



*Enabling you to reach your peak*



**ANNUAL REPORT AND  
FINANCIAL STATEMENTS**

**2014**

# Contents

Vision & Mission .....	2
Corporate Information .....	3
Report of Directors.....	4
Statement on Corporate Governance .....	5-6
Chairman's Report .....	7-8
Statement of Director's Responsibility .....	13
Independent Auditors Report .....	14
Statement of profit or loss and other comprehensive income .....	15
Statement of Financial Position .....	16
Statement of changes in Equity .....	17
Statement of Cashflow .....	18
Note to the Financial Statements .....	19-65



## Vision

To be one of the best regarded Banks in Kenya providing the highest quality products and services.

## Mission

To develop a motivated professional staff that will profitably deliver high quality customer services that fill the financial needs of our customers and their businesses.

## CORPORATE INFORMATION

### ▶ DIRECTORS

Anwarali Padany - Chairman  
Ayaz Merali - Chief Executive Officer (CEO)  
Noorez Padamshi  
Mohamed Mujtaba  
Mercy Kamau  
Angela Musimba

### ▶ AUDIT COMMITTEE

Angela Musimba - Chairlady  
Noorez Padamshi  
Mercy Kamau  
Kapil Deo Sharma  
Henry Onkunya

### ▶ CREDIT COMMITTEE

Mercy Kamau - Chairlady  
Angela Musimba  
Anwarali Padany  
Ayaz Merali  
Mohamed Mujtaba  
Michael Riitho

### ▶ ASSET LIABILITY COMMITTEE

Ayaz Merali - Chairman  
Nicholas Odera  
Mohamed Mujtaba  
Fred Maina

### ▶ RISK MANAGEMENT COMMITTEE

Angela Musimba - Chairlady  
Anwarali Padany  
Noorez Padamshi  
Stanley Ngaruiya Ndungu

### ▶ COMPANY SECRETARY

Winniefred Nyagoha Jumba  
Certified Public Secretary (Kenya)  
C/o Livingstone Associates  
P O Box 30029 Nairobi - GPO 00100

### ▶ REGISTERED OFFICE

LR Plot No 1870/IX/140  
4th Floor, Sound Plaza  
Woodvale Groove  
P O Box 14001 Nairobi - Westlands 00800

### ▶ AUDITORS

Deloitte & Touche  
Certified Public Accountants (Kenya)  
Deloitte Place, Waiyaki Way, Muthangari  
P O Box 40092 Nairobi GPO 00100

### ▶ PRINCIPAL CORRESPONDENTS

Deutsche Bank AG, Germán  
Deutsche Bank Trust Co, New York  
Habibsons Bank Limited, London  
Standard Bank of South Africa,  
Johannesburg  
Standard Chartered Bank, New York  
Standard Chartered Bank, London  
HDFC Bank, India

### ▶ LEGAL ADVISERS

Walker Kontos - Hakika House, Bishops Road  
P O Box 60680 - Nairobi City Square 00200

Ngatia & Associates Advocates - Bishop Garden Towers, 1st  
Ngong Avenue  
P O Box 56688 - Nairobi City Square 00200

Mwaniki Gachoka & Co Advocates  
Design Centre, 3rd Floor Office suite no.1A & 3A  
P O Box 13439 Nairobi GPO 00800

## REPORT OF THE DIRECTORS

The directors have the pleasure of submitting their report together with the audited financial statements for the year ended 31 December 2014, in accordance with Section 22 of the Banking Act and Section 157 of the Companies Act, which disclose the state of affairs of Paramount Universal Bank Limited ("the Bank").

### PRINCIPAL ACTIVITY

The principal activity of the bank, which is licensed under the Banking Act, is the provision of banking, financial and related services.

### FINANCIAL RESULTS FOR THE YEAR

	2014	2013
	Sh'000	Sh'000
Profit before taxation	160,871	105,816
Taxation charge	(13,025)	(11,158)
Profit for the year transferred to retained earnings	<u>147,846</u>	<u>94,658</u>
	=====	=====

### DIVIDENDS

The directors do not recommend the payment of a dividend in respect of the year ended 31 December 2014(2013: Sh nil).

### DIRECTORS

The present members of the Board of Directors are shown on page 3. Angela Musimba was appointed a director with effect from 28th August 2014.

### AUDITORS

Deloitte & Touche, having expressed their willingness, continue in office in accordance with section 159 (2) of the Kenyan Companies Act and subject to approval by the Central Bank of Kenya under section 24(1) of the Banking Act.

### BY ORDER OF THE BOARD



Secretary

2015 Nairobi

## STATEMENT ON CORPORATE GOVERNANCE

The bank's board of directors is responsible for the governance of the bank and is accountable to the shareholders for ensuring that the bank complies with the law, the highest standards of corporate governance and business ethics. The directors attach great importance to the need to conduct the business and operation of the bank with integrity and in accordance with generally accepted corporate practice and endorse the internationally developed principles of good corporate governance.

### Board of Directors

The full board meets at least four times a year. The directors are given appropriate and timely information so that they can maintain full and effective control over strategic, financial, operational and compliance issues.

Except for direction and guidance on general policy, the board has delegated authority for conduct of day-to-day business to the Chief Executive Officer. The board nonetheless retains responsibility for establishing and maintaining the bank's overall internal control of financial, operational and compliance issues.

Every board member attended at least 80% of the board meetings. An evaluation of the board members was undertaken during the period and it was regarded reasonable.

### Committees of the Board

#### Audit Committee

The board has constituted an audit committee that meets as required. Its responsibilities include review of financial information, budgets, development plans, compliance with accounting standards in financial reporting, and liaison with the external auditors, remuneration of external auditors and overseeing internal control systems. Internal and external auditors and other executives attend audit committee meetings as required.

#### Credit Committee

The board has constituted a credit committee that meets as required. Its responsibilities include a review of the overall lending policy of the bank, ensuring that there are effective policies and procedures to effectively manage credit risk, monitor and review all matters, which may materially impact the present and future quality of the institution's credit risk management.

#### Assets Liability Committee

The board has constituted an Assets and Liabilities Committee (ALCO) that meets as required. Its responsibilities include deriving the most appropriate strategy in respect of the assets and liabilities of the bank given future expectations, changes and consequence of liquidity constraints, interest rate movements, changes in prices and foreign exchange exposures.

#### Risk Management Committee

The board has constituted a Risk Management Committee that meets as required. Its responsibilities include carrying out risk assessment and putting in place risk indicators and monitoring the risk.

## Board Nominations and Remuneration Committee

The board has constituted Nominations and Remuneration Committee. The committee deals with all aspects of appointment of an institution's directors, review the mix of skills and experience and other qualities in order to assess the effectiveness of the board. The committee is also responsible for overseeing the compensation system in place on behalf of the Board of Directors.

## Statement on risk management

Paramount Universal Bank Limited recognises the responsibility to manage risks related to its business as a financial institution. The bank has built strong internal systems to ensure that sound banking practices results in income streams commensurating with the risks taken.

The Integrated Risk Management Policy of the bank is fully committed to adopting best practices in identifying measuring, controlling and monitoring the risks faced.

## Corporate Governance Statement on Conflict of Interest

The board of directors has approved a code of conduct that gives disclosure guidance on potential conflicts of interest situations. Reporting procedures are in place for this. The code of conduct has to be signed annually by all staff members.

### The bank aims at:

- Integrating risk management into the culture of the organization.
- Eliminating or reducing risk to the lowest acceptable levels.
- Developing risk sensitivity as a core competency of all stakeholders.
- Continually identifying potential risks and pro-actively mitigating them.
- Focusing on key risks and controlling them cost-effectively.

The bank has developed a risk infrastructure that is appropriate to the size and volatility of the business. Decision making at all levels are inspired by the aspiration to be a risk intelligent organization. Risk management is used as an enabler to exploit the potential for increased business by taking informed risks with awareness and control.



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**Director**  
**2015**



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**Director**

## CHAIRMAN'S REPORT FOR YEAR 2014

On behalf of the bank's Board of Directors, I am once again honoured to present to you our Annual Financial Results for the year ended on 31st December 2014.

Let me begin by highlighting the various factors that impacted on the bank's operating environment during the year. As is now the trend, the financial services sector recorded steady growth in the year despite the challenges that the economy faced. The recent report 'Kenya Economic Survey 2015' indicates that the GDP was 5.3% in 2014 compared to 5.7% in 2013. Even though other East African Community countries like Tanzania and Rwanda recorded GDP figures of 7.2% and 6% respectively, Kenya's slowdown could be attributed to among other factors low returns from tourism due to rampant insecurity and terrorism threats. However, other sectors of the economy like agriculture, construction and real estate, wholesale and retail trade and financial services continued to be the main drivers of the economy and will likely remain so in the year 2015.

The negative economic sentiments have been somehow offset by stable inflation and interest rates. These two factors are related and normally influence the monetary policy stance of the Central Bank. It is worth noting that rising inflation normally leads to higher interest rates and hence increases the cost of doing business. The Board of Directors of the bank is always monitoring the business environment to enable them manage current and emerging risks in the market. It is for that reason that I am confident that the bank's risk management program is robust enough to respond to any challenges that may arise.

I am delighted to point out that despite the challenges faced during the year 2014, the bank still maintained its focus of sustainable business growth. This was marked by the 2nd Runners Up Position in the Fastest Growing Bank category by Think Business. The bank's key financial performance indicators were as follows:

- Profit before Taxes (PBT) grew from 106 Million in 2013 to 161 Million in 2014.
- Profit after Taxes (PAT) grew from 95 Million in 2013 to 148 Million 2014.
- Earnings per Share (EPS) grew from 95 shillings to 148 shillings per share.
- Total Assets grew from 8 Billion in 2013 to 10.4 Billion in 2014.
- Customer Deposits grew to 8.05 Billion in 2014 compared to 6.6 Billion in 2013.



## CHAIRMAN'S REPORT FOR YEAR 2014 (Continued)

- Liquidity remained healthy at 60% compared to 63% in 2013.

The above results reaffirm our commitment to all the stakeholders of the bank that we shall strive to continue delivering the required results to their expectations. In particular, I would also like to thank all our esteemed clients, well wishers and staff who supported us during the official opening of our Industrial Area Branch by the Colombian Ambassador to Kenya Her Excellency Maria Eugenia Correa Olarte. We are delighted and overwhelmed by the positive feedback we got from the local community, a true reflection that the bank is headed in the right direction.

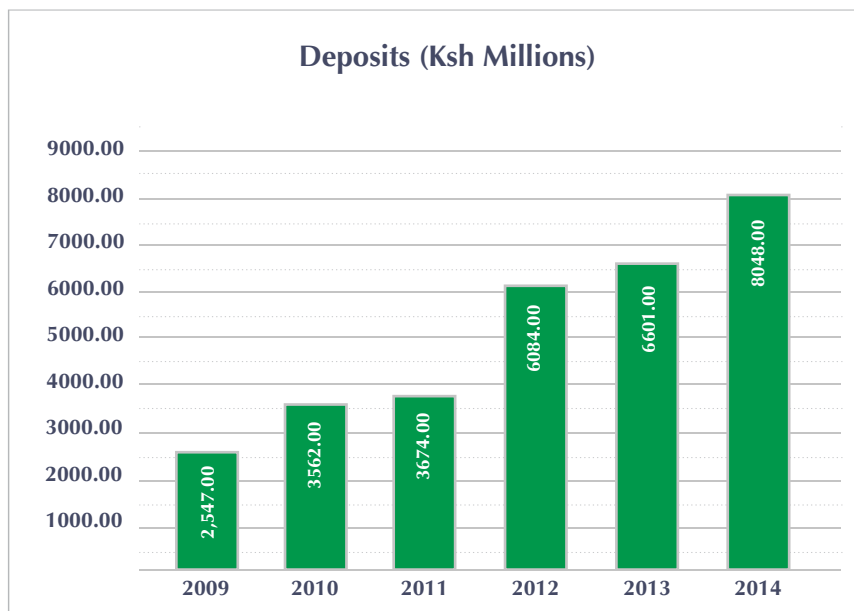
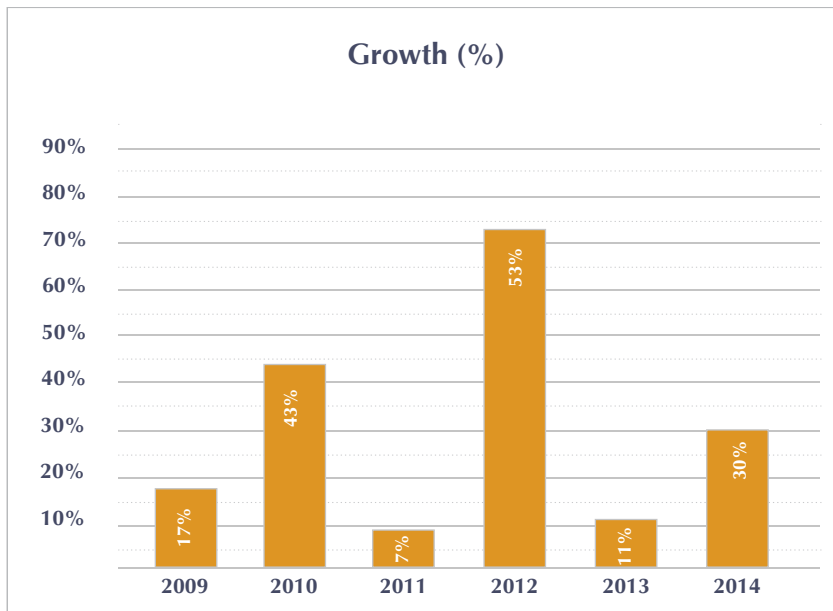
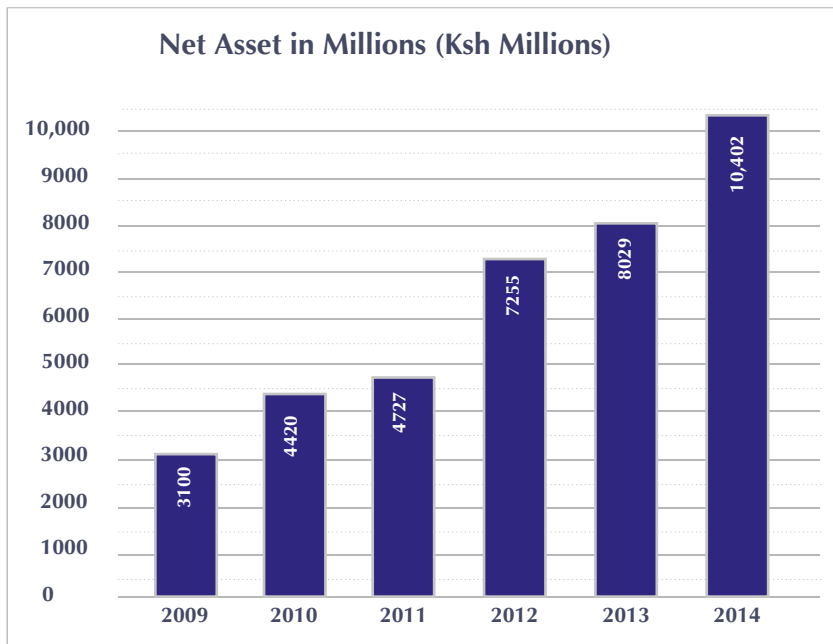
Thank you.



