# Wethaq Takaful Insurance Company K.S.C. (Closed)

**FINANCIAL STATEMENTS**

**31 DECEMBER 2005**

# STATEMENT OF INCOME

Year ended 31 December 2005

| | Notes | ***2005 KD*** | *2004 KD* |
|---|---|---|---|
| Net investment income | 3 | **1,006,883** | 837,188 |
| Shareholders' share of insurance surplus | 9 | **361,018** | 266,071 |
| Murabaha profit | | **71,052** | 145,912 |
| Write back of provision no longer required | | **-** | 75,000 |
| **INCOME** | | **1,438,953** | 1,324,171 |
| Allowances and other benefits | | **77,000** | 77,140 |
| General and administration expenses | | **6,526** | 33,069 |
| **EXPENSES** | | **83,526** | 110,209 |
| **PROFIT BEFORE CONTRIBUTION TO KUWAIT FOUNDATION FOR THE ADVANCEMENT OF SCIENCES (KFAS), DIRECTORS' FEES AND NATIONAL LABOUR SUPPORT TAX** | | **1,355,427** | 1,213,962 |
| Contribution to KFAS | | **(12,199)** | (10,709) |
| Directors' fees | 4 | **(60,000)** | (50,000) |
| National Labour Support tax (NLST) | | **(28,692)** | (24,888) |
| **PROFIT FOR THE YEAR** | | **1,254,536** | 1,128,365 |
| **EARNINGS PER SHARE** | 5 | **23 fils** | 21 fils |

The attached notes 1 to 19 form part of these financial statements.

# BALANCE SHEET

At 31 December 2005

| | Notes | *2005* *KD* | *2004* *KD* |
|---|---|---|---|
| **ASSETS** | | | |
| Bank balances and cash | | **56,381** | - |
| Investments at fair value through the statement of income | 6 | **2,331,765** | 1,797,994 |
| Investments available for sale | 7 | **5,845,726** | 3,137,206 |
| Murabaha receivables | 8 | **534,018** | 1,835,608 |
| Amount due from investment manager | | **-** | 25,310 |
| Due from policyholders | 9 | **579,867** | 415,363 |
| Other assets | | **3,645** | - |
| **TOTAL ASSETS** | | **9,351,402** | 7,211,481 |
| **EQUITY AND LIABILITIES** | | | |
| **Capital and reserves** | | | |
| Share capital | 10 | **5,512,500** | 5,250,000 |
| Share premium | 11 | **312,500** | 312,500 |
| Statutory reserve | 12 | **308,359** | 172,816 |
| Voluntary reserve | 13 | **308,359** | 172,816 |
| Cumulative changes in fair values | | **1,471,586** | 139,891 |
| Retained earnings | | **1,205,438** | 1,009,488 |
| **Total equity** | | **9,118,742** | 7,057,511 |
| **Liabilities** | | | |
| Other liabilities | | **232,660** | 153,970 |
| **Total liabilities** | | **232,660** | 153,970 |
| **TOTAL EQUITY AND LIABILITIES** | | **9,351,402** | 7,211,481 |

Abdulla Yousef Al-Saif
Chairman

Nabil Ahmed Amin
Vice Chairman

The attached notes 1 to 19 form part of these financial statements.

# STATEMENT OF CASH FLOWS
Year ended 31 December 2005

| | ***2005*** | *2004* |
|---|---|---|
| | ***KD*** | *KD* |
| **OPERATING ACTIVITIES** | | |
| Profit for the year | **1,254,,536** | 1,128,365 |
| Adjustments for: | | |
| Net investment income | **(1,006,883)** | (837,188) |
| Murabaha profit | **(71,052)** | (145,912) |
| Shareholders' share of insurance surplus | **(361,018)** | (266,071) |
| Write back of provision no longer required | **-** | (75,000) |
| | **(184,417)** | (195,806) |
| Changes in operating assets and liabilities: | | |
| Other assets | **(3,645)** | **-** |
| Other liabilities | **78,690** | 78,438 |
| Net cash used in operating activities | **(109,372)** | (117,368) |
| **INVESTING ACTIVITIES** | | |
| Proceeds from sale of managed portfolio | **-** | 448,908 |
| Net movements in murabaha receivables | **1,301,590** | 93,655 |
| Net sale (purchase) of investments at fair value through statement of income | **331,852** | (329,029) |
| Purchase of investments available for sale | **(1,376,825)** | (974,085) |
| Murabaha profit received | **71,052** | 145,912 |
| Profit received on investment deposit | **-** | 9,945 |
| Dividends received | **141,260** | 83,332 |
| Amount received from investment manager | **25,310** | 616,690 |
| Net cash from investing activities | **494,239** | 95,328 |
| **FINANCING ACTIVITIES** | | |
| Issuance of share capital | **-** | 562,500 |
| Net movement in policyholders' account | **196,514** | (240,460) |
| Dividend paid | **(525,000)** | (300,000) |
| Net cash (used in) from financing activities | **(328,486)** | 22,040 |
| **INCREASE IN BANK BALANCES AND CASH** | **56,381** | **-** |
| **BANK BALANCES AND CASH AT THE END OF THE YEAR** | **56,381** | - |

