

**KENYA RAILWAYS  
STAFF RETIREMENT BENEFITS  
SCHEME**

**REPORTS AND FINANCIAL  
STATEMENTS**

**FOR THE YEAR ENDED 30 JUNE 2014**

**RECEIVED**

**19 DEC 2014**

**RETIREMENT BENEFITS  
AUTHORITY**

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## REPORTS AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2014

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## KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

### CORPORATE TRUSTEE AND PROFESSIONAL ADVISERS

#### Corporate Trustee

Corporate & Pension Trust Services Limited  
10th Floor, Landmark Plaza, Argwings Kodhek Road  
P O Box 52439, 00200  
Nairobi

#### Investment Manager

Co-op Trust Investment Services Limited  
Cooperative House  
Haile Selassie Avenue  
P O Box 48231, GPO 00100  
Nairobi

#### Custodian

Kenya Commercial Bank Limited Custody Services  
Pledmont Plaza, 3rd Floor  
Ngong Road  
P O Box 30644, GPO 00100  
Nairobi

#### Legal Advisors

Millimo, Muthomi & Co. Advocates  
Agip House, 4<sup>th</sup> Floor  
Haile Selassie Avenue  
P O Box 8154 - 00200  
Nairobi

#### Auditors

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

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## REPORT OF THE CORPORATE TRUSTEE

The corporate trustee presents the report together with the audited financial statements for the year ended 30 June 2014.

### ESTABLISHMENT, NATURE AND STATUS OF THE SCHEME

The Kenya Railways Staff Retirement Benefits Scheme was established as a defined benefit scheme in March 2006.

The main purpose of the scheme is the provision of pension and other retirement benefits for employees of the sponsor upon their retirement from the sponsor's services and relief for the dependants of deceased employees and, for that purpose, the trustees shall hold the contributions paid to them by the sponsor and the members and any other sums, investments and income and all lump sums representing the same upon trust for the respective persons for whose benefit such sums and other benefits are expressed to be payable in accordance with the provisions of the Deed and the Rules.

The scheme's assets comprise mainly investment property which was transferred from the sponsor, Kenya Railways Corporation by a Kenya gazette notice in February 2007.

The Scheme is run by the corporate trustee who is responsible for its affairs. Expenses of the scheme are met by the scheme. The Scheme is closed to new members.

### CONTRIBUTIONS

The scheme is closed and thus does not receive any contributions. However given its nature the sponsor is obliged to meet any actuarial deficits that could arise.

### MEMBERSHIP

|                             | 2014<br>No. | 2013<br>No. |
|-----------------------------|-------------|-------------|
| Members as at start of year | 9,744       | 9,771       |
| Joiners                     | 429         | 385         |
| Leavers                     | (383)       | (412)       |
|                             | <hr/>       | <hr/>       |
| At the end of the year      | 9,790       | 9,744       |

Included in the membership above are 468 suspended members. These are members who have not returned their pension census forms. The suspended members' benefits continue to accrue and they will be reinstated and paid their accrued benefits once they return the census forms.

There are 1,580 deferred pensioners included in the members above currently in the employment of Kenya Railways Corporation and Rift Valley Railways Limited.

Joiners relate to employees who used to work for Kenya Railways Corporation up to 2006 and their dependents who had not been included in the list of pensioners since they had not provided required documents to the scheme to be included as members. It is expected that more members will join the scheme in future when suspended members return pension census forms.

### PENSION PAYMENTS

The corporate trustee has undertaken various initiatives as disclosed in note 2 to the financial statements to improve on the scheme's liquidity and settle the pension arrears.

### CORPORATE TRUSTEE

The corporate trustee is responsible for the security of the scheme's assets and as such regularly reviews the arrangements relating to custody, security and disposition of the assets. The corporate trustee holds regular meetings to discuss the affairs of the scheme and to deal with any other discretionary matters.

The current corporate trustee is shown on page 2.



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## REPORT OF THE CORPORATE TRUSTEE (Continued)

### FINANCIAL REVIEW

The statement of changes in net assets on page 9 shows an increase in the net assets of the scheme for the period of Sh 1,086,424,000 (2013: a decrease of Sh 162,512,000) and the statement of net assets on page 10 shows that the scheme's net assets as at 30 June 2014 amounted to Sh 21,251,343,000 (2013: Sh 20,164,919,000).

### INVESTMENT

We confirm that there is no self investment, nor have the Scheme's assets been used as security or collateral on behalf of the employer or any connected business or individual. As disclosed on note 11 to the financial statements some of the scheme's investment property has been pledged to secure borrowings by the scheme.

The scheme is self administered.

Currently, there are injunctive orders against four (4) properties for disposal namely; Nairobi Railway Club, Makongeni, Mubray and Muthurwa as per HCCC No 294 of 2012, Erdemann Property Limited vs KRSRBS & Another. However, the Scheme has appealed for the release of the four (4) properties.

### ACTUARIAL POSITION

The Scheme is subjected to a triennial valuation by independent actuaries to fulfil the statutory requirements under the Retirement Benefits Act.

Actuarial valuation of Kenya Railways Staff Retirement Benefits Scheme was undertaken for the period ended 30 June 2011 by Alexander Forbes Financial Services Limited.

In accordance with average experience of other similar schemes property assets and quoted equities are taken at 80% and 70% respectively of the values shown in the statement of net assets at the date of valuation. Other assets are taken at the values shown in the statement of net assets as at 30 June 2011.

The results of the valuation are summarised below:

|                                                                                                       | Sh'000     |
|-------------------------------------------------------------------------------------------------------|------------|
| Value placed on scheme assets                                                                         | 16,771,800 |
| Value of:                                                                                             |            |
| Future benefits to current pensioners<br>(Including dependants in receipt of pension)                 | 6,841,900  |
| Past service pension benefits for active members (deferred pensioners)<br>based on projected earnings | 3,780,500  |
| Cost of pension increases                                                                             | 1,145,400  |
| Pension increase arrears                                                                              | 473,100    |
|                                                                                                       | 12,240,900 |
| Actuarial surplus                                                                                     | 4,530,900  |
| Funding level (ratio of scheme assets to accrued past<br>service liabilities)                         | 137%       |

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## REPORT OF THE CORPORATE TRUSTEE (Continued)

### STATUTORY ASPECTS

The Retirement Benefits Authority (RBA) allows a maximum investment of 30% of the scheme's funds in immovable property. The scheme currently holds over 97% of its total assets as immovable property. The corporate trustee is taking the necessary steps to ensure that the management of the fund and its assets comply with the Retirement Benefits Act 1997 and the Retirement Benefits Regulations 2000.