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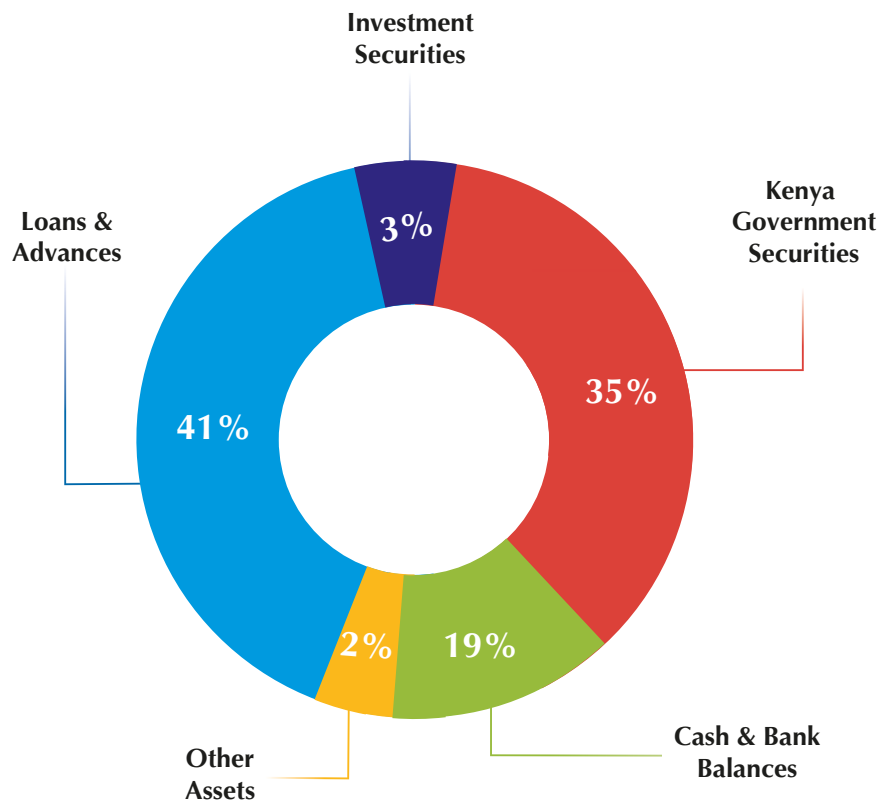
Anwarali Padany  
Chairman

# GRAPHIC REPORT

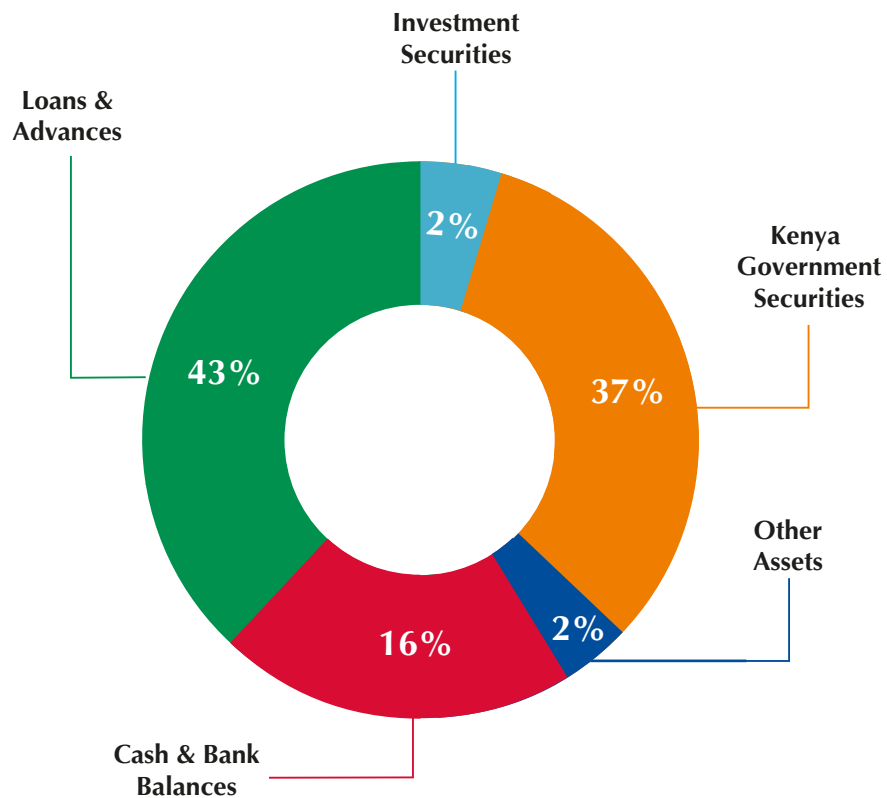


# GRAPHIC REPORT

## % Assets Distribution 2013



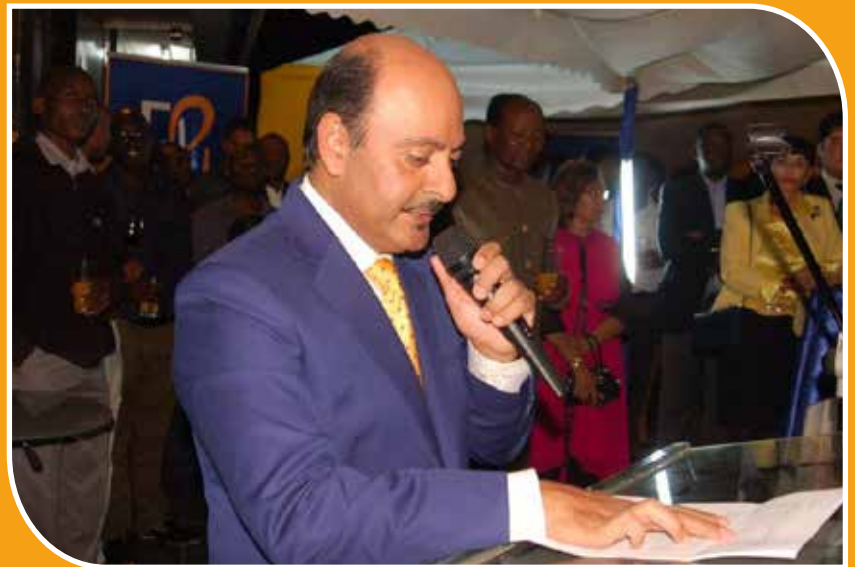
## % Assets Distribution 2014





Guest of honour Her Excellency Maria Eugenia Correa Olarte (Colombian Ambassador) CEO of the bank Mr. Ayaz Merali and the Chairman of the bank Mr. Anwarali Padany during the official opening of Industrial Area Branch.

CEO Mr. Ayaz Merali giving his speech during the opening of the Industrial Area Branch.



Guest Of Honour Her Excellency Maria Eugenia Correa Olarte (Colombian Ambassador), Mrs. Nurjehan Padany, Chairman of the bank Mr. Anwarali Padany and CEO Mr. Ayaz Merali at the cake cutting to officially open the Industrial Area Branch.

# Congratulations



*Runner up Fastest  
Growing Bank*



“The board of directors, management and all staff wish to sincerely thank all our esteemed customers for their support and contribution in winning this prestigious award. Together, we look forward for even better 2015!”

[www.paramountbank.co.ke](http://www.paramountbank.co.ke)

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Kenyan Companies Act requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the bank as at the end of the financial year and of its operating results for that year. It also requires the directors to ensure that the bank keeps proper accounting records which disclose with reasonable accuracy at any time the financial position of the bank. They are also responsible for safeguarding the assets of the bank.

The directors are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards and the requirements of the Kenya Companies Act, and for such internal controls as the directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The directors accept responsibility for the annual financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgements and estimates, in conformity with International Financial Reporting Standards and in the manner required by the Kenyan 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 bank and of its operating results. The directors further accept responsibility for the maintenance of accounting records which may be relied upon in the preparation of financial statements, as well as adequate systems of internal financial control.

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



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**Director**  
**2015**



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**Director**



## INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF PARAMOUNT UNIVERSAL BANK LIMITED

### Report on the Financial Statements

We have audited the accompanying financial statements of Paramount Universal Bank Limited, set out on pages 16 to 61, which comprise the statement of financial position as at 31 December 2014, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows 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 of financial statements that give a true and fair view in accordance with International Financial Reporting Standards and the requirements of the Kenyan Companies Act, and for such internal controls as the directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' Responsibility

Our responsibility is to express an opinion on these 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 the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our 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, we considered the internal controls relevant to the bank's preparation of the financial statements that give a true and fair view in order to design audit procedures that were appropriate in the circumstances, but not for the purpose of expressing an opinion on the bank's internal controls. 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 audit opinion.

### Opinion

In our opinion, the financial statements give a true and fair view of the state of financial affairs of the bank as at 31 December 2014 and of its profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the Kenyan Companies Act and the Banking Act.

### Report on Other Legal Requirements

As required by the Kenyan Companies Act we report to you, based on our audit, 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 bank, so far as appears from our examination of those books; and
- iii) the bank's statement of financial position (balance sheet) and statement of profit or loss (profit and loss account) are in agreement with the books of account.

The engagement partner responsible for the audit resulting in this independent auditors' report is CPA Fred Okwiri - P/No. 1699.

