Streamlining the financial sector

Deepening financial sector reforms for growth

Aiming for an efficient, globally competitive financial sector

Capital and risk based supervision

The Cabinet Secretary has proposed to progressively increase the minimum core capital requirements for banks and insurance companies. Banks will be required to hold KES 5 billion by December 2018 from the current KES 1 billion. Insurance companies will be required to hold KES 600 million and KES 400 million by June 2018 for life and general insurance companies from the current KES 300 million and KES 150 million respectively.

Whilst the raising of absolute capital is a welcome move, the financial condition of this industry can only be truly monitored once the risk based capital requirements recently introduced for the banking sector and now for the insurance sector are in place.

Only 20 out of the 44 banks, six out of 25 life insurers and ten out of 39 general insurers have met these core capital requirements based on most recently available financial information. This is expected to result in mergers and acquisitions in the financial services sector and to create larger, better funded and more stable financial institutions.

Central Bank of Kenya (CBK) has now been empowered to issue non-renewable perpetual licenses for banks. This will reduce the administrative burden for application of annual licenses. The risk based monitoring and periodic inspections by CBK will continue and could be the basis for withdrawing licenses.

Governance

Greater emphasis has been placed on sound governance of pension schemes, with the proposal that trustees will not be allowed to serve for more than two, three-year terms. It is unclear whether this rule will apply to corporate trustees. In addition, pension schemes will be required to submit audited accounts within 3 months after year end. Trustees will need to ensure that they have adequate financial reporting processes to enable them meet this deadline.

The Sacco Societies Regulatory Authority (SASRA) is expected to vet directors and key officers of deposit taking Sacco societies. This will align with the practice adopted by other financial services regulators.

When defined benefit schemes are wound up or converted into defined contribution schemes, there has been uncertainty as to who should benefit from surpluses arising. The Cabinet Secretary has proposed that the surplus be shared equally between the members and the employers.

Expanding horizons

The financial markets have seen the emergence of new investment vehicles. These are aimed at providing alternative sources of capital and investment.

The Cabinet Secretary has proposed the following:

- Stamp duty exemption on transfer of assets into Real Estate Investment Trusts (REITs) and Asset Backed Securities (ABS).
- Creation of a new category in the Retirement Benefits Investment guidelines to allow schemes to invest up to 10 percent of their assets in private equity funds and venture capital funds licensed by the Capital Markets Authority.
- Introduction of an M-Akiba bond which will allow Kenyans to purchase Government Securities with as little as KES 3,000 using their mobile phones. Given the enthusiasm for similar products such as M-Shwari, we expect a lot of interest in this product. It remains to be seen what impact this will have on bank deposits.

Notably missing

The Cabinet Secretary did not deal with some issues that the financial sector anticipated would be addressed in the budget speech:

- Although the Cabinet Secretary has proposed exemption of stamp duty on transfer of assets into REITs and ABS, he has not addressed the uncertainty relating to Value Added Tax (VAT) and Capital Gains Tax on such transfers.
- The contentious issue of excise duty on fees charged by insurance companies and commissions earned has not been fully clarified.
- There was no comment on the progress made in regards to the parastatal reforms and formation of the Financial Services Authority (FSA).
- Though there was a commitment to submit the CBK Bill to parliament, there have been significant delays in submitting similar bills in the past, notably the Insurance Bill and the Banking Bill.