The attached notes 1 to 19 form part of these financial statements.

# STATEMENT OF CHANGES IN EQUITY
Year ended 31 December 2005

| | *Share capital KD* | *Share premium KD* | *Statutory reserve KD* | *Voluntary reserve KD* | *Cumulative changes in fair values KD* | *Retained earnings KD* | *Total equity KD* |
|---|---|---|---|---|---|---|---|
| At 1 January 2004 | 5,000,000 | - | 53,832 | 53,832 | 271,538 | 419,091 | 5,798,293 |
| Investments available for sale: | | | | | | | |
| Valuation gain taken to equity | - | - | - | - | 18,909 | - | 18,909 |
| Amount recycled to statement of income | - | - | - | - | (150,556) | - | (150,556) |
| Net expenses recognised directly in equity | - | - | - | - | (131,647) | - | (131,647) |
| Profit for the year | - | - | - | - | - | 1,128,365 | 1,128,365 |
| Total recognised income for the year | - | | | | (131,647) | 1,128,365 | 996,718 |
| Issuance of share capital | 250,000 | 312,500 | - | - | - | - | 562,500 |
| Dividend for 2003 | - | - | - | - | - | (300,000) | (300,000) |
| Transfer to reserves | - | - | 118,984 | 118,984 | - | (237,968) | - |
| At 31 December 2004 | 5,250,000 | 312,500 | 172,816 | 172,816 | 139,891 | 1,009,488 | 7,057,511 |
| At 1 January 2005 | 5,250,000 | 312,500 | 172,816 | 172,816 | 139,891 | 1,009,488 | 7,057,511 |
| Investments available for sale: | | | | | | | |
| Valuation gain taken to equity | - | - | - | - | 1,331,695 | - | 1,331,695 |
| Net income recognised directly in equity | - | - | - | - | 1,331,695 | - | 1,331,695 |
| Profit for the year | - | - | - | - | - | 1,254,536 | 1,254,536 |
| Total recognised income for the year | - | - | - | - | 1,331,695 | 1,254,536 | 2,586,231 |
| Issuance of bonus shares (Note 15) | 262,500 | - | - | - | - | (262,500) | - |
| Dividend for 2004 (Note 15) | - | - | - | - | - | (525,000) | (525,000) |
| Transfer to reserves | - | - | 135,543 | 135,543 | - | (271,086) | - |
| **At 31 December 2005** | **5,512,500** | **312,500** | **308,359** | **308,359** | **1,471,586** | **1,205,438** | **9,118,742** |

The attached notes 1 to 19 form part of these financial statements.

## 1 ACTIVITIES

The financial statements of Wethaq Takaful Insurance Company K.S.C. (Closed) (the company) for the year ended 31 December 2005 were authorised for issue in accordance with a resolution of the Board of Directors on 21 February 2006 and are issued subject to the approval of the Ordinary Annual General Assembly of the shareholders.

The company is a Kuwaiti Shareholding Company incorporated on 2 October 2000 and is registered under the Insurance Companies and Agents Law No. 24 of 1961 and its subsequent amendments. It is engaged in transacting co-operative insurance operations and all related activities, including reinsurance.

Takaful is an Islamic alternative to a conventional insurance and investment program, based on the mutual funds concept, where each policyholder will receive his share in the surplus arising from the insurance activities, in accordance with the company's articles of association and the approval of Fatwa and Shareea'a Supervisory Board.

The company conducts business on behalf of the policyholders and advances funds to the policyholders' operations as and when required. The shareholders are responsible for liabilities incurred by policyholders in the event the policyholders' fund is in deficit and the operations are liquidated. The company holds the physical custody and title of all assets related to the policyholders' and shareholders' operations, however, policyholders' assets and liabilities do not form part of the primary financial statements. Such assets and liabilities together with the results of policyholders' lines of business are disclosed in the notes.