**Certified Public Accountants (Kenya)**

2015

## STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2014

	Note	2014 Sh'000	2013 Sh'000
INTEREST INCOME	4	1,017,440	976,342
INTEREST EXPENSE	5	(681,025)	(666,650)
NET INTEREST INCOME		336,415	309,692
Fees and commission income	6	66,045	42,379
Gains on foreign exchange dealings	7	9,754	7,182
Net trading income/(loss)	8(a)	42,533	(18,237)
Other operating income	8(b)	3,167	7,178
OPERATING INCOME		457,914	348,194
Operating expenses	9	(286,729)	(228,673)
Impairment losses on loans and advances	18	(10,314)	(13,705)
PROFIT BEFORE TAXATION		160,871	105,816
TAXATION CHARGE	11(a)	(13,025)	(11,158)
PROFIT FOR THE YEAR		147,846	94,658
OTHER COMPREHENSIVE INCOME		-	-
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		147,846	94,658
		Sh	Sh
EARNINGS PER SHARE – Basic and diluted	12	147,85	94.66



## STATEMENT OF FINANCIAL POSITION FOR THE YEAR ENDED 31 DECEMBER 2014

	Note	2014 Sh'000	2013 Sh'000
<b>ASSETS</b>			
Cash and balances with Central Bank of Kenya	13	483,561	394,460
Deposits and balances due from banking institutions	14	1,226,879	1,124,377
Government securities	15	3,828,558	2,782,597
Corporate bonds	16	198,314	242,215
Advances to customers (net)	17	4,447,615	3,272,190
Other assets	19	103,144	118,242
Taxation recoverable	11(c)	16,125	21,221
Equipment	20	89,640	58,337
Intangible assets	21	5,801	4,629
Deferred taxation asset	22	2,679	10,608
		-----	-----
<b>TOTAL ASSETS</b>		<b>10,402,316</b>	<b>8,028,876</b>
		=====	=====
<b>LIABILITIES</b>			
Customer deposits	23	8,048,012	6,600,517
Amount due to local banks	24	936,243	135,676
Other liabilities	25	39,801	62,269
		-----	-----
<b>TOTAL LIABILITIES</b>		<b>9,024,056</b>	<b>6,798,462</b>
		-----	-----
<b>SHAREHOLDERS' FUNDS</b>			
Share capital	26	1,000,000	1,000,000
Retained earnings		316,832	186,044
Statutory reserve		61,428	44,370
		-----	-----
<b>TOTAL SHAREHOLDERS' FUNDS</b>		<b>1,378,260</b>	<b>1,230,414</b>
		-----	-----
<b>TOTAL SHAREHOLDERS' FUNDS AND LIABILITIES</b>		<b>10,402,316</b>	<b>8,028,876</b>
		=====	=====

The financial statements on pages 16 to 61 were approved and authorised for issue by the board of directors on 2015 and were signed on its behalf by:




Director



Chief Executive Officer



Director



Company Secretary

## STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2014

	Share capital Sh'000	Retained earnings Sh'000	Statutory reserve Sh'000	Total Sh'000
At 1 January 2013	1,000,000	105,871	29,885	1,135,756
Total comprehensive income for the year	-	94,658	-	94,658
Transfer to statutory reserve	-	(14,485)	14,485	-
At 31 December 2013	1,000,000	186,044	44,370	1,230,414
At 1 January 2014	1,000,000	186,044	44,370	1,230,414
Total comprehensive income for the year	-	147,846	-	147,846
Transfer to statutory reserve	-	(17,058)	17,058	-
At 31 December 2014	1,000,000	316,832	61,428	1,378,260

The statutory reserve represents an appropriation from retained earnings in compliance with Central Bank of Kenya's prudential guidelines on impairment of loans and advances. It represents the excess of loans provisions as computed as per the Central Bank of Kenya prudential guidelines over impairment of loans and receivables computed as per IAS 39. The statutory reserve is not distributable.

## STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2014

	Note	2014 Sh'000	2013 Sh'000
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Cash generated from operations	27(a)	240,233	1,096,341
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchase of equipment	20	(46,591)	(16,167)
Purchase of intangible assets	21	(2,474)	(2,722)
Net cash used in investing activities		(49,065)	(18,889)
INCREASE IN CASH AND CASH EQUIVALENTS		191,168	1,077,452
CASH AND CASH EQUIVALENTS AT 1 JANUARY		1,510,202	432,750
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	27(b)	1,701,370	1,510,202

# NOTES TO THE FINANCIAL STATEMENTS

## ACCOUNTING POLICIES

### Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards.

For the Kenyan Companies Act reporting purposes, in these financial statements the balance sheet is represented by/ is equivalent to the statement of financial position and the profit and loss account is presented in the statement of profit or loss and other comprehensive income.

### Adoption of new and revised International Financial Reporting Standards (IFRSs)

#### i) New standards and amendments to published standards effective for the year ended 31 December 2014

The following new and revised IFRSs were effective in the current year and had no material impact on the amounts reported in these financial statements.

<p>Amendments to IFRS 10, IFRS 12 and IAS 27 Investment Entities</p>	<p>The amendments to IFRS 10 define an investment entity and require a reporting entity that meets the definition of an investment entity not to consolidate its subsidiaries but instead to measure its subsidiaries at fair value through profit or loss in its consolidated and separate financial statements.</p> <p>To qualify as an investment entity, a reporting entity is required to:</p> <ul style="list-style-type: none"><li>• Obtain funds from one or more investors for the purpose of providing them with investment management services;</li><li>• Commit to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and</li><li>• Measure and evaluate performance of substantially all of its investments on a fair value basis.</li></ul> <p>Consequential amendments have been made to IFRS 12 and IAS 27 to introduce new disclosure requirements for investment entities.</p> <p>Application of these standards has not had any impact on the disclosures or the amounts recognised in these financial statements as the bank is not an investment entity (assessed based on the criteria set out in IFRS 10 as at 1 January 2014).</p>
<p>Amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities</p>	<p>The amendments to IAS 32 clarify the requirements relating to the offset of financial assets and financial liabilities. Specifically, the amendments clarify the meaning of 'currently has a legally enforceable right of set-off' and 'simultaneous realisation and settlement'. The amendments have been applied retrospectively.</p> <p>As the bank does not have any financial assets and financial liabilities that qualify for offset, the application of the amendments has had no impact on the disclosures or on the amounts recognised in the bank's financial statements.</p>

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Adoption of new and revised International Financial Reporting Standards (IFRSs) (Continued)

##### i) New standards and amendments to published standards effective for the year ended 31 December 2014 (Continued)

<p>Amendments to IAS 36 Recoverable Amount Disclosures for Non-Financial Assets</p>	<p>The amendments to IAS 36 remove the requirement to disclose the recoverable amount of a cash-generating unit (CGU) to which goodwill or other intangible assets with indefinite useful lives had been allocated when there has been no impairment or reversal of impairment of the related CGU. Furthermore, the amendments introduce additional disclosure requirements applicable to when the recoverable amount of an asset or a CGU is measured at fair value less costs of disposal. These new disclosures include the fair value hierarchy, key assumptions and valuation techniques used which are in line with the disclosure required by IFRS 13 Fair Value Measurements. As the bank does not have any cash-generating units (CGU) to which goodwill or other intangible assets with indefinite useful lives had been allocated, the application of the amendments has had no impact on the disclosures or on the amounts recognised in the bank's financial statements.</p>
<p>Amendments to IAS 39 Novation of Derivatives and Continuation of Hedge Accounting</p>	<p>The amendments to IAS 39 provide relief from the requirement to discontinue hedge accounting when a derivative designated as a hedging instrument is novated under certain circumstances. The amendments also clarify that any change to the fair value of the derivative designated as a hedging instrument arising from the novation should be included in the assessment and measurement of hedge effectiveness.</p> <p>As the bank does not have any derivatives that are subject to novation, the application of these amendments has had no impact on the disclosures or on the amounts recognised in the bank's financial statements.</p>
<p>IFRIC 21 Levies</p>	<p>IFRIC 21 addresses the issue as to when to recognise a liability to pay a levy imposed by a government. The Interpretation defines a levy, and specifies that the obligating event that gives rise to the liability is the activity that triggers the payment of the levy, as identified by legislation. The Interpretation provides guidance on how different levy arrangements should be accounted for, in particular, it clarifies that neither economic compulsion nor the going concern basis of financial statements preparation implies that an entity has a present obligation to pay a levy that will be triggered by operating in a future period.</p> <p>The application of this Interpretation has had no material impact on the disclosures or on the amounts recognised in the bank's financial statements.</p>

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Application of new and revised International Financial Reporting Standards (IFRSs) (Continued)

##### (ii) New and amended standards and interpretations in issue but not yet effective in the year ended 31 December 2014

New and Amendments to standards	Effective for annual periods beginning on or after
IFRS 9	1 January 2018
IFRS 15	1 January 2017
Amendments to IFRS 11	1 January 2016
Amendments to IAS 16 and IAS 38	1 January 2016
Amendments to IAS 16 and IAS 41	1 January 2016
Amendments to IAS 19	1 July 2014
Amendments to IFRS's Annual improvements 2010- 2012 cycle	1 July 2014
Amendments to IFRS's Annual improvements 2011- 2013cycle	1 July 2014

##### (iii) Impact of relevant new and amended standards and interpretations on the financial statements for the year ended 31 December 2014 and future annual periods

#### IFRS 9 Financial Instruments

IFRS 9, issued in November 2009, introduced new requirements for the classification and measurement of financial assets. IFRS 9 was amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for derecognition.

#### Key requirements of IFRS 9:

- All recognised financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement are required to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognised in profit or loss.
- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.

The directors of the bank anticipate that the application of IFRS 9 in the future may have a significant impact on amounts reported in respect of the bank's financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 9 until a detailed review has been completed by the bank.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Application of new and revised International Financial Reporting Standards (IFRSs) (Continued)

##### (iii) Impact of relevant new and amended standards and interpretations on the financial statements for the year ended 31 December 2014 and future annual periods

##### IFRS 15 Revenue from Contracts with Customers)

In May 2014, IFRS 15 was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related Interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a 5-step approach to revenue recognition:

Step 1: Identify the contract(s) with a customer

Step 2: Identify the performance obligations in the contract

Step 3: Determine the transaction price

Step 4: Allocate the transaction price to the performance obligations in the contract

Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

Under IFRS 15, an entity recognises revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 15 until a detailed review has been completed.

##### Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortisation

The amendments to IAS 16 prohibit entities from using a revenue-based depreciation method for items of property, plant and equipment. The amendments to IAS 38 introduce a rebuttable presumption that revenue is not an appropriate basis for amortisation of an intangible asset. This presumption can only be rebutted in the following two limited circumstances:

- a) when the intangible asset is expressed as a measure of revenue; or
- b) when it can be demonstrated that revenue and consumption of the economic benefits of the intangible asset are highly correlated.

The amendments apply prospectively for annual periods beginning on or after 1 January 2016. Currently, the bank uses the straight-line method for depreciation and amortisation for its equipment, and intangible assets respectively. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 15 until a detailed review has been completed.

##### Amendments to IFRS 11 Accounting for Acquisitions of Interests in Joint Operations

The amendments to IFRS 11 provide guidance on how to account for the acquisition of an interest in a joint operation in which the activities constitute a business as defined in IFRS 3 Business Combinations. Specifically, the amendments state that the relevant principles on accounting for business combinations in IFRS 3 and other standards (e.g. IAS 36 Impairment of Assets regarding impairment testing of a cash generating unit to which goodwill on acquisition of a joint operation has been allocated) should be applied. The same requirements should be applied to the formation of a joint operation if and only if an existing business is contributed to the joint operation by one of the parties that participate in the joint operation.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Application of new and revised International Financial Reporting Standards (IFRSs) (Continued)

#### (iii) Impact of relevant new and amended standards and interpretations on the financial statements for the year ended 31 December 2014 and future annual periods (Continued)

#### Amendments to IFRS 11 Accounting for Acquisitions of Interests in Joint Operations (Continued)

A joint operator is also required to disclose the relevant information required by IFRS 3 and other standards for business combinations.

The amendments to IFRS 11 apply prospectively for annual periods beginning on or after 1 January 2016.

The directors of the bank do not anticipate that the application of these amendments to IFRS 11 will have a material impact on the bank's financial statements.

#### Amendments to IAS 19 Defined Benefit Plans: Employee Contributions

The amendments to IAS 19 clarify how an entity should account for contributions made by employees or third parties to defined benefit plans, based on whether those contributions are dependent on the number of years of service provided by the employee.

For contributions that are independent of the number of years of service, the entity may either recognise the contributions as a reduction in the service cost in the period in which the related service is rendered, or to attribute them to the employees' periods of service using the projected unit credit method; whereas for contributions that are dependent on the number of years of service, the entity is required to attribute them to the employees' periods of service.

The directors of the bank do not anticipate that the application of these amendments to IAS 19 will have a significant impact on the bank's financial statements.

#### Annual Improvements to IFRSs 2010-2012 Cycle

The Annual Improvements to IFRSs 2010-2012 Cycle include a number of amendments to various IFRSs, which are summarised below

- The amendments to IFRS 2 (i) change the definitions of 'vesting condition' and 'market condition'; and (ii) add definitions for 'performance condition' and 'service condition' which were previously included within the definition of 'vesting condition'. The amendments to IFRS 2 are effective for share-based payment transactions for which the grant date is on or after 1 July 2014.
- The amendments to IFRS 3 clarify that contingent consideration that is classified as an asset or a liability should be measured at fair value at each reporting date, irrespective of whether the contingent consideration is a financial instrument within the scope of IFRS 9 or IAS 39 or a non-financial asset or liability. Changes in fair value (other than measurement period adjustments) should be recognised in profit and loss. The amendments to IFRS 3 are effective for business combinations for which the acquisition date is on or after 1 July 2014.
- The amendments to IFRS 8 (i) require an entity to disclose the judgements made by management in applying the aggregation criteria to operating segments, including a description of the operating segments aggregated and the economic indicators assessed in determining whether the operating segments have 'similar economic characteristics'; and (ii) clarify that a reconciliation of the total of the reportable segments' assets to the entity's assets should only be provided if the segment assets are regularly provided to the chief operating decision-maker.



## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Application of new and revised International Financial Reporting Standards (IFRSs) (Continued)

#### (iii) Impact of relevant new and amended standards and interpretations on the financial statements for the year ended 31 December 2014 and future annual periods (Continued)

##### Annual Improvements to IFRSs 2010-2012 Cycle

- The amendments to the basis for conclusions of IFRS 13 clarify that the issue of IFRS 13 and consequential amendments to IAS 39 and IFRS 9 did not remove the ability to measure short-term receivables and payables with no stated interest rate at their invoice amounts without discounting, if the effect of discounting is immaterial. As the amendments do not contain any effective date, they are considered to be immediately effective.
- The amendments to IAS 16 and IAS 38 remove perceived inconsistencies in the accounting for accumulated depreciation/amortisation when an item of property, plant and equipment or an intangible asset is revalued. The amended standards clarify that the gross carrying amount is adjusted in a manner consistent with the revaluation of the carrying amount of the asset and that accumulated depreciation/amortisation is the difference between the gross carrying amount and the carrying amount after taking into account accumulated impairment losses.
- The amendments to IAS 24 clarify that a management entity providing key management personnel services to a reporting entity is a related party of the reporting entity. Consequently, the reporting entity should disclose as related party transactions the amounts incurred for the service paid or payable to the management entity for the provision of key management personnel services. However, disclosure of the components of such compensation is not required.

