



The Institute of Certified Public Accountants of Kenya

SUBMISSION

ON

THE DRAFT CENTRAL BANK OF KENYA (AMENDMENT) BILL, 2020

March 2021

PREAMBLE

The CBK Amendment Bill 2020 attempts to introduce direct regulation of the digital financial sector in Kenya and also expands the CBK regulatory jurisdiction over non-digital financial products and services. It gives the CBK power to regulate and supervise the conduct of providers of digital financial products and services; digital credit service providers; providers of financial products and the conduct of financial services.

The financial sector has experience the evolution and emergence of different players that have been regulated under the existing frameworks such as the Capital Markets Act, Chapter 485A of the laws of Kenya and the Insurance Act, Chapter 487 of the laws of Kenya. This Bill intends to make the Central Bank of Kenya a super regulator which mirrors the new industry-wide prudential regulator as was proposed in the Financial Market Conduct Bill, 2018 (Kenya Markets Authority).

It is worth noting that the evolution and growth of innovation particularly fintech products and services in the market has brought valid regulatory concerns that need to be addressed. However, care must be taken to establish clear and targeted regulatory interventions that will address the consumer protection and public interest needs whilst maintaining a conducive environment for innovation and market growth.

The Institute has considered the Bill and admits that the unregulated financial sector requires some legislative supervision to ensure they operate within the ambit of clearly defined structures and guidelines. According to FSD, digital loans accounted for 54% of the market yearly loans making consumer protection integral in regulation. In the study, it was found that several borrowers did not adequately understand the costs of borrowing which other than the interest, include; service fees, rollover fees and excise duty.

As seen in the table below, the monthly interest rates charged by these platforms are extremely high since when annualized they come to a rate of over 150% which is well over what commercial banks currently offer. This is exploitative to the consumers who may not otherwise be able to access more formal lines of credit from commercial banks or other financial institutions.

Table 1: Interest rates charged by digital financial services platforms

#	Platform	Maximum Monthly Interest Rate	Maximum amount (Ksh)
1.	Mshwari	7.5%	50,000
2.	Eazzy Loan	14%	3,000,000
3.	KCB Mobi Loan	4.08%	300,000
4.	Timiza	14%	150,000

#	Platform	Maximum Monthly Interest Rate	Maximum amount (Ksh)
5.	Branch	16%	70,000
6.	Tala	15%	50,000
7.	Okash	14%	60,000
8.	Berry	16%	50,000
9.	IPesa	12%	50,000
10.	Zenka	30%	30,000

Source: compilation from various digital information sources

The Bill is therefore timely to the extent that it establishes a framework through which the unregulated FSD will be brought under regulation. However, the greatest concern inherent in the provisions of the Bill is the absolute discretion and powers that the Central Bank of Kenya will have in terms of control which might be inimical to innovation and might also attract backlash from other regulators in the financial sector. There is also the issue of ease of doing business with the banks and microfinance which must also be reexamined.

The legal framework to be established to govern digital financial services in Kenya requires a multifaceted approach that brings on board the different players in the sector, each with specific regulatory role assigned to execute. This will avoid overlap of regulations and laws with other regulated financial services. This means that other regulators must be brought on board to take care of the three interrelated aspects of DSF; communication, banking, and lending. They include Communications Authority of Kenya, Credit Reference Bureau, Data Protection Act, Competition Authority of Kenya, and Central Bank of Kenya.

Regulation of digital financial services and fintech firms is not a completely new phenomenon. Drawn from practice in other jurisdictions, it is high time Kenya adopted the best practices that would not only regulate digital financial services provision but also enhance innovation in the sector to address the versatile market needs.

Table 2: DFS regulations in other jurisdictions

#	Country	Regulation
1.	Japan	The Bank of Japan (BOJ) is neither regulating nor supervising fintech firms, but it established the Fintech Center dedicated to being a catalyst for promoting the interaction among financial practices and innovative technologies, research and study, and the needs of economic society.

