Financial Services Sector Report

Q2 2021

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BANKING

In the last quarter, proposals were introduced in the Central Bank of Kenya Amendment Bill to regulate digital credit service providers. Reintroduction of mobile money transaction charges was also proposed.

I. Guidelines, Notices & Circulars

Reintroduction of mobile money transaction charges.

The Central Bank of Kenya published a press release on 1st April 2021 announcing the resumption of charges for transactions above Kenya Shillings One Hundred (KES 100.00) carried out through bank specific mobile money wallets closely linked to the Sacco sector. CBK noted that the Sacco sector accounts for a significant share of such transactions with banks providing a bridge to domestic and cross-border payment systems. The press release stated that owing to the lack of alternatives to connect to the mobile money ecosystem, the resumption of charges would provide space to increase connection options for the Saccos.

II. Judicial Decisions

Kenya Commerce Exchange Service Bureau Limited (Kenex) v Central Bank of Kenya [2021] eKLR

Issue for Determination:

Whether the Petitioner met the legal threshold for grant of a conservatory order restraining the Central Bank of Kenya from deliberating on and/or directing banks and financial institutions to migrate from the Petitioner's SWIFT platform and connect directly to the SWIFT network.

Held:

1. The Petitioner met the legal threshold for grant of conservatory orders by demonstrating a prima facie case and the loss it stood to suffer if the conservatory order was not granted.
2. The Central Bank of Kenya did not demonstrate the prejudice it stood to suffer if the conservatory order sought was granted.

Implication:

The Central Bank of Kenya's directive requiring financial institutions to discard Kenya Commerce Exchange Service Bureau's SWIFT platform and get direct access to SWIFT's network has been suspended pending the hearing and determination of the substantive Petition.

The Central Bank of Kenya is precluded from considering, deliberating or making any decision regarding connectivity to SWIFT and backup for banking business continuity pending the determination of the substantive petition.

Find Case Link here

FINTECH

The Finance Act 2021 has defined what a Digital Marketplace is and also expanded on the definition of what constitutes digital services. It has also introduced provisions on timing of payments, submission of returns and empowers the Commissioner to take certain measures to collect digital services taxes.

I. Acts of Parliament

Definition of the Digital Marketplace and the digital service tax

The Finance Act 2021 has amended the Income Tax Act by including a new definition - Digital Marketplace, which is defined as an online platform which enables users to sell or provide services, goods, or other property to other users.

The Act further expands the definition of digital services to include supplies made "over the internet or an electronic network."

The effective date for the same is 1st July 2021.

The Act has also amended the Tax Procedures Act by including a provision which enhances the collection of tax on income generated over the internet or through an electronic network including through a Digital Marketplace. The Commissioner is now empowered to seek intervention from any relevant authority to collect such taxes.

Lastly, the Act also states that a person subject to digital service tax shall submit a return and pay the tax due to the Commissioner on or before the twentieth day of the month following the end of the month in which the digital service was offered.

Find link here

III. Parliamentary Bills

The Central Bank of Kenya (Amendment) Bill, 2021 published on 6 April 2021

To amend the Central Bank of Kenya Act to provide for licensing of digital credit service providers, who are not regulated under any other law.

The primary objective of this bill is to regulate the provision of digital credit by the Central Bank of Kenya (CBK).

Currently, there exists no legal framework governing digital credit service providers. To remedy the gap in the law, this bill proposes to widen CBK's mandate to include the regulation of digital credit service providers. A digital credit service provider is defined as a person licensed by the CBK to carry on digital credit business. A digital credit business is further defined as the business of providing credit facilities or loan services through a digital channel.

Effectively, once this bill passes into law, all digital credit service providers must be licensed by the CBK. Consequently, the CBK will also be empowered to:

a) determine the capital adequacy requirements for digital credit providers;
b) determine their minimum liquidity requirements;
c) approve the business models through which the digital credit business may be conducted;
d) supervise digital credit providers;
e) suspend or revoke their license; and
f) direct or require such changes as it may consider.

The bill additionally guarantees that its supporting regulations shall be made within three (3) months of the coming into force of the Act. Find link here

INSURANCE

The Finance Act 2021 introduced a few changes affecting the insurance sector which touch on regulation of reinsurance brokers and introduction of an annual fee for insurers; the removal of requirement for the Kenya Reinsurance Corporation to certify reinsurance contracts; and the regulation of closed insurance funds.

I. Acts of Parliament

Amendment of the Insurance Act for the regulation of foreign reinsurance brokers

The Finance Act 2021 has amended the Insurance Act to provide for the regulation of foreign reinsurance brokers by amending the definition of brokers which previously excluded the brokers who are not resident in Kenya. The regulation of insurance brokers is likely to enhance the Insurance Regulatory Authority's supervision of insurance industry players.