Wethaq Takaful Insurance Company K.S.C. (Closed) maintains separate books of accounts for policyholders and shareholders. Income and expenses clearly attributable to either activity are recorded in the respective accounts. Management and the board of directors determine the basis of allocation of expenses from joint operations.

The company's registered head office is at P. O. Box 371, Safat 13004, Kuwait.

## 2 SIGNIFICANT ACCOUNTING POLICIES

**Basis of preparation:**
The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and applicable requirements of Ministerial Order No. 18 of 1990.

The financial statements are prepared under the historical cost convention modified to include the measurement at fair value of investments at fair value through statement of income and investments available for sale.

The financial statements are presented in Kuwaiti Dinars.

The accounting policies used in the preparation of these financial statements are consistent with those used in the previous year, with the exception of the following policies which have been revised due to certain IFRS's that became mandatory for financial years beginning on or after 1 January 2005. The principal effects are discussed below:

**IAS 32: "Financial Instruments: Disclosure and Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement".**

*Classification*
The Company has designated "trading investments" as "investments at fair value through statement of income".

*Impairment of investments available for sale*
In the case of available for sale equity investments reversal of previously recognised losses are no longer recognised in the statement of income but as increase in cumulative changes in fair values. There is no impact on the statement of income for the comparative year ended 31 December 2004 or on retained earnings at 1 January 2004 as there were no such reversals in the prior year.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

*Transition adjustment*
The adoption of the revised IAS 39 has not resulted in any adjustment of the previously reported amounts. The carrying amount of held for trading investments reclassified as “investments carried at fair value through statement of income” as at 1 January 2004 were KD 968,962.

*Derecognition of financial assets*
With effect from 1 January 2005 a financial asset (in whole or in part) is derecognised when the contractual rights to cash flows from the financial asset expire, the Company has transferred substantially all the risks and rewards of ownership or when it has neither transferred nor retained substantially all the risks and rewards and when it no longer has control over the asset or a proportion of the asset.

**Revenue recognition**
Income from murabaha and investment deposits is recognised on a time apportionment basis. Dividend income is recognised when the right to receive payment is established.

Shareholders’ share of insurance surplus is determined based on the company’s bye-laws and Takaful practices and is recognised in the income statement upon approval by the board of directors.

**Investments**
These are classified as follows:

- Investments at fair value through statement of income
- Investments available for sale

All investments are initially recognised at fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial instrument except for investments at fair value through statement of income. Transaction costs in the case of investments at fair value through statement of income are recognised in the statement of income immediately.

*Investments at fair value through statement of income*
Investments are classified as investments at fair value through statement of income if the fair value of the investment can be reliably measured and the management designates them as investments at fair value through statement of income. After initial recognition investments at fair value through statement of income are carried at fair value with all changes in fair value recognised in the statement of income.

*Investments available for sale*
After initial recognition investments available for sale are carried at fair value. All changes in the fair value are recognised in separate component of equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment the cumulative gain or loss previously reported as “cumulative changes in fair values” within equity is recognised in the statement of income. Investments whose fair value cannot be reliably measured are carried at cost less impairment losses, if any.

**Fair value**
For investments quoted in an active market, fair value is determined with reference to quoted bid prices. Bid prices are used for assets and offer prices are used for liabilities. The fair value of investments in funds, or similar investment vehicles are based on the last published bid price. The fair value of profit-bearing items is estimated based on discounted cash flows using profit for items with similar terms and risk characteristics. For unquoted equity investments, fair value is determined with reference to the market value of a similar investment or is based on the expected discounted cash flows.

***Derecognition***
A financial asset (in whole or in part) is derecognised when the contractual rights to cash flows from the financial asset expire, the Company has transferred substantially all the risks and rewards of ownership or, when it has neither transferred or retained substantially all the risks and rewards, and when it no longer has control over the asset or a proportion of the asset. A financial liability is derecognized when the obligation specified in the contract is discharged, cancelled or expired.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Murabaha receivables**
Investments in murabaha are stated on the balance sheet at amounts due on maturity less that portion of the profit, which is attributable to the period after the balance sheet date.

**Impairment and uncollectibility of financial assets**
An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, any impairment loss is recognised in the statement of income.