The Retirement Benefits Authority (RBA) also requires that an actuarial valuation of a scheme should be carried out every three years. The actuarial valuation of Kenya Railways Staff Retirement Benefits Scheme was last undertaken for the period ended 30 June 2011. The corporate trustee will arrange for an actuarial valuation in 2015 to comply with RBA regulations.

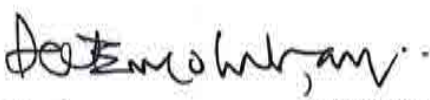
### AUDITORS

Deloitte & Touché have expressed their willingness to continue in office as auditors.

### FURTHER INFORMATION

Individual members of the Scheme are welcome to obtain further information about the Scheme. The Scheme's Chief Executive Officer will be pleased to answer any queries, general or about individual entitlements to benefits, which can be sent to him at Kenya Railways Staff Retirement Benefits Scheme offices.

BY ORDER OF THE CORPORATE TRUSTEE

  
 Corporate Trustee

18 December 2014

## KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

### STATEMENT OF CORPORATE TRUSTEE'S RESPONSIBILITIES

The Kenyan Retirement Benefits Act requires the corporate trustee to prepare financial statements for each financial year which show a true and fair view of the financial transactions of the Scheme for the period and of the disposition of its assets and liabilities as at period end. It also requires the corporate trustee to ensure that the Scheme keeps proper accounting records which disclose with reasonable accuracy at any time the financial position of the Scheme. The corporate trustee is also responsible for safeguarding the assets of the Scheme.

The corporate trustee is 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 Retirement Benefits Act, and for such internal controls as the corporate trustee determines are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The corporate trustee accepts responsibility for the annual financial statements, which have been prepared using appropriate accounting policies supported by reasonable and prudent judgments and estimates, in conformity with International Financial Reporting Standards and the Scheme's rules except for the departure from certain provisions of International Accounting Standard No. 40 (IAS 40) on Investment Property and International Financial Reporting Standard No. 13 (IFRS 13) on Fair Value Measurement as explained in note 1 to the financial statements. The corporate trustee is of the opinion that the financial statements give a true and fair view of the financial affairs of the Scheme and of its operating results. The corporate trustee further accepts 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.

The corporate trustee certifies that to the best of their knowledge and belief, the information furnished to the auditors for the purpose of the audit was correct and complete in every respect.

The corporate trustee acknowledges that over 97% of the scheme's investments are held in immovable properties and has undertaken various initiatives to improve the scheme's liquidity.

  
Corporate Trustee



18 December 2014



## INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

We have audited the accompanying financial statements of Kenya Railways Staff Retirement Benefits Scheme, set out on pages 9 to 29, which comprise the statement of net assets available for benefits as at 30 June 2014, and the statement of changes in net assets available for benefits and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### *Corporate Trustee's Responsibility for the Financial Statements*

The corporate trustee is 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 Retirement Benefits Act, and for such internal controls as the corporate trustee determines 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 about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on 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 Scheme's preparation of 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 effectiveness of the Scheme's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the corporate trustee, 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 qualified audit opinion.

### *Basis for Qualified Opinion*

*Non-compliance with International Accounting Standard No. 40 (IAS 40), Investment Property, and International Financial Reporting Standard No. 13 (IFRS 13), Fair Value Measurement*

As stated in note 11 to the financial statements, most of the scheme's investment properties totalling Sh 17,872,424,000 (2013: Sh 18,232,523,000) are carried at forced sale value and were last revalued on 30 June 2011. This is not consistent with the requirements of IAS 40 which requires that the fair value of the investment property shall reflect market conditions at the end of the reporting period. In addition, the values of most of the investment properties are based on forced sale values which is not consistent with the requirements of IFRS 13 which requires that fair value of an investment property should be determined based on highest and best use of the property. Due to lack of adequate information, we were unable to determine the financial effects on the financial statements of the non-compliance with IAS 40 and IFRS 13.



INDEPENDENT AUDITORS' REPORT  
TO THE MEMBERS OF KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME  
(Continued)

*Qualified opinion*

In our opinion, except for the effect of the matter described in the basis for qualified opinion paragraph above, the accompanying financial statements give a true and fair view of the financial transactions of the Scheme during the year ended 30 June 2014 and of the disposition of its assets and liabilities as at that date, other than liabilities to pay pensions and benefits falling due after the end of the year in accordance with International Financial Reporting Standards and the requirements of the Kenyan Retirement Benefits Act.

*Emphases of matter*

Without further qualifying our opinion, we wish to draw your attention to the following:

a) Non-compliance with the Retirement Benefits Act

The Retirement Benefits Authority Investment Guidelines require that investments in immovable property in Kenya be limited to a maximum of 30% of the scheme's investments. As at 30 June 2014, over 97% of the scheme's investments were in immovable assets.

b) Note 2 to the financial statements which gives disclosures on the liquidity position of the scheme. Due to the high concentration of the scheme's assets in immovable property as discussed above and injunctive orders against disposal of the scheme's properties as discussed below. The conditions indicate a material uncertainty on the scheme's ability to meet its obligations as they fall due.

c) Note 11 to the financial statements which gives disclosures on investment properties some of whose titles are not in the scheme's name and there are injunctive orders against disposal of the scheme's properties as per court case reference HCCC No 294 of 2012, Erdemann Property Limited vs KRSRBS & Another.

d) Note 25 to the financial statements which gives disclosures on suspended members who have been left out of the actuarial valuation.

*The engagement partner responsible for the audit resulting in this independent auditors' report is Fred Aloo P/No 1537.*

*Debita & Tonko*

Certified Public Accountants (Kenya)  
Nairobi, Kenya

*18 December* 2014

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS FOR THE YEAR ENDED 30 JUNE 2014