The Finance Act 2021 has also amended the Insurance Act to remove the requirement to have the Kenya Reinsurance Corporation certify reinsurance contracts. This shows that there are several reinsurance players in Kenya and therefore any regulation of reinsurance contracts is a role for the regulator as opposed to an active market player.

The Finance Act 2021 has amended the Insurance Act to provide for the continuation of the operation of a closed fund insurance business without the need for registration but subject to the insurer furnishing the Commissioner with information as may be required and honouring existing policies.

Further, there is an imposition of a fine not exceeding KES 200,000 and a further fine of KES 10,000 for each day in which the insurer fails to honour its policy obligations. Moreover, the Act provides that the assets of a closed fund shall not be disposed of except with the permission of the Commissioner. This is an indication that the proposed regulation of closed funds will protect policy holders and provide an avenue for the orderly winding up of closed funds businesses.

Lastly, and quite importantly, the Finance Act 2021 has also amended the Insurance Act by stating that each insurer issued with a license under the Insurance Act shall be required to pay an annual fee which shall be prescribed.

Find link here

II. Subsidiary Legislation

The Insurance (Amendment) Regulations Legal Notice 70 of 2021

These regulations were published to amend the Insurance Regulations,1986, by deleting the class of business of 'liability insurance – including public liability, products' liability and professional indemnity' and its sub-classes of '(a) products' liability, (b) professional indemnity and (c)other liability'. This definition of this class of business has now been refined to be more specific; with the class now called 'liability insurance' and the following new sub-classes of business under it:

(a) product liability
(b) professional indemnity
(c) latent defects liability
(d) structural defects liability
(e) public liability and
(f) others.

You may find a copy of the notice here.

III. Guidelines, Notices & Circulars

The National Insurance Policy aimed at strengthening the insurance sector in Kenya.

Through a public notice dated 1st April 2021, the National Treasury invited public and stakeholder comments on the draft National Insurance Policy. The policy intends to improve access, usage and affordability of insurance products and services as well as maintain an inclusive, fair and stable insurance sector. Submission of public input closed on 16th April 2021.

On 19th May 2021 the Insurance Regulatory Authority issued a public notice inviting stakeholder and public comments on proposed amendment to the Third Schedule of the Insurance Act. The purpose of the proposed amendment is to include Latent Defects Liability and Structural Defects Liability as new classes of insurance business to cover risks related to construction projects. The notice also indicated that the amendment aims to safeguard building owners as well as third parties against financial consequences of damages occasioned by structural and latent defects. Submission of comments closed on 20th May 2021.

IV. Judicial Decisions

1) Constitutional Court

Kenyan Alliance Insurance Company Limited v Naomi Wambui Ngira & another (Suing as the Legal Representatives and Administrators of the Estate of Nelson Machari Maina (Deceased) [2021] eKLR

Issues for Determination:

(a) Whether an insurer is, pursuant to the provisions of Section 10 (4) of the Insurance (Motor Vehicle Third Party Risks) Act (hereinafter, "**the Act**"), under a duty to repudiate liability by way of declaratory suit upon receipt of notice, in all instances where it deems itself not liable.

(b) Whether failure by an insurance company to respond to a statutory notice under section 12 (1A) of the Act implies automatic assumption of liability for settlement of a judgment entered against an insured.

Held:

1. An insurer cannot be compelled to settle judgment arising from liability that falls outside the scope of:
   (a) the Act; and/or
   (b) the insurance contract executed between the insurer and the insured.
2. The legal obligation for an insurer to file a declaratory suit under section 10 (4) of the Act only applies to instances where the liability in question is required to be covered by a policy and the liability is in fact covered by the terms of the policy.
3. Failure by an insurer to respond to a statutory notice served upon it under section 12 (1A) of the Act, even though an offence, does not automatically make the insurer liable for settlement of judgments entered against its insureds.

Implication:

1. There is no obligation for an insurer to file a declaratory suit pursuant to section 10 (4) of the Insurance (Motor Vehicle Third Party Risks) Act **where the liability in question is not required to be covered by a policy and the liability is in fact not covered by the terms of the policy**.
2. Insurers should, as a matter of good practice and avoidance of criminal exposure, respond to statutory notices served upon them under Section 10 (2) of the Insurance (Motor Vehicle Third Party Risks) Act.
   Find Link here

2) Supreme Court

Christopher Onyango & 23 Others v Heritage Insurance Company Limited [2021] eKLR

Issue for Determination:

Whether the Applicants met the legal threshold (that the matters raised in the appeal are of general public importance) for leave to be granted to appeal to the Supreme Court from the decision of the Court of Appeal arising out of an employment claim where the Applicants were terminated by way of a redundancy.