The directors do not anticipate that the application of these amendments will have a significant impact on the bank's financial statements.

##### Annual Improvements to IFRSs 2011-2013 Cycle

The Annual Improvements to IFRSs 2011-2013 Cycle include a number of amendments to various IFRSs, which are summarised below:

The amendments to IFRS 3 clarify that the standard does not apply to the accounting for the formation of all types of joint arrangement in the financial statements of the joint arrangement itself.

The amendments to IFRS 13 clarify that the scope of the portfolio exception for measuring the fair value of a group of financial assets and financial liabilities on a net basis includes all contracts that are within the scope of, and accounted for in accordance with, IAS 39 or IFRS 9, even if those contracts do not meet the definitions of financial assets or financial liabilities within IAS 32.

The amendments to IAS 40 clarify that IAS 40 and IFRS 3 are not mutually exclusive and application of both standards may be required.

Consequently, an entity acquiring investment property must determine whether:

- (a) the property meets the definition of investment property in terms of IAS 40; and
- (b) the transaction meets the definition of a business combination under IFRS 3

The directors do not anticipate that the application of these amendments will have a significant impact on the bank's financial statements.

#### (iv) Early adoption of standards

The bank did not early adopt new or amended standards in 2014.

# NOTES TO THE FINANCIAL STATEMENTS (continued)

## 1. ACCOUNTING POLICIES (Continued)

### Basis of preparation

The bank prepares its financial statements under the historical cost convention, as modified to include the revaluation of certain financial assets.

### Interest income and expense

Interest income and interest expense for all interest bearing financial instruments are accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Interest income and expense on all trading assets and liabilities are considered to be incidental to the bank's trading operations and are presented together with all other changes in the fair value of trading assets and liabilities in net trading income. Fair value changes on other financial assets and liabilities carried at fair value through profit or loss, are also presented in net trading income included in the profit or loss.

Once a financial asset or a group of financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest that was used to discount the future cash flows for purposes of measuring the allowance for impairment.

Interest income includes interest on loans and receivables, placements with other banks and investments in government securities, and is recognised in the year in which it is earned.

### Fees and commission income

In the normal course of business, the bank earns fees and commission income from a diverse range of services to its customers. Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including account servicing fees, investment management fees, placement fees and syndication fees, are recognised as the related services are performed. When a loan commitment is not expected to result in the draw-down of a loan, loan commitment fees are recognised on a straight-line basis over the commitment period. Fees and commission expense relates mainly to transaction and service fees, which are expensed as the services are received.

### Net trading income

Net trading income arises from the margins which are achieved through market marking and customer business and from changes in market caused by movements in interest and exchange rates, prices and other market variables. It comprises gains less losses related to trading assets and liabilities, and includes all realised and unrealised fair value changes.

### Equipment

Equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is calculated on a straight line basis at annual rates estimated to write off the cost of equipment over their expected useful lives using the following rates:

Computers and office equipment	20%
Motor vehicles	25%
Furniture, fittings and office renovations	12.5%

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Intangible assets-computer software costs

Generally, costs associated with developing computer software programmes are recognised as an expense incurred. However, a cost that is clearly associated with an identifiable and unique product which will be controlled by the bank and has a probable benefit exceeding the cost beyond one year, are recognised as an intangible asset.

Expenditure which enhances and extends computer software programmes beyond their original specifications and lives is recognised as a capital improvement and added to the original costs of the software. Computer software development costs recognised as assets are stated at cost less amortisation. Amortisation is calculated on a straight line basis over the estimated useful lives not exceeding a period of 5 years.

#### Impairment of non-financial assets

At the end of each reporting period, the bank reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the company estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. 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 which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

#### Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

##### (i) Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the statement of comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The bank's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

##### (ii) Deferred tax

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Taxation (Continued)

Such deferred tax assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in associates, except where the bank is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities and assets are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the bank expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

#### (iii) Current and deferred tax for the year

Current and deferred tax are recognised in profit or loss, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income or directly in the equity respectively.

#### Foreign currencies

Transactions in foreign currencies during the year are translated at the rates ruling at the time of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into Kenya Shillings at the rates of exchange ruling at the end of each reporting date. Non-monetary items that are measured in terms of historical costs in a foreign currency are not retranslated. Gains and losses on exchange of monetary items are dealt with in the profit or loss in the period in which it arises.

#### Provisions

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

#### Statutory reserve

IAS 39 requires the bank to recognise an impairment loss when there is objective evidence that loans and receivables are impaired. However, Central Bank of Kenya prudential guidelines require the bank to set aside amounts for impairment losses on loans and advances in addition to those losses that have been recognised under IAS 39. Any such amounts set aside represent appropriations of retained earnings and not expenses in determining profit or loss. These amounts are dealt with in the statutory reserve.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Financial instruments

##### i) Recognition

A financial asset or liability is recognised when the bank becomes party to the contractual provisions of the instrument.

##### ii) Classification and measurement

###### Financial assets

The bank classifies its financial assets into the following categories:

- Financial assets at fair value through profit or loss.
- Loans and receivables.
- Held to maturity financial assets.
- Available for sale financial assets.

Management determines the appropriate classification of its investments at initial recognition.

###### Financial assets at fair value through profit or loss

Financial assets are classified as fair value through profit or loss (FVTPL) when the financial asset is either held for trading or is designated as at FVTPL. A financial asset is classified as held for trading if acquired principally for the purpose of selling in the short term; or on initial recognition it is part of a portfolio of identified financial instruments that the bank manages together and has a recent actual pattern of short term profit taking; or it is a derivative that is not designated and effective as a hedging instrument. Financial assets at FVTPL are stated at fair value, with gains or losses arising on re-measurement recognised in profit or loss.

###### Loans and receivables

Loans and receivables including advances originated by the bank are non-derivative financial assets with fixed or determinable payments with fixed maturities that are not quoted in an active market. Loans and receivables are recognised when cash is advanced to borrowers. These are held to maturity and are measured at amortised cost using the effective interest method, less any impairment.

###### Held to maturity investments

Financial assets with fixed or determinable payments and fixed maturity where the bank has the positive intent and ability to hold to maturity other than loans and receivables originated by the bank are classified as held to maturity investments and are measured at amortised cost using effective interest rate method less any impairments with revenue recognised on an effective yield basis.

###### Available-for-sale financial assets

Financial assets that are not (a) loans and receivable originated by the company, (b) held –to-maturity investments, or (c) financial assets held for trading are measured at their fair values. Gains and losses arising from changes in fair value are recognised in other comprehensive income and accumulated in the investments revaluation reserve with the exception of impairment losses; interest calculated using the effective interest method, and foreign exchange gains and losses on monetary assets, which are recognised in profit or loss. Where the investment is disposed and or if determined to be impaired, the cumulative gain or loss previously accumulated in the investments revaluation reserves is reclassified to profit or loss.

Fair values of quoted investments in active markets are based on quoted bid prices. Equity securities for which fair values cannot be measured reliably are measured at cost less impairment.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Financial instruments (Continued)

##### Impairment and uncollectability of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each reporting date. The bank 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 and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after initial recognition of the asset (a 'loss' event) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated

If it is probable that the bank will not be able to collect all amounts due (principal and interest) according to the contractual terms of loans and receivables, or held-to-maturity investments carried at amortised cost, an impairment or bad debt loss has occurred. The amount of the loss is the difference between the asset's carrying amount and the present value of expected future cash flows discounted at the financial instrument's original effective interest rate (recoverable amount). The carrying amount of the asset is reduced to its estimated recoverable amount through use of the provision for bad and doubtful debts account. The amount of the loss incurred is included in profit or loss for the period.

The bank assesses whether objective evidence of impairment exist individually for assets that are individually significant and individually or collectively for assets that are not individually significant. If the bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

##### (i) Assets carried at amortised cost

If there is objective evidence that an impairment loss on financial assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial instruments effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss.

##### (ii) Loans and receivables

Loans and receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of loans and receivables is established when there is objective evidence that the bank will not be able to collect all amounts due according to the original terms of the loans. The amount of provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the profit or loss as 'impairment loss on loans and receivables'. When a loan or advance is uncollectible, it is written off against the related allowance account. Subsequent recoveries of amounts previously written off are credited through profit or loss.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Financial instruments (Continued)

#### (ii) Loans and receivables (Continued)

Objective evidence that loans and receivables are impaired can include significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group are considered indicators that the loans or receivable is impaired.

In assessing impairment losses, the bank considers the following factors, in each category:

#### a) Individually assessed loans

- The aggregate exposure to the bank.
- The viability of the customer's business model and its capacity to trade successfully out of financial difficulties and generate sufficient cash flows to meet its debt obligations.
- The realisable value of the security (or other mitigants) and likelihood of successful repossession net of any costs involved in recovery of amounts.
- The amount and timing of expected receipts and, in cases of liquidation or bankruptcy, dividend available.
- The extent and complexity of other creditors commitment ranking pari passu with the bank and the likelihood of other creditors continuing to support the customer.

#### b) Collectively assessed

- For loans not subject to individual assessment, to cover losses which have been incurred but have not yet been identified.
- For homogeneous groups of loans that are not considered individually significant, where there is objective evidence of impairment.

#### Homogeneous groups of loans

For homogeneous groups of loans that are not considered individually significant, or in other cases, when the portfolio size is small or when information is insufficient or not reliable enough, the bank adopts a formulaic approach which allocates progressively higher percentage loss rates in line with the period of time for which a customer's loan is overdue. Loss rates are calculated from the discounted expected future cash flows from a portfolio. These rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

#### Loan write – offs

An uncollectible loan is written off against the relevant provision for impairment, either partially or in full, when there is no realistic prospect of recovery and the proceeds from realising the security have been substantially or fully recovered.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Financial instruments (Continued)

#### Impairment and uncollectability of financial assets (Continued)

##### (iii) Available-for-sale financial assets

In the case of investment classified as available for sale, significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the asset is impaired. Impairment losses on available-for-sale investment securities are recognised by transferring the difference between the amortised acquisition cost and current fair value out of equity to profit or loss. When a subsequent event causes the amount of impairment loss on an available-for-sale debt security to decrease, the impairment loss is reversed through profit or loss.

However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised directly in equity. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

#### Financial liabilities

After initial recognition, the bank measures all financial liabilities including customer deposits other than liabilities held for trading at amortised cost. Liabilities held for trading (financial liabilities acquired principally for the purpose of generating a profit from short-term fluctuations in price or dealer's margin) are subsequently measured at their fair values.

#### Derecognition of financial liabilities

Financial liabilities are derecognised when and only when the bank obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

#### Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

#### Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with Central Bank of Kenya (CBK), items in the course of collection from other banks, deposits held at call with banks and treasury bills with original maturities of less than three months. Such assets are generally subject to insignificant risk of changes in their fair value, and are used by the bank in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

#### Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. Rentals payable under operating leases are charged to profit or loss for the year on a straight-line basis over the term of the relevant lease.

#### Contingent liabilities

Letters of credit, acceptances, guarantees and performance bonds are generally written by the bank to support performance by a customer to third parties. The bank will only be required to meet these obligations in the event of the customer's default. These obligations are accounted for as off financial position transactions and disclosed as contingent liabilities.



## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. ACCOUNTING POLICIES (Continued)

#### Fiduciary activities

Assets and income arising thereon together with related undertakings to return such assets to customers are excluded from these financial statements where the bank acts in a fiduciary capacity such as nominee, trustee or agent.

#### Employee benefit costs

##### i) Statutory defined benefit obligation pension scheme

The bank contributes to the National Social Security Fund (NSSF). This is a defined contribution scheme registered under the National Social Security Act. Contributions are determined by local statute and are currently limited to Sh 200 per employee per month. The bank's contributions to the statutory retirement benefit scheme are charged to the profit or loss for the year to which they relate.

##### ii) Other employee entitlements

Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the liability for annual leave outstanding at the financial position date,

#### Comparatives

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year.

### 2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING THE BANK'S ACCOUNTING POLICIES

In the process of applying the bank's accounting policies, management has made 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. These are dealt with below:

##### i) Critical judgements in applying the bank's policies

###### Impairment losses on loans and receivables

The bank reviews its loan portfolios to assess impairment regularly. In determining whether an impairment loss should be recorded in the profit or loss for the year, the bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans, before a decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a bank, or national or local economic conditions that correlate with defaults on assets in the bank.

Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING THE BANK'S ACCOUNTING POLICIES (CONTINUED)

#### Financial instruments (Continued)

##### i) Critical judgements in applying the bank's policies (Continued)

###### Held -to-maturity investments

The bank follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgement. In making this judgement, the bank evaluates its intention and ability to hold such investments to maturity. If the bank fails to keep these investments to maturity other than for the specific circumstances – for example, selling an insignificant amount close to maturity – it will be required to reclassify the entire class as available-for-sale. The investments would therefore be measured at fair value not amortised cost.

##### ii) Key sources of estimation uncertainty

###### Equipment

Critical estimates are made by directors in determining the useful lives and residual values for equipment and intangible assets based on the intended use of the assets and the economic lives of those assets. Subsequent changes in circumstances such as technological advances or prospective utilisation of the assets concerned could result in the actual useful lives or residual values differing from initial estimates.

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES

The Board of Directors retains the overall responsibility for the risk management of the bank. The Board Risk Management Committee (RMC) is responsible for monitoring compliance with the bank's risk management policies and procedures, and review of the adequacy of risk management framework in relation to the risks faced by the bank. The Board Risk Management Committee is assisted in these functions by various management committees which undertake both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Board.

The following are the key risk categories that have been elaborated in these financial disclosures:

- Credit risk
- Liquidity risk
- Market risk
  - Interest rate risk
  - Foreign exchange risk
  - Price risk
- Capital management
- Operational risk

##### a) Credit risk

Credit risk refers to the current or prospective risk to earnings and capital arising from an obligator's failure to meet the terms of any contract with the bank or if an obligator otherwise fails to perform as agreed. It arises principally from lending, leasing, trade finance and treasury activities. The bank's credit risk is primarily attributable to its loans and receivables. The amounts presented in the statement of financial position are net of allowances for doubtful advances, estimated by the bank's management based on prior experience and their assessment of the current economic environment.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### a) Credit risk (Continued)

##### Management of credit risk

The Board of directors has delegated responsibility for the management of credit risk to its Credit Committee (CC).

The bank structures the level of credit risk it undertakes by placing limits on amounts of risk accepted in relation to one borrower or a group of borrowers. Such risks are monitored on a revolving basis and are subject to annual or more frequent review.

Credit risk is the risk of financial loss to the bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the bank's loans and receivables to customers and other banks and investment securities.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate guarantees.

##### Maximum exposure to credit risk before collateral held

The amount that best represents the bank's maximum exposure to credit at the end of the period is analysed as follows:-

	2014 Sh '000	%	2013 Sh '000	%
<b>On balance sheet items</b>				
Items in the course of collection from other banks (note 19)	8,228	-	5,131	-
Deposits and balances due from banking institution (note 14)	1,226,879	13	1,124,377	15
Loans and receivables to customers (note 17)	4,447,615	46	3,272,190	44
Government securities (note 15)	3,828,558	39	2,782,597	37
Corporate bonds (note 16)	198,314	2	242,215	3
	<hr/>		<hr/>	
Total	9,709,594	100	7,426,510	100
	<hr/>		<hr/>	
Off – balance sheet items (note 28 (a))				
Letters of credit	182,159	33	102,516	43
Letters of guarantee and performance bonds	283,340	51	100,797	43
Bills for collection	94,687	17	32,805	14
	<hr/>		<hr/>	
	560,186	100	236,118	100
	<hr/>		<hr/>	
Grand total	10,269,780		7,662,628	
	<hr/> <hr/>		<hr/> <hr/>	

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### a) Credit risk (Continued)

The table below represents the worst case scenario of credit exposure for both years, without taking account of any collateral held or other credit enhancements attached.

#### Classification of loans and receivables to customers

	Gross loan amount Sh '000	Impairment allowance Sh '000	Net loan amount Sh '000	%
At 31 December 2014				
Neither past due nor impaired	3,417,329	-	3,417,329	77
Past due but not impaired	908,479	-	908,479	20
Impaired	293,906	172,099	121,807	3
Total	4,619,714	172,099	4,447,615	100
At 31 December 2013				
Neither past due nor impaired	2,429,728	-	2,429,728	75
Past due but not impaired	669,077	-	669,077	20
Impaired	335,772	162,387	173,385	5
Total	3,434,577	162,387	3,272,190	100

Apart from the loans and receivables to customers all other credit exposures are neither past due nor impaired.

#### Neither past due nor impaired

These are well documented facilities granted to financially sound customers where no weaknesses exist. All such facilities are performing in accordance with the contractual terms and are expected to continue doing so. Loans in this category are normally fully protected by the current sound net worth and paying capacity of the borrower. These exposures are categorised as normal in line with Central Bank of Kenya (CBK) prudential guidelines and a provision of 1 % is made and appropriated under statutory reserves.

#### Past due but not impaired

These are accounts which may be currently protected but, though not past due, reveal weaknesses in the financial conditions or credit worthiness of the borrower. Such weaknesses, if not corrected, may weaken the asset or inadequately protect the bank's position at some future date. These exposures are graded category 2 in line with CBK guidelines.

#### Impaired

Impaired loans and securities are loans and securities for which the bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan / securities agreement(s). These loans are graded categories 3 to 5 in the bank's internal credit risk grading system. These accounts under CBK guidelines are termed as non-performing loans.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### a) Credit risk (Continued)

##### Allowances for impairment

The bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loan loss allowance established for banks of homogeneous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

##### Collateral held

The bank holds collateral against loans and advances to customers in the form of mortgage interests over property, registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired.

An estimate of the fair value of collateral and other security enhancements held against impaired financial assets is shown below:

	2014 Sh '000	2013 Sh '000
Loans and advances to customers		
Discounted value of securities for past due and impaired loans		
90 - 180 days	71,900	46,697
180 days +	218,402	190,011
	-----	-----
Total	290,302	236,708
	=====	=====

##### Concentration of risk

The bank has no significant concentration of credit risk, with exposure spread over a diversity of personal and commercial customers as set out in the table below:

#### a) Advances to customers

	2014 Sh '000	%	2013 Sh '000	%
Real estate	1,425,340	31	1,421,563	41
Social community and personal services	327,701	7	159,271	5
Manufacturing	54,690	1	13,253	0
Transport and communications	352,317	8	652,627	19
Other	2,459,666	53	1,187,863	35
	-----		-----	
Total	4,619,714	100	3,434,577	100
	=====		=====	

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### a) Credit risk (Continued)

##### Concentration of risk (Continued)

#### b) Customer deposits

	2014 Sh '000	%	2013 Sh '000	%
Co-operatives societies	13,133	-	3,127	-
Private enterprises	6,124,698	76	5,015,821	76
Non profit institutions and individuals	1,910,181	24	1,581,569	24
<b>Total</b>	<b>8,048,012</b>	<b>100</b>	<b>6,600,517</b>	<b>100</b>

#### c) Off – balance sheet items

	2014 Sh '000	%	2013 Sh '000	%
Business services	39,213	7	16,072	7
Wholesale and retail	453,751	81	191,257	81
Transport and communications	22,407	4	9,800	4
Other	44,815	8	18,989	8
<b>Total</b>	<b>560,186</b>	<b>100</b>	<b>236,118</b>	<b>100</b>

#### Summary of credit risk exposure taking into account collateral

	2014 Sh '000	2013 Sh '000
Loans and advances		
Individually impaired		
Grade 5 : Impaired (loss)	39,074	19,660
Grade 3 & 4 : Impaired (doubtful)	254,832	316,112
Gross amount	293,906	335,772
Allowance for impairment	(172,099)	(162,387)
Carrying amount	121,807	173,385
Collectively impaired		
Grade 1 : Normal	3,417,329	2,429,728
Grade 2 : Watch	908,479	669,077
Gross amount	4,325,808	3,098,805
Carrying amount	4,447,615	3,272,190

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### a) Credit risk (Continued)

##### Write-off policy

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the profit or loss for the year.

#### b) Liquidity risk

Liquidity risk is the risk that the bank cannot obtain the necessary funds to meet its obligations associated with financial instruments as they fall due. The amount of liquidity required depends very much on the banks ability to forecast demand and its access to outside sources. The board of directors has assigned the authority for the management oversight of the liquidity risk policy to the Assets and Liability Committee (ALCO). The committee which is composed of the CEO, Treasury Manager, and other bank officers as necessary review various liquidity and funding decisions and related risks. Formal minutes pertaining to committee actions are recorded and maintained for review by the board of directors.

##### Liquidity management

The bank manages the liquidity structure of assets, liabilities and commitments so that cash flows are appropriately matched to ensure that all funding obligations are met when due. Banking operations are such that mismatch of assets and liabilities according to their maturity profiles cannot be avoided. However, management ensures that the mismatch is controlled in line with allowable risk levels. Liquidity is managed on a daily basis and incorporates assets and liabilities of the bank based on the remaining period up to 31 December 2014 to the contractual maturity date.

Liquidity risk is addressed through the following measures:

- The bank enters into lending contracts subject to availability of funds.
- The bank has an aggressive strategy aimed at increasing the customer deposit base.
- The bank invests in short term liquid instruments which can easily be sold in the market when the need arises.
- Investments in equipment are properly budgeted for and done when the bank has sufficient cash flows.

The table below details the liquidity ratio trends over the year:

	2014	2013
As at 31 December	%	%
Average for the period	60	67
Maximum for the period	65	70
Minimum for the period	57	63
Statutory minimum requirement by Central Bank of Kenya	20	20
	=====	=====

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### b) Liquidity risk (Continued)

##### Undiscounted cash flows

The table below shows the undiscounted cash outflows on the bank's financial liabilities based on their contractual maturity dates and the undiscounted cash inflows on the bank's financial assets based on their expected maturity dates. The banks expected cash flows on these instruments could vary significantly from this analysis. For example, demand deposits from customers are expected to maintain a stable or increasing balance; and unrecognised loan commitments are not all expected to be drawn down immediately

	Upto 1 Month Sh '000	1-3 Months Sh '000	4-12 Months Sh '000	1-5 Years Sh '000	Over 5 Years Sh '000	Total Sh'000
<b>FINANCIAL ASSETS</b>						
Cash and balances with CBK	240,249	234,400	8,912	-	-	483,561
Deposits and balances from banking institutions	1,226,879	-	-	-	-	1,226,879
Treasury bonds	2,372,161	89,258	345,914	514,319	667,580	3,989,232
Corporate bonds	-	-	50,034	169,223	-	219,257
Advances to customers	376,799	778,933	1,085,131	2,085,922	489,751	4,816,536
	4,216,088	1,102,592	1,489,991	2,769,464	1,157,331	10,735,465
<b>FINANCIAL LIABILITIES</b>						
Customer deposits	4,363,306	2,262,858	1,680,924	-	-	8,307,088
Amounts due to local banks	937,074	-	-	-	-	937,074
	5,300,380	2,262,858	1,680,924	-	-	9,244,162
Net liquidity gap	(1,084,292)	(1,160,267)	(190,933)	2,769,464	1,157,331	1,491,303
As at 31 December 2012						
Total financial assets	3,227,006	777,426	1,038,860	1,765,181	1,007,366	7,815,839
Total financial liabilities	6,748,038	490,947	164,045	-	-	7,403,030
Net liquidity gap	(3,521,032)	286,479	874,815	1,765,181	1,007,366	412,811

The gross nominal inflow/(outflow) disclosed is the contractual, undiscounted cash flow on the financial liability or commitment.



## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### c) Market Risk

##### (i) Interest rate risk

The bank is exposed to the risk that the value of a financial instrument will fluctuate due to changes in market interest rate. Interest rates on advances to customers are either pegged to the bank's base lending rate or Treasury bill rate.

The interest rates, therefore, fluctuate depending on the movement in the market interest rates. The bank also invests in fixed interest rate instruments issued by the Central Bank of Kenya. Interest rate on customer deposits is negotiated between the bank and the customer. The bank has the discretion to change the rates in line with changes in market trends.

The board of directors has assigned the authority for the management oversight of the interest rate risk policy to the Assets and Liability Committee (ALCO). The committee which is composed of the CEO, Treasury Manager, and other bank officers meets as necessary for specific credit risk situations, reviews various liquidity and funding decisions and related risks.

Formal minutes pertaining to committee actions are recorded and maintained for review by the board of directors.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### c) Market Risk (Continued)

##### (i) Interest rate risk (Continued)

	Up to 1 Month Sh '000	1-3 Months Sh '000	4-12 Months Sh '000	1-5 years Years Sh '000	Over 5 Years Sh '000	Non-interest bearing Sh '000	Total Sh'000
<b>FINANCIAL ASSETS</b>							
Cash in hand	-	-	-	-	-	72,583	72,583
Balances with Central Bank of Kenya	-	-	-	-	-	410,978	410,978
Deposits and balances due from banking institutions	1,226,879	-	-	-	-	-	1,226,879
Government securities	2,352,556	87,081	314,467	467,563	606,891	-	3,828,558
Corporate bonds	-	-	44,475	153,839	-	-	198,314
Advances to customers	4,447,615	-	-	-	-	-	4,447,615
Total financial assets	8,027,050	87,081	358,942	621,402	606,891	483,561	10,184,927
<b>FINANCIAL LIABILITIES</b>							
Customer deposits	4,363,306	2,262,858	-	1,680,924	-	832,757	8,048,012
Amounts due to local banks	936,243	-	-	-	-	-	936,243
Total financial liabilities	1,609,711	5,427,763	-	1,114,024	-	832,757	8,984,255
Interest rate sensitivity gap	6,417,339	(5,340,682)	358,942	(492,622)	606,891	(349,196)	1,200,672
As at 31 December 2012	5,331,621	1,005	38,413	916,629	809,334	718,837	7,815,839
Total financial assets	246,599	4,432,363	449,816	463,244	-	1,144,171	6,736,193
Total financial liabilities	5,085,022	(4,431,358)	411,403	453,385	809,334	(425,334)	1,079,646

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the bank. It is unusual for a bank's interest to completely be matched due to the nature of business terms and types.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### c) Market Risk (Continued)

##### (i) Interest rate risk (Continued)

##### Exposure to interest rate risk

The bank is exposed to various risks associated with the effects of fluctuation in the prevailing levels of market interest rates on its financial position and cash flows. ALCO closely monitors the interest rate trends to minimize the potential adverse impact of interest rate changes. The table below summarises the exposure to interest rate risk at the statement of financial position date.