Impairment is determined as follows:

a) For assets carried at fair value, impairment is the difference between cost and fair value;
b) For assets carried at cost, impairment is the difference between cost and the present value of future cash flows discounted at the original rate of return for a similar financial asset.

Reversal of impairment losses recognised in prior years is recorded when there is an indication that the impairment losses recognised for the financial asset no longer exist or have decreased. The reversal of impairment losses are recognised in the statement of income except for available for sale equity investments which are recognized in the cumulative changes in fair values.

**Payables**
Liabilities are recognised for amounts to be paid in the future for goods or services received, whether billed by the supplier or not.

**Foreign currencies**
Foreign currency transactions are recorded in Kuwaiti Dinars at the approximate rates of exchange prevailing on the date of the transactions. Monetary assets and liabilities denominated in foreign currency at the balance sheet date are translated to Kuwaiti Dinars at the rates of exchange prevailing on that date. Any resultant gains or losses are recognised in the statement of income. Non-monetary assets denominated in foreign currencies that are stated at fair value are translated to Kuwaiti Dinars at the foreign exchange rates prevailing at the dates that values were determined. Any resultant gain or loss on non-monetary investments at fair value through statement of income are recognised in the statement of income and on non-monetary investments available for sale are recognised directly in equity.

**Estimation uncertainty**
The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

*Valuation of unquoted equity investments*
Valuation of unquoted equity investments is normally based on one of the following:
- recent arm’s length market transactions;
- current fair value of another instrument that is substantially the same;
- the expected cash flows discounted at current rates applicable for items with similar terms and risk characteristics; or
- other valuation models.

**Judgements**
In the process of applying the company’s accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect in the amounts recognised in the financial statements.

## 2 SIGNIFICANT ACCOUNTING POLICIES (continued)

*Classification of investments*
Management has to decide on acquisition of an investment whether it should be classified as available for sale or investments carried at fair value through statement of income.

*Impairment of investments*
The company treats available for sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgement. In addition the company evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the discount factors for unquoted equities.

The significant accounting policies used in accounting for insurance business are set out in Note 14.

## 3 NET INVESTMENT INCOME

| | ***2005*** ***KD*** | *2004* *KD* |
|---|---|---|
| Dividend income | **131,260** | 83,332 |
| Realised and unrealised gain on investments at fair value through statement of income | **865,623** | 500,003 |
| Realised gain on investments available for sale | **-** | 243,908 |
| Others | **10,000** | 9,945 |
| | **1,006,883** | 837,188 |

## 4 DIRECTORS' FEES

Directors' fees are subject to the approval of the Shareholders' General Assembly.

## 5 EARNINGS PER SHARE

Earnings per share is computed on the basis of profit for the year and the weighted average number of shares outstanding during the year as follows:

| | ***2005*** | *2004* |
|---|---|---|
| Profit for the year (KD) | **1,254,536** | 1,128,365 |
| Weighted average number of shares outstanding | **55,125,000** | 53,549,658 |
| Earnings per share (fils) | **23** | 21 |

Earnings per share for 2004 have been restated for the bonus shares issued in 2005 (Note 15).

## 6 INVESTMENTS AT FAIR VALUE THROUGH STATEMENT OF INCOME

Investments at fair value through statement of income consist of managed portfolios with underlying investments in marketable securities.

## 7 INVESTMENTS AVAILABLE-FOR-SALE

| | *2005* | *2004* |
|---|---|---|
| | ***KD*** | *KD* |
| Quoted securities | **2,107,682** | - |
| Unquoted securities | **1,520,679** | 1,315,335 |
| Managed funds | **2,217,365** | 1,821,871 |
| | **5,845,726** | 3,137,206 |

The investment in unquoted securities is carried at cost due to the unpredictable nature of future cash flows and lack of suitable other methods for arriving at a reliable measure of fair value. Management is not aware of any circumstances that would indicate any impairment in the value of these investments at the balance sheet date.

## 8 MURABAHA RECEIVABLES

Murabaha receivables represent short-term receivables resulting from participations in murabaha deals. The maximum maturity of such participations is twelve months from date of origination of the deal.

Average profit rate attributable to deals during the year was 6.3% (2004: 5.8%) per annum.