|                                                                | Note | 2014<br>Sh'000    | 2013<br>Sh'000    |
|----------------------------------------------------------------|------|-------------------|-------------------|
| <b>DEALINGS WITH MEMBERS</b>                                   |      |                   |                   |
| Pension payment                                                | 4    | (764,634)         | (773,336)         |
| <b>RETURNS ON INVESTMENTS PROPERTY</b>                         |      |                   |                   |
| Rental income                                                  |      | 542,233           | 533,671           |
| Property management expenses                                   | 5    | (248,077)         | (33,351)          |
| Fair value gain on investment property                         | 11   | 1,687,370         | -                 |
| Gain on disposal of investment property                        | 11   | 174,007           | 224,600           |
|                                                                |      | <hr/>             | <hr/>             |
| NET RETURN ON INVESTMENT PROPERTY                              |      | 2,155,533         | 724,920           |
|                                                                |      | <hr/>             | <hr/>             |
| <b>RETURNS/(LOSS) ON OTHER INVESTMENTS</b>                     |      |                   |                   |
| Investment income                                              | 6    | 765               | 156               |
| Market gain on revaluation of quoted equity investments        |      | -                 | 1                 |
| Investment management expenses                                 | 7    | (632)             | (554)             |
|                                                                |      | <hr/>             | <hr/>             |
| NET RETURNS/(LOSS) ON INVESTMENTS                              |      | 133               | (397)             |
|                                                                |      | <hr/>             | <hr/>             |
| OTHER INCOME                                                   | 8    | 16                | 236               |
|                                                                |      | <hr/>             | <hr/>             |
| Administrative expenses                                        | 9    | (279,983)         | (93,945)          |
| Finance costs                                                  | 10   | (24,641)          | (19,989)          |
|                                                                |      | <hr/>             | <hr/>             |
| NET INCREASE/(DECREASE) IN NET ASSETS FOR THE YEAR             | 19   | 1,086,424         | (162,512)         |
| NET ASSETS AVAILABLE FOR BENEFITS AT THE BEGINNING OF THE YEAR |      | 20,164,919        | 20,327,431        |
|                                                                |      | <hr/>             | <hr/>             |
| NET ASSETS AVAILABLE FOR BENEFITS AT THE END OF THE YEAR       |      | <u>21,251,343</u> | <u>20,164,919</u> |

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AS AT 30 JUNE 2014

|                                          | Note | 2014<br>Sh'000     | 2013<br>Sh'000     |
|------------------------------------------|------|--------------------|--------------------|
| <b>Assets</b>                            |      |                    |                    |
| Investment property                      | 11   | 22,039,394         | 20,712,123         |
| Equipment                                | 12   | 2,181              | 1,875              |
| Intangible assets                        | 13   | -                  | -                  |
| Receivables and prepayments              | 14   | 479,841            | 632,233            |
| Quoted equity investments                |      | -                  | 2                  |
| Fixed deposits                           | 15   | 114,090            | 930                |
| Bank balance                             |      | 6,288              | 30,121             |
| <b>Total assets</b>                      |      | <b>22,641,794</b>  | <b>21,377,284</b>  |
| <b>Liabilities</b>                       |      |                    |                    |
| Payables                                 | 17   | (1,165,451)        | (1,155,847)        |
| Borrowings                               | 18   | (225,000)          | (56,518)           |
| <b>Total liabilities</b>                 |      | <b>(1,390,451)</b> | <b>(1,212,365)</b> |
| <b>NET ASSETS AVAILABLE FOR BENEFITS</b> |      | <b>21,251,343</b>  | <b>20,164,919</b>  |
| <b>REPRESENTED BY:</b>                   |      |                    |                    |
| <b>FUND BALANCE</b>                      | 19   | <b>21,251,343</b>  | <b>20,164,919</b>  |

The financial statements on pages 9 to 29 were approved by the corporate trustee on 18 December 2014 and were signed by:

*[Signature]*  
*[Signature]*



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 30 JUNE 2014

|                                                        | Note | 2014<br>Sh'000 | 2013<br>Sh'000 |
|--------------------------------------------------------|------|----------------|----------------|
| <b>Cash flows from operating activities</b>            |      |                |                |
| Other income                                           | 8    | 16             | 236            |
| Benefits paid                                          |      | (1,070,112)    | (666,318)      |
| Administrative and management expenses paid            |      | (225,690)      | (175,013)      |
|                                                        |      | <hr/>          | <hr/>          |
| Net cash used in operating activities                  |      | (1,295,786)    | (841,095)      |
|                                                        |      | <hr/>          | <hr/>          |
| <b>Cash flows from investing activities</b>            |      |                |                |
| Rental income and deposits received on property        |      | 687,114        | 573,346        |
| Proceeds from sale of investment property              |      | 552,525        | 363,750        |
| Investment income received                             | 6    | 765            | 156            |
| Sale of equity shares                                  |      | 2,196          | -              |
| Purchase of equipment                                  | 12   | (1,328)        | (157)          |
|                                                        |      | <hr/>          | <hr/>          |
| Net cash generated from investing activities           |      | 1,241,272      | 937,095        |
|                                                        |      | <hr/>          | <hr/>          |
| <b>Cash flows from financing activities</b>            |      |                |                |
| Interest paid                                          | 10   | (24,641)       | (19,989)       |
| Loan proceeds/(repayment)                              |      | 168,482        | (71,400)       |
|                                                        |      | <hr/>          | <hr/>          |
| Net cash generated from/(used in) financing activities |      | 143,841        | (91,389)       |
|                                                        |      | <hr/>          | <hr/>          |
| Net increase in cash and cash equivalents              |      | 89,327         | 4,611          |
| Cash and cash equivalent at beginning of the year      |      | 31,051         | 26,440         |
|                                                        |      | <hr/>          | <hr/>          |
| Cash and cash equivalent at end of the year            |      | 120,378        | 31,051         |
|                                                        |      | <hr/>          | <hr/>          |
| <b>Represented by:</b>                                 |      |                |                |
| Fixed deposits                                         | 15   | 114,090        | 930            |
| Bank balance                                           |      | 6,288          | 30,121         |
|                                                        |      | <hr/>          | <hr/>          |
|                                                        |      | 120,378        | 31,051         |
|                                                        |      | <hr/>          | <hr/>          |

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2014

### 1 ACCOUNTING POLICIES

#### **Departure from certain provisions of International Accounting Standard No. 40 (IAS 40) on Investment Property and International Financial Reporting Standard No. 13 (IFRS 13) on Fair Value Measurement**

In preparation of these financial statements the corporate trustee decided to depart from certain provisions of International Accounting Standard No. 40 (IAS 40) on Investment Property and International Financial Reporting Standard No. 13 (IFRS 13) on Fair Value Measurement with regard to fair valuation of its investment properties. The corporate trustee is of the opinion that the financial statements as prepared present a true and fair view of the financial transactions of the Scheme for the year and of the disposition of its assets and liabilities as at year end. The financial statements comply with all other applicable International Financial Reporting Standards and the requirements of the Kenyan Retirement Benefits Act.

#### **Adoption of new and revised International Financial Reporting Standards**

##### **(i) *New standards and amendments to published standards effective for the year ended 30 June 2014***

At the date of authorisation of these financial statements, various revised standards and interpretations were issued and effective. These standards and interpretations did not result in the change in the scheme's accounting policies or result in any material impact on the financial statements of the scheme.

Specifically, IFRS 13 on Fair Value Measurement has been adopted in these financial statements. IFRS 13 replaces the guidance on fair value measurement in existing IFRS accounting literature with a single standard.

