long-term insurance contracts are measured based on assumptions set out at the inception of the contract. When the liability adequacy test requires the adoption of new best estimate assumptions, such assumptions (without margins for adverse deviation) are used for the subsequent measurement of these liabilities.

v) Reinsurance contracts held

Contracts entered into by the Group with reinsurers under which the Group is compensated for losses on one or more contracts issued by the Group and that meet the classification requirements for insurance contracts are classified as reinsurance contracts held. Contracts that do not meet these classification requirements are classified as financial assets. Insurance contracts entered into by the Group under which the contract holder is another insurer (inwards reinsurance) are included with insurance contracts. The benefits to which the Group is entitled under its reinsurance contracts held are recognised as reinsurance assets. These assets consist of short-term balances due from reinsurers, as well as longer term receivables that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts.

Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised as an expense when due.

The Group assesses its reinsurance assets for impairment on a quarterly basis. If there is objective evidence that the reinsurance asset is impaired, the Group reduces the carrying amount of the reinsurance asset to its recoverable amount and recognises that impairment loss in the income statement. The Group gathers the objective evidence that a reinsurance asset is impaired using the same process adopted for financial assets held at amortised cost. The impairment loss is also calculated following the same method used for these financial assets. These processes are described in Note 2 (k).

vi) Receivables and payables related to insurance contracts and investment contracts

Receivables and payables are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders.

If there is objective evidence that the insurance receivable is impaired, the Group reduces the carrying amount of the insurance receivable accordingly and recognises that impairment loss in the income statement. The processes followed by the Group in assessing impairment of these receivables are described in Note 2 (k)

vii) Salvage and subrogation reimbursements

Some insurance contracts permit the Group to sell (usually damaged) property acquired in settling a claim (for example, salvage). The Group may also have the right to pursue third parties for payment of some or all costs (for example, subrogation).

Estimates of salvage recoveries are included as an allowance in the measurement of the insurance liability for claims, and salvage property is recognised in other assets when the liability is settled.

The allowance is the amount that can reasonably be recovered from the disposal of the property.

Subrogation reimbursements are also considered as an allowance in the measurement of the insurance liability for claims and are recognised in other assets when the liability is settled. The allowance is the assessment of the amount that can be recovered from the action against the liable third party.

e) Other income recognition

Commissions receivable are recognised as income in the period in which they are earned. Investment income is stated net of investment expenses. Interest income is recognised on a time proportion basis that takes into account the effective yield on the asset. Dividends are recognised as income in the period in which the right to receive payment is established. Rental income is recognised as income in the period in which it is earned.

f) Investment contracts

The Group issues investment contracts without fixed terms (unit-linked) and investment contracts with fixed and guaranteed terms (fixed interest rate). The investment contracts include funds administered for a number of retirement benefit schemes.

Investment contracts without fixed terms are financial liabilities whose fair value is dependent on the fair value of underlying financial assets, derivatives and/or investment property (these contracts are also known as unit-linked investment contracts) and are designated at inception as at fair value through profit or loss. The Group designates these investment contracts to be measured at fair value through profit or loss because it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as ‘an accounting mismatch’) that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

See Note 2 (l) for the financial assets backing these liabilities.

The best evidence of the fair value of these financial liabilities at initial recognition is the transaction price (i.e. the fair value received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets.

When such evidence exists, the Group recognises profit on day 1. The Group has not recognised any profit on initial measurement of these investment contracts because the difference is attributed to the prepayment liability recognised for the future investment management services that the Group will render to each contract holder.

The Group's main valuation techniques incorporate all factors that market participants would consider and make maximum use of observable market data. The fair value of financial liabilities for investment contracts without fixed terms is determined using the current unit values in which the contractual benefits are denominated. These unit values reflect the fair values of the financial assets contained within the Group's unitised investment funds linked to the financial liability. The fair value of the financial liabilities is obtained by multiplying the number of units attributed to each contract holder at the financial reporting date by the unit value for the same date.

When the investment contract has an embedded put or surrender option, the fair value of the financial liability is never less than the amount payable on surrender, discounted for the required notice period, where applicable.

For investment contracts with fixed and guaranteed terms, the amortised cost basis is used. In this case, the liability is initially measured at its fair value less transaction costs that are incremental and directly attributable to the acquisition or issue of the contract.

Subsequent measurement of investment contracts at amortised cost uses the effective interest method. This method requires the determination of an interest rate (the effective interest rate) that exactly discounts to the net carrying amount of the financial liability, the estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period if the holder has the option to redeem the instrument earlier than maturity.

The Group re-estimates at each reporting date the expected future cash flows and recalculates the carrying amount of the financial liability by computing the present value of estimated future cash flows using the financial liability's original effective interest rate. Any adjustment is immediately recognised as income or expense in the income statement.

g) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost using the effective interest method; any differences between proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the financial reporting date.

h) Share capital

Ordinary shares are classified as 'share capital' in equity. Any premium received over and above the par value of the shares is classified as 'share premium' in equity.

i) Investment in subsidiaries

Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights.

The investment in subsidiary is stated at cost less any provision for impairment. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

j) Intangible assets

Goodwill

Goodwill arises on the acquisition of subsidiaries, associates and joint ventures and represents the excess of the consideration transferred over the Company's interest in net fair value of the net identifiable assets, liabilities and contingent liabilities of the acquiree and the fair value of the non-controlling interest in the acquiree.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the CGUs, or groups of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal management purposes. Goodwill is monitored at the operating segment level.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs to sell. Any impairment is recognised immediately as an expense and is not subsequently reversed.

Computer software

Generally, costs associated with developing or maintaining computer software programmes and the acquisition of software licenses are recognised as an expense as incurred. However, direct computer software development costs that are clearly associated with an identifiable and unique system, which will be controlled by the Group and have a probable future economic benefit beyond one year, are recognised as intangible assets.

Capitalisation is further limited to development costs where the Group is able to demonstrate its intention and ability to complete and use the software, the technical feasibility of the development, the availability of resources to complete the development, how the development will generate probable future economic benefits and the ability to reliably measure costs relating to the development.

Direct costs include software development employee costs and an appropriate portion of relevant overheads.

Subsequent expenditure on computer software is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates.

Direct computer software development costs recognised as intangible assets are amortised on the straight-line basis at rates appropriate to the expected useful lives of the assets (two to 10 years), and are carried at cost less accumulated amortisation and accumulated impairment losses.

The carrying amount of capitalised computer software is reviewed annually and is written down when impaired.

Other intangible assets

The Group recognises the costs incurred on internally generated intangible assets such as brands, customer lists, customer contracts and similar rights and assets, in the income statement as incurred.

Prepayment assets are recognised for advertising or promotional expenditure until the Group has obtained the right to access the goods purchased or received the services.

The Group capitalises brands, customer lists, customer contracts and similar rights acquired in business combinations. Capitalised intangible assets are measured at cost less accumulated amortisation and accumulated impairment losses. Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, not exceeding 20 years, from the date that they are available for use.

Amortisation methods, useful lives and residual values are reviewed at each financial year-end and adjusted, if necessary. There have been no changes in the estimated useful lives from those applied in the previous financial year.

k) Cash and cash equivalents

Cash and cash equivalents are carried in the date of financial reporting at amortised cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts.

l) Financial instruments

Financial instruments include all financial assets and liabilities held for liquidity, investment, trading or hedging purposes.

All financial instruments are initially recognised at fair value plus directly attributable transaction costs, except those carried at fair value through the income statement where transaction costs are recognised immediately in the income statement. Financial instruments are recognised (derecognised) on the date the Group commits to purchase (sell) the instruments (trade date accounting).

Subsequent to initial measurement, financial instruments are measured either at fair value or amortised cost, depending on their classification.

Classification

i) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that management has both the positive intent and ability to hold to maturity. Held-to-maturity investments are carried at amortised cost, using the effective interest method, less any impairment losses.

Were the Group to sell more than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available-for-sale assets with the difference between amortised cost and fair value being accounted for in other comprehensive income.

ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those classified by the Group as at fair value through the income statement or available-for-sale. This category includes purchased loans.

Loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses. Origination transaction costs and origination fees received that are integral to the effective rate are capitalised to the value of the loan and amortised through interest income as part of the effective interest rate. The majority of the Group’s advances are included in the loans and receivables category.

iii) Financial assets and liabilities designated at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term. Derivatives are also categorised as held for trading. Assets in this category are classified as current assets if expected to be settled within 12 months; otherwise, they are classified as non-current.

The Group designates certain financial assets and liabilities, other than those held for trading, as at fair value through profit or loss when:

- this designation eliminates or significantly reduces an accounting mismatch that would otherwise arise. The designation significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortised cost.

  This category also includes financial assets used to match investment contracts or insurance contract liabilities; or

- Groups of financial assets, financial liabilities or both are managed, and their performance evaluated, on a fair value basis in accordance with a documented risk management or investment strategy, and reported to the Group’s key management personnel on a fair value basis; or

- financial instruments contain one or more embedded derivatives that significantly modify the instruments’ cash flows.

The fair value designation is made on initial recognition and is irrevocable. Subsequent to initial recognition, the fair values are re-measured at each reporting date. Gains and losses arising from changes in fair value are recognised in interest income (expense) for all dated financial assets (financial liabilities) and in other revenue within non-interest revenue for all undated financial assets.

iv) Available-for-sale

Financial assets classified by the Group as available-for- sale are generally strategic capital investments held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices, or non-derivative financial assets that are not designated as another category of financial assets.

Available-for-sale financial assets are subsequently measured at fair value. Unrealised gains or losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in the available-for-sale reserve in other comprehensive income until the financial asset is derecognised or impaired. When dated (undated) available-for-sale financial assets are disposed of, the cumulative fair value adjustments in other comprehensive income are transferred to interest income.

Interest income, calculated using the effective interest method, is recognised in the income statement. Dividends received on available-for-sale instruments are recognised in the income statement when the Group's right to receive payment has been established. Foreign exchange gains or losses on available-for-sale debt instruments are recognised in the income statement.

Impairment of financial assets

The Group assesses at each reporting date whether there is objective evidence that a financial asset or Group of financial assets is impaired. A financial asset or Group of financial assets is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset and that loss event had a negative effect on the estimated future cash flows of the financial asset or Group of financial assets that can be estimated reliably.

i) Assets carried at amortised cost

The Group first assesses whether there is objective evidence of impairment individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant.

ii) Available-for-sale financial assets

Available-for-sale financial assets are impaired if there is objective evidence of impairment, resulting from one or more loss events that occurred after initial recognition but before the reporting date, that have a negative impact on the future cash flows of the asset. In addition, an available-for-sale equity instrument is considered impaired if a significant or prolonged decline in the fair value of the instrument below its cost has occurred.

In that instance, the cumulative loss, measured as the difference between the acquisition price and the current fair value, less any previously recognised impairment losses on that financial asset, is transferred from other comprehensive income to the income statement.

If, in a subsequent period, the amount relating to impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement for available-for-sale debt instruments. An impairment loss in respect of an available-for-sale equity instrument is not reversed through the income statement but accounted for directly in other comprehensive income.

Derecognition of financial instruments

Financial assets are derecognised when the contractual rights to receive cash flows from the financial assets have expired, or where the Group has transferred its contractual rights to receive cash flows on the financial asset such that it has transferred substantially all the risks and rewards of ownership of the financial asset. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

Financial liabilities are derecognised when they are extinguished, i.e. when the obligation is discharged, cancelled or expires.

m) Investment property

Property held to earn rental income and/or for capital appreciation that is not owner-occupied is classified as investment property. Investment property includes property under construction or development for future use as investment property.

Investment property is measured initially at cost, including transaction costs. Subsequent to initial recognition, investment property is measured at fair value with fair value changes recognised in the income statement as investment gains or losses.

The fair value of investment property is based on valuation information at the reporting date. If the valuation information cannot be reliably determined, the Group uses alternative valuation methods such as discounted cash flow projections or recent prices on active markets.

Fair value adjustments on investment property recognised in the income statement are adjusted for any double-counting arising from the recognition of lease income on the straight-line basis compared to the accrual basis normally assumed in the fair value determination.

When the use of a property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

n) Property and equipment

Equipment and owner-occupied properties

All categories of property and equipment are initially recorded at cost. Buildings and freehold land are subsequently shown at fair value, based on periodic, but at least triennial, valuations by external independent valuers, less subsequent depreciation for buildings. All other equipment, furniture, vehicles and other tangible assets are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits will flow to the Group and the cost of the item can be measured reliably.

Maintenance and repairs, which do not meet these criteria, are recognised in the income statement as incurred. Depreciation, impairment losses and gains or losses on disposal of assets are included in the income statement. Owner-occupied properties are held for use in the supply of services or for administrative purposes.

Property and equipment are depreciated on the straight-line basis over the estimated useful lives of the assets to their residual values. Land is not depreciated. Leasehold buildings are depreciated over the period of the lease or over a lesser period, as is considered appropriate.

The assets' residual values and useful lives and the depreciation method applied are reviewed, and adjusted if appropriate, at each financial year-end.

n) Property and equipment

The estimated useful lives of tangible assets for the current financial year are as follows:

Leasehold buildings	The shorter of the lease period or 50 years
Furniture & fittings	3 - 10 years
Motor vehicles	4 - 5 years
Computers and office equipment	3 - 10 years

There has been no change to the estimated useful lives from those applied in the previous financial year.

o) Impairment of non-financial assets

Intangible assets that have an indefinite useful life and goodwill are tested annually for impairment. Intangible assets that are subject to amortisation and other non-financial assets are reviewed for impairment at each reporting date and tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised in the income statement for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Fair value less costs to sell is determined by ascertaining the current market value of an asset and deducting any costs related to the realisation of the asset.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purposes of assessing impairment, assets that cannot be tested individually are Grouped at the lowest levels for which there are separately identifiable cash inflows from continuing use (cash-generating units).