## 9 DUE FROM POLICYHOLDERS

| | ***2005*** | *2004* |
|---|---|---|
| | ***KD*** | *KD* |
| At 1 January | **415,363** | (91,168) |
| Shareholders' share of insurance surplus (Note 14) | **361,018** | 266,071 |
| Other movement in funds advanced to policyholders | **(196,514)** | 240,460 |
| | **579,867** | 415,363 |

Shareholders' share of insurance surplus comprises 50% of the net surplus from insurance operations. Net surplus from insurance operations is shared equally between the shareholders and policyholders as stipulated in Article (48) of the company's bye-laws and is subject to the approval of the Shareholders' General Assembly.

## 10 SHARE CAPITAL

| | *Authorised, issued and fully paid* | |
|---|---|---|
| | ***2005*** | *2004* |
| | ***KD*** | *KD* |
| Shares of 100 fils each | **5,512,500** | 5,250,000 |

## 11 SHARE PREMIUM

The share premium account is not available for distribution.

## 12 STATUTORY RESERVE

In accordance with the Law of Commercial Companies and the company's articles of association, 10% of the profit for the year before contribution to KFAS, NLST and directors fees is transferred to statutory reserve. The company may resolve to discontinue such transfers when the reserve equals 50% of paid up share capital.

Distribution of the reserve is limited to the amount required to enable the payment of a dividend of 5% of paid up share capital to be made in years when accumulated profits are not sufficient for the payment of a dividend of that amount.

## 13 VOLUNTARY RESERVE

In accordance with the company's articles of association, 10% of the profit for the year before contribution to KFAS, NLST and directors fees has been transferred to the voluntary reserve. The reserve is freely distributable.

## 14 POLICYHOLDERS' RESULT BY LINE OF BUSINESS AND FUND

The significant accounting policies used in accounting for the insurance business are set out below. Policies used in accounting for other accounts and transactions are the same as those adopted by the company. The accounting policies are consistent with those used in the previous year, with the exception of IFRS 4 which has become mandatory for financial years beginning on or after 1 January 2005. The adoption of IFRS 4 has affected disclosures with respect to insurance contracts issued and reinsurance contracts held. All comparative disclosures have been amended accordingly.

**Revenue recognition**
*Premium earned*
Premiums are taken into income over the terms of the policies to which they relate on a pro-rata basis. Unearned premium represent the portion of net premium written relating to the unexpired period of coverage.

*Policy issuance fees and policy acquisition cost*
Policy issuance fees and policy acquisition cost are recognised at the time of recognition of the related premium.

**Reinsurance**
In the normal course of business, the Company cedes and assumes certain levels of risk in various areas of exposure with other insurance companies or reinsurers. Such reinsurance includes quota share, excess of loss, facultative and other forms of reinsurance on essentially all lines of business.

**Claims**
Claims, comprising amounts payable to contract holders and third parties and related loss adjustment expenses, net of salvage and other recoveries, are recognised in the statement of income as incurred.

**Liability adequacy test**
At each balance sheet date, the Company assesses whether its recognised insurance liabilities are adequate using current estimates of future cash flows under its insurance contracts. If that assessment shows that the carrying amount of its insurance liabilities (less related deferred policy acquisition costs) is inadequate in the light of estimated future cash flows, the entire deficiency is immediately recognised in income and an unexpired risk provision created.

**Receivables**
Accounts receivable are carried at amortised cost less impairment losses, if any.

**14 POLICYHOLDERS' RESULT BY LINE OF BUSINESS AND FUND (continued)**

**Outstanding claims reserve**
Outstanding claims comprise the estimated cost of claims incurred and reported but not settled at the balance sheet date. Provisions for reported claims not paid as at the balance sheet date are made on the basis of individual case estimates.

Any difference between the provisions at the balance sheet date and settlements and provisions in the following year is included in the surplus of insurance operations for that year.

**Reserve for claims incurred but not reported (IBNR)**
The reserve for claims incurred but not reported includes amounts reserved for claims incurred but not reported at the balance sheet date in addition to other contingencies and any differences that may arise. Provision based on management's judgement and the company's prior experience is maintained for the cost of settling claims incurred but not reported at the balance sheet date.

**Estimation uncertainty**
The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

*Provision for outstanding claims and IBNR*
Considerable judgement by management is required in the estimation of amounts due to contract holders arising from claims made under insurance contracts. Such estimates are necessarily based on significant assumptions about several factors involving varying, and possible significant, degrees of judgement and uncertainly and actual results may differ from management's estimates resulting in future changes in estimated liabilities. The company generally estimates its claims based on previous experience. Claims requiring court or arbitration decisions are estimated individually. Management reviews its provisions for claims incurred, and claims incurred but not reported, on a quarterly basis.