The IFRS is the result of joint efforts by the IASB and FASB to develop a converged fair value framework. The IFRS defines fair value, provides guidance on how to determine fair value and requires disclosures about fair value measurements. However, IFRS 13 does not change the requirements regarding which items should be measured or disclosed at fair value.

IFRS 13 applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements). With some exceptions, the standard requires entities to classify these measurements into a 'fair value hierarchy' based on the nature of the inputs:

- **Level 1** - quoted prices in active markets for identical assets or liabilities that the entity can access at the measurement date
- **Level 2** - inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly
- **Level 3** - unobservable inputs for the asset or liability

Entities are required to make various disclosures depending upon the nature of the fair value measurement (e.g. whether it is recognised in the financial statements or merely disclosed) and the level in which it is classified.

The application of the standard has led to additional disclosures in the financial statements.

##### **(ii) *Relevant new and revised IFRSs and interpretations in issue but not yet effective***

#### **IFRS 9, Financial Instruments**

IFRS 9 *Financial Instruments* issued in November 2009 and amended in October 2011 introduces new requirements for the classification and measurement of financial assets and financial liabilities and for derecognition.



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

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

#### (ii) *Relevant new and revised IFRSs and interpretations in issue but not yet effective*

IFRS 9 requires all recognised financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement 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 values at the end of subsequent accounting periods.

The most significant effect of IFRS 9 regarding the classification and measurement of financial liabilities relates to the accounting for changes in fair value of a financial liability (designated as at fair value through profit or loss) attributable to changes in the credit risk of that liability. Specifically, under IFRS 9, for financial liabilities that are designated as at fair value through profit or loss, 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 recognised 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. Previously, under IAS 39, the entire amount of the change in the fair value of the financial liability designated as at fair value through profit or loss was recognised in profit or loss.

IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with earlier application permitted.

The corporate trustee anticipates that IFRS 9 that will be adopted in the fund's financial statements for the annual period beginning 1 January 2018 and that the application of the new Standard will not have a significant impact on amounts reported in respect of the Scheme's financial assets and financial liabilities.

At the date of authorization of these financial statements several other new and revised or amended standards and interpretations were in issue but not yet effective. The corporate trustee anticipates that the adoption of these new or revised standards and interpretations will have no material impact on the financial statements of the fund in future periods.

#### (iii) *Early adoption of standards*

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

### Basis of preparation

The financial statements are prepared under the historical cost convention as modified for the revaluation of investment properties and financial instruments. The principal accounting policies adopted remain unchanged from the previous year and are set out below:-

### Benefits

Benefits payable to leavers are recognised in the period in which they fall due.



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1 ACCOUNTING POLICIES (Continued)

#### **Rental income**

Investment property includes rental houses. However, some of the tenants in these houses specifically in Makongeni and Muthurwa do not have lease agreements and therefore the collection of rent is not guaranteed. All rental income other than that from Kenya Railways Corporation is recognised when received.

Rental income from Kenya Railways Corporation is recognised on a straight-line basis over the term of the relevant lease.

#### **Investment income**

Interest income is accrued on a time basis, by reference to the principal outstanding at the effective interest rate applicable.

#### **Dividend income**

Dividend income from investments is recognised when the scheme's right to receive payment as a shareholder has been established.

#### **Financial instruments**

Financial assets and liabilities are recognised on the Scheme's statement of net assets when the scheme becomes a party to the contractual provisions of the Instruments.

#### **(i) Financial assets**

##### *Classification*

The scheme classifies its financial assets into the following categories: Financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale assets. Management determines the appropriate classification of its investments at initial recognition.

##### *Quoted equity investments*

Quoted equity investments are held for trading and are stated at market values as at 30 June.

##### *Government securities*

Government securities comprise treasury bills and treasury bonds, which debt securities are issued by the Government of Kenya. Treasury bills are held to maturity and are stated at face value less unearned discount while treasury bonds are held for trading and are stated at fair value.

##### *Receivables*

Trade receivables are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts. Trade receivables are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the receivable, and that the loss event has an impact on the future cash flows on the receivable that can be estimated reliably.

Objective evidence that trade receivables are impaired could include default or delinquency by a customer, indications that a customer will enter bankruptcy as well as observable changes in national or local economic conditions that correlate with default on receivables. Bad debts are written off when all reasonable steps to recover them have failed.

Bad debts are written off in the year in which they are identified.

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1 ACCOUNTING POLICIES (Continued)

#### Financial instruments (Continued)

##### (ii) Financial liabilities

Financial liabilities are stated at amortised cost. Amortised cost of a financial liability is the amount at which the financial liability was measured at initial recognition less principal repayments, plus accrued interest on the outstanding principal.

##### *Accounts payable*

The liabilities for accounts payable are carried at cost, which is measured at the fair or contractual value of the consideration to be paid in future in respect of goods and services supplied by the suppliers, whether billed or not, to the scheme.

##### *Borrowings*

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in profit or loss over the period of the borrowings using the effective interest method. Borrowings are classified as current liabilities unless the scheme has an unconditional right to defer settlement of the liability for more than 12 months after the reporting period.

#### Investment property

Investment property, which is property held to earn rentals and/or for capital appreciation, is measured initially at its cost, including transaction costs. Subsequent to initial recognition, part of the investment property is measured at fair value. This is not in compliance with the requirements of IAS 40 and the audit opinion is qualified in this respect. Gains and losses arising from changes in the fair value of investment property are dealt with in statement of changes in net assets in the period in which they arise.

#### Equipment

Equipment is stated at historical cost less accumulated depreciation and any accumulated impairment losses.

#### Depreciation

Depreciation on equipment is calculated on a straight-line basis to write off the cost of the equipment over the expected useful lives at the following annual rates:

|                       |                    |
|-----------------------|--------------------|
| Computer equipment    | 33 $\frac{1}{3}$ % |
| Fixtures and fittings | 12 $\frac{1}{2}$ % |

The gains and losses arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the statement of changes in net assets.

#### Intangible assets

Intangible assets comprise software licences and is amortised on a straight line basis over the useful life of the licence which is five years.

#### Impairment of assets

The carrying amounts of the Scheme's assets are reviewed annually at the year end to determine if there is any indication of impairment. If such condition is identified, the asset's net recoverable amount is estimated. Where the asset's carrying amount exceeds its net recoverable amount, it is written down immediately to the recoverable amount and the resulting impairment loss is treated as an expense in the statement of changes in net assets.



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1 ACCOUNTING POLICIES (Continued)

#### **Foreign currencies**

Foreign currency balances are translated into Kenyan Shillings at the rates of exchange ruling at the year end. Transactions during the year are translated at the rates ruling when the transactions are effected.