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units, and then to reduce the carrying amounts of the other assets in the unit on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other non-financial assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed through the income statement only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

p) Leases

Group as lessee

Leases, where the Group assumes substantially all the risks and rewards of ownership, are classified as finance leases. Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Lease payments are separated using the interest rate implicit in the lease to identify the finance cost, which is recognised in the income statement over the lease period, and the capital repayment, which reduces the liability to the lessor.

Leases of assets are classified as operating leases if the lessor retains a significant portion of the risks and rewards of ownership. Payments made under operating leases, net of any incentives received from the lessor, are recognised in the income statement on a straight-line basis over the term of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Group as lessor

Lease and instalment sale contracts are primarily financing transactions in banking activities, with rentals and instalments receivable, less unearned finance charges, being included in loans and advances in the statement of financial position.

Finance charges earned are computed using the effective interest method, which reflects a constant periodic rate of return on the investment in the finance lease. Initial direct costs and fees are capitalised to the value of the lease receivable and accounted for over the lease term as an adjustment to the effective rate of return. The benefits arising from investment allowances on assets leased to clients are accounted for in tax.

Leases of assets under which the Group retains a significant portion of the risks and rewards of ownership are classified as operating leases. Operating lease income from properties held as investment properties, net of any incentives given to lessees, is recognised on the straight-line basis over the lease term.

When an operating lease is terminated before the lease period has expired, any payment required by the lessee by way of a penalty is recognised as income in the period in which termination takes place.

q) Provisions and contingent liabilities

Provisions are recognised when the Group has a present legal or constructive obligation if as a result of past events it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made.

Provisions are determined by discounting the expected future cash flows using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the liability.A provision for restructuring is recognised when the Group has approved a detailed formal plan, and the restructuring either has commenced or has been announced publicly. Future operating costs or losses are not provided for.

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Group recognises any impairment loss on the assets associated with that contract.

Contingent liabilities include certain guarantees, other than financial guarantees, and letters of credit pledged as collateral security. Contingent liabilities are not recognised in the financial statements but are disclosed in the notes to the financial statements unless they are remote.

r) Employee benefits

Defined contribution plan

The majority of the Group's employees are eligible for retirement benefits under a defined contribution plan. The Group and all its employees also contribute to the respective Social Security Funds, which are defined contribution schemes. A defined contribution plan is a retirement benefit plan under which the Group pays fixed contributions into a separate entity.

The Group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

The assets of all schemes are held in separate trustee administered funds, which are funded by contributions from both the Group and employees. The Group's contributions to the defined contribution schemes are charged to the profit and loss account in the year in which they fall due.

Short-term benefits

Short-term benefits consist of salaries, accumulated leave payments, profit share, bonuses and any non-monetary benefits such as medical aid contributions.

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus plans or accumulated leave if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

s) Tax expense

Direct taxation includes current and deferred tax. Current tax and deferred tax are recognised in the income statement except to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

Current tax represents the expected tax payable on taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustments to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date.

Deferred tax is not recognised for the following temporary differences:

- the initial recognition of goodwill;
- the initial recognition of assets and liabilities in a transaction that is not a business combination, which affects neither accounting nor taxable profits or losses; and

- investments in subsidiaries and jointly controlled entities (excluding mutual funds) where the Group controls the timing of the reversal of temporary differences and it is probable that these differences will not reverse in the foreseeable future.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of the asset or liability and is not discounted.

Deferred tax assets are recognised to the extent that it is probable that future taxable income will be available against which the unused tax losses can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

t) Reinsurance premiums

Reinsurance premiums are recognised when due for payment, in accordance with the terms of each reinsurance contract.

u) Acquisition costs

Acquisition costs for insurance contracts represent commissions payable to agents and brokers and other costs that relate to the securing of new contracts and the renewing of existing contracts. These costs are expensed as incurred.

v) Deferred acquisition costs (DAC) in respect of investment contracts

Commissions paid and other incremental acquisition costs are incurred when new investment contracts are obtained or existing investment contracts are renewed. These costs are expensed as incurred, unless specifically attributable to an investment contract with an investment management service element.

Such costs are deferred and amortised on a straight-line basis over the expected life of the contract (10 to 16 years for linked annuities and five years for other investment contracts), taking into account all decrements, as they represent the right to receive future management fees. A DAC asset is recognised for all applicable policies with the amortisation being calculated on a portfolio basis. The DAC asset is assessed for impairment at the reporting date.

w) Dividends on ordinary shares

Dividends are recognised in equity in the period in which they are declared. Dividend declared after the reporting date is disclosed in the dividend note 17.

x) Segment reporting

An operating segment is a component of the Group engaged in business activities, whose operating results are reviewed regularly by management in order to make decisions about resources to be allocated to segments and assessing segment performance.

The Group's identification of segments and the measurement of segment results is based on the Insurance Act and internal reporting to management. Transactions between

segments are priced at market-related rates.

y) Comparative figures

Where necessary, comparative figures within notes have been restated to conform to changes in presentation, in the current year. Refer to Note 4 Segment reporting.

3. Critical accounting estimates and judgments in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

a) Impairment of goodwill

The Group tests annually whether goodwill has suffered any impairment, in accordance with the accounting policy stated in Note 2(j). The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. The carrying amount of the goodwill and the key assumptions made are set out in Note 18.

b) Fair value estimation

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Group uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting date. The Group has used a discounted cash flow analysis for various available-for-sale financial assets that are not traded in active markets.

c) Income taxes

The Group is subject to income taxes in various jurisdictions. Significant judgment is required in determining the Group's provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

d) Impairment of available-for-sale assets

The Group determines that available-for-sale equity investments are impaired when there has been significant or prolonged decline in fair value below its cost. The determination of what is significant or prolonged requires judgement. In making this judgement, the Group evaluates among other factors, the normal volatility in share price. In addition, impairment may be appropriate when there is evidence of deterioration of the financial health of the investee, industry and sector performance, changes in technology and operational and financial cash flows.

e) The classification of financial investments

In applying the Groups accounting policies, management has made judgement in determining the classification of financial investments as held-to-maturity, available

for sale and loans and receivables in line with IAS 39. The classifications require judgement of the Group's ability and intention to hold the investments to maturity.

f) Insurance contract liabilities

It is the statutory requirement in Kenya that the insurance contract liabilities are calculated on the statutory Net Present Valuation (NPV) basis. The NPV is intended to measure the solvency of the life operation on a stable basis and examines the business from the point of view of premiums that are net of standard expense allowances the value of future net premium is compared with the cost of providing contractual policyholder benefits over the duration of the policy. When performing the liability adequacy test, all classes for which undiscounted liabilities were calculated, a discounted cash flow model was created based on the "best estimate" assumptions. Prudent margins are added to these to project cash flows. These are then discounted at the valuation interest rate.

(i) Mortality

An appropriate base table of standard mortality is chosen depending on the type of contract and class of business. Industry standard tables are used for smaller classes of business, while Group specific tables are used for larger classes. Estimates are made as to the expected number of deaths for each of the years in which the Group is exposed to risk.

The Group bases these estimates on standard mortality tables that reflect historical mortality experience. The estimated number of deaths determines the value of the benefit payments and the value of the valuation premiums.

The main source of uncertainty is that epidemics such as AIDS could result in future mortality being significantly worse than in the past for the age Groups in which the Group has significant exposure to mortality risk.

However, continuing improvements in medical care and social conditions could result in improvements in longevity in excess of those allowed for in the estimates used to determine the liability for contracts where the Company is exposed to longevity risk.

For contracts without fixed terms, it is assumed that the Group will be able to increase mortality risk charges in future years in line with emerging mortality experience.

An investigation into mortality experience is performed annually. The period investigation extends over the latest three full years for larger classes of business. Investigations relating to smaller classes usually extend over five years in order to gain sufficient credibility of the data. The results of the investigation are used to set the valuation assumptions, which are taken as an adjustment to the respective standard table.

In setting the assumptions, provision is made for the expected increase in AIDS-related claims. In general, Actuarial Society of South Africa (ASSA) models are used to allow AIDS-related claims. The practice differs by class of business, however for major classes of business, a basic allowance for AIDS related deaths is included in the base mortality rates against which annual mortality investigations are conducted. A further

discretionary margin is then held using the ASSA2000 lie model.

(ii) Morbidity

The incidence of disability claims is derived from industry experience studies, adjusted, where appropriate, for Group Companies own experience. The same is true for the incidence of recovery from disability.

(iii) Medical

The incidence of medical claims is derived from the risk premium rates determined from annual investigations. This is adjusted, where appropriate, to allow for the future expected experience.

(iv) Withdrawal

The withdrawal assumptions are based on the most recent withdrawal investigations, taking into account past as well as expected future trends. The withdrawal rates are analysed by product type and policy duration. These withdrawal rates vary considerably by duration and policy term. Typically the rates are higher for risk type products versus investment type products, and are higher at early durations.

(v) Correlation

No correlations between assumptions are allowed for.

4. Segmental reporting

The Group is currently organised in line with the Insurance Act which classifies insurance and investment contracts into two main categories (long-term and general) depending on the duration of risk.

The results of the business units are reviewed regularly by Board in order to make decisions about resources to be allocated to segments and assessing segment performance.

The Group is required to produce segmented financial statements i.e. income statement and statement of financial position in compliance with IFRS 8.

An operating segment is a component of the Group engaged in business activities, whose operating results are reviewed regularly by management in order to make decisions about resources to be allocated to segments and assessing segment performance. Identification of segments and the measurement of segment result is based on the Group's internal reporting to management.

The geographical spread (across borders) is also used as a part of performance analysis.

a) Long term insurance business

Includes insurance business of all or any of the following classes, namely, life assurance business, superannuation business, industrial life assurance business and bond investment business and business incidental to any such class of business;

Life assurance business means the business of, or in relation to, the issuing of, or the undertaking of liability to pay money on death (not being death by accident or in specified sickness only) or on the happening of any contingency dependent on the termination or continuance of human life (either with or without provision for a

benefit under a continuous disability insurance contract), and include a contract which is subject to the payment of premiums for term dependent on the termination or continuance of human life and any contract securing the grant of an annuity for a term dependent upon human life;

Superannuation business means life assurance business, being business of, or in relation to, the issuing of or the undertaking of liability under superannuation, Group life and permanent health insurance policy.

b) General insurance business

Includes insurance business of any class or classes not being long term insurance business. Classes of General Insurance include Aviation insurance, Engineering insurance, Fire insurance - domestic risks, Fire insurance - industrial and commercial risks, Liability insurance, Marine Insurance, Motor insurance - private vehicles , Motor insurance - commercial vehicles, Personal accident insurance, Theft insurance ,Workmen's Compensation and Employer's Liability insurance and Miscellaneous insurance (i.e. class of business not included under those listed above)

Motor insurance business means the business of affecting and carrying out contracts of insurance against loss of, or damage to, or arising out of or in connection with the use of, motor vehicles, inclusive of third party risks but exclusive of transit risks.

Personal Accident insurance business means the business of affecting and carrying out contracts of insurance against risks of the persons insured sustaining injury as the result of an accident or of an accident of a specified class or dying as the result of an accident or of an accident of a specified class or becoming incapacitated in consequence of disease or of disease of a specified class.

Fire insurance business means the business of affecting and carrying out contracts of insurance, otherwise than incidental to some other class of insurance business against loss or damage to property due to fire, explosion, storm and other occurrences customarily included among the risks insured against in the fire insurance business.

Major Customers

The Group does not have any one major customer that contributes more than 10 percent of its revenues.

i) Results by business units

	31 December 2012		
	Long term business Shs'000	General business Shs'000	Total Shs'000
Net insurance premium revenue	**1,329,424**	**2,652,962**	**3,982,386**
	2,235,968	**1,242,510**	**3,478,478**
Commissions earned	70,890	589,551	660,441
Investment income	2,151,786	440,110	2,591,896
Administration fees	13,292	-	13,292
Other income	-	212,849	212,849
Total income	**3,565,392**	**3,895,472**	**7,460,864**
Net insurance benefits and claims	**(1,978,637)**	**(1,130,285)**	**(3,108,922)**
Total expenses and commissions	**(1,166,371)**	**(2,006,374)**	**(3,172,745)**
Result of operating activities	**420,384**	**758,813**	**1,179,197**
Earnings from associates	-	23,704	23,704
Profit before taxation	**420,384**	**782,517**	**1,202,901**
Income tax expense	(50,210)	(266,020)	(316,230)
Profit for the year	**370,174**	**516,497**	**886,671**
Total assets	**19,970,373**	**7,419,973**	**27,390,346**
Property and equipment	660,922	436,677	1,097,599
Intangible assets	63,180	4,314	67,494
Investment property	428,449	282,000	710,449
Financial investments	2,332,111	12,501,251	14,833,362
Reinsurers' share of insurance liabilities	779,028	1,261,864	2,040,892
Total liabilities	**16,504,841**	**5,463,914**	**21,968,755**
Insurance contract liabilities	5,353,724	2,185,133	7,538,857
Payable under deposit administration contracts	10,104,276	-	10,104,276
Unearned premium reserve	45,296	2,279,991	2,325,287
Borrowings	239,898	239,898	479,796
Additions to property and equipment	74,688	25,296	99,984
Additions to intangible assets	13,909	2,028	15,937

	31 December 2011		
	Long term business Shs'000	**General business Shs'000**	**Total Shs'000**
Net insurance premium revenue	1,292,262	2,945,671	4,237,933
Commissions earned	62,739	450,286	513,025
Investment income	1,201,073	439,557	1,640,630
Administration fees	12,010	1,927	13,937
Other income	-	27,730	27,730
Total income	**2,568,084**	**3,865,171**	**6,433,255**
Net insurance benefits and claims	**(961,814)**	**(1,520,680)**	**(2,482,494)**
Total expenses and commissions	**(872,248)**	**(2,068,679)**	**(2,940,9270**
Result of operating activities	**734,022**	**275,812**	**1,009,834**
Earnings from associates	-	2,381	2,381
Profit before taxation	**734,022**	**278,193**	**1,012,215**
Income tax expense	7,538	(69,335)	(61,797)
Profit for the year	**741,560**	**208,858**	**950,418**
Total assets	**16,977,464**	**7,316,069**	**24,293,533**
Property and equipment	656,623	399,938	1,056,561
Intangible assets	100,935	19,031	119,966
Investment property	412,500	211,053	623,553
Financial investments	5,316,180	9,194,696	14,510,876
Reinsurers' share of insurance liabilities	459,465	1,657,670	2,117,135
Total liabilities	**14,366,885**	**5,752,051**	**20,118,936**
Insurance contract liabilities	4,356,511	2,332,799	6,689,310
Payable under deposit administration contracts	9,237,856	-	9,237,856
Unearned premium reserve	-	2,242,031	2,242,031
Borrowings	252,311	252,311	504,621
Additions to property and equipment	14,090	63,277	77,367
Additions to intangible assets	8,047	3,553	11,600

ii) Results by geographical spread

The Tanzanian subsidiary contributed approximately 19% of the Group's consolidated income.