#	Country	Regulation
2.	France	The Autorité de Contrôle Prudentiel et de Résolution (ACPR) and Autorité des Marchés Financiers (AMF) hubs were set up in 2016 with primary responsibility for fintech and work most closely with the Banque de France and the Ministry for the Economy and Finance on fintech issues. The ACPR Fintech Innovation Unit is the interface between fintech project initiators and ACPR's various departments while the conduct regulator's AMF Fintech Innovation and Competitiveness Division focuses on the risks and opportunities to consumers. The AMF has created a "coach system" consisting of regulatory support for new entrants, which leads to a better understanding and adoption of the applicable regulations and avoids non-compliant business models developing.
3.	United Kingdom	The Bank of England's (BoE) Fintech Hub considers how fintech impacts the BoE's policies including the Prudential Regulatory Authority's (PRA) objectives and how fintech could be used to support the BoE's core functions, while the Financial Conduct Authority (FCA), whose mandate includes competition, has an Innovate Department that focuses on innovations of importance to consumers and investors.
4.	Singapore	The Monetary Authority of Singapore (MAS) acts as the central bank and is the integrated supervisor for the financial sector where responsibilities for supervision of fintech fall "under one roof." It revealed that it is developing a pilot program with the Singapore Academy of Law to connect fintech companies with legal service providers. The program, known as the Payments Regulatory Evaluation Program, launched in November of 2019, and targets fintech companies in payment services.
5.	United States of America	Two formal coordination mechanisms are prominent among US federal financial regulators, the Financial Stability Oversight Council (FSOC) and the Federal Financial Institutions Examination Council (FFIEC). Both take up fintech issues from time to time and have set up working groups to deal with particular fintech issues. In addition, the Financial and Banking Information Infrastructure Committee (FBIIC) has a role to play in improving coordination and communication among financial regulators, promoting public-private partnerships within the financial sector.

Source: IMF Fintech Notes 2019

From the above, it is worth noting that instead of setting up new agencies, these countries have assigned new responsibilities to existing institutions. Adopting a cross agency approach will be needed to support consistency, limit regulatory arbitrage, and contain

new risks and therefore enable a holistic approach to regulation. There is therefore need for interlinkages between various regulators to provide the needed support in executing their functions to support the overall regulation of digital financial services.

In this regard, the Institute proposes the following power arrangement for the regulators to enhance collaboration for the success of the bill;

Table 3: interlinkages between various regulators

#	Risk	Relevant Regulation	Mandate	Justification
1.	Fraud, ability to repay loans (positive and negative credit history)	Credit Reference Bureau	<ul style="list-style-type: none"> ▪ Credit Reporting ▪ Risk profiling ▪ Blacklisting 	<ul style="list-style-type: none"> ▪ A case in point is where the digital lenders were delinked from CRB during the Covid-19 pandemic. DLAK explained that without access to these bureaus, digital lenders had limited means of assessing the customers' ability to pay hence customers complaints of deletion of their loan limits. ▪ Regulation through Credit Bureaus can assist in risk management especially where digital lenders have contracts with foreigners, and they have no means to access and assess their risk profiles
2.	Consumer protection issues such as data mining, for borrowers, lack of full disclosure leading to predatory lending, no clear documentation on scoring list and how lenders profile borrowers, lack of knowledge on viability and compliance of	Consumer Protection Commission Data Protection Act	<ul style="list-style-type: none"> ▪ Data protection against phishing, mining; ▪ Disclosure of terms and conditions in the agreement forms; ▪ Effective consent by making the 	<ul style="list-style-type: none"> ▪ Cases have been reported of misuse of borrowers' data by the Digital platforms ▪ Lack of full disclosure to the borrowers is viewed as predatory making people at the base of the economic pyramid to live off loans through a debt culture orchestrated by the digital lenders. ▪ There is need to control and monitor the debt culture through regulation.

#	Risk	Relevant Regulation	Mandate	Justification
	player, threat of security on the protection of authenticity, customer and data.		<p>language simple and accessible;</p> <ul style="list-style-type: none"> Consumer protection against predatory lending practices 	<ul style="list-style-type: none"> Currently, there is no data protection law in Kenya
3.	Communication; some digital lenders have misused data from social media and other personal data for scoring. In case of defaults, some lenders reach out to the borrowers' contact lists shaming the borrowers and asking third parties to enforce payments.	Communication Authority of Kenya	Monitoring the activities of licensees to enforce compliance with the license terms and conditions as well as the law.	<ul style="list-style-type: none"> Digital lending is conducted through mobile network service providers which are under the regulation of Communications Authority of Kenya. The Authority can best deal with the issues of communication better than CBK Reforms should be made on how to access government data or information held with public authorities such as ID, land records, demographic information, income tax records, education records, and employment history. These should be made available in an efficient manner using automated interfaces to reduce their costs and improve customer experience.
4.	Financial Inclusion	Central Bank of Kenya Anti-Money Laundering Act	<ul style="list-style-type: none"> Establish prudential guidelines specific to digital lenders who are 'credit only' Oversight 	<ul style="list-style-type: none"> Some digital lenders self-regulate through Digital Lenders Association of Kenya (DLAK). However, this is voluntary and lacks the legal underpinning for proper regulation. There is no legal framework for digital borrowing platforms since they are exempt from classification as financial institutions under the Banking Act, Cap 488 Laws of