Held:

1. The Applicants failed to meet the legal threshold for appealing to the supreme court as the issues they raised did not transcend the parties.
2. Application for leave to appeal denied.

Implication:

Obiter – Company policies and contractual provisions on employment termination are binding in so far as they do not breach the Employment Act.

Employment disputes between parties can only be litigated on up to the Court of Appeal unless they raise constitutional issues – which would grant an automatic access by way of appeal to the Supreme Court.

INVESTMENTS

The Finance Act 2021 has introduced a common reporting standard to be adhered to by financial institutions. CMA also sent out a word of caution on unregulated products, warning it would offer no protection and advised investors to verify investments entities via their website.

I. Acts of Parliament

Introduction of a common reporting standard for financial institutions.

The Finance Act 2021 amends the Tax Procedures Act by introducing a common reporting standard to be adhered to by financial institutions. Under this section of the Act, a financial institution is defined as a custodial institution, a repository institution, an investment entity or a specified insurance company.

The Cabinet Secretary to the Treasury is required to first prescribe the common reporting standard via regulations. Once the common reporting standards have been prescribed, investment entities will be required to identify the reportable accounts specified by the standard and thereafter make the following filings with the Commissioner of Tax:

(a) An information return on reportable accounts held, managed or administered by the investment entity; and
(b) A return marked nil if no account is held, managed or administered by the investment entity.

The Act also provides for the imposition of penalties where financial institutions fail to comply with the common reporting standards obligation. Find link here

II. Guidelines, Notices & Circulars

Caution against unlicensed and unapproved entities

The Capital Markets Authority issued a press release on 17th June 2021 cautioning investors against investing in unregulated products offered by unlicensed and unapproved entities. The CMA chief executive noted that capital markets regulatory framework would only afford protection to investors investing through licensed and approved entities. The Authority advised investors to use the CMA website to verify the names of entities approved to offer services in the capital markets industry. Members of the public who have been affected or are aware of illegal entities were advised to reports the same to the Authority or the Capital Markets Fraud Investigation Unit.

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RETIREMENT BENEFITS

The Finance Act 2021 has introduced a few changes to the retirement benefits sector which include: providing for the registration requirements and regulation of corporate trustees; extension of time of filing pension scheme accounts; and providing for the definition of what constitutes a post-retirement medical fund.

I. Acts of Parliament

Amendment of the Finance Act 2021 to provide for post-retirement benefits

The Finance Act 2021 has amended the Retirement Benefits Act, 1997, to provide for the registration and regulation of corporate trustees that provide services to pension schemes. This amendment will expand the scope of regulation of the Retirement Benefits Authority to include corporate trustees. It is also likely to increase the public's confidence in the corporate trustees who manage their retirement benefits.

The Finance Act 2021 has amended the RBA to provide an additional three months for trustees to file audited accounts where the delay is justified. Where an extension is provided, the trustees are not subject to late submission penalty. The amendment will enhance compliance by trustees because in some instances, the audited accounts are not ready within the six months period that is provided under the Act.

The Finance Act 2021 has amended the RBA to provide for a post-retirement medical fund which shall be within a scheme and from which the costs of medical benefits shall be met in accordance with the medical fund rules. The amendment will ensure that retirees are able to access quality healthcare. Find link here

SACCO SOCIETIES

I. Guidelines, Notices & Circulars

Deadline For Non-Deposit Taking Business Authorization

The Saccos Societies Regulatory Authority (SASRA) published three public notices on 29th April 2021, 6th May 2021, and 19th May 2021 reminding members of the public and stakeholders within the Sacco sector that all Saccos undertaking non-deposit taking business ought to apply for authorization by SASRA before the statutory deadline of 30th June 2021. SASRA emphasized that no Sacco Society shall be allowed to undertake non-deposit taking business transactions without requisite authorization.

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NOTARIES PUBLIC • COMMISSIONERS FOR OATHS • PATENT AGENTS
OFFICES: 1st Floor, Wing B, Capitol Hill Square, Off Chyulu Road, Upper Hill, Nairobi
POSTAL ADDRESS: P. O. Box 8418-00200, Nairobi Kenya TELEPHONE: +254 20 259 69 94 / +254 20 273 75 75 / +254 20 273 75 72 /+254 20 273 75 78 / +254 71 826 86 83
EMAIL: mman@mman.co.ke WEBSITE: www.mman.co.ke