	31 December 2012		
	Kenya Shs'000	**Tanzania Shs'000**	**Total Shs'000**
Net insurance premium revenue	**3,408,824**	**573,562**	**3,982,386**
	2,987,382	**491,096**	**3,478,478**
Commissions earned	462,995	197,446	660,441
Investment income	2,496,512	95,384	2,591,896
Administration fees	13,292	-	13,292
Other income	14,583	198,266	212,849
Total income	**6,396,206**	**1,064,658**	**7,460,864**
Net insurance benefits and claims	**(2,818,300)**	**(290,622)**	**(3,108,922)**
Total expenses and commissions	**(2,692,575)**	**(480,170)**	**(3,172,745)**
Result of operating activities	**885,331**	**293,866**	**1,179,197**
Earnings from associates	-	23,704	23,704
Profit before taxation	**885,331**	**317,570**	**1,202,901**
Income tax expense	(166,301)	(149,929)	(316,230)
Profit for the year	**719,030**	**167,641**	**886,671**
Total assets	**24,143,508**	**3,246,838**	**27,390,346**
Property and equipment	1,085,880	11,719	1,097,599
Intangible assets	67,224	270	67,494
Investment property	710,449	-	710,449
Financial investments	14,006,211	827,151	14,833,362
Reinsurers' share of insurance liabilities	909,534	1,131,358	2,040,892
Total liabilities	**19,526,419**	**2,442,336**	**21,968,755**
Insurance contract liabilities	6,560,922	977,935	7,538,857
Payable under deposit administration contracts	10,104,276	-	10,104,276
Unearned premium reserve	1,432,543	892,744	2,325,287
Borrowings	479,796	-	479,796
Additions to property and equipment	92,511	7,473	99,984
Additions to intangible assets	15,937	-	15,937

	31 December 2011		
	Kenya	**Tanzania**	**Total**
	Shs'000	**Shs'000**	**Shs'000**
Net insurance premium revenue	**3,708,527**	**529,406**	**4,237,933**
	1,894,879	**300,443**	**2,195,322**
Commissions earned	334,714	178,311	513,025
Investment income	1,537,612	103,018	1,640,630
Administration fees	13,937	-	13,937
Other income	8,616	19,114	27,730
Total income	**5,603,406**	**829,849**	**6,433,255**
Net insurance benefits and claims	**(2,174,282)**	**(308,212)**	**(2,482,494)**
Total expenses and commissions	**(2,531,223)**	**(409,704)**	**(2,940,927)**
Result of operating activities	**897,901**	**111,933**	**1,009,834**
Earnings from associates	-	2,381	2,381
Profit before taxation	**897,901**	**114,314**	**1,012,215**
Income tax expense	(29,682)	(32,115)	(61,797)
Profit for the year	**868,219**	**82,199**	**950,418**
Total assets	**20,752,478**	**3,541,055**	**24,293,533**
Property and equipment	1,041,067	15,494	1,056,561
Intangible assets	105,660	14,306	119,966
Investment property	623,553	-	623,553
Financial investments	13,779,743	731,133	14,510,876
Reinsurers' share of insurance liabilities	643,941	1,473,194	2,117,135
Total liabilities	**17,329,835**	**2,789,101**	**20,118,936**
Insurance contract liabilities	5,440,982	1,248,328	6,689,310
Payable under deposit administration contracts	9,237,856	-	9,237,856
Unearned premium reserve	1,343,097	898,934	2,242,031
Borrowings	504,621	-	504,621
Additions to property and equipment	66,798	10,569	77,367
Additions to intangible assets	10,806	794	11,600

5. Financial risk management objectives and policies

Liberty Kenya Holdings Limited (the Group) offers a comprehensive range of financial products and services to the retail and corporate markets, distributing tailored risk, insurance, investment, retirement and health products through its network. The Group is committed to increasing shareholder value through the prudent management of risks inherent in the production, distribution and maintenance of these products and services. The Group is mindful of achieving this objective in the interests of all stakeholders. The Group continues to explore opportunities to develop and grow its business organically, with strategic plans being subject to careful consideration of the trade-off between risk and reward, taking into account the risk appetite limits approved by the board

The Group's main value creation activities can be summarised into the following categories:

- *Providing risk cover* – Liberty Kenya Holdings Limited's core competency is to understand the life, health and asset related risk needs of individuals and Groups, and design sustainable products that provide financial security to policyholders and their families in times of death, sickness or ill health, disability and other losses.
- *Providing asset management services* – through its subsidiaries, the Group uses its financial skills to provide competitive investment products and investment advice to a broad range of customers.
- *Assuming market risk* – through the management of assets backing shareholder funds and of exposures arising from asset-liability mismatches which the Group wishes to retain.

Ultimate responsibility for risk management resides with the Board which ensures that all business unit executives are responsible and are held accountable for risk management within the subsidiaries. Risks are controlled at the level of individual exposures and at portfolio level, as well as in aggregate across all businesses and risk types.

a) Risk management objectives

The Group's key risk management objectives are to:

- Grow shareholder value by generating a long-term sustainable return on capital;
- Ensure the protection of policyholder and investor interests by maintaining adequate solvency levels;
- Meet the statutory requirements of the Kenyan Insurance Act, and other regulators; and
- Ensure that capital and resources are strategically focused on activities that generate the greatest value on a risk adjusted basis.

The management of risks is currently focused on managing shareholder exposures within strategic limits whilst ensuring sufficient allocation of capital on both a regulatory and economic capital basis given the limits in place.

b) Capital management

The capital management strategy seeks to ensure that the Group is adequately capitalised to support the risks assumed by the Group in accordance with the Group's

risk appetite. It further seeks to fund working capital and strategic requirements, thereby protecting policyholder and customer interests while optimising shareholder risk adjusted returns and delivering in accordance with the Group's dividend policy.

Due to varying requirements of different stakeholders, the Group reports and manages capital on a number of different bases. The capital management process ensures that the Group's available capital exceeds the capital required both currently and going forward and to ensure that the Group has unfettered access to its capital at all times to meet its requirements.

Capital management – Company

The Company's objective in capital management is to safeguard the Company's ability to continue as going concern in order to provide returns for share holders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Company may limit the amount of dividends paid to shareholders, issue new shares or sell assets to reduce debt.

The Company monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings less cash and cash equivalents.

Total capital is calculated as equity plus net debt.

	Company	
	2012	**2011**
	Shs'000	**Shs'000**
Total borrowings	637,443	660,125
Due to group companies (Note 34)	(124,054)	(124,054)
Total borrowing	513,389	536,071
Less: cash and cash equivalents (Note 24)	(54,638)	(188,218)
Net debt	458,751	347,853
Total equity	**3,119,528**	**2,730,426**
Gearing ratio	**14.71%**	**12.74%**

Capital management – Group

The Board of Directors at the subsidiary Companies are responsible for monitoring and ensuring compliance with the regulatory framework as established by the Kenyan Insurance Regulatory Authority.

The subsidiaries are regulated by the Kenyan and Tanzanian Insurance Acts, Companies Acts and Insurance Regulatory Authorities. The objectives when managing capital are to:

- comply with the capital requirements as set out in the Insurance Acts;
- comply with regulatory solvency requirements as set out in the Insurance Acts.
- safeguard the companies' ability to continue as going concerns, so that they can continue to provide returns to shareholders and benefits for other stakeholders; and

- provide an adequate return to shareholders by pricing insurance and investment contracts commensurately with the level of risk.

The Kenyan Insurance Act requires each insurance Company to hold the minimum level of paid up capital as follows;

	Regulatory requirement Shs' 000	CfC Life Assurance Limited Shs' 000	Heritage Insurance (Kenya) Shs' 000
General insurance business	300,000	-	500,000
Long-term insurance business	150,000	612,340	-

General insurance businesses are required to keep a solvency margin i.e. admitted assets less admitted liabilities equivalent to the higher of Shs 10 million or 15% of the net premium income during the preceding financial year.

Long term insurance businesses are required to keep a solvency margin i.e. admitted assets less admitted liabilities equivalent to the higher of Shs 10 million or 5% of total admitted liabilities.

The Tanzanian Insurance Act requires each insurance Company to hold the minimum level of paid up capital as follows;

- Composite insurance companies TShs 1,000 million
- General insurance business companies TShs 500 million and
- Long term insurance business companies TShs 500 million

As at the year end, The Heritage Insurance Company (T) Limited had authorised number of ordinary shares of 100,000 with a par value of TShs 100,000, of these 60,000 shares were issued and fully paid (2011: 40,000 shares of TShs 100,000 each). This was in excess of the minimum requirement.

The solvency margin of the subsidiaries as at 31 December 2012 and 31 December 2011 are set out below:

CfC Life Assurance Limited

	Long-term business 2012 Shs'000	Long-term business 2011 Shs'000
Admitted assets	17,866,625	13,063,634
Admitted liabilities	(16,058,367)	(12,371,249)
Solvency margin	**1,808,258**	**692,385**
Required margin	**802,918**	**618,562**

Heritage Insurance Kenya Limited

	Long-term business 2012 Shs'000	Short-term business 2012 Shs'000	Long-term business 2011 Shs'000	Short-term business 2011 Shs'000
Total admitted assets	-	4,250,522	1,957,813	3,415,205
Total admitted liabilities	-	(2,968,364)	(1,624,186)	(2,771,205)
Add: 5% of admitted liabilities	-	-	(81,209)	-
Add: 15% of previous year's net written premium	-	(356,443)	-	(272,261)
Total liabilities and minimum requirement	-	(3,324,807)	(1,705,395)	(3,043,466)
Solvency margin	-	925,715	252,418	371,739
Required margin	-	356,443	85,270	152,117

Heritage Insurance Tanzania Limited

	2012 Shs'000	2011 Shs'000
Total admitted assets	1,575,067	1,547,011
Total admitted liabilities	(1,229,626)	(1,255,572)
Add: 15% of previous year's net written premium	(121,176)	(114,571)
Total liabilities and minimum requirement	(1,350,802)	(1,370,142)
Solvency margin	224,265	176,869
Required margin	121,176	35,973

c) Credit risk

Definition

Credit risk refers to the risk of loss or of adverse change in the financial position resulting, directly or indirectly from fluctuations in the credit standing of counterparties and any debtors to which shareholders and policyholders are exposed. Credit risk is a function of exposure at default and probability of default and comprises default, settlement and spread risk.

- Default risk is the risk of credit loss as a result of failure by counterparty to meet its financial and/or contractual obligations. It has three components:

- Issuer risk: the exposure at default (EAD) arising from traded credit products.
- Primary credit risk: the EAD arising from lending and related product activities. Primary credit risk generally refers to non-tradable, illiquid or hold-to-maturity credit risk.

- Settlement risk is the risk of loss from a transaction settlement, where value is exchanged, failing which the counter value is not received in whole or part.
- Spread risk (also known as credit migration risk) is the result of changes to spreads due to changing circumstances (micro and macro). It is the risk that a portfolio or counterparty's credit quality will materially deteriorate over time without allowing for a repricing of the exposure to compensate for the higher probability of default risk being carried.

Key activities that result in the origination of credit risk are:

- financial asset instruments including debt instruments (including bonds, loan, term deposits and investment policies);
- reinsurance assets including amounts due from reinsurers in respect of claims already paid;
- certain debtor accounts within the financial position categories of prepayments, insurance and other receivables;
- rental due where tenants have signed lease contracts for space within the Group's investment properties; and
- cash and cash equivalents.

Counterparty types to which the Group is exposed to credit risk include sovereigns (governments), state owned enterprises, financial institutions, corporate entities and loans to policyholders and staff. In addition, the Group is also exposed to credit risk through investment in securitisation issuance, mutual funds and investment policies.

Reinsurance assets

Reinsurance is used to manage insurance risk and consequently, in the liability valuation process, reinsurance assets are raised for expected recoveries on projected claims. This does not, however, discharge the Group's liability as primary insurer. In addition, reinsurance debtors are raised for specific recoveries on claims recognised.