Gains and losses arising from the translations are dealt with in the statement of changes in net assets.

#### **Cash and cash equivalents**

For the purposes of the statement of cashflows, cash and cash equivalents comprise cash and bank balances, treasury bills and term deposits maturing within three months from date of acquisition.

#### **Comparatives**

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

### 2 LIQUIDITY OF THE SCHEME

As at 30 June 2014, over 97% of the scheme's investments were held in immovable properties. The scheme therefore does not always have sufficient liquid funds to meet its monthly pension obligations leading to pension arrears.

In addition, as disclosed in note 11, currently, there are injunctive orders against disposal of the scheme's properties valued at Sh 10,325,901,060 as per court case reference HCCC No 294 of 2012, Erdemann Property Limited vs KRSRBS & Another.

The corporate trustee has undertaken various initiatives to improve on the scheme's liquidity including; planned disposal of some investment properties, improvements on existing properties to enhance rent collections, developing undeveloped properties to earn rentals or for future sale and establishing a line of credit with a financial institution.

### 3 CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the process of applying the scheme's accounting policies, the corporate trustee 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:

#### *Impairment losses*

At the end of each reporting period, the scheme reviews the carrying amounts of its 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. Where it is not possible to estimate the recoverable amount of an individual asset, the scheme estimates the recoverable amount of the cash generating unit to which the asset belongs.

#### *Equipment*

Critical estimates are made by the corporate trustee in determining the useful lives and residual values to equipment 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.

### 4 PENSION PAYMENTS

Pension payments represent pensions paid to members of the scheme who are retired employees of Kenya Railways Corporation as per the scheme rules.



KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME  
NOTES TO THE FINANCIAL STATEMENTS (Continued)

|   | 2014<br>Sh'000                                   | 2013<br>Sh'000 |
|---|--------------------------------------------------|----------------|
| 5 | PROPERTY MANAGEMENT EXPENSES                     |                |
|   | Casual wages                                     | 10,627         |
|   | Repairs and maintenance                          | 622            |
|   | Valuation fees                                   | 6,953          |
|   | Title conveyance expenses                        | 23,120         |
|   | Land rates                                       | 11,324         |
|   | Legal charges                                    | 172,651        |
|   | Estate water bills                               | 928            |
|   | Other expenses                                   | 21,700         |
|   | Auction and rent recovery                        | 53             |
|   | Estate demolition costs                          | 99             |
|   |                                                  | <u>248,077</u> |
| 6 | INVESTMENT INCOME                                |                |
|   | Interest on short term deposits                  | <u>765</u>     |
| 7 | MANAGEMENT EXPENSES                              |                |
|   | Custodial fees                                   | 52             |
|   | Investment management fees                       | 580            |
|   |                                                  | <u>632</u>     |
| 8 | OTHER INCOME                                     |                |
|   | Prequalification income                          | 1              |
|   | Miscellaneous income                             | 15             |
|   |                                                  | <u>16</u>      |
| 9 | ADMINISTRATIVE EXPENSES                          |                |
|   | Audit fees                                       | 1,771          |
|   | Actuarial fees                                   | -              |
|   | Staff costs                                      | 42,249         |
|   | Bad debts written off                            | -              |
|   | Increase in provision for bad and doubtful debts | 125,384        |
|   | Depreciation                                     | 1,022          |
|   | Pension Bank Transfer Commission                 | 10,890         |
|   | Fund administration costs                        | 64,052         |
|   | Penalties                                        | 117            |
|   | Input Tax                                        | -              |
|   | Retirement Benefit Authority Levy - current year | 12,500         |
|   | - penalties                                      | 22,000         |
|   |                                                  | <u>279,983</u> |
|   |                                                  | <u>93,945</u>  |

## KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

|                                                                        | 2014<br>Sh'000 | 2013<br>Sh'000 |
|------------------------------------------------------------------------|----------------|----------------|
| 10 FINANCE COST                                                        |                |                |
| Interest on borrowings                                                 | 24,641         | 19,989         |
| 11 INVESTMENT PROPERTY                                                 |                |                |
| At forced sale value                                                   |                |                |
| L.R 209/6829 - Makongeni Estate, Nairobi **                            | 5,865,901      | 5,950,000      |
| L.R 209/6502 (Part) - Muthurwa Estate, Nairobi**                       | 2,450,000      | 2,450,000      |
| L.R. No. 209/19382 - Ngara Railway Estate - Nairobi*                   | 2,178,400      | 2,178,400      |
| L.R 209/11953 - Nairobi Railway Club, Nairobi **                       | 1,946,000      | 1,946,000      |
| L.R 209/12088 - Landmawe, Nairobi*                                     | 1,655,923      | 1,655,923      |
| L.R 209/12178 - Upper Hill (Part), Nairobi*                            | 1,155,000      | 1,155,000      |
| L.R 209/11954/2 (Part) - HQ (Eastern "Wing including Block D) Nairobi* | 1,138,400      | 1,138,400      |
| L.R 209/6506 - Matumbato, Nairobi                                      | 721,600        | 721,600        |
| L.R 209/6507 - Matumbato, Nairobi                                      | 349,600        | 349,600        |
| L.R 209/1064/1,2,3,4 & 5 - Valley Road, Nairobi                        | -              | 276,000        |
| L.R 1/422 - Ngong Road, Nairobi*                                       | 104,800        | 104,800        |
| L.R 1/423 - Ngong Road, Nairobi*                                       | 104,800        | 104,800        |
| L.R 1/420 - Kindaruma Road, Nairobi*                                   | 93,600         | 93,600         |
| L.R 1/437 - Kindaruma Road, Nairobi **                                 | 64,000         | 64,000         |
| L.R 209/378/5 - Hurlingham Nairobi                                     | 44,400         | 44,400         |
|                                                                        | 17,872,424     | 18,232,523     |
| At open market value                                                   |                |                |
| L.R 209/12401 - Goods Shed Area, Nairobi*                              | 2,000,000      | 1,470,000      |
| L.R 209/6505 - Matumbato, Nairobi                                      | 1,715,200      | 811,200        |
| L.R XXVI/941 - Chambilo, Mombasa                                       | 451,770        | 198,400        |
|                                                                        | 4,166,970      | 2,479,600      |
|                                                                        | 22,039,394     | 20,712,123     |

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 11 INVESTMENT PROPERTY (Continued)

|                                          | 2014       | 2013       |
|------------------------------------------|------------|------------|
| <b>Movement in investment properties</b> |            |            |
| At the beginning of the year             | 20,712,123 | 21,162,523 |
| Disposal                                 | (360,099)  | (450,400)  |
| Fair value gains                         | 1,687,370  | -          |
|                                          | <hr/>      | <hr/>      |
| At the end of the year                   | 22,039,394 | 20,712,123 |
|                                          | <hr/>      | <hr/>      |
| <b>Disposal of investment properties</b> |            |            |
| Disposal proceeds                        | 534,106    | 675,000    |
| Book value of disposed property          | (360,099)  | (450,400)  |
|                                          | <hr/>      | <hr/>      |
| Gain on disposal                         | 174,007    | 224,600    |
|                                          | <hr/>      | <hr/>      |

The investment properties were revalued by Knight Frank Limited registered valuers on 30 June 2011. Since then, only three properties: Goods Shed Area, Nairobi; Matumbato, Upperhill (L.R. No. 209/6505) and Chambilo, Mombasa have been revalued in 2014 by Gimco Limited.