##### Interest rate risk – stress test-as at 31 December 2014

	Amount Sh'000	Scenario 10% increase in net margin Sh'000	Scenario 10% decrease in net margin Sh'000
Profit before taxation	160,871	196,790	124,952
Adjusted core capital	1,314,153	1,350,072	1,278,234
Adjusted total capital	1,375,581	1,411,500	1,339,662
Risk weighted assets (RWA)	3,966,022	3,966,022	3,966,022
Adjusted core capital to RWA	33%	34%	32%
Adjusted total capital to RWA	35%	36%	34%
	=====	=====	=====

##### Interest rate risk – stress test-as at 31 December 2013

	Amount Sh'000	Scenario 10% Increase in net margin Sh'000	Scenario 10% Decrease in net margin Sh'000
Profit before taxation	105,816	120,120	91,512
Adjusted core capital	1,175,436	1,292,980	1,057,892
Adjusted total capital	1,219,805	1,341,786	1,097,825
Risk weighted assets (RWA)	2,914,374	3,205,811	2,622,937
Adjusted core capital to RWA	40%	40%	40%
Adjusted total capital to RWA	42%	42%	42%
	=====	=====	=====

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### c) Market Risk (Continued)

##### ii) Foreign exchange risk (Continued)

Foreign exchange risk is the risk that may occur to earnings or capital that results from movement of foreign exchange rates. This type of risk affects the bank due to cross-border investing and operating activities. The board of directors has assigned authority for management oversight of the foreign exchange risk policy to the CEO and Treasury manager.

##### Management of foreign exchange risk

The bank operates wholly within Kenya and its assets and liabilities are reported in the local currency. The bank's currency risk is managed within the Central Bank of Kenya exposure guideline of 20% core capital. The bank's management monitors foreign currency exposure on a daily basis.

The bank's currency position is as follows:

	KES Sh '000	GBP Sh '000	USD Sh '000	EURO Sh '000	OTHERS Sh '000	Total Sh '000
<b>FINANCIAL ASSETS</b>						
Cash in hand	59,147	1,063	7,861	4,512	-	72,583
Balances with CBK	244,804	4,343	157,025	4,806	-	410,978
Deposits and balances due from banking institutions	1,127,771	14,757	52,804	21,415	10,132	1,226,879
Government securities	3,828,558	-	-	-	-	3,828,558
Other securities	198,314	-	-	-	-	198,314
Advances to customers	4,096,375	-	262,561	88,679	-	4,447,615
<b>Total financial assets</b>	<b>9,554,969</b>	<b>20,163</b>	<b>480,251</b>	<b>119,412</b>	<b>10,132</b>	<b>10,184,927</b>
<b>FINANCIAL LIABILITIES</b>						
Customer deposits	7,702,378	20,046	284,272	41,316	-	8,048,012
Amounts due to local banks	650,000	-	209,117	77,126	-	936,243
<b>Total financial liabilities</b>	<b>8,352,378</b>	<b>20,046</b>	<b>493,389</b>	<b>118,442</b>	<b>-</b>	<b>8,984,255</b>
<b>Net balance sheet position</b>	<b>1,202,591</b>	<b>117</b>	<b>(13,138)</b>	<b>970</b>	<b>10,132</b>	<b>1,200,672</b>
<b>At 31 December 2013</b>						
Total financial assets	7,297,340	20,789	392,315	102,972	2,423	7,815,839
Total financial liabilities	6,284,728	21,938	358,362	71,166	-	6,736,194
<b>Net balance sheet position</b>	<b>1,012,612</b>	<b>(1,149)</b>	<b>33,953</b>	<b>31,806</b>	<b>2,423</b>	<b>1,079,645</b>

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### c) Market Risk (Continued)

##### ii) Foreign exchange risk (Continued)

The table below shows the foreign exchange risk sensitivity analysis. The net position is after a 10% increase or decrease in foreign currency exchange rates against the Kenya shilling.

##### At 31 December 2014

	Amount Sh'000	Scenario 10% increase in foreign currency rate Sh'000	Scenario 10% decrease in foreign currency rate Sh'000
Profit before taxation	160,871	161,037	160,705
Adjusted core capital	1,314,153	1,314,319	1,313,462
Adjusted total capital	1,375,581	1,375,747	1,374,890
Risk weighted assets (RWA)	3,964,340	3,964,340	3,964,340
Adjusted core capital to RWA	33%	33%	33%
Adjusted total capital to RWA	35%	34%	35%
	=====	=====	=====

##### At 31 December 2013

	Amount Sh'000	Scenario 10% increase in foreign currency rate Sh'000	Scenario 10% decrease in foreign currency rate Sh'000
Profit before taxation	105,816	120,120	91,512
Adjusted core capital	1,175,436	1,292,980	1,057,892
Adjusted total capital	1,219,805	1,341,786	1,097,825
Risk weighted assets (RWA)	2,914,374	3,205,811	2,622,937
Adjusted core capital to RWA	40%	40%	40%
Adjusted total capital to RWA	42%	42%	42%
	=====	=====	=====

##### iii) Price risk

Treasury bonds held at fair value are stated at their market value on the last day of business in the year. These are subject to frequent variations due to changes in their market prices.

An increase or decrease in rates by 10% with all other variables held constant, will have a decrease/increase in shareholders' equity of Sh 4,253,300 (2013: Sh 9,922,057).

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### d) Capital Management

##### Regulatory capital

The Central Bank of Kenya sets and monitors capital requirements for the bank.

The bank's objectives when managing capital are:

- To safeguard the bank's ability to continue as a going concern so that it can continue to provide returns for the shareholders and benefits for the other stakeholders.
- To maintain a strong capital base to support the current and future development needs of the business.
- To comply with the capital requirements set by the Central Bank of Kenya.

Capital adequacy and use of regulatory capital are monitored by management employing techniques based on the guidelines developed by the Central bank of Kenya for supervisory purposes. The required information is filed with the Central Bank of Kenya on a monthly basis.

The Central Bank of Kenya requires each bank to:

- a) Hold the minimum level of regulatory capital of Sh 1 billion.
- b) Maintain a ratio of total regulatory capital; to risk weighted assets plus risk weighted off balance assets at above the required minimum of 8%;
- c) Maintain a core capital of not less than 8% of total deposit liabilities and
- d) Maintain total capital of not less than 12% of risk weighted assets plus risk weighted off financial position items.

In addition to the above minimum capital adequacy ratios of 8% and 12%, with effect from 1 January 2013, institutions are required to hold a capital conservation buffer of 2.5% over and above these minimum ratios to enable institutions withstand future periods of stress. This brings the minimum core capital to risk weighted assets and total capital to risk weighted assets requirements to 10.5% and 14.5% respectively. The capital conservation buffer is made up of high quality capital which should comprise mainly of common equity, premium reserves and retained earnings.

Institutions that currently meet the minimum capital ratios of 8% and 12% but remain below the buffer-enhanced ratios of 10% and 14.5% should maintain prudent earnings retention policies with a view to meeting the conservation buffer within 24 months effective from 1 January 2013.

The bank's regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes ordinary share capital, share premium, retained earnings, after deductions for intangible assets (excluding computer software), investments in equity instruments of other institutions and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.
- Tier 2 capital, which includes 25% revaluation surplus which have received prior CBK approval, qualifying subordinated liabilities and collective impairment allowances.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### iv) Capital Management (Continued)

The bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The bank has complied with all externally imposed capital requirements throughout the period.

The bank's regulatory capital position at 31 December was as follows:

	Nominal financial position amounts		Risk weighted amounts	
	2014 Sh'000	2013 Sh'000	2014 Sh'000	2013 Sh'000
<b>ASSETS</b>				
Cash (including foreign notes and coins)	72,583	67,233	-	-
Cash balances with Central Bank of Kenya	410,978	327,227	-	-
Government securities	3,828,558	2,782,597	-	-
Corporate bonds	198,314	242,215	-	-
Deposits and balances due from banking institutions	1,226,879	1,124,377	238,172	221,943
Loans and advances to customers	4,447,615	3,272,190	3,111,092	2,270,203
Other assets	103,144	118,242	103,144	118,242
Property and equipment	89,640	58,337	89,640	58,337
Intangible assets	5,801	4,629	5,801	4,629
Deferred tax asset	2,679	10,608	2,679	10,608
Tax recoverable	16,125	21,221	16,125	21,221
	-----	-----	-----	-----
Total assets on balance sheet	10,402,316	8,028,876	3,566,653	2,705,183
	-----	-----	-----	-----
Total asset off balance sheet	560,186	236,118	397,686	209,212
	-----	-----	-----	-----
Total risk weighted assets	10,962,502	8,264,994	3,964,339	2,914,395
	=====	=====	=====	=====
Tier 1 Capital	1,314,153	1,175,436		
Tier 1 + Tier 2 Capital	1,375,581	1,219,805		
	=====	=====		
Basel ratio				
Tier 1 (CBK minimum – 8%)	33%	40%		
Tier 1 + Tier 2 (CBK min – 12%)	35%	42%		
	=====	=====		

The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation, by Risk and Credit, and is subject to review by the Credit Committee or ALCO as appropriate.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### v) Operating risk

##### Non-financial risk management disclosures

The Board of Directors has put in place a framework for management of non-financial risk management of the bank. The Board Risk Management Committee (BMRC) is responsible for monitoring compliance of this framework with the bank's overall risk management policies and procedures, and review of the adequacy of the risk management framework in relations to non-financial risks faced by the bank.

The key non-financial risks the bank faces are strategic risk, operational risks, reputational risk, compliance/legal risk.

##### i) Strategic risk

Strategic risk is a function of the internal and the external environment. The strategic risk policy of the bank provides direction and guidance to the board of directors for anticipating change, both externally and internally.

The bank uses key indicators to measure strategic risk such as: Current and forecasted economic conditions such as economic growth, inflation, interest rates, foreign exchange trends and other useful key economic data such as demography and demographic structures; trends within the banking sector such as, Competition both from existing players and new entrants; Merger and acquisition activities; Changes in customer needs, wants and behaviour; development of new products and use of technology; Changes in the bank's various sector exposures and the associated risks; and achievement of the targets, goals and objectives set by the board.

##### Responsibilities of strategic risk

The board of directors is responsible for the formulation and overall implementation of the bank's strategy. Strategy execution, strategic risk planning and overall strategic risk management is delegated to managing director.

##### Management of strategic risk

The board and management use the board, committees, and strategic plan to manage strategic risk. Regular and adhoc meetings of the board, the board committees review reports of the management and take corrective action. The execution of the bank's 5 year strategic plan is a key tool for strategic risk with the current strategic plan being 2010-2015. The next strategic plan cycle plan is being developed.

##### ii) Bank operational risk

The bank's operational risk framework is designed to identify risks, measures and mitigate operational risks. These are risks associated with human error, system failures or technological failure, inadequate procedures and controls, unforeseen catastrophes, or other operational problems which may result in unexpected losses.

##### Responsibilities for operational risk management

The General Manager-Operations, continually reports to the Managing Director on all the key risks of the bank. Risk & Compliance department as well as Internal Audit reports both report to the managing director and their respective board committees.

Through use of key performance indicators (KPI's) so as to adequately reflect the key risk area, and report on them. KPI's are reported monthly, quarterly, or on emergencies, whichever is appropriate. An examples of a KPI is 'Incident/Fraud/ Suspicious Activities and Transaction Reports.'



## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### e) Operating risk (Continued)

These detail those process related operational risk incidents combined with what remedial action was taken and what steps implemented to avoid a repeat occurrence. These reports are submitted as soon as the incident is discovered and notable trends reported quarterly on a summary report. Reporting operational risk is a key part of risk management and staff are required to report all incidents which could fall within any of the six key risk areas (as above) – whether or not they resulted in any actual loss to the Bank.

#### iii) Reputational risk

Reputational risk is the potential that negative publicity may lead to decline of its customer base, costly litigation, revenue reduction and subsequently its value and brand. All other risks may lead to reputational risks.

Main source of reputational risks are: business viability, business practices, fraudulent activities, litigations, customer satisfaction, anti-money laundering (AML) and rumours.