Creditworthiness is assessed when appointing reinsurers. Financial position strength,

performance, track record, relative size and ranking within the industry and credit ratings of reinsurers are taken into account when determining the allocation of business to reinsurers. Credit exposure to reinsurers is also limited through the use of several reinsurers. A review of these reinsurers is continuously done.

Furthermore to mitigate credit exposures to reinsurers, reassurance management performs the following annual checks on reinsurers:

- copies of reinsurers' claim paying abilities, as assessed by reputable rating agencies, and copies of valuators' certificates are obtained and analysed;
- meetings and administration process audits are conducted with reinsurers with whom the Group has larger exposures; and
- reinsurance agreements are reviewed and amended, as appropriate, with accurate and complete records kept up to date.

Insurance and other receivables

The Group has formalised procedures in place to collect or recover amounts receivable. In the event of default, these procedures include industry supported lists that help to prevent rogue agents, brokers and intermediaries from conducting further business with the Group. Full impairment is made for non-recoverability as soon as management is uncertain as to the recovery.

Credit assessment changes recognised in the income statement

Fair value instruments

The Group invests in both listed and unlisted debt instruments. Changes to credit spreads for listed instruments are based on available market information and/or a proxy (where appropriate), combined with management input and override depending on the liquidity of the listed asset. Unlisted financial assets are generally not actively traded and changes to the credit spread for these instruments are fair valued with reference to proxy listed assets (where appropriate), combined with management input and override, market research and other compelling evidence which is all collated to form a view on current value.

Mortgages and loans, comprising policy loans, are impaired when the amount of the loan exceeds the policyholder's investment balance. The mortgages and loans are recoverable through offset against their respective liabilities (policy benefits) at policy maturity date.

The impairment loss is determined on an incurred loss approach as the difference between the instrument's carrying value and the present value of the asset's estimated future cash flows, including any recoverable collateral, discounted at the instrument's original effective interest rate. To provide for latent losses in a portfolio of loans where the loans have not yet been individually identified as impaired, impairment for incurred but not reported losses is recognised based on historic loss patterns and estimated emergence periods.

The amount that best represents the Group's maximum exposure to credit risk at 31 December 2012 is made up as follows:

Maximum exposure to credit risk before collateral held

	Group		Company	
	2012	2011	2012	2011
	Shs '000	Shs '000	Shs '000	Shs '000
Financial investments	14,833,362	14,510,876	-	-
Receivable arising from reinsurance	224,848	216,266	-	-
Receivable arising from direct insurance	662,212	740,559	-	-
Reinsurers' share of insurance liabilities	2,040,892	2,117,135	-	-
Other receivables	784,869	300,121	500,000	-
Cash and bank balances	5,478,339	2,699,606	54,638	188,218
	24,024,522	**20,584,563**	**554,638**	**188,218**

None of the above assets are past due or impaired except for insurance receivables (which are due upon invoicing):

	Group	
	2012	2011
	Shs '000	Shs '000
Neither past due nor impaired	365,556	465,600
Past due but not impaired	296,656	274,959
Impaired	215,507	153,165
Gross	**877,719**	**893,724**
Less: allowance for impairment	(215,507)	(153,165)
Net	**662,212**	**740,559**

	Group	
	2012	2011
	Shs '000	Shs '000
Past due but not impaired:		
- by up to 30 days	94,433	72,296
- by 31 to 60 days	38,805	41,720
- by 61 to 150 days	155,749	149,240
- by 151 to 360 days	7,669	11,703
Total past due but not impaired	**296,656**	**274,959**

All receivables past due by more than 360 days are considered to be impaired, and are carried at their estimated recoverable value.

Consideration of own credit risk for financial liabilities measured at fair value through profit or loss

Liberty Kenya Holdings Limited has considered the impact of changes in credit risk in the fair value measurement of its policyholder investment contract liabilities. Credit risk changes will only have a significant impact in extreme circumstances, when the Group's ability to fulfil the contract terms is considered to be under threat. The Group remains well capitalised and accordingly no adjustment to the valuation for credit risk has been made for the years under review.

d) Operational risk

Definition

Operational risk is the risk of loss caused by inadequate or failed internal processes, people and systems, or from external events. Operational risk is therefore pervasive across all financial institutions and all other operational companies.

Operational risk is recognised as a distinct risk category which the Group strives to manage within acceptable levels through sound operational risk management practices. The Group's approach to managing operational risk is to adopt practices that are fit for purpose to suit the organisational maturity and particular business environments.

Executive management defines the operational risk appetite at a Group and subsidiary level. This operational risk appetite supports effective decision-making and is central to embedding effective risk management. The objective in managing operational risk is to increase the efficiency and effectiveness of the Group's resources, minimise losses and utilise opportunities.

Ownership and accountability

Management and staff at every level of the business are accountable for the day-to-day identification and management of operational risks. It is also management's responsibility to report any material operational risks, risk events and issues identified to senior management through certain pre-defined escalation procedures.

Risk identification, assessment and measurement

The process of operational risk management starts with the operational risk assessment of identified areas. Consideration is then given to the need for a Group or business unit policy to define the approach to mitigating this risk.

Risk and compliance policies are developed where necessary to:

- ensure compliance with internal principles and with legal and regulatory requirements,
- address associated risks in the business, define roles, responsibilities and expectations at all levels,
- guide staff at all levels on how to conduct Group's business
- ensure that staff apply consistent processes throughout the Group, and
- help management to develop operating processes.

Policies are approved at the appropriate governance level subject to compliance with Group policy principles. Once identified, operational risks are assessed to determine

the potential impact to the Group should the risk events occur, and reviewed against the Group's risk appetite. Mitigating actions are developed for any operational risks that fall outside of management's assessment of risk appetite.

Risk management activities in relation to operational risks include but are not limited to:

Information technology (IT) risk: The Group is highly dependent on and constantly increasing its use of information technology to ensure improved operations and customer service. The Group's IT systems enable it to take its products to markets across the East African Region and so carry out its expansion strategy.

The Group is, therefore, exposed to various IT risks which include the disruption of transaction processing, information loss and/or malicious attacks from third parties.

Maintaining technological advantage requires a strong IT risk management culture and function that allows the Group to identify and manage IT risks effectively. In order to prevent potential risk events and ensure best practice levels of continuous IT service and security, management review and ensure compliance with relevant IT policies and procedures, conduct control and risk self-assessments and are subject to internal and external audits.

Process risk: The Group's approach to process improvement focuses on process efficiency and work quality. The processes undergoing improvement incorporate input from risk and compliance specialists, as well as other generic process stakeholders and Group finance.

Regulatory risk: The regulatory environment is monitored closely to ensure that the Group implements new or amended legislation requirements promptly to ensure compliance and avoid unnecessary fines and penalties or the revocation of any business license.

Compliance risk: The risk of regulatory sanctions, financial loss or damage to reputation as a result of not complying with legislation, regulation or internal policies is managed through the established compliance functions within the Group and a compliance policy. The policy ensures that compliance requirements are identified and implemented through the development of appropriate policies and procedures and that regular monitoring and reporting of breaches is carried out within the businesses and at the centre to provide the board with assurance on the status of compliance within the organization.

Taxation risk: Tax risk is the risk of suffering a loss, financial or otherwise, as a result of an incorrect interpretation and application of taxation legislation or the impact of new taxation legislation on existing products. Tax risk can also arise if the Group's objectives in relation to its tax strategy are not met.Corporate governance, increasingly complex tax legislation as well as improved tax collection and enforcement by revenue authorities, are driving increased focus on tax risk and the controls that mitigate tax risk to an acceptable level.

Human resources: The Group remains concerned about the availability of specialist technical skills available in East Africa to provide first world financial services. It focuses on recruitment, development and retention through a number of Group-wide initiatives.

Business continuity management (BCM): BCM is implemented to reduce the risk of not continuing normal business activities should a crisis occur. BCM is an integral component of the Group's risk management framework. The various subsidiaries are regularly exposed to deployment of updated methodologies, testing and training to ensure increased capability to deal with interruptions to business. The Group's has established a BCM site at Mlolongo along Mombasa road where critical staff and core services can be relocated incase of disruptions to business at the usual business premises.

Internal and external fraud: The Group adopts a 'zero-tolerance' approach to fraud. The Group internal audit function supports management in meeting their objective of minimising fraud risk. In terms of the Group's anti- fraud policy, line management is responsible for ensuring that controls at all stages of a business process are adequate for the prevention and detection of fraud. Prevention and detection measures are periodically rolled out by forensic services to support management.

e) Liquidity risk

Definition

Liquidity risk is the risk that the Group, although solvent, is not able to settle its obligations as they fall due because of insufficient cash in the Group. This might arise in circumstances where the Group's assets are not marketable, or can only be realised at excessive cost. The principal risk relating to liquidity comprises the Group's exposure to policyholder behaviour.

Ownership and accountability

The ownership and accountability for liquidity risk is the same as for market risk. Liquidity requirements are reviewed on an ongoing basis as part of the Group's normal operating activities at the subsidiary level.

Liquidity profile of assets

The Group's assets are liquid however given the quantum of investments held relative to the volumes of trading a substantial short-term liquidation may result in current values not being realised due to demand and supply principles. It is considered highly unlikely, however, that a short-term realisation of that magnitude would occur.

Liquidity risks arising out of obligations to policyholders

On unit-linked business, liquidity risk and asset-liability matching risk arising as a result of changes in lapse and withdrawal experience is limited through policy terms and conditions that restrict claims to the value at which assets are realised. Similarly the liquidity and asset-liability matching risk arising from a change in withdrawal experience on business with DPF is limited through policy terms and conditions that permit withdrawal benefits to be altered in the event of falling asset prices.

The table below presents the cash flows receivable and payable by the Group under financial assets and liabilities by remaining expected maturities at the reporting date.

Liquidity risk management

As at 31 December 2012	1-3 months Shs'000	3-12 months Shs'000	1-5 years Shs'000	Over 5 years Shs'000	Total Shs'000
Liabilities					
Insurance contract liabilities	3,048,057	1,809,573	1,504,395	1,176,833	7,538,857
Payable under deposit administration	1,555,789	778,167	4,247,839	3,522,481	10,104,276
Creditors arising from reinsurance	(120,137)	473,924	-	-	353,787
Creditors arising from direct insurance	(27,320)	72,731	-	-	45,411
Other payables	899,497	6,942	3,996	-	910,435
Borrowings	479,796	-	-	-	479,796
Total financial liabilities	**5,835,682**	**3,141,336**	**5,756,230**	**4,699,314**	**19,432,562**
Assets					
Other receivables	765,645	19,224	-	-	784,869
Reinsurers' share of insurance liabilities	1,277,500	656,094	107,298	-	2,040,892
Receivable arising from reinsurance	97,745	127,103	-	-	224,848
Financial investments	7,697,049	465,304	3,950,357	2,720,653	14,833,362
Receivable arising from direct insurance	141,696	520,516	-	-	662,212
Cash and cash equivalents	5,478,339	-	-	-	5,478,339
Total financial assets	**15,457,973**	**1,788,241**	**4,057,655**	**2,720,653**	**24,024,522**
Net liquidity gap	**9,622,291**	**(1,353,095)**	**(1,698,575)**	**(1,978,661)**	**4,591,960**

As at 31 December 2012	1-3 months Shs'000	3-12 months Shs'000	1-5 years Shs'000	Over 5 years Shs'000	Total Shs'000
As at 31 December 2011					
Liabilities					
Insurance contract liabilities	2,198,510	1,809,572	1,504,395	1,176,833	6,689,310
Payable under deposit administration	689,369	778,167	4,247,839	3,522,481	9,237,856
Creditors arising from reinsurance	1,556	473,924	-	-	475,480
Creditors arising from direct insurance	-	72,731	-	-	72,731
Other payables	705,031	6,942	3,996	-	715,969
Bank overdraft	70,091	-	-	-	70,091
Borrowings	504,621	-	-	-	504,621
Total financial liabilities	**4,169,178**	**3,141,336**	**5,756,230**	**4,699,314**	**17,766,058**
Assets					
Other receivables	280,897	19,224	-	-	300,121
Reinsurers' share of insurance liabilities	1,353,743	656,094	107,298	-	2,117,135
Receivable arising from reinsurance	89,163	127,103	-	-	216,266
Financial investments	7,374,563	465,304	3,950,357	2,720,652	14,510,876
Receivable arising from direct insurance	220,043	520,516	-	-	740,559
Cash and cash equivalents	2,699,606	-	-	-	2,699,606
Total financial assets	**12,018,015**	**1,788,241**	**4,057,655**	**2,720,652**	**20,584,563**
Net liquidity gap	**7,848,837**	**(1,353,095)**	**(1,698,575)**	**(1,978,662)**	**2,818,505**

Long term insurance and deposit administration contracts can be surrendered before maturity for a cash surrender value specified in the contractual terms and conditions. Prudent liquidity risk management includes maintaining sufficient cash balances to cover anticipated surrenders before the contractual maturity dates. In addition, the Group invests only a limited proportion of its assets in investments that are not actively traded. The Group's listed securities are considered readily realisable, as they are actively traded on the Nairobi Stock Exchange.

Liquidity risk – Company

Ultimate responsibility for liquidity risk management rests with the Board of Directors, which has built an appropriate liquidity risk management framework for the management of the Company's short, medium and long-term funding and liquidity management requirements. The Company manages liquidity risk by continuous monitoring of banking facilities, cash flow forecasts and actual cash flows.

The table below analyses the Company's financial liabilities that will be settled on a net basis into relevant maturity Groupings based on the remaining period at the balance sheet date to the contractual maturity date.

The amounts disclosed in the table below are the contractual undiscounted cash flows.