*Reinsurance*
The company is exposed to disputes with, and possibility of defaults by, its reinsurers. The company monitors on a quarterly basis the evolution of disputes with and the strength of its reinsurers.

**14 POLICYHOLDERS' RESULT BY LINE OF BUSINESS AND FUND (continued)**

**Year ended 31 December 2005**

| | *Marine and Aviation* | *General Accident* | *Fire* | ***Total*** |
|---|---|---|---|---|
| | *KD* | *KD* | *KD* | ***KD*** |
| Premium written | 487,477 | 6,360,486 | 764,010 | **7,611,973** |
| Less: insurance premium ceded to reinsurance | (467,068) | (777,246) | (700,907) | **(1,945,221)** |
| | 20,409 | 5,583,240 | 63,103 | **5,666,752** |
| Movement in unearned premium | (14,981) | (467,801) | (18,943) | **(501,725)** |
| Net premium earned | 5,428 | 5,115,439 | 44,160 | **5,165,027** |
| Policy issuance fees and others | 16,371 | 172,215 | 1,169 | **189,755** |
| Reinsurance commission | 73,841 | 120,515 | 53,913 | **248,269** |
| Total revenues | 95,640 | 5,408,169 | 99,242 | **5,603,051** |
| Claims incurred | 8,160 | 2,845,416 | 9,087 | **2,862,663** |
| Provision for claims incurred but not reported | 19,814 | 707,753 | 25,993 | **753,560** |
| Policy acquisition costs | 10,738 | 187,139 | 42,548 | **240,425** |
| Other insurance expenses | 15,267 | 473,602 | 16,172 | **505,041** |
| Total expenses | 53,979 | 4,213,910 | 93,800 | **4,361,689** |
| Surplus from insurance operations | 41,661 | 1,194,259 | 5,442 | **1,241,362** |
| Allocation of general and administration expenses | (75,674) | (987,379) | (118,603) | **(1,181,656)** |
| Net (deficit) surplus from insurance operations | (34,013) | 206,880 | (113,161) | **59,706** |
| Investment income | 42,416 | 553,436 | 66,478 | **662,330** |
| **Net surplus (deficit) from insurance operations** | **8,403** | **760,316** | **(46,683)** | 722,036 |
| Shareholders' share of insurance surplus (Note 9) | | | | **(361,018)** |
| Insurance surplus transferred to policyholders' fund | | | | **361,018** |

## 14 POLICYHOLDERS' RESULT BY LINE OF BUSINESS AND FUND (continued)

Year ended 31 December 2004

| | *Marine and Aviation* | *General Accident* | *Fire* | *Total* |
|---|---|---|---|---|
| | *KD* | *KD* | *KD* | *KD* |
| Premium written | 297,096 | 5,409,583 | 590,308 | 6,296,987 |
| Less: insurance premium ceded to reinsurance | (268,732) | (821,724) | (572,150) | (1,662,606) |
| | 28,364 | 4,587,859 | 18,158 | 4,634,381 |
| Movement in unearned premium | 1,996 | 629,561 | (720) | 630,837 |
| Net premium earned | 30,360 | 5,217,420 | 17,438 | 5,265,218 |
| Policy issuance fees and others | 2,784 | 235,784 | 1,161 | 239,729 |
| Reinsurance commission | 57,489 | 102,668 | 49,918 | 210,075 |
| Total revenues | 90,633 | 5,555,872 | 68,517 | 5,715,022 |
| Claims incurred | 9,247 | 2,481,141 | 12,233 | 2,502,621 |
| Provision for claims incurred but not reported | 222 | 659,381 | 1,577 | 661,180 |
| Policy acquisition costs | 11,614 | 623,625 | 15,616 | 650,855 |
| Other insurance expenses | 9,201 | 345,387 | 1,144 | 355,732 |
| Total expenses | 30,284 | 4,109,534 | 30,570 | 4,170,388 |
| Surplus from insurance operations | 60,349 | 1,446,338 | 37,947 | 1,544,634 |
| Allocation of general and administration expenses | (40,436) | (736,268) | (80,344) | (857,048) |
| Net (deficit) surplus from insurance operations | 19,913 | 710,070 | (42,397) | 687,586 |
| Investment income | 10,482 | 190,862 | 20,827 | 222,171 |
| **Surplus (deficit) by line of business** | 30,395 | 900,932 | (21,570) | 909,757 |
| Qard Hassan reclaimed by shareholders | (30,395) | (368,790) | 21,570 | (377,615) |
| **Net surplus from insurance operations** | - | 532,142 | - | 532,142 |
| Shareholders' share of insurance surplus (Note 9) | | | | (266,071) |
| Insurance surplus transferred to policyholders' fund | | | | 266,071 |