Property L.R. No. 209/6506 Matumbato, Upperhill, Nairobi has been used as security over a loan received from Kenya Commercial Bank Limited.

\* Included in investment properties are properties valued at Sh 8,430,923,000 (2013 – Sh 7,900,923,000) whose titles are not in the scheme's name. These were however transferred to the scheme by Kenya Railways Corporation via a Kenya Gazette notice of 7 September 2006. According to the Legal Notice No. 169 of September 2006, the Trustees of the scheme were vested with 5 Acres of Good Shed property although the actual allotment size to the sponsor Kenya Railways Corporation was 8.11 Acres. It is on the basis of 5 acres the valuation was done and adopted by the Trustees. The corporate trustee is pursuing the transfer of titles and these processes are in different stages of completion.

\*\* Currently, there are injunctive orders against disposal of the scheme's properties valued at Sh 10,325,901,060 as per court case reference HCCC No 294 of 2012, Erdemann Property Limited vs KRSRBS & Another.



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 12 EQUIPMENT

|                       | Computers<br>Sh'000 | Office<br>equipment and<br>furniture<br>Sh'000 | Total<br>Sh'000 |
|-----------------------|---------------------|------------------------------------------------|-----------------|
| <b>COST</b>           |                     |                                                |                 |
| At 1 July 2012        | 3,959               | 4,099                                          | 8,058           |
| Additions             | 157                 | -                                              | 157             |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| At 30 June 2013       | 4,116               | 4,099                                          | 8,215           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| At 1 July 2013        | 4,116               | 4,099                                          | 8,215           |
| Additions             | 1,328               | -                                              | 1,328           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| At 30 June 2014       | 5,444               | 4,099                                          | 9,543           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| <b>DEPRECIATION</b>   |                     |                                                |                 |
| At 1 July 2012        | 3,617               | 2,008                                          | 5,625           |
| Charge for the year   | 202                 | 513                                            | 715             |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| At 30 June 2013       | 3,819               | 2,521                                          | 6,340           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| At 1 July 2013        | 3,819               | 2,521                                          | 6,340           |
| Charge for the year   | 509                 | 513                                            | 1,022           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| At 30 June 2014       | 4,328               | 3,034                                          | 7,362           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| <b>NET BOOK VALUE</b> |                     |                                                |                 |
| 30 June 2014          | 1,116               | 1,065                                          | 2,181           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |
| 30 June 2013          | 297                 | 1,578                                          | 1,875           |
|                       | <hr/>               | <hr/>                                          | <hr/>           |

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

|                                               | 2014<br>Sh'000 | 2013<br>Sh'000 |
|-----------------------------------------------|----------------|----------------|
| 13 COMPUTER SOFTWARE                          |                |                |
| COST                                          |                |                |
| At the beginning and end of the year          | 10,000         | 10,000         |
| AMORTISATION                                  |                |                |
| At the beginning and end of the year          | 10,000         | 10,000         |
| NET BOOK VALUE                                | -              | -              |
| 14 RECEIVABLES AND PREPAYMENTS                |                |                |
| Rent receivable                               | 60,449         | 63,038         |
| Receivables arising from disposal of property | 434,080        | 452,500        |
| Other receivables                             | 110,696        | 116,695        |
| Provision for doubtful receivables            | (125,384)      | -              |
|                                               | 479,841        | 632,233        |

Other receivables relate to amounts due from the former Ministry of Local Government, Kenya Power and Lighting Company Limited amounting to Sh 105,000,000, prepayments of Sh 5,000,000 as well as pension recoveries from pensioners for under-deductions amounting to Sh 696,000. The amount due from the former Ministry of Local Government is still outstanding due the restructuring of ministries under the new constitution making it difficult to establish which ministry should settle the debt. The amount has provided for on the basis that it might take long to recover as a specific budgetary allocation is required in the new ministry.

Receivables arising from disposal of investment property relate to amounts due from Chinook Limited, to whom Valley Road - Scruby Court & Sudbrook Court was sold and Kenya Power and Lighting Limited to whom Makongeni (L.R. No. 209/6829-part) was sold.

|                                 | 2014<br>Sh'000 | 2013<br>Sh'000 |
|---------------------------------|----------------|----------------|
| 15 FIXED DEPOSITS               |                |                |
| Held to maturity                |                |                |
| Maturing within 90 days:        |                |                |
| Housing Finance Company Limited | -              | 930            |
| NIC Bank Limited                | 845            | -              |
| Equity Bank Limited             | 113,245        | -              |
|                                 | 114,090        | 93,945         |

The weighted average effective interest rate during the year on the short term deposits held at 30 June 2014 was 8.8% (2013: 16.78 %).

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 16 QUOTED EQUITY INVESTMENTS

At fair value through profit or loss

|                                      | Number of Shares           |                                |                    |  | Disposal<br>Units | At 30 June<br>2014<br>Units | Market value<br>at 1 Jul 2013<br>Sh' 000 | Disposal<br>Sh' 000 | Gain on<br>disposal<br>Sh' 000 | Market<br>gain/(loss)<br>Sh' 000 | Market value<br>at 30 June<br>2014<br>Sh' 000 |
|--------------------------------------|----------------------------|--------------------------------|--------------------|--|-------------------|-----------------------------|------------------------------------------|---------------------|--------------------------------|----------------------------------|-----------------------------------------------|
|                                      | At 1 July<br>2013<br>Units | Additions<br>/bonuses<br>Units | Disposals<br>Units |  |                   |                             |                                          |                     |                                |                                  |                                               |
| BANKING & FINANCE                    |                            |                                |                    |  |                   |                             |                                          |                     |                                |                                  |                                               |
| Centum Investment Company<br>Limited | 69                         | -                              | 69                 |  | -                 | 1,501                       | 2,196                                    | 695                 | -                              | -                                | -                                             |
|                                      |                            |                                |                    |  |                   | 1,501                       | 2,196                                    | 695                 | -                              | -                                | -                                             |

Market values for quoted equity investments are determined by reference to the Nairobi Securities Exchange prices at close of business at year end.



**KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**

**17 PAYABLES**

|                               | 2014<br>Sh'000   | 2013<br>Sh'000   |
|-------------------------------|------------------|------------------|
| Benefits payable              | 510,145          | 815,623          |
| Deposits                      | 49,535           | 33,004           |
| Accruals and other payables   | 569,879          | 248,746          |
| Leave provision               | 1,392            | 1,974            |
| RBA levy payable              | 12,500           | 25,000           |
| Penalties on RBA levy payable | 22,000           | 31,500           |
|                               | <u>1,165,451</u> | <u>1,155,847</u> |

Accruals and other payables includes amounts due to Flexus Estate amounting to Sh 21,250,000 that relates to a deposit they made with respect to the sale of Mobray Court (L.R. No. 1/437 – Kindaruma Road) that never materialised since the property has a court injunction against disposal of the mentioned properties as per HCCC No 294 of 2012, Erdemann Property Limited vs KRSRBS & Another.

**18 BORROWINGS (Secured)**

|                                        | 2014<br>Sh'000 | 2013<br>Sh'000 |
|----------------------------------------|----------------|----------------|
| Analysis of changes in bank borrowings |                |                |
| Opening balance                        | 56,518         | 127,918        |
| Repayment                              | (56,518)       | (71,400)       |
| Additions                              | 225,000        | -              |
|                                        | <u>225,000</u> | <u>56,518</u>  |
| At 31 December                         | 225,000        | 56,518         |
| Maturity analysis                      |                |                |
| Repayable within 12 months             | 225,000        | 56,518         |

The loan is from Kenya Commercial Bank Limited and is secured by legal charge over L.R. No. 209/6506 Matumbato, Upperhill, Nairobi.

The effective interest rate on loan on 30 June 2014 was 21.71 % (2013 – 18.70%)

**KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**

|                                                    | 2014<br>Sh'000    | 2013<br>Sh'000    |
|----------------------------------------------------|-------------------|-------------------|
| <b>19 FUND BALANCE</b>                             |                   |                   |
| Opening fund balance                               | 20,164,919        | 20,327,431        |
| Net increase/(decrease) in net assets for the year | 1,086,424         | (162,512)         |
|                                                    | <u>21,251,343</u> | <u>20,164,919</u> |
| Fund balance at the end of the year                | <u>21,251,343</u> | <u>20,164,919</u> |

**20 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.

|                              | 2014<br>Sh'000 | 2013<br>Sh'000 |
|------------------------------|----------------|----------------|
| Key management remuneration: |                |                |
| Salaries and other benefits  | 12,751         | 14,569         |
|                              | <u>12,751</u>  | <u>14,569</u>  |

The following transactions and balances were held with the scheme sponsor, Kenya Railways Corporation Limited:

|                 | 2014<br>Sh'000 | 2013<br>Sh'000 |
|-----------------|----------------|----------------|
| Rent receivable | 22,525         | 6,674          |
|                 | <u>22,525</u>  | <u>6,674</u>   |

**21 FINANCIAL RISK MANAGEMENT**

The sponsor, Kenya Railways Corporation, transferred investment property to the scheme to cover the liabilities of the scheme at its inception.

The schemes main source of revenue is therefore rental income from the investment properties as well as proceeds from the disposal of property. The scheme also generates revenues by investing in various income generating activities which involve trading in the stock exchange, government and other securities. These activities expose the fund to a variety of financial risks, including credit risk and the effects of changes in debt and equity market prices, foreign and interest rates. The scheme's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on its financial performance.

Risk management is carried out by the corporate trustee together with the investment manager under policies approved by the corporate trustee. The investment manager reviews the market trends and information available to evaluate the potential exposures. They then arrive at strategies to mitigate against market risks. The corporate trustee provides principles for overall risk management, as well as policies covering specific areas such as foreign exchange risk, interest rate risk, credit risk, use of derivative and non-derivative financial instruments and investing excess liquidity. The scheme also follows guidelines issued by the Retirements Benefits authority in respect of maximum investment in different types of investments.

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 21 FINANCIAL RISK MANAGEMENT (Continued)

#### A Market risk

##### (i) Foreign exchange risk

The scheme does not hold any off shore investment or investments denominated in foreign currencies, thus it's not exposed to foreign exchange risk.

##### (ii) Price risk

The scheme's exposure to equity securities price risk is insignificant.

As at 30 June 2014, if the market price of investment property were to appreciate/depreciate by 5% with all other variables held constant, the impact on return on investment the year would have been higher by Sh 1,161,970 (2013- Sh 1,036,000).

##### (iii) Interest rate risk

The scheme's interest bearing assets are investments in fixed deposits. All of these instruments are at fixed interest rates.

The nature of financial instruments held, that is, fixed interest instruments mitigates risk exposure of the scheme. Fluctuations in interest rates will have an insignificant effect on the scheme.

#### B Credit risk

Credit risk refers to the risk that counterparty will default on its contractual obligations resulting in financial loss to the company.

Credit risk arises from bank balances, fixed deposits, interest bearing investments, deposits with banks, and receivables. As part of the credit risk management system, the Investment Manager and the Corporate Trustee monitor and review information on significant investment.

The amount that best represents the scheme's maximum exposure to credit risk at 30 June is made up as follows:

|                           | Fully performing<br>Sh'000 | Past due<br>Sh'000 | Impaired<br>Sh'000 | Total<br>Sh'000 |
|---------------------------|----------------------------|--------------------|--------------------|-----------------|
| <b>30 June 2014</b>       |                            |                    |                    |                 |
| Receivables               | 439,080                    | 166,144            | (125,384)          | 479,841         |
| Bank balances             | 6,288                      | -                  | -                  | 6,288           |
| Fixed deposits            | 114,090                    | -                  | -                  | 114,090         |
|                           | <u>559,458</u>             | <u>166,144</u>     | <u>(125,384)</u>   | <u>600,218</u>  |
| <b>30 June 2013</b>       |                            |                    |                    |                 |
| Receivables               | 36,619                     | 595,614            | -                  | 632,233         |
| Bank balances             | 30,121                     | -                  | -                  | 30,121          |
| Fixed deposits            | 930                        | -                  | -                  | 930             |
| Quoted equity investments | 2                          | -                  | -                  | 2               |
|                           | <u>67,672</u>              | <u>595,614</u>     | <u>-</u>           | <u>663,286</u>  |

Bank balances and fixed deposits are held with reputable financial institutions that have high credit ratings.