At 31 December 2012	**Less than 1 year Shs'000**	**Over 1 year Shs'000**	**Total Shs'000**
Due to group companies (Note 34)	124,054	-	124,054
Borrowings	479,796	-	479,796
	603,850	**-**	**603,850**
At 31 December 2011			
Due to group companies (Note 34)	124,054	-	155,504
Borrowings	504,621	-	504,621
	628,675	**-**	**660,125**

Capital requirements

The Group's view is that liquidity risk has to be managed by means other than capital. If assets and liabilities are not well matched by term, even a large amount of capital may provide only a small buffer in an extreme liquidity event.

Liquidity risk is most likely to arise due to a sharp increase in benefit withdrawals or risk-related claims. The liquidity risk arising from withdrawals is largely managed by policy terms and conditions in the contract that enable the Group to reduce withdrawal benefits in the event that asset prices fall. The liquidity risk arising from risk-related claims is managed by having reinsurance arrangements in place for catastrophic events.

Liquidity risks arising on maturity benefits are managed by closely monitoring the expected future maturities and realising assets in advance if large outflows are expected.

Liquidity risk is also managed by matching liabilities with backing assets that are of similar maturity, duration and risk nature. The liquidity profile of the total financial position is reviewed on a regular basis to ensure that the cash flow profile of liabilities can be met as they fall due.

As a result of the liquidity risk mitigation measures in place, the Group's exposure to liquidity risk is expected to be small and no allowance is currently made for liquidity risk.

f) Market risk

Definition

Market risk is the risk of adverse financial impact due to changes in fair values or future cash flows of financial instruments from fluctuations in equity prices, interest rates and foreign currency exchange rates (as well as their associated volatilities). In addition, in light of the Group's significant investment in investment properties, there is exposure to fluctuation in property values.

The Group's shareholders are exposed to market risk arising from policyholder asset-liability mismatch risk. This is where the Group's property and financial assets do not move in the same direction and magnitude as the obligations arising under its insurance and investment contracts.

The key components of market risk are as follows:

- *Price risk:* is the risk arising from a change in the value and/or future cash flows of an asset or liability, as a result of securities price and/or dividend changes;
- *Interest rate risk:* is the risk arising from a change in the value and/or future cash flows of an asset or liability, as a result of interest rate changes;
- *Currency risk:* is the risk arising from a change in the value and/or future cash flows of an asset or liability as a result of changes in exchange rates. This can either be in the form of a mismatch between currencies of assets and liabilities, or on assets supporting capital, or the functional currency of the local entity being different to the reporting currency of the Group; and
- *Property market risk:* is the risk arising from a change in the value and/or future cash flows of an asset or liability, as a result of changes in property market prices and/or rental income.

Risk identification, assessment and measurement

In the case of market risks which arise from shareholder funds, the risk can be identified, assessed and measured by considering the market risks that apply to the assets in which these funds have been invested.

In the case of asset-liability mismatches, risks both to the assets and corresponding liabilities need to be assessed together. The Group is exposed to market risk to the extent that these exposures may result in a loss due to the assets increasing by less than the liabilities or the assets falling by more than the liabilities.

The Group assesses its asset-liability mismatch exposures with respect to the key components of market risk at subsidiary level.

i) Price risk

The Group is exposed to equity securities price risk because of investments in quoted and unquoted shares classified as available-for-sale. The Group is not exposed to commodity price risk. To manage its price risk arising from investments in equity and debt securities, the Group diversifies its portfolio. Diversification of the portfolio is done in accordance with limits set by the Group in the Investment Policy. All quoted shares held by the Group are traded on the Stock Exchange.

At 31 December 2012, if the market prices of equity had increased/decreased by 5% all other variables held constant, the fair value of equities held by the Group would have changed by Shs 51.2 Million (2011 Shs 112.3 Million). This would result in a change in 'other comprehensive income'.

ii) Interest rate risk

Fixed interest rate financial instruments expose the Group to fair value interest rate risk. Variable interest rate financial instruments expose the Group to cash flow interest rate risk. The Group's fixed interest rate financial instruments are government securities and deposits with financial institutions. The Group's variable interest rate financial instruments are quoted corporate bonds.

No limits are placed on the ratio of variable rate financial instruments to fixed rate financial instruments. The Group manages its cash flow interest rate risk by diversification of its portfolio.

The sensitivity analysis for interest rate risk illustrates how changes in the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates at the reporting date.

For liabilities under long-term insurance contracts with fixed and guaranteed terms, changes in interest rate will not cause a change to the amount of the liability, unless the change is severe enough to trigger a liability adequacy test adjustment. The level of the reduction of the level of interest rate that will trigger an adjustment is an interest rate of 1 % (2011: 1 %). Investment contracts with fixed and guaranteed terms, government securities and deposits with financial institutions held to maturity are accounted for at amortised cost and their carrying amounts are not sensitive to changes in the level of interest rates.

At 31 December 2012, if interest rates on quoted corporate bonds at that date had been 50 basis points higher/lower with all other variables held constant, post-tax profit for the period would have been Shs 9,070,080 (2011: 1,407,007) lower/higher, mainly as a result of higher/lower interest income on floating rate quoted corporate bonds.

iii) Currency risk

The Group operates regionally and is exposed to foreign exchange risk arising from various foreign currency transactions, primarily with respect to the US dollar. Foreign exchange risk arises from reinsurance transactions with foreign reinsurance brokers. This risk is not significant and is mitigated through the use of dollar-denominated accounts. In the year ending 31 December 2012, the Group had an equivalent of Shs 4 Million (2011: Shs. 12.8 Million) in reinsurance balances denominated in foreign currency and foreign currency deposit accounts. The impact of normal exchange fluctuations in the Kenya and Tanzania shilling against the US dollar would not have a material effect on Groups results.

iv) Property market risk

The Group is exposed to tenant default and unlet space within its investment property portfolio affecting property values and rental income. This risk is mainly attributable to the matching policyholder liability and the shareholder exposure is mainly limited to management fees and profit margins. The managed diversity of the property portfolio and the existence of multi-tenanted buildings significantly reduce the exposure to this risk.

g) Insurance risk

Definition

Insurance risk from management's perspective is the risk that future claims (in relation to death, disability, ill health and withdrawal) and expenses will exceed the allowance for expected claims and expenses in the measurement of policyholder liabilities and in product pricing. In addition to these insurance risks, the Group assumes further risks in relation to policyholder behaviour (including lapses and converting recurring premium policies to paid up) and tax which could have adverse impacts on the Group's earnings and capital if different from that assumed in the measurement of policyholder liabilities. From a risk management perspective, management Groups these risks under insurance risk.

Ownership and accountability

The management and staff in all subsidiaries taking on insurance risk are responsible for the day-to-day identification, management and monitoring of insurance risk. It is also management's responsibility to report any material insurance risks, risk events and issues identified to senior management through certain pre-defined escalation procedures.

The statutory actuaries and the heads of risk in the subsidiaries provide independent oversight of the compliance with the Group's risk management policies and procedures and the effectiveness of the Group's insurance risk management processes.

Risk identification, assessment and measurement

Insurance risks arise due to the uncertainty of the timing and amount of future cash flows arising under insurance contracts. The timing is specifically influenced by future mortality, longevity, morbidity, withdrawal and expenses about which assumptions are

made in the measurement of policyholder liabilities and in product pricing. Deviations from assumptions will result in actual cash flows being different from those expected. As such, each assumption represents a source of uncertainty.

Experience investigations are conducted at least annually on all insurance risks to ascertain the reasons for deviations from assumptions and their financial impacts. If the investigations indicate that these deviations are likely to persist in future, the assumptions will be adjusted accordingly in the subsequent measurement of policyholder liabilities. Insurance risks are assessed and reviewed against the risk appetite. Mitigating actions are developed for any risks that fall outside of management's assessment of risk appetite in order to reduce the level of risk to within the approved tolerance limits.

Risk management

The management of insurance risk is effectively the management of deviations of actual experience from the assumed best estimate of future experience. On the published reporting basis, earnings are expected as a result of the release of margins that have been added to the best estimate assumptions. The risk is that these earnings are less than expected due to adverse actual experience.

The statutory actuaries provide oversight of the insurance risks undertaken by the Group in that they are required to:

- report at least annually on the financial soundness of the life companies within the Group;
- approve policy for assumptions used to provide best estimates plus compulsory and discretionary margins.
- oversee the setting of these assumptions; and
- report on the actuarial soundness of premium rates in use for new business, and the profitability of the business, taking into consideration the reasonable benefit expectations of policyholders and the associated insurance and market risks.

The Group makes use of reinsurance to reduce its exposures to some insurance risks.

i) Policyholder behaviour risk

Policyholder behaviour risk is the risk of loss arising due to actual policyholder behaviour being different from expected.

The primary policyholder behaviour risk is persistency risk. This arises due to policyholders discontinuing or reducing contributions or withdrawing benefits partially or in total when this is not in line with expectations. This behaviour results in a loss of future charges that are designed to recoup expenses and commission incurred early in the life of the contract and to provide a profit margin or return on capital. Deterioration in persistency generally gives rise to a loss as the loss of these future charges generally exceeds the charges that the Group applies to the policyholder benefits in these events.

ii) Mortality and morbidity risk

Mortality risk is the risk of loss arising due to actual death rates on life assurance business being higher than expected. Morbidity risk is the risk of loss arising due to policyholder health-related claims being higher than expected. The Group has the following processes and procedures in place to manage mortality and morbidity risk:

- Premium rates are differentiated by factors which historical experience has shown are significant determinants of mortality and morbidity claim experience.
- Terms are built into the policy contracts that permit risk premiums to be reviewed on expiry of a guarantee period. Delays in implementing increases in premiums, and market or regulatory restraints over the extent of the increases may reduce their mitigating effects.
  Furthermore, charges can only be increased to the extent that they can be supported by gross premiums, although this is not relevant on contracts where gross premiums can be reviewed.
- Underwriting guidelines concerning authority limits and procedures to be followed are in place.
- All retail business applications for risk cover are underwritten. For smaller sums assured this process is largely automated. For retail and corporate business, larger sums assured in excess of specified limits are reviewed by experienced underwriters and evaluated against established processes. For corporate risk business, these specified limits are scheme specific based on the size of the scheme and distribution of sums assured.
- Part of the underwriting process involves assessing the health condition and family medical history of applicants. Terms and conditions are varied accordingly.
- The policy terms and conditions contain exclusions for non-standard and unpredictable risks that may result in severe financial loss (e.g. on life policies, a suicide exclusion applies to the sum assured for death within two years from the date of issue).
- The actual claims experience is monitored on a regular basis so that deteriorating experience can be timeously identified. Product pricing and the measurement of the liabilities is changed if the deteriorating experience is expected to continue and cannot be mitigated. Detailed mortality and morbidity investigations are conducted on a bi-annual basis, but mortality claim ratios are reviewed monthly.
- For morbidity, experienced claims assessors determine the merits of the claim in relation to the policy terms and conditions. In the case of disability annuitants, claim management ensures the continued eligibility for monthly income and includes interventions that may result in the full or partial medical recovery of the claimant. The actual disability experience is highly dependent on the quality of the claim assessments.
- Reinsurance arrangements are put in place to reduce the mortality and morbidity exposure per individual and provide cover in catastrophic events.

The Group views mortality and morbidity risks as risks that are core to the business.

iii) Longevity risk

Longevity risk is the risk of loss arising due to annuitants living longer than expected.

For life annuities, the loss arises as a result of the Group having undertaken to make regular payments to policyholders for their remaining lives, and possibly to the policyholders' spouses for their remaining lives. The most significant risk on these liabilities is continued medical advances and improvement in social conditions that lead to longevity improvements being better than expected.

The Group manages the longevity risk by:

- annually monitoring the actual longevity experience and identifying trends over time; and
- making allowance for future mortality improvements in the pricing of new business and the measurement of policyholder liabilities – this allowance will be based on the trends identified in experience investigations and external data.

iv) Expense risk

Expense risk is the risk of loss arising due to expenses incurred in the administration of policies being higher than expected.

Allowance is made for expected future expenses in the measurement of policyholder liabilities. These expected expenses are dependent on estimates of the number of in-force and new business policies. As a result, the risk of expense loss arises due to expenses increasing by more than expected as well as the number of in-force and/or new business policies being less than expected.

The Group manages the expense risk by:

- regularly monitoring actual expenses against the budgeted expenses;
- regularly monitoring new business;
- regularly monitoring withdrawal rates including lapses; and
- implementing cost control measures in the event of expenses exceeding budget or of significant unplanned reductions in in-force policies.

v) Tax risk

Tax risk is the risk of loss arising due to the actual tax assessed being more than the tax expected. Allowance for tax is made in the measurement of policyholder liabilities at the rates applicable at the financial reporting date. Adjustments may be made for known future changes in the tax regime.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be. In addition, a more diversified portfolio is less likely to be affected across the board by a change in any subset of the portfolio.

The Group has developed its insurance underwriting strategy to diversify the type of insurance risks accepted and within each of these categories to achieve a sufficiently large population of risks to reduce the variability of the expected outcome. Factors

that aggravate insurance risk include lack of risk diversification in terms of type and amount of risk, geographical location and type of industry covered.