**14 POLICYHOLDERS' RESULT BY LINE OF BUSINESS AND FUND (continued)**

**POLICYHOLDERS' ASSETS AND LIABILITIES**

| | ***2005 Marine and Aviation, General Accident and Fire KD*** | *2004 Marine and Aviation, General Accident and Fire KD* |
|---|---|---|
| **Assets** | | |
| Bank balances and cash | **841,999** | 566,818 |
| Investment deposits | **1,956,000** | 1,956,000 |
| Investments at fair value through statement of income | **1,713,832** | 320,889 |
| Investments available for sale | **1,670,665** | 550,000 |
| Murabaha receivables | **2,323,057** | 4,690,215 |
| Accounts receivable and prepayments | **611,262** | 697,107 |
| Premium receivable | **1,209,282** | 1,399,480 |
| Reinsurance recoverable on outstanding claims | **779,953** | 657,335 |
| Leasehold land | **277,750** | - |
| Furniture and equipment | **129,627** | 112,059 |
| | **11,513,427** | 10,949,903 |
| **Liabilities** | | |
| Reinsurance balances payable | **755,760** | 1,130,348 |
| Unearned premiums | **2,282,694** | 1,780,970 |
| Outstanding claims reserve | **2,908,523** | 2,190,145 |
| Reserve for claims incurred but not reported | **1,839,061** | 1,085,500 |
| Reserve retained on reinsurance business | **133,601** | 143,832 |
| Premiums received in advance | **1,577,830** | 3,085,178 |
| Due to shareholders | **579,867** | 415,363 |
| Accounts payable and accruals | **846,371** | 852,496 |
| | **10,923,707** | 10,683,832 |
| **Policyholders' fund** | **589,720** | 266,071 |
| | **11,513,427** | 10,949,903 |

**CHANGES IN POLICYHOLDERS' FUND**

| | ***2005 KD*** | *2004 KD* |
|---|---|---|
| At 1 January | **266,071** | (377,615) |
| Qard Hassan reclaimed by shareholders | - | 377,615 |
| Distribution to policyholders for 2004 | **(37,369)** | - |
| Net surplus from insurance operations | **361,018** | 266,071 |
| | **589,720** | 266,071 |

Investment deposits are held in Kuwait as security for the order of the Minister of Commerce and Industry in accordance with the Ministerial Order No. 27 of 1966 and its amendments.

### 14 POLICYHOLDERS' RESULT BY LINE OF BUSINESS AND FUND (continued)

Net surplus from insurance operations is available for distribution to the policyholders upon the approval of the shareholders' Annual General Assembly and the company's Fatwa and Shareea'a Supervisory Board.

### 15 PROPOSED CASH DIVIDEND AND BONUS SHARES

The board of directors has proposed bonus shares of 15% (2004: 5%) and increase in share capital by 85% by way of issue of stock rights to existing shareholder at a premium of 150 fils per share for the year ended 31 December 2005 for approval at the Annual General Meeting of the shareholders. Cash dividend of 10% was paid during the year for 2004.

### 16 RELATED PARTY TRANSACTIONS

These represent transactions made, in the ordinary course of business, with related parties i.e. directors and major shareholders and companies of which they are principal owners. Management approves prices and terms of these transactions.

Transactions with related parties included in the financial statements are as follows:

| | ***2005*** | *2004* |
|---|---|---|
| | ***KD*** | *KD* |
| **Shareholders** | | |
| *Statement of income* | | |
| Murabaha profit | **71,052** | 145,912 |
| *Balance sheet* | | |
| Investments at fair value through statement of income | **2,289,992** | 1,541,720 |
| Murabaha receivables | **534,018** | 1,835,608 |
| Available for sale investments | **2,217,365** | 3,137,206 |
| Amount due from investment manager | **-** | 25,310 |
| *Key management personnel compensation* | | |
| Short-term employee benefits | **53,000** | 53,000 |
| **Policyholders** | | |
| *Statement of income* | | |
| Premium written | **676,992** | 1,610,324 |
| Investment income | **61,097** | 155,857 |
| *Balance sheet* | | |
| Investments at fair value through statement of income | **1,017,569** | 320,889 |
| Available for sale investments | **787,500** | 550,000 |
| Murabaha receivables | **1,519,620** | 3,376,497 |
| Premium receivable | **123,691** | 167,857 |
| *Key management personnel compensation* | | |
| Short-term employee benefits | **180,214** | 102,006 |
| Termination benefits | **8,756** | 1,060 |

## 17 RISK MANAGEMENT

The risks faced by the company and the way these risks are mitigated by management are summarised below.