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 21 FINANCIAL RISK MANAGEMENT (Continued)

#### C Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. The scheme is required to make periodic payment in respect of pensions to members and is therefore exposed to the risk of difficulty in raising funds to make such payments. It therefore invests a portion of its assets in investments that are readily convertible to cash. More than 97% of the scheme's portfolio is made up investment property which is not readily liquid. The corporate trustee has however made plans to dispose some of the investment property as well as improve rent collections on its existing properties in order to increase the schemes liquidity. Disposal of the some of the property is a viable option for raising liquidity as the schemes portfolio comprises of prime property.

The table below analyses the scheme's financial liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table below are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of discounting is not significant.

|                              | Less than<br>1 month<br>Shs'000 | Between<br>1 – 3 months<br>Shs'000 | Over<br>3 months<br>Shs'000 | Total<br>Shs'000 |
|------------------------------|---------------------------------|------------------------------------|-----------------------------|------------------|
| <b>At 30 June 2014</b>       |                                 |                                    |                             |                  |
| Benefits payable             | 45,233                          | 167,661                            | 297,251                     | 510,145          |
| Creditors and other payables | 145,011                         | 234,164                            | 276,131                     | 655,306          |
| Borrowings                   | -                               | -                                  | 225,000                     | 225,000          |
|                              | <u>190,244</u>                  | <u>401,825</u>                     | <u>798,382</u>              | <u>1,390,451</u> |
| <b>At 30 June 2013</b>       |                                 |                                    |                             |                  |
| Benefits payable             | 53,705                          | 68,503                             | 693,415                     | 815,623          |
| Creditors and other payables | 41,928                          | 26,871                             | -                           | 68,799           |
| Borrowings                   | -                               | -                                  | 56,518                      | 56,518           |
|                              | <u>95,633</u>                   | <u>95,374</u>                      | <u>749,933</u>              | <u>940,940</u>   |
|                              |                                 |                                    | 2014<br>Sh'000              | 2013<br>Sh'000   |

### 22 CAPITAL COMMITMENTS

Authorised but not contracted for

# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

|                                                                                                                                                               | 2014<br>Sh'000    | 2013<br>Sh'000 |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|----------------|
| <b>23 OPERATING LEASE RECEIVABLE</b>                                                                                                                          |                   |                |
| Amounts receivable in respect of obligations under operating leases                                                                                           |                   |                |
| Within one year                                                                                                                                               | 60,329            | 60,329         |
| Between two and five years                                                                                                                                    | 114,718           | 175,047        |
| After five years                                                                                                                                              | -                 | -              |
|                                                                                                                                                               | <u>175,047</u>    | <u>235,376</u> |
| <b>24 CONTINGENT LIABILITIES</b>                                                                                                                              |                   |                |
| Legal suits                                                                                                                                                   | -                 | -              |
| Currently, there are injunctive orders against disposal of the scheme's properties as per HCCC No 294 of 2012, Erdemann Property Limited vs KRSRBS & Another. |                   |                |
| <b>25 ACTUARIAL VALUATION AND STATEMENT</b>                                                                                                                   |                   |                |
| The Scheme operates on a defined benefits basis and its assets are held in funds managed by an independent investment manager.                                |                   |                |
| The Scheme is subjected to a triennial valuation by independent actuaries to fulfil the statutory requirements under the Retirement Benefits Act.             |                   |                |
| The last actuarial valuation was carried out by Alexander Forbes Financial Services Limited as at 30 June 2011.                                               |                   |                |
| The results of the valuation are summarised below:                                                                                                            | Sh'000            |                |
| Value placed on scheme assets                                                                                                                                 | 16,771,800        |                |
| Value of:                                                                                                                                                     |                   |                |
| Future benefits to current pensioners<br>(Including dependants in receipt of pension)                                                                         | 6,841,900         |                |
| Past service pension benefits for active members (deferred pensioners)<br>based on projected earnings                                                         | 3,780,500         |                |
| Cost of pension increases                                                                                                                                     | 1,145,400         |                |
| Pension increase arrears                                                                                                                                      | 473,100           |                |
|                                                                                                                                                               | <u>12,240,900</u> |                |
| Actuarial surplus                                                                                                                                             | <u>4,530,900</u>  |                |
| Funding level (ratio of scheme assets to accrued past service liabilities)                                                                                    |                   | <u>137%</u>    |



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 25 ACTUARIAL VALUATION AND STATEMENT (Continued)

The Retirement Benefits Rules and Regulations 2000, require all funds in Kenya to satisfy a minimum funding requirement of 100% of the fund's accrued liabilities. The funding level disclosed for the Scheme at 137.1% at this valuation was above the minimum funding requirement.

The above actuarial valuation does not include members who have not returned their pension census forms and it is expected that the valuation will change when the members who have been left out are included. The corporate trustee does not expect a significant change in the scheme's liabilities when suspended members are included in the actuarial valuation. As at the end of the reporting period, 468 members (2013: 492 members) had not returned their pension census forms.

Alexander Forbes resigned as actuaries in June 2011.

### 26 FAIR VALUE OF NON-FINANCIAL ASSETS

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the scheme takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date.

The investment properties were revalued by Knight Frank Limited registered valuers on 30 June 2011. Since then, only three properties: Goods Shed Area, Nairobi; Matumbato, Upperhill (L.R. No. 209/6505) and Chambilo, Mombasa have been revalued in 2014. This is not consistent with International Accounting Standard No 40, Investment Property which requires investment property carried at fair value to be revalued at the end of each reporting period. The investment property values are based on the forced sale value obtained during this valuation.

IFRS 13 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the fund's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchanges.
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).
- Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components. This hierarchy requires the use of observable market data when available. The scheme considers relevant and observable market prices in its valuations where possible.

The following table shows an analysis of investment property recorded at fair value by level of the fair value hierarchy:

|                           | Level 1<br>Shs '000' | Level 2<br>Shs '000' | Level 3<br>Shs '000' | Total<br>Shs '000' |
|---------------------------|----------------------|----------------------|----------------------|--------------------|
| <b>At 30 June 2014</b>    |                      |                      |                      |                    |
| Total investment property | -                    | 23,239,394           | -                    | 23,239,394         |
| <b>At 30 June 2013</b>    |                      |                      |                      |                    |
| Total investment property | -                    | 20,712,123           | -                    | 20,712,123         |



# KENYA RAILWAYS STAFF RETIREMENT BENEFITS SCHEME

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 27 REGISTRATION

The scheme is registered in Kenya under the Retirement Benefits Act.

### 28 CURRENCY

The financial statements are presented in Kenya Shillings rounded to the nearest thousands (Sh'000) which is also the functional currency.