The following tables disclose the concentration of insurance liabilities by the class of business in which the contract holder operates and by the maximum insured loss limit included in the terms of the policy:

Year ended 31 December 2012 (Shs '000)

General insurance business		Shs 0m to Shs 15 m	Shs 15m to Shs 250m	Shs 250m to Shs 1,000m	Total
Personal accident	Gross	20,172,000	12,599,300	-	32,771,300
	Net	16,137,600	10,079,440	-	26,217,040
Motor	Gross	22,947,740	350,078	95,611,015	118,908,833
	Net	20,000,746	350,078	11,419,400	31,770,224
Fire	Gross	503,478,339	85,231,140	3,464,500	592,173,979
	Net	40,358,131	69,498,900	2,771,600	112,628,631
Other	Gross	181,287,493	40,920,900	7,462,600	229,670,993
	Net	56,569,169	35,579,700	3,770,880	95,919,749
Life assurance business					
Ordinary life	Gross	20,177,761	274,165	-	20,451,926
	Net	17,001,846	12,000	-	17,013,846
Group life	Gross	55,751,491	17,505,081	300,000	73,556,572
	Net	34,068,563	1,460,000	2,000	35,530,563
Total	**Gross**	**803,814,824**	**156,880,664**	**106,838,115**	**1,067,533,603**
	Net	**184,136,055**	**116,980,118**	**17,963,880**	**319,080,053**

Year ended 31 December 2011 (Shs '000)

General insurance business		**Shs 0m to Shs 15 m**	**Shs 15m to Shs 250m**	**Shs 250m to Shs 1,000m**	**Total**
Personal accident	Gross	18,451,445	7,544,210	600,000	26,595,655
	Net	18,451,445	7,544,210	600,000	26,595,655
Motor	Gross	18,877,793	3,002,541	2,141,373	24,021,707
	Net	18,665,263	863,967	819,135	20,348,365
Fire	Gross	40,648,298	56,599,945	514,348,195	611,596,438
	Net	39,330,651	43,405,208	11,089,732	93,825,591
Other	Gross	18,643,213	45,737,553	142,703,967	207,084,733
	Net	18,330,104	37,369,287	20,536,867	76,236,258
Life assurance business					
Ordinary life	Gross	19,966,633	3,013,700	-	22,980,333
	Net	16,536,549	47,500	-	16,584,049
Group life	Gross	26,647,742	12,519,867	718,086	39,885,695
	Net	14,439,718	962,500	4,000	15,406,218
Total	**Gross**	**143,235,124**	**128,417,816**	**660,511,621**	**932,164,561**
	Net	**125,753,730**	**90,192,672**	**33,049,734**	**248,996,136**

The concentration by sector or maximum insured loss at the end of the period is broadly consistent with the prior year.

h) Fair value hierarchy

Introduction

Fair value is the amount for which an asset could be exchanged or liability settled between knowledgeable willing parties in an arm's length transaction. IFRS 7 requires disclosure of fair value measurements by level according to the following fair value measurement hierarchies:

- level 1 – Values are determined using readily and regularly available quoted prices in an active market for identical assets or liabilities. These prices would primarily originate from the Nairobi Securities Exchange, or an international stock or bond exchange.
- level 2 – Values are determined using valuation techniques or models, based on assumptions supported by observable market prices or rates either directly (that is, as prices) or indirectly (that is, derived from prices) prevailing at the balance sheet date. The valuation techniques or models are periodically reviewed and the outputs validated. In 2012 and 2011, level 2 was composed of government securities which were valued based on quoted yield curves.
- level 3 – Values are estimated indirectly using valuation techniques or models for which one or more of the significant inputs are reasonable assumptions (that is unobservable inputs), based on market conditions.

The following table presents the Group's assets and liabilities that are measured at fair value at 31 December 2012.

31 December 2012	**Level 1 Shs'000**	**Level 2 Shs'000**	**Level 3 Shs'000**	**Total Shs'000**
Available-for-sale financial assets				
Quoted shares	1,023,974	-	-	1,023,974
Unquoted shares	-	-	212,172	212,172
Government securities and bonds	-	2,888,164	-	2,888,164
	1,023,974	**2,888,164**	**212,172**	**4,124,310**
31 December 2011				
Available-for-sale financial assets				
Quoted shares	2,301,229	-	-	2,301,229
Unquoted shares	-	-	226,880	226,880
Government securities and bonds	-	1,749,930	-	1,749,930
	2,301,229	**1,749,930**	**226,880**	**4,278,039**

6. Gross earned premium

	Group	
	2012 Shs' 000	**2011 Shs' 000**
Motor	1,262,691	1,183,386
Fire	1,499,039	1,299,887
Personal accident and medical	1,670,355	1,295,069
Retail life	1,156,761	1,260,993
Group life	357,711	339,636
Others	1,007,285	1,010,064
	6,953,842	**6,389,035**

7. Investment income

	Group		Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
Interest from Government securities	1,107,557	833,800	-	-
Interest on bank deposits	336,934	126,299	-	-
Interest from corporate bonds and commercial paper	197,996	197,241	-	-
Interest on loans and receivables	125,634	88,864	-	-
Rental income from investment property	46,750	34,659	-	-
Gain on sale of financial investments	536,186	254,084	-	-
Fair value gain on investment property	111,406	93,000	-	-
Dividend income	123,755	178,784	500,000	615,000
Impairment loss on available for sale investments	(18,930)	(94,348)	-	-
Others	24,608	(71,753)	-	-
	2,591,896	**1,640,630**	**500,000**	**615,000**

The Company's dividend income of Shs 500 Million (2011: 615 Million) was earned from the subsidiaries in the year.

8. Other income

	Group	
	2012	2011
	Shs' 000	Shs' 000
Profit on sale of property, plant and equipment	8,861	2,901
Foregn exchange gain	-	20,482
Miscellaneous income	10,803	4,347
Profit on sale of investment in associate (Note 13)	193,185	-
	212,849	**27,730**

9. Claims and policy holder benefits payable

	2012	2011
	Shs' 000	Shs' 000
Motor	605,788	615,143
Fire	11,452	498,641
Personal accident and medical	778,615	1,001,327
Death, maturity and surrender benefits	703,062	608,339
Interest payable on deposit administration contracts	834,249	351,828
Others	404,270	304,139
	3,337,436	**3,379,417**

10. Finance costs

	Group		Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
Interest on financial liabilities at amortised cost	95,179	74,233	97,254	78,534
	95,179	**74,233**	**97,254**	**78,534**

11. Other operating expenses

	Group		Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
Staff costs (Note 12)	996,069	1,006,195	-	-
Auditors' remuneration	17,751	11,796	2,447	3,076
Depreciation (Note 20)	116,144	101,276	-	-
Amortisation of intangible assets (Note 22)	68,437	74,003	-	-
Impairment charges/(reversal) for doubtful receivables	58,164	21,216	-	-
Operating lease rental - land and buildings	53,351	70,395	-	-
Operating lease rentals - software	-	3,626	-	-
Directors' fees	14,222	14,931	3,492	2,599
Repairs and maintenance	91,042	20,438	-	-
Advertising	34,830	86,881	-	-
Legal and other professional fees	30,163	30,412	3,195	2,069
Others	705,304	422,457	4,510	2,922
	2,185,477	**1,863,626**	**13,644**	**10,666**

12. Staff costs

	Group	
	2012	2011
	Shs' 000	Shs' 000
Employee benefits expense includes the following:		
Salaries and wages	715,193	791,773
Social security benefit costs	41,650	35,048
Retirement benefit cost	37,080	26,329
Other	202,146	153,045
	996,069	**1,006,195**

The number of persons employed by the Group at the end of the year was 342 (2011: 366)

13. Investment in subsidiaries and associates

	Group 2012 Shs'000	2011 Shs'000
At 1 January 2012	355,400	313,180
Additions to Strategis Insurance (Tanzania) Limited shares	-	41,659
Share of profit after tax	23,704	2,381
Dividend received	(30,312)	(9,405)
Share of fair value reserve	17,847	17,847
Disposal of investments in Alliance Insurance Corporation Ltd	(303,154)	-
Currency adjustment	(1,537)	(10,262)
At 31 December	**61,948**	**355,400**

31 December 2012	Total assets Shs`000	Total liabilities Shs`000	Revenue Shs`000	Loss after tax Shs`000	Interest % held Shs`000
Strategis Insurance (Tanzania) Ltd	412,380	258,573	272,827	(78,554)	39.18%
31 December 2011					
Alliance Insurance Corporation Ltd	1,419,351	799,043	576,043	93,292	45%
Strategis Insurance (Tanzania) Ltd	689,306	504,256	576,511	(101,074)	39.18%

The Group concluded the disposal of its interest (indirect through Heritage Insurance Tanzania Limited) in Alliance Insurance Corporation Tanzania Limited in December 2012. Regulatory approval was granted by the Commissioner, Tanzania Insurance Regulatory Authority (TIRA) on 21 December 2012. The realised gain was as follows:

	Group 2012 Shs'000	2011 Shs'000
Investment in Alliance Insurance Corporation Limited as at 1 January 2012	280,123	-
Share of profit after tax	(30,312)	-
Dividend received	35,763	-
Realised fair value reserve	(47,044)	-
Proceeds on disposal of shares	(440,508)	-
Currency adjustment	8,793	-
Gain on disposal of investment in Alliance Insurance Corporation Limited	**(193,185)**	**-**

Subsidiaries

The Company's interest in its subsidiaries, all of which are unlisted and all of which have the same year end as the Company, were as follows:

	Beneficial ownership	Country of incorporation	Company 2012 Shs'000	2011 Shs'000
CfC Life Assurance Limited	100%	Kenya	1,826,254	1,826,254
The Heritage Insurance Company (K) Limited	100%	Kenya	741,287	741,287
The Heritage Insurance Company (T) Limited	60%	Tanzania	-	-
Azali Limited	100%	Kenya	-	-
CfC Investments Limited	100%	Kenya	634,792	634,792
			3,202,333	**3,202,333**

14. Income tax expense

The Group's current tax charge is computed in accordance with income tax rules applicable to composite insurance companies. A reconciliation of the tax charge is shown below:

	Group 2012 Shs'000	2011 Shs'000
Current income tax	348,200	165,401
Deferred income tax (Note 30)	(31,970)	(103,604)
	316,230	**61,797**

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

Reconciliation of income tax expense to tax based on accounting profit

	Group 2012 Shs'000	2011 Shs'000
Profit before income tax	1,202,901	1,012,215
Tax at statutory tax rate of 30% (2011 – 30%)	360,870	303,665
Tax effect of:		
Income not subjected to tax	67,231	(50,793)
Prior year tax under/(over) provision	(40,928)	(92,613)
Expenses not deductible for tax purposes	40,410	25,975
Income from associates	(23,704)	(714)
Difference between transfer from long term business and accounting profit	(87,649)	(123,723)
Income tax expense	**316,230**	**61,797**

There was no tax charge relating to components of other comprehensive income.

15. Earnings per share

Basic earnings per share have been calculated by dividing the net profit for the year by the weighted average number of ordinary shares in issue during the year.

	Group		Company	
	2012 Shs' 000	2011 Shs' 000	2012 Shs' 000	2011 Shs' 000
Earnings for the purposes of basic earnings per share	886,671	950,418	389,102	525,800
Number of shares				
Weighted average number of ordinary shares for the purpose of basic earnings per share (in thousands)	515,270	515,270	515,270	515,270
Earnings per share (Shs) basic and diluted	**1.72**	**1.84**	**0.76**	**1.02**

There were no potentially dilutive shares outstanding as at 31 December 2012 or 2011. Diluted earnings per share are therefore the same as basic earnings per share.

16. Ordinary share capital and share premium

Ordinary share capital

	Authorised number of shares	Issued number of shares	Ordinary (Shs) share capital	Nominal (Shs) value per share
As at 1 January 2011	515,270,364	515,270,364	515,270,364	1
At 31 December 2011 and 31 December 2012	**515,270,364**	**515,270,364**	**515,270,364**	**1**

Share premium

	Group	
	2012 Shs'000	2011 Shs'000
At January	1,701,239	1,701,239
At 31 December	**1,701,239**	**1,701,239**

17. Revenue and other reserves

			Company	
	Beneficial ownership	Country of incorporation	2012 Shs'000	2011 Shs'000
Statutory reserve	226,066	263,246	-	-
Fair value reserve	433,302	92,636	-	-
Revaluation reserve	279,680	225,471	-	-
Currency translation reserve	(21,739)	(58,984)	-	-
Total other reserves	917,309	522,369	-	-
Revenue reserve	1,759,864	1,134,938	696,911	513,917
Proposed dividend	206,108	-	206,108	-
At end of year	**2,883,281**	**1,657,307**	**903,019**	**513,917**

Other reserves include fair value reserve arising from revaluation of assets carried as available for sale, revaluation reserve on property and statutory reserve. Currency translation reserve represents exchange differences arising on the translation of the foreign subsidiary. Statutory reserve represents:

a) Accumulated surpluses from the life fund whose distribution is subject to the restrictions imposed by the Kenyan Insurance Act. The Insurance Act limits the amounts of surpluses of the life business available for distribution to shareholders to 30% of the accumulated surplus of the life business. A transfer to or from retained earnings is recorded each year to ensure that only amounts available for distribution to shareholders are held in the retained earnings.
b) The Tanzania subsidiary maintains a capital reserve in accordance with the Tanzania Insurance Act. Amounts appropriated to the capital reserve are calculated at 20% of the after tax profit of the subsidiary, accumulated on an annual basis.
c) A contingency reserve is maintained by the Tanzania subsidiary as required by the Tanzania Insurance Act. The reserve is calculated annually as the greater of 3% of net written premium or 20% of the net profit. This reserve shall accumulate until it reaches the minimum paid-up share capital or 50% of the net premiums, whichever is greater.

Proposed dividends

At the annual general meeting to be held on 22 May 2013, a final dividend in respect of the year ended 31 December 2012 of Kshs 0.40 (2011: Nil) per share amounting to a total of Kshs 206,108,146 (2011: Nil) is to be proposed. These financial statements do not reflect this dividend payable, the proposed dividend has however been transferred to a separate category of equity.