***Insurance risk***
Insurance risk is the risk that actual claims payable to contract holders in respect of insured events exceed the carrying amount of insurance liabilities. This could occur because the frequency or amounts of claims are more than expected.

*Frequency and amounts of claims*
The frequency and amounts of claims can be affected by several factors. The company underwrites mainly general accident, fire and marine risks. These are regarded as short-term insurance contracts as claims are normally advised and settled within one year of the insured event taking place. This helps to mitigate insurance risk.

*Fire and accident*
*Property*
For property insurance contracts the main risks are fire and business interruption. In recent years the company has only underwritten policies for properties containing fire detection equipment.

These contracts are underwritten by reference to the replacement value of the properties and contents insured. The cost of rebuilding properties and obtaining replacement contents and the time taken to restart operations which leads to business interruptions are the main factors that influence the level of claims. The company has reinsurance cover for such damage to limit losses for any individual claim to KD 2,400,000.

*Motor*
For motor contracts the main risks are claims for death and bodily injury and the replacement or repair of vehicles. In recent years the company has only underwritten comprehensive polices for owner/drivers over 21 years of age. The company does not have reinsurance cover to limit losses for any individual claim.

The level of court awards for deaths and to injured parties and the replacement costs of, and repairs to motor vehicles are the key factors that influence the level of claims.

*Marine*
For marine insurance the main risks are loss or damage to marine craft and accidents resulting in the total or partial loss of cargoes.

The underwriting strategy for the marine class of business is to ensure that policies are well diversified in terms of vessels and shipping routes covered. The company has reinsurance cover to limit losses for any individual claim to KD 1,000,000.

*Reinsurance risk*
In order to minimise financial exposure arising from large claims, the company, in the normal course of business, enters into agreements with other parties for reinsurance purposes. Such reinsurance arrangements provide for greater diversification of business, allow management to control exposure to potential losses arising from large risks, and provide additional capacity for growth.

To minimise its exposure to significant losses from reinsurer insolvencies, the company evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities or economic characteristics of the reinsurers.

Reinsurance ceded contracts do not relieve the company from its obligations to policyholders and as a result the company remains liable for the portion of outstanding claims reinsured to the extent that the reinsurer fails to meet the obligations under the reinsurance agreements.

The five largest reinsurers account for 45% of the credit exposure at 31 December 2005 (2004: 57%).

## 17 RISK MANAGEMENT (continued)

*Credit risk*
Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. For all classes of financial assets held by the company, the maximum credit risk exposure to the company is the carrying value as disclosed in the balance sheet.

*Foreign currency risk*
Foreign currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. Management believes that there is minimal risk of significant losses due to exchange rate fluctuations and consequently the company does not hedge foreign currency exposure.

*Liquidity risk*
Liquidity risk is the risk that an enterprise will encounter difficulty in raising funds to meet commitments associated with financial liabilities. Liquidity requirements are monitored on a monthly basis and management ensures that sufficient funds are available to meet any commitments as they arise.

*Market price risk*
Market price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual security, or its issuer, or factors affecting all securities traded in the market. The company is exposed to market risk with respect to its listed equity financial instruments.

The company limits market risk by maintaining a diversified portfolio and by monitoring of developments in equity markets. The majority of the company's equities are listed on the Kuwait stock exchange.

## 18 FAIR VALUES OF FINANCIAL INSTRUMENTS

Financial assets include bank balances and cash, murabaha receivables, investments at fair value through statement of income, investments available for sale and certain other assets and liabilities.

The fair values of the financial assets and liabilities, with the exception of certain investments available-for-sale carried at cost (see note 7), are not materially different from their carrying values.

## 19 COMPARATIVE AMOUNTS

The corresponding figures for 2004 have been reclassified in order to conform with the presentation for the current year. Such reclassifications do not affect previously reported profit or equity.