#### Responsibilities for reputational risk

The responsibility for management of reputational risk lies with the board of directors of the bank. Nonetheless, risk and audit management committees are responsible for reviewing adequacy and effectiveness of internal control systems relating to reputation risk and means through which exposures related to reputation risk are managed. Their purpose is to ensure that all stakeholders meet the bank's reputational risk objectives.

#### Management of Reputational risk

Overall, the bank promotes a corporate culture that adequately addresses stakeholder concerns and result in a gain of confidence. Internally, the bank have developed a code of conduct for directors and senior management and all staff. The bank also fully complies with applicable laws, legislation, and regulations. Finally, we continually communicate to the staff and regulators and the public on our compliance and standards.

#### iv) Compliance (legal/regulatory) risk

Compliance risk refers to the potential of loss arising from non-compliance or violation of laws, rules, regulations, obligatory practices/standards, contractual agreements. The bank is variously exposed to compliance risk due to relations with a wide number of stakeholders, e.g. regulators, customers, counter parties, as well as tax authorities, local authorities and other authorized agencies. The bank meets high standards of compliance with the Central Bank of Kenya, County governments, Occupational Safety and Health Administration (OSHA) and National Environment Management Authority (NEMA) etc.

#### Management of regulatory and legal risk

The risk & compliance department identifies and monitors the key risks and is responsible for ensuring that the day to day business controls comply with applicable legislation and are in line with best practice. Internal and external legal counsel work closely with business units to identify areas of existing and potential regulatory/legal risks and actively manage them to reduce the bank's exposures.

The board risk management committee receive the risk & compliance department's report on the strength of the bank's compliance risk framework to enable them determine whether it is under control.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### e) Operating risk (Continued)

##### iv) Compliance (legal/regulatory) risk (Continued)

###### Management of regulatory risks

The board of directors and senior management through adoption of the bank's corporate governance and code of conduct sets a culture of integrity. All employees are required to attest to this code when they join the bank and thereafter annually, indicating that they have understood it and that they have complied with its provisions.

The bank has implemented compliance risk in key areas such as Know Your Customer (KYC) policy. Customer due diligence (CDD) and transactions monitoring has been ongoing. Cash transaction reporting (CTR) and Suspicious Account Transactions Reporting (SATR) is done as required by FRC. The risk and compliance department periodically update business units on the Anti Money Laundering's on UN Security Committees reports on individuals and entities who been place on travel ban and funds frozen and embargo on arms as well as other regional and national bodies involved in fighting Money Laundering and Combating terrorism including the FAFT 40 and the Wolfsberg-Private Banking Principles.

##### v) IT risk

The bank's information technology risk management ensures presence of an effective mechanism to identify, measure, monitor, and control the risks inherent in the banks' IT systems, ensure data integrity, availability, confidentiality and consistency and provide the relevant early warning mechanism.

###### Responsibilities for Management of IT Risk

The three key functions responsible are the board, senior management and IT Head. The board ensures there is an IT governance structure that meets its risk tolerance. Senior management ensures staff understands and adheres to IT Risk Management. The Head of IT is key in decision making on business development that require the use of IT and that such system meet the bank's needs.

###### Management of IT Risk

By restricted access to both the IT system and physical access to IT infrastructure(s), IT security deployment and periodic IT Audit.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. FINANCIAL RISK MANAGEMENT OBJECTIVES & POLICIES (Continued)

#### f) Fair value of financial assets and liabilities

The table below shows an analysis of financial instruments at fair value by level of the fair value hierarchy. The financial instruments are grouped into levels 1 to 3 based on the degree to which the fair value is observable.

- i) Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- ii) Level 2 fair value measurements are those derived from inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as a price) or indirectly (i.e. derived from prices); and
- iii) Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs)

	Note	Level 1 Shs'000	Level 2 Shs'000	Level 3 Shs'000	Total Shs'000
<b>31 December 2014</b>					
Financial assets designated at fair value through profit and loss					
Treasury bonds	15	1,543,167	-	-	1,543,167
		=====	=====	=====	=====
<b>31 December 2013</b>					
Financial assets designated at fair value through profit or loss					
Treasury bonds	15	1,259,431	-	-	1,259,431
		=====	=====	=====	=====

The above were valued at quoted bid prices in an active market (Nairobi Securities Exchange). Except as detailed above, the directors consider that the carrying amounts of financial assets and liabilities recognised in the statement of financial position approximate their fair values.

There were no transfers between levels 1, 2, and 3 in the period (2013: none).

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

4. INTEREST INCOME	2014 Sh'000	2013 Sh'000
Advances to customers	668,077	615,568
Government securities: - Held to maturity	101,841	100,069
Government securities: - At fair value through profit or loss	196,588	218,544
Corporate bonds: - Held to maturity	15,783	18,940
Deposits/balances due from other financial institutions	35,151	23,221
	1,017,440	976,342
	=====	=====

5. INTEREST EXPENSE	2014 Sh'000	2013 Sh'000
Customer deposits	679,941	666,500
Amounts due to local banks	1,084	150
	681,025	666,650
	=====	=====

6. FEES AND COMMISSION INCOME	2014 Sh'000	2013 Sh'000
Transaction related fees	44,255	31,695
Credit related fees and commissions	21,790	10,684
	66,045	42,379
	=====	=====

### 7. GAIN ON FOREIGN EXCHANGE DEALINGS

Gains on foreign currency dealings arose from trading in foreign currency transactions and also on the translation of foreign currency assets and liabilities.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 8. OTHER OPERATING INCOME

	2014 Sh'000	2013 Sh'000
a) Net trading income/(loss)		
Gain arising on financial assets designated at fair value		
Income on treasury bonds trading	18,492	11,064
Fair value gains/(loss) on treasury bonds (note 15)	24,041	(29,301)
	<u>42,533</u>	<u>(18,237)</u>
	=====	=====
b) Other operating income		
Bad debts recovered	-	3,549
Locker rental income	1,274	1,228
Other operating income	1,893	2,401
	<u>3,167</u>	<u>7,178</u>
	=====	=====

### 9. OPERATING EXPENSES

	2014 Sh'000	2013 Sh'000
Staff costs (note 10)	97,423	74,605
Contribution to Deposit Protection Fund	9,698	7,884
Depreciation (note 20)	15,288	14,978
Amortisation of intangible assets (note 21)	1,302	1,009
Directors' emoluments	19,887	17,522
Auditors' remuneration	2,410	2,250
Rent and rates	37,039	32,389
Legal and professional fees	9,633	9,328
Insurance	9,475	7,842
Security	8,916	6,274
Telephone and postage	10,092	7,374
Repairs and maintenance	3,387	3,840
Other expenses	62,179	43,377
	<u>286,729</u>	<u>228,673</u>
	=====	=====

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 10. STAFF COSTS

	2014 Sh'000	2013 Sh'000
Salaries and allowances	92,162	71,789
Staff training	105	38
Terminal dues	651	2,071
NSSF contributions	184	153
Pension contributions-defined contribution scheme	3,239	-
Leave pay expense	800	365
Medical expenses	282	189
	<u>97,423</u>	<u>74,605</u>
	=====	=====

### 11. TAXATION

(a) Taxation credit		
Current taxation based on the taxable profit for the period at 30%	5,096	-
	<u>5,096</u>	<u>-</u>
Deferred taxation charge(note 22):-		
- current year charge	7,929	11,158
	<u>7,929</u>	<u>11,158</u>
	<u>13,025</u>	<u>11,158</u>
	=====	=====
(b) Reconciliation of taxation credit to the expected taxation based on accounting profit		
Accounting profit before taxation	160,871	105,816
	<u>160,871</u>	<u>105,816</u>
Tax at the applicable rate of 30%	48,261	31,745
Effect of expenses disallowed for taxation purposes	11,251	22,442
Effect of income not subject to taxation	(46,488)	(43,029)
	<u>13,024</u>	<u>11,158</u>
	=====	=====

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

(c) Taxation recoverable movement		
At 1 January	21,221	21,221
Taxation charge	(5,096)	-
At 1 January and 31 December	16,125	21,221

### 12 . EARNINGS PER SHARE

Earnings per share are calculated by dividing the profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year.

	2014 Sh'000	2013 Sh'000
<b>Earnings</b>		
Earnings for the year attributable to ordinary shareholders (Sh'000)	147,846	94,658
Number of shares		
Weighted average number of ordinary shares in issue	1,000,000	1,000,000
Earnings per share-Basic (Sh)		
Ordinary shares	147.85	94.66

The diluted earnings per share is the same as the basic earnings per share as there were no potentially dilutive shares as at 31 December 2013 or 31 December 2012.

### 13. CASH AND BALANCES WITH CENTRAL BANK OF KENYA

	2014 Sh'000	2013 Sh'000
Cash on hand	72,583	67,233
Balances with Central Bank of Kenya		
- Cash ratio requirement	234,400	205,505
- Deposits held under lien	9,070	8,635
- Current account with CBK	167,508	113,087
	483,561	394,460

The cash ratio requirement is based on the customer deposits with the bank as adjusted by the Central Bank of Kenya requirements. As at 31 December 2014 the cash reserve ratio requirement was 5.25% (2013: 5.25%) of all customer deposits. The deposits held under lien are to support foreign currency clearing. These funds are not available for the day to day operations of the bank.

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 14. DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS

	2014 Sh'000	2013 Sh'000
Deposits due from banking institutions	950,000	800,000
Balances due from banking institutions	276,879	324,377
	<u>1,226,879</u>	<u>1,124,377</u>
	=====	=====

The weighted average effective interest rate for deposits and balances due from banking institutions at 31 December 2014 was 8 % (2013 – 4.67%).

### MATURITY ANALYSIS OF DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS

	2014 Sh'000	2013 Sh'000
Due on demand	950,000	324,377
Maturing within one month	276,879	800,000
	<u>1,226,879</u>	<u>1,124,377</u>
	=====	=====

### 15. GOVERNMENT SECURITIES

	2014 Sh'000	2013 Sh'000
(a) Treasury bills held to maturity		
At amortized cost – maturing within 90 days		
Face value	800,000	-
Less: unearned discount	(14,026)	-
	<u>785,974</u>	<u>-</u>
	=====	=====
(b) Treasury bonds		
At fair value through profit or loss - maturing after 3 years	1,543,167	1,259,431
Held to maturity – at amortised cost (maturing within 5 years)	869,111	754,329
Held to maturity – at amortised cost (maturing after 5 years)	630,306	768,837
	<u>3,828,558</u>	<u>2,782,597</u>
	=====	=====



## NOTES TO THE FINANCIAL STATEMENTS (Continued)

(c) Movement in treasury bonds (at fair value through profit or loss) can be summarised as follows:

	2014 Shs'000	2013 Shs'000
At 1 January	1,259,431	2,073,552
Additions	4,976,095	51,592
Disposals	(4,716,400)	(836,412)
gains/(Losses) from changes in fair value	24,041	(29,301)
At 31 December	1,543,167	1,259,431

The weighted average effective interest rate for treasury bonds as at 31 December 2014 was 9.00 % (2013 – 6.83%). Included in the above balances are treasury bonds amounting to Sh 70,000,000 (2013 – Sh 70,000,000) pledged with local commercial banks as security for letters of credit and guarantee facilities.

### 16. CORPORATE BONDS

	2014 Sh'000	2013 Sh'000
Held to maturity- at amoritised cost		
Corporate bonds maturing within 5 years	198,314	201,717
Corporate bonds maturing after 5 years	-	40,498
	198,314	242,215

The weighted average effective interest rate on the bonds at 31 December 2014 was 7.00 % (2013 – 7.00%).

Movement in corporate bonds held to maturity can be summarised as follows:

	2014 Shs'000	2013 Shs'000
At 1 January		
Redemption	242,215	287,295
Net amortisation	(34,725)	(34,725)
	(9,176)	(10,355)
At 31 December	198,314	242,215

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 17. ADVANCES TO CUSTOMERS

	2014 Sh'000	2013 Sh'000
Loans and advances to customers	4,612,607	3,427,470
Bills discounted	7,107	7,107
	<u>4,619,714</u>	<u>3,434,577</u>
Provision for impaired loans and advances (note 18)	(172,099)	(162,387)
	<u>4,447,615</u>	<u>3,272,190</u>

The weighted average effective interest rate on advances to customers as at 31 December 2014 was 17.7% (2013 – 18%).

Included in net advances are loans and advances amounting to Sh 121,807,000 (2013 – Sh 173,385,000), net of specific provisions, which have been classified as non-performing.

Advances to related parties are disclosed in note 29.