18. Goodwill

	Group	
	2012	2011
	Shs '000	Shs '000
Cost		
At 1 January	1,254,995	1,254,995
At 31 December	**1,254,995**	**1,254,995**

During the year, the Group assessed the recoverable amount of goodwill and determined that goodwill associated with the life and general assurance businesses was not impaired. The recoverable amount of the businesses was assessed by reference to the Cash Generating Unit's value in use which takes into account projected cash flows for the Group entities which are referenced to the respective entities budgets. A discount factor of 17.6% (estimate of parent company's cost of capital) was applied in the valuation.

19. Financial investments

	Group	
	2012	2011
	Shs '000	Shs '000
a) Financial investments - held-to-maturity	9,346,452	8,900,449
b) Financial investments - available for sale	4,124,310	4,278,039
c) Loans and receivables	1,362,600	1,332,388
	14,833,362	**14,510,876**

a) Held to maturity

	2012	2011
Short term	4,609,050	6,931,947
Long term	4,737,402	1,968,502
	9,346,452	**8,900,449**

Maturity analysis

	2012	2011
Maturing within 1 year	4,609,050	610,058
Maturing after 1 year but within 5 years	1,644,165	5,025,130
Maturing after 5 years but within 10 years	1,387,692	2,248,445
Maturing after 10 years	1,705,545	1,016,816
	9,346,452	**8,900,449**

HTM Movement analysis

	2012	2011
At start of year	8,900,449	4,175,977
Additions	1,545,165	1,292,932
Maturities	(1,108,552)	(326,737)
Transfer from available for sale and loans and receivables	-	3,769,365
Currency adjustment	9,390	(11,088)
	9,346,452	**8,900,449**

b) Available - for - sale investments

	Group	
	2012	2011
	Shs '000	Shs '000
i) Quoted shares	1,023,974	2,301,229
ii) Unquoted shares	212,172	226,880
iii) Government securities	2,888,164	1,749,930
	4,124,310	**4,278,039**

i) Quoted shares

At start of year	2,301,229	4,163,511
Additions	265,286	16,277
Disposals	(1,636,813)	(801,334)
Fair value gains/(losses)	92,387	(1,073,529)
Currency translation	1,885	(3,696)
At end of year	**1,023,974**	**2,301,229**

ii) Unquoted shares

At start of year	226,880	275,864
Additions	-	12,375
Disposals	(12,066)	(110,138)
Fair value gains	(3,135)	54,096
Currency translation	493	(5,317)
At end of year	**212,172**	**226,880**

iii) Government securities

At start of year	1,749,930	4,916,496
Additions	2,396,434	2,096,817
Disposals	(1,509,424)	(1,602,446)
Fair value gains /(losses)	251,224	(509,228)
Transfer to HTM	-	(3,151,709)
At end of year	**2,888,164**	**1,749,930**

c) Loans and receivables

	Group	
	2012	2011
	Shs '000	Shs '000
Mortgage loans	496,023	409,241
Policy loans	615,992	673,461
Other loans and deposits marturing after 90 days	250,585	249,686
	1,362,600	**1,332,388**

20. Property and equipment

Cost / valuation	Building on leasehold land Shs'000	Motor vehicles Shs'000	Furniture and equipment Shs'000	Computer equipment Shs'000	Total Shs'000
At 1 January 2012	622,975	96,923	706,344	240,103	1,666,345
Additions	19,570	11,937	43,074	25,403	99,984
Disposals	-	(40,165)	(44,224)	(2,016)	(86,405)
Reclassification from investment property (Note 21)	28,978	-	-	-	28,978
Revaluation	54,209	-	-	-	54,209
Currency adjustment	-	404	817	428	1,649
Other transfers	-	-	(10,369)	10,369	-
At 31 December 2012	725,732	69,099	695,642	274,287	1,764,760
Depreciation					
At 1 January 2012	1,803	61,358	362,857	183,776	609,794
Charge for the year	(857)	13,313	76,675	27,013	116,144
Disposals	-	(37,178)	(21,118)	(2,016)	(60,312)
Currency adjustment	-	325	783	427	1,535
At 31 December 2012	**946**	**37,818**	**419,197**	**209,200**	**667,161**
Net book amount at 31 December 2012	**724,786**	**31,281**	**276,445**	**65,087**	**1,097,599**

There were no items of property and equipment pledged by the Group to secure liabilities. Buildings were revalued as at 31 December 2012 by Tysons Limited and Lloyd Masika Limited, independent valuers, on the basis of the market value for existing use. There was no change in the fair value of the property and equipment items in the year.

Cost / valuation	Building on leasehold land Shs'000	Motor vehicles Shs'000	Furniture and equipment Shs'000	Computer equipment Shs'000	Total Shs'000
At 1 January 2011	666,927	97,401	680,892	183,862	1,629,082
Additions	1,688	26,466	3,578	45,635	77,367
Disposals	-	(26,246)	(10,008)	(28)	(36,282)
Reclassification from investment property (Note 21)	15,000	-	-	-	15,000
Reclassification to intangibles (Note 220	-	-	(15,680)	-	(15,680)
Intra-transfers	-	-	(11,373)	11,373	-
Currency adjustment	-	(698)	(1,705)	(739)	(3,142)
Other transfers	(60,640)	-	60,640	-	-
At 31 December 2011	622,975	96,923	706,344	240,103	1,666,345
Depreciation					
At 1 January 2011	17,960	66,196	295,846	156,117	536,119
Charge for the year	834	20,246	51,750	28,446	101,276
Disposals	-	(24,346)	(161)	-	(24,507)
Currency adjustment	-	(738)	(1,569)	(787)	(3,094)
Other transfers	(16,991)	-	16,991	-	-
At 31 December 2011	**1,803**	**61,358**	**362,857**	**183,776**	**609,794**
Net book amount at 31 December 2011	**621,172**	**35,565**	**343,487**	**56,327**	**1,056,551**

21. Investment property

		Group
	2012 Shs '000	**2011 Shs '000**
As at January	623,553	545,000
Additions	4,468	553
Reclassification to property and equipment (Note 20)	-	(15,000)
Net gain from fair value adjustments	-	93,000
At 31 December	**628,021**	**623,553**

Investment properties are stated at fair value. This has been determined based on independent valuations performed by Lloyd Masika Limited and Tysons Limited (professional valuers) as at 31 December 2012/11. The fair values represent the amount at which the assets could be exchanged between knowledgeable willing buyer and seller at an arm's length transaction at the date of the valuation. The valuations are performed on an annual basis and the fair value gains and losses are recognised as investment gains in the income statement.

The investment property rental income earned by the Group from its investment property leased out under operating leases as at 31 December 2012 amounted to Shs 47 million (2011: Shs 35 million)

22. Intangible assets

	Group	
	2012	2011
	Shs '000	Shs '000
At 1 January	359,614	334,146
Additions	15,937	11,600
Reclassification from property and equipment (Note 20)	-	15,680
Currency adjustment	882	(1,812)
At 31 December	376,433	359,614
Amortisation		
At 1 January	239,648	167,096
Charge for the year	68,437	74,003
Currency adjustment	854	(1,451)
At 31 December	308,939	239,648
Net book amount at 31 December	**67,494**	**119,966**

23. Reinsurers share of insurance liabilities

	Group	
	2012	2011
	Shs' 000	Shs' 000
Reinsurer's share of;		
Unearned premium	1,276,218	1,087,701
Notified claims outstanding	659,958	922,136
Claims incurred but not reported	104,716	107,298
	2,040,892	**2,117,135**

Amounts due from re-insurers in respect of claims already paid by the Group on contracts that are reinsured are included in re-insurance receivables on the statement of financial position.

24. Cash and cash equivalents

	Group		Company	
	2012 Shs' 000	2011 Shs' 000	2012 Shs' 000	2011 Shs' 000
Cash at bank and in hand	527,123	660,945	54,638	188,218
Short term bank deposits (maturing within 90 days)	4,951,216	2,038,661	-	-
Cash and cash equivalents (excluding bank overdrafts)	**5,478,339**	**2,699,606**	**54,638**	**188,218**

Cash and cash equivalents include the following for the purpose of statement of cash flows:

	Group	
	2012 Shs' 000	2011 Shs' 000
Cash and cash equivalents	5,478,339	2,699,606
Bank overdraft	-	(70,091)
	5,478,339	**2,629,515**

25. Insurance contract liabilities

	Group	
	2012 Shs' 000	2011 Shs' 000
Short term non-life insurance contracts		
Reported claims and claims handling expenses	1,837,007	1,978,901
Claims incurred but not reported	348,127	353,897
Long term insurance contracts		
Reported claims and claims handling expenses	161,031	103,048
Actuarial value of long term liabilities	5,192,692	4,253,464
	7,538,857	**6,689,310**

(i) Short term insurance contracts

Gross claims reported, claims handling expenses liabilities and the liability for claims incurred but not reported are net of expected recoveries from salvage and subrogation. The expected recoveries at the end of 2012 and 2011 are not material.

The Group uses chain-ladder techniques to estimate the ultimate cost of claims and the IBNR provision. Chain ladder techniques are used as they are an appropriate technique for mature classes of business that have a relatively stable development pattern. This involves the analysis of historical claims development factors and the selection of estimated development factors based on this historical pattern. The selected development factors are then applied to cumulative claims data for each accident year that is not fully developed to produce an estimated ultimate claims cost for each accident year.

The development of insurance liabilities provides a measure of the Group's ability to estimate the ultimate value of claims.

(ii) Long term insurance contracts

The Group determines its liabilities on the long-term insurance contracts using the Net Premium Valuation (NPV) methodology. The NPV method and assumptions are prescribed by the Insurance Act, 1997 (CAP 487), as the minimum valuation basis. The liabilities on the long-term insurance contracts are also determined on a realistic basis, namely the Gross Premium Valuation (GPV) method. The NPV method is considered to be appropriate because it arrives at prudent and conservative actuarial liabilities at the valuation date, emphasised by the GPV which provides lower liabilities than the NPV.

The NPV method makes explicit assumptions (as prescribed by the Insurance Act) in respect of expected future deaths and investment returns. The NPV basis makes implicit assumptions regarding expected experience in respect of lapses, expenses, bonuses and a margin for uncertainty on these assumptions. The liabilities are determined by the Group on the advice of the consulting actuary and actuarial valuations are carried out on an annual basis. The latest actuarial valuation of the Group's life fund was undertaken as at 31 December 2012 by the consulting actuaries – AON Actuaries and Consultants (Pty) Limited.

Valuation assumptions:

The significant valuation assumptions for the actuarial valuation as at 31 December 2012 are summarised below.

i) Mortality

The Group uses 100% of the KE 2001/2003 ultimate mortality table as per prescribed minimum basis (NPV) for mortality rates. No explicit allowance is made for AIDS on the NPV basis. The GPV basis uses 100% of the SA85/90 ultimate mortality table plus an AIDS allowance of 100% of the AB1 Select and Ultimate tables (2008 ASSA model).

F or Group Life contracts which is only valued as an IBNR, there is a mitigating effect of changing premium rates on an annual basis as contracts are reviewed annually and no mortality guarantees are offered.

ii) Investment returns

The NPV actuarial valuation as at 31 December 2012 used a discount rate of 4% p.a. compounded annually for individual long term insurance contracts and 6.5% p.a. compounded annually for the annuity business. The same rates were used for the valuation as at 31 December 2011.

The weighted average rate of return on a Fair Value basis as earned by the assets backing the life fund for the year ended 31 December 2012 was 25.59% p.a. (2011: negative 6.91% p.a.) and the average over the last three years was 13.37% p.a.

The valuation interest rate assumption (on the GPV basis) allows for a margin over the expected future investment return, hence strengthening the prudence in the GPV valuation basis. The expected future investment return is 12% on a GPV basis.

iii) Expenses and expense inflation

The NPV method makes no explicit assumptions on the level of expenses and expense

inflation. As at 31 December 2012 the implied proportion of annual premiums reserved for future expenses in the NPV was 42% p.a. (2011: 33.38% p.a.) This is higher than the actual current level of management expenses being incurred in the life fund. The current level of management expenses is taken to be an appropriate expense base for the GPV basis.

iv) Sensitivity analysis

The NPV method is not very sensitive to changes in most of the key assumptions used in determining the actuarial liabilities. For example the worsening of mortality assumption by 100% will result in an increase in actuarial liabilities of not more than 3%.

The Company markets long-term insurance contracts with fixed and guaranteed terms only. For liabilities under these contracts key assumptions are unchanged for the duration of the contract.

26. Amounts payable under deposit administration contracts

	Group	
	2012	**2011**
	Shs' 000	**Shs' 000**
At January	9,237,856	8,703,273
Pension fund deposits received	1,697,150	1,832,836
Surrenders and annuities paid	(1,757,843)	(1,650,081)
Interest payable to policy holders	927,113	351,828
	10,104,276	**9,237,856**

27. Unearned premium reserve

This reserve represents the liability for short term business contracts where the Group's obligations are not expired at the year end. Movements in the reserve are shown below:

	Group	
	2012	**2011**
	Shs' 000	**Shs' 000**
At January	2,242,031	1,853,053
Increase/(decrease) in the year	64,433	415,886
Currency adjustment	18,823	(26,908)
	2,325,287	**2,242,031**

28. Other liabilities

	Group		Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
Amount due to related companies	139,544	181,251	143,410	124,054
Accrued expenses	229,648	120,840	14,237	31,450
Other liabilities	541,243	413,878	-	-
	910,435	**715,969**	**157,647**	**155,504**

29. Contingent liabilities and commitments

As is common with the insurance industry in general, the Group is subject to litigation arising in the normal course of insurance business. The Directors are of the opinion that these litigations will not have material effect on the financial position or profits of the Group.