#	Risk	Relevant Regulation	Mandate	Justification
			<ul style="list-style-type: none"> ▪ Licensing and compliance ▪ Publishing a list of all licensed digital money lenders in the Kenya Gazette. 	<p>Kenya, and Microfinance Act Number 19 of 2006.</p> <p>The Institute further recommends that CBK adopts other functions that will facilitate the regulation of the digital financial providers within the specified functions. These include;</p> <ol style="list-style-type: none"> a. Create an enabling policy and regulatory environment for transformational DFS over time; b. Develop a shared understanding of the risk profiles of emerging DFS business models, which is essential to design appropriate regulatory framework c. Provide a platform for capturing, tracking and sharing information on innovative DFS, products, business models, and appropriate new policy responses d. Establish linkages and provide inputs, where appropriate, to global standard setting bodies, seeking to establish proportionate supervisory practices for DFS e. Play a more proactive role in financial education programs geared towards people at the base of the economic pyramid to help improve the understanding, opportunities and risks associated with the financial system and its products and services.

#	Risk	Relevant Regulation	Mandate	Justification
				f. The Institute of Certified Public Accountants of Kenya (ICPAK) is committed to collaborating with the Central Bank of Kenya in providing essential financial literacy programs targeting people at the bottom of the pyramid.
5.	Malpractices such as imposing usurious interests and unfair pricing to the borrowers	Competition Authority of Kenya	<ul style="list-style-type: none"> Standards of pricing for digital financial providers via digital channels Price transparency- Obliging financial service providers to disclose to the consumers the cost of products such as person-to-person bill payments, merchant payments and loans. 	<ul style="list-style-type: none"> Competition Authority of Kenya is the body mandated to enforce and enhance the welfare of the people of Kenya by promoting and protecting effective competition in markets and preventing misleading market conduct throughout Kenya. It will be better suited to handle information relating to pricing and also enforce price transparency across all the players in the FSD. The Regulator should act as the consumers ombudsman and ensuring that terms and conditions and transaction pricing conform to fairness and disclosure standards.

The Institute has reviewed the Bill and made the following recommendations:

SUMMARY OF ICPAK SUBMISSION ON CENTRAL BANK OF KENYA (AMENDMENT) BILL, 2020

CLAUSE OF THE BILL 2020	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS	JUSTIFICATION
Section 2A: Amended functions of Central Bank of Kenya	The proposals have not considered the monitoring and reporting aspect of regulation and supervision	Amend as follows by inserting a new entry immediately after 2 dd as follows; (e) Regularly monitor compliance status and publish a list of all licensed digital money lenders in the Kenya Gazette.	<p>The regulator is duty-bound to not only regulate and supervise the activities of digital financial service providers but also monitor the compliance and publish reports for the benefit of consumers.</p> <p>The consumers are entitled to know the list of licensed digital financial service providers and their compliance status for informed choices.</p> <p>Knowledge of digital financial services and products programs should be made available to a broad range of audiences, through a variety of delivery channels including digital and non-digital.</p>
Section 2A 1 da: Definition of financial service	The Bill has not defined the scope of digital financial services under regulation.	Amend to include DFS providers as follows; a. Peer-peer SME lenders b. Online balance sheet lenders c. Online loan aggregators d. Third-party analytic, data and lending platform providers	This is to provide clarity on the category of providers targeted for regulation.

		e. Tech and ecommerce giants f. Invoice financing, supply chain and trade credit providers g. Mobile-based lending models	
Section 2A 1 da: Definition of financial service	The Definition has excluded digital assets.	Amend by inserting a new entry immediately after 2A (da) (a) as follows; (b) Digital Assets	With the shift towards the use of digital platforms, it is important to include digital assets under the purview of supervision alongside financial services. The digital assets include digital tokens (cryptocurrency); social media accounts; photographs; images; files or data stored on mobile phone; computer or cloud service; music bought on iTunes account; online shopping accounts; email accounts used to access various online banking platforms and utility accounts; domain names and network infrastructure assets such as IP addresses