	2014 Sh'000	2013 Sh'000
Analysis of gross advances by maturity:		
Maturing within one year	2,106,094	2,364,620
Over one year to three years	1,896,293	494,017
Over three to five years	617,327	575,940
	<u>4,619,714</u>	<u>3,434,577</u>

### 18. PROVISION FOR IMPAIRED LOANS AND ADVANCES

	2014 Sh'000	2013 Sh'000
At 1 January	162,387	152,231
Provisions in the year	10,314	13,705
Write offs	(602)	(3,549)
	<u>172,099</u>	<u>162,387</u>

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 19. OTHER ASSETS

	2014 Shs'000	2013 Shs'000
Items in course of collection		
Prepayments	8,228	5,131
Other receivables	49,222	59,604
	45,694	53,507
	<hr/>	<hr/>
	103,144	118,242
	=====	=====

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 20. EQUIPMENT

	Computers & office equipment Sh'000	Motor vehicles Sh'000	Furniture, fittings and office renovations Sh'000	Total Sh'000
<b>COST</b>				
At 1 January 2013	59,513	6,147	116,297	181,957
Additions	5,922	1,800	8,445	16,167
Disposal	-	(800)	-	(800)
At 31 December 2013	65,435	7,147	124,742	197,324
At 1 January 2014	65,435	7,147	124,742	197,324
Additions	11,327	1,124	34,140	46,591
At 31 December 2014	76,762	8,271	158,882	243,915
<b>DEPRECIATION</b>				
At 1 January 2013	44,859	5,352	74,598	124,809
Charge for the year	5,262	383	9,333	14,978
Disposal	-	(800)	-	(800)
At 31 December 2013	50,121	4,935	83,931	138,987
At 1 January 2014	50,121	4,935	83,931	138,987
Charge for the year	5,108	658	9,522	15,288
At 31 December 2014	55,229	5,593	93,454	154,275
<b>NET BOOK VALUE</b>				
At 31 December 2014	21,533	2,678	65,429	89,640
At 31 December 2013	15,314	2,213	40,811	58,337

Included in equipment are assets with a cost of Sh 95,004,543 (2013 - Sh 74,896,453) which were fully depreciated. The notional depreciation charge in respect of these assets for the year is Sh 15,844,482 (2013 - Sh 12,218,713).

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 21. INTANGIBLE ASSETS COMPUTER SOFTWARE

	2014 Sh'000	2013 Sh'000
<b>COST</b>		
At 1 January	29,294	26,572
Additions	2,474	2,722
	-----	-----
At 31 December	31,768	29,294
	-----	-----
<b>AMORTISATION</b>		
At 1 January	24,665	23,656
Charge for the year	1,302	1,009
	-----	-----
At 31 December	25,967	24,665
	-----	-----
<b>NET BOOK VALUE</b>		
At 31 December	5,801	4,629
	=====	=====

### 22. DEFERRED TAXATION ASSET

	2014 Sh'000	2013 Sh'000
The deferred tax asset, computed at the enacted rate of 30%, is attributable to the following items:		
Accelerated capital allowances	1,367	2,517
Leave pay provision	1,312	1,179
Tax losses	-	6,912
	-----	-----
	10,608	10,608
	=====	=====
The movement on the deferred tax account is as follows:		
As at 1 January	10,608	21,766
Charge for the year – note 11 (a)	(7,929)	(11,158)
	-----	-----
At 31 December	2,679	10,608
	=====	=====

The bank had no accumulated tax losses as at 31 December 2014 (2013: Sh 23,039,157).

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 23. CUSTOMER DEPOSITS

	2014 Sh'000	2013 Sh'000
Current accounts	509,679	556,801
Savings accounts	277,981	285,676
Call deposits	669,123	320,878
Fixed deposits	6,591,229	5,437,162
	<u>8,048,012</u>	<u>6,600,517</u>
	=====	=====
Analysis of customer deposits by maturity:		
Payable within 90 days	6,331,212	5,192,497
Payable after 90 days and within one year	570,775	468,117
Payable after one year	1,146,025	939,903
	<u>8,048,012</u>	<u>6,600,517</u>
	=====	=====

The weighted average effective interest rate on interest bearing customer deposits at 31 December 2014 was 9.6% (2013 – 10.00 %).

Customers deposits from related parties are disclosed in note 29 and concentrations of customer deposits are covered under note 3(a).

### 24. DEPOSITS AND BALANCES DUE TO BANKING INSTITUTIONS

	2014 Sh'000	2013 Sh'000
Deposits due to banking institutions	936,243	135,676
	<u>936,243</u>	<u>135,676</u>
	=====	=====

The weighted average effective interest rate for deposits and balances due to banking institutions at 31 December 2014 was 8% (2013 - 6%).

### 25. OTHER LIABILITIES

	2014 Sh'000	2013 Sh'000
Sundry payables	25,754	42,148
Accruals	9,674	16,192
Leave pay provision	4,373	3,929
	<u>39,801</u>	<u>62,269</u>
	=====	=====

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 26. SHARE CAPITAL

	2014 Sh'000	2013 Sh'000
Authorised, issued and fully paid: 1,000,000 ordinary shares of Sh 1,000 each	1,000,000	1,000,000

### 27. NOTES TO THE STATEMENT OF CASH FLOWS

	2014 Sh'000	2013 Sh'000
(a) Reconciliation of profit before taxation to cash generated from operations		
Profit before taxation	160,871	105,816
Adjustments for:		
Depreciation	15,288	14,978
Amortization of intangible assets	1,302	1,009
Working capital changes :	177,461	121,803
Increase in balances held by Central Bank of Kenya under lien	(435)	(30)
Increase in advances to customers	(1,175,425)	(532,577)
(Increase)/decrease in treasury bonds	(1,045,961)	836,412
Decrease in corporate bonds	43,901	45,080
(Decrease)/increase in other assets	15,098	(54,004)
Increase in customer deposits	1,447,495	516,232
Increase in advances from other local banks	800,567	135,676
(Decrease)/increase in other liabilities	(22,468)	27,749
Cash generated from operations	240,233	1,096,341

	2014 Sh'000	2013 Sh'000
(b) Analysis of balances of cash and cash equivalents as shown in the financial position and notes		
Cash on hand	72,583	67,233
Deposits and balances due from banking institutions	1,226,879	1,124,377
Current account with Central Bank of Kenya	401,908	318,592
	1,701,370	1,510,202

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 27. NOTES TO THE STATEMENT OF CASH FLOWS (Continued)

For the purposes of the statement of cash flows, cash equivalents include short term liquid investments which are readily convertible into known amounts of cash and which were within three months of maturity when acquired, less advances from banks repayable within three months from the dates of the advances.

### 28. CONTINGENCIES AND COMMITMENTS INCLUDING OFF FINANCIAL POSITION ITEMS

	2014 Sh'000	2013 Sh'000
(a) Contingent liabilities		
Letters of credit	182,159	102,516
Letters of guarantee and performance bonds	283,340	100,797
Bills for collection	94,687	32,805
	560,186	236,118
	=====	=====

Letters of credit are commitments by the bank to make payments to third parties, on production of documents, on behalf of customers and are reimbursed by customers.

Letters of guarantee and performance bonds are issued by the bank, on behalf of customers, to guarantee performance by customers to third parties. The bank will only be required to meet these obligations in the event of default by the customers.

Contingent liabilities arising from law suits as at 31 December 2014 amounted to Sh 96,424,916 (2013- Sh 36,814,592)

(b) The bank had no capital commitments as at 31 December 2014 (2013 – Sh 15,853,487).

(c) Commitments to extend credit

Commitments to lend are agreements to lend to a customer in future subject to certain conditions. Such commitments are normally made for a fixed period. The bank may withdraw without incurring any charges from its contractual obligation to extend credit by giving reasonable notice to the customer.

(d) Operating lease arrangements

#### The bank as a lessee

At the financial position date, the bank had outstanding commitments under operating leases which fall due as follows:

	2014 Sh'000	2013 Sh'000
Within one year	31,061	25,084
In the second to fifth year inclusive	33,010	32,608
	64,071	57,692
	=====	=====



## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 29. RELATED PARTY TRANSACTIONS

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

Placings are made in the bank by directors, their associates and companies associated to directors. Advances to customers at 31 December 2014 include advances and loans to companies associated to directors employees of the bank. Contingent liabilities at 31 December 2014 include guarantees and letters of credit for companies associated to directors.

	Directors' associated companies		Employees/staff	
	2014 Sh'000	2013 Sh'000	2014 Sh'000	2013 Sh'000
Movement in related party balances was as follows:				
<b>Loans and advances:</b>				
At 1 January	325,092	262,183	22,794	14,442
Net movement during the year	199,462	62,909	10,288	8,352
At 31 December	524,554	325,092	33,082	22,794
Interest earned	83,929	58,517	3,970	3647
<b>Deposits:</b>				
At 1 January	312,766	301,976	9,809	11,827
Net movement during the year	(41,312)	10,790	(1,068)	(2,018)
At 31 December	271,454	312,766	8,741	9,809
Interest paid	27,145	31,277	699	981

	2014 Sh'000	2013 Sh'000
Guarantees and letters of credit to companies associated to directors	123,436	60,098

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 29. RELATED PARTY TRANSACTIONS (Continued)

#### Key management compensation

The remuneration of directors and other members of key management during the year were as follows:

	2014 Sh'000	2013 Sh'000
Key management salaries and other benefits	43,780 =====	31,805 =====
Directors emoluments	19,887 =====	17,522 =====

The remuneration of directors and key executives is determined by the board of directors having regard to the performance of the individuals and market trends.

### 30. FAIR VALUE

The directors consider that there is no material difference between the fair value and carrying value of the company's financial assets and liabilities where fair value details have not been presented.

### 31. FIDUCIARY ACTIVITIES

At 31 December 2014, the bank did not hold asset security documents on behalf of customers (2013: none).

### 32. COUNTRY OF INCORPORATION

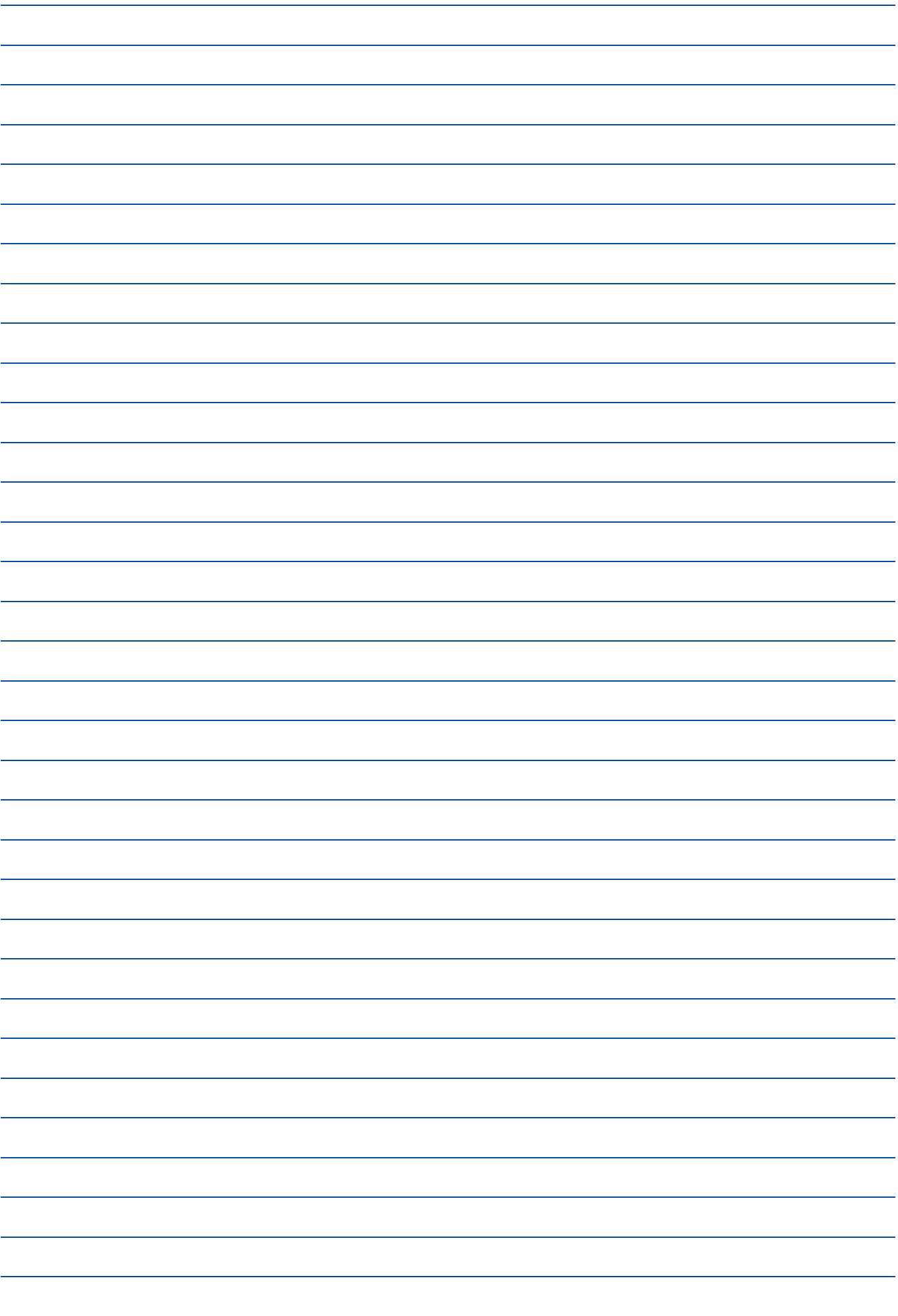
The company is incorporated in Kenya under the Companies Act and domiciled in Kenya.


### 33. CURRENCY

The financial statements are presented in Kenya Shillings thousands (Sh'000).

### 34. EVENTS AFTER REPORTING PERIOD

There are no significant events after the reporting period which has been reported in these financial statements.





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