Capital commitments

There was no capital expenditure on property and equipment contracted for at the reporting date. However Shs 236,542,730 (2011: Shs 141,823,000) of capital expenditure on property and equipment were authorised by the directors but not contracted as at the reporting date.

Operating lease commitments

The Group leases various outlets under non-cancellable operating lease. The lease terms are between 1 and 5 years, and the majority of the lease agreements are renewable at the end of the lease period at market rates.

	Group	
	2012	2011
	Shs' 000	Shs' 000
Not later than 1 year	13,962	39,467
Later than 1 year and not later than 5 years	54,361	124,612
	68,323	**164,079**

30. Deferred income tax

Deferred income tax is calculated, in full, on all temporary differences under the liability method using the enacted tax rate of 30% (2011: 30%). The movement on the deferred income tax account is as follows:

a) Deferred tax asset.

	Group 2012 Shs' 000	2011 Shs' 000
At start of year	35,959	16,095
Charge/(credit) to income statement (IS)	-	(56)
Charge to equity	(48,963)	19,920
At end of year	**(13,004)**	**35,959**

	1/01/12 Shs'000	Credit / (charge) to IS Shs'000	Credit / (charge) to equity Shs'000	31/12/12 Shs'000
Arising from: Property and equipment	7,789	1,315	-	9,104
Other provisions	8,250	29,058	-	37,308
Fair value gains	20,510	2,114	(49,847)	(27,223)
Currency translation	(590)	(517)	884	(223)
Net deferred tax asset	**35,959**	**31,970**	**(48,963)**	**18,966**

	1/01/11 Shs'000	Credit / (charge) to IS Shs'000	Credit / (charge) to equity Shs'000	31/12/11 Shs'000
Property and equipment	6,006	1,783	-	7,789
Other provisions	10,089	(1,839)	-	8,250
Fair values of available for sale investments	-	-	20,510	20,510
Currency translation	-	-	(590)	(590)
Net deferred tax asset	**16,095**	**(56)**	**19,920**	**35,959**

b) Deferred tax liability

	Group	
	2012	2011
	Shs' 000	Shs' 000
At start of year	30,269	(73,391)
Charge/(credit) to income statement	-	103,660
At end of year	**30,269**	**30,269**

	1/01/11	Credit/ (charge) to IS	31/12/2011
	Shs'000	Shs'000	Shs'000
Property and equipment	32,516	(16,446)	16,070
Revaluation surplus	(2,998)	-	(2,998)
Fair value gains	(102,499)	95,729	(6,770)
Other provisions	(410)	24,377	23,967
Net deferred tax liability	**(73,391)**	**103,660**	**30,269**

31. Cash generated from operations

Reconciliation of profit before tax to cash generated from operations:

	Group	
	2012	2011
	Shs' 000	Shs' 000
Profit before taxation	1,202,901	1,012,215
Interest income	(1,768,121)	(1,246,204)
Depreciation (Note 20)	116,144	101,276
Amortisation of intangible assets (Note 22)	68,437	74,003
Gain on sale of property and equipment	(8,861)	(2,901)
Share of income from associate (Note 13)	(23,704)	(2,381)
Amortisation of prepaid operating lease rentals	11	11
Fair value gain on investment property (Note 7)	(111,406)	(93,000)
Foreign exchange gain	545	(20,482)
Dividend and rental income	(170,505)	(213,443)
Impairment charges/(recovery) for doubtful receivables	(58,164)	(21,216)
Other net investment expenses	(24,608)	71,753
Finance costs	95,179	74,233
Gain on sale of financial investments	(536,186)	(254,084)
Fair value gain on available for sale investments	-	-
Impairment loss on available for sale assets	18,930	94,348
Changes in;		
-technical provisions	1,712,962	434,495
-trade and other payables	194,466	(494,241)
-trade and other receivables	(484,748)	(129,384)
	223,272	**(615,002)**

32. Borrowings

	Group		Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
Term loan	479,796	504,621	479,796	504,621
At end of year	**479,796**	**504,621**	**479,796**	**504,621**

During the year the Company repaid the term loan of Shs 500 Million from NIC Bank Limited and obtained a new one for the same amount from the same lender. The borrowing is unsecured and payable in eight instalments in six months intervals beginning 24 August 2012. The Company incurred total interest of Shs 95 Million (2011: Shs 79 Million) at a weighted average rate of 19.84% (2011: 14.85%).

33. Related party transactions

The Group is controlled by Liberty Holdings Limited incorporated in the Republic of South Africa. The ultimate parent of Liberty Holdings Limited is Standard Bank Group Limited, which is incorporated in South Africa. There are other companies which are related to Liberty Kenya Holdings Limited through common shareholdings or common directorships. The following transactions were carried out with related parties:

a) Gross premiums written

		Group
	2012	2011
	Shs' 000	Shs' 000
CfC Stanbic Bank Ltd	207,911	274,797
Alliance Insurance Corporation Ltd	4,743	9,308
Strategis Insurance (Tanzania) Ltd	39,951	57,607
STANLIB Kenya Limited	5,567	5,061
	258,172	**346,773**

b) Claims incurred

		Group
	2012	2011
	Shs' 000	Shs' 000
CfC Stanbic Bank Ltd	1,907	9,319
Strategis Insurance (Tanzania) Ltd	28,088	114,363
STANLIB Kenya Limited	1,125	1,023
	31,120	**124,705**

c) Rental income

		Group
	2012	2011
	Shs' 000	Shs' 000
CfC Stanbic Bank Ltd	7,492	7,492
STANLIB Kenya Limited	7,235	7,235
	14,727	**14,727**

d) Interest income and (expense)

		Group	Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
CfC Stanbic Bank Ltd	150,485	40,810	-	-
CfC Life Assurance Ltd	-	-	(2,849)	(124)
Heritage Insurance (K) Ltd	-	-	(2,647)	(4,177)
	150,485	**40,810**	**(5,496)**	**(4,301)**

e) Dividend income

	Group		Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
CfC Life Assurance Company Ltd	-	-	100,000	300,000
Heritage Insurance (K) Ltd	-	-	400,000	315,000
	-	**-**	**500,000**	**615,000**

f) Investment management expenses

	Group	
	2012	2011
	Shs' 000	Shs' 000
STANLIB Kenya Limited	51,756	36,830
	51,756	**36,830**

g) Outstanding balances with related parties

i) Accounts receivable

	Group	
	2012	2011
	Shs' 000	Shs' 000
Strategis Insurance (Tanzania) Ltd	38,300	745
STANLIB Kenya Limited	10,581	102
Liberty Life Assurance Uganda Ltd	48	18
	48,929	**865**

ii) Accounts payable

	Group		Company	
	2012	2011	2012	2011
	Shs' 000	Shs' 000	Shs' 000	Shs' 000
CfC Stanbic Bank Ltd	11,083	11,139	6,519	6,519
Strategis Insurance (Tanzania) Ltd	36,744	-	-	-
CfC Investments Ltd	-	-	106,669	106,669
STANLIB Kenya Limited	7,243	954	-	-
CfC Stanbic Holdings Ltd	10,866	10,866	10,866	10,866
Liberty Africa Holdings Ltd	70,451	10,678	-	-
	136,387	**33,637**	**124,054**	**124,054**

These amounts are unsecured and have no specific repayment period.

h) Financial investments

	Group 2012 Shs' 000	Group 2011 Shs' 000	Company 2012 Shs' 000	Company 2011 Shs' 000
CfC Stanbic Bank balances and deposits	1,099,542	670,046	44,705	188,218
CfC Stanbic Bank corporate bonds	408,893	264,708	-	-
CfC Stanbic Holdings Ltd equity investments	11,501	10,720	-	-
	1,519,936	**945,474**	**44,705**	**188,218**

i) Key management compensation

	Company 2012 Shs'000	Company 2011 Shs'000
Fees for dervices as a director	3,492	2,599
	3,492	**2,599**

	Group 2012 Shs' 000	Group 2011 Shs' 000	Company 2012 Shs' 000	Company 2011 Shs' 000
Salaries and other employment benefits	210,378	224,477	-	-
	210,378	**224,477**	**-**	**-**

Directors' remuneration

	Company 2012 Shs'000	Company 2011 Shs'000
Fees for services as a director	-	2,599
	-	**2,599**

Shareholding

i) Top ten shareholders

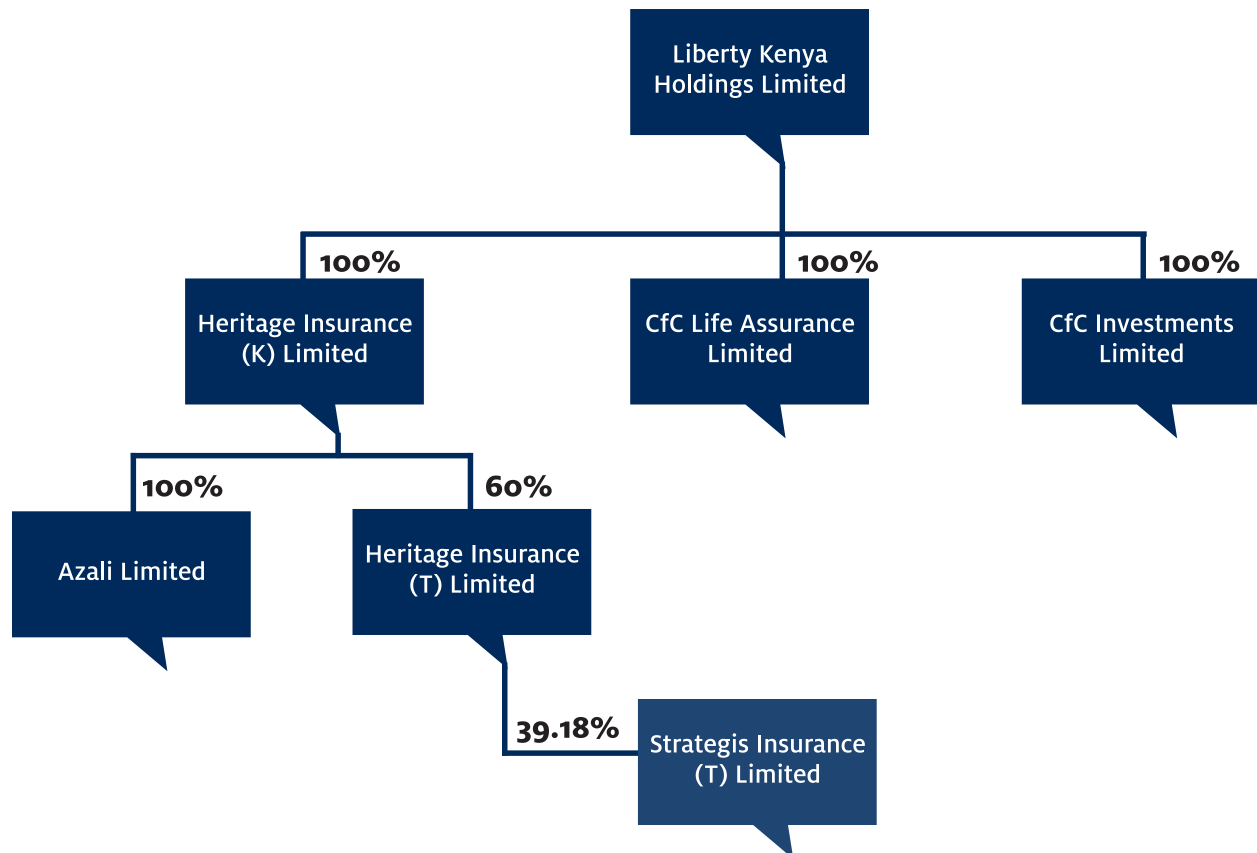
Name	Number of shares held	shareholding (%)
1. Liberty Holdings Limited	292,762,096	56.82%
2. African Liaison and Consultants Services Limited	156,098,266	30.29%
3. Sovereign Trust Limited	14,441,154	2.80%
4. Archer and Wilcock Nominees Limited	6,125,000	1.19%
5. Kingsway Nominees Limited	5,198,498	1.01%
6. The Government of Kenya	4,342,548	0.84%
7. Jani, Uday Prahlad	3,500,000	0.68%
8. Feneast Nominees Limited	3,360,000	0.65%
9. Beechwood Overseas Limited	2,658,501	0.52%
10. Standard Chartered Nominees Non-resd A/C 9866	1,114,900	0.22%

ii) Distribution of shareholding

The distribution of shareholders is as follows:

	Number of shareholders	Number of shares held	Shareholding (%)
1 – 500	1,758	371,521	0.07%
501 – 5,000	1,520	2,643,864	0.51%
5,001 – 10,000	447	3,358,787	0.65%
10,001 – 100,000	328	9,207,098	1.79%
100,001 – 1,000,000	38	10,088,131	1.96%
Over 1,000,000	10	489,600,963	95.02%
Total	**4,101**	**515,270,364**	**100%**

Annexure A: Group structure



To: The Company Secretary
Liberty Kenya Holdings Limited
P O Box 30390 – 00100
NAIROBI

PROXY FORM

I/We, ____

of P O Box ____

being a member of **LIBERTY KENYA HOLDINGS LIMITED** hereby appoint

____

of ____

or failing him ______________________________________

of ____

as my/our proxy to vote on my/our behalf at the Annual General Meeting of the Company to be held on Wednesday 22 May 2013 and at any adjournment thereof.

Dated this ______________ **day of** ______________ **2013** ______________

Signed: ____________________________ **Name:** ____________________________

The proxy form should be completed and returned not later than 48 hours before the meeting or any adjournment thereof.

LIBERTY KENYA HOLDINGS
LIMITED