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Enforcement of the Prudential Guideline no.13 (enforcement of banking laws and regulations-CBKPG13) by The Central Bank of Kenya (CBK) a case study of Chase Bank (Now SBM) *for the period before and after its being placed under statutory management*

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**Enforcement
of the Prudential Guideline no.13 (Enforcement of Banking Laws and
Regulations-CBK/PG/13) by The Central Bank of Kenya (CBK): A case study of
Chase Bank (Now SBM Bank), for the period before and after its being placed
under statutory management**

Samuel Munge Kiongera

**Submitted in partial fulfillment of the requirements for the Degree of Master of
Laws at Strathmore University**



**Strathmore University
Strathmore Law School
Nairobi, Kenya**

December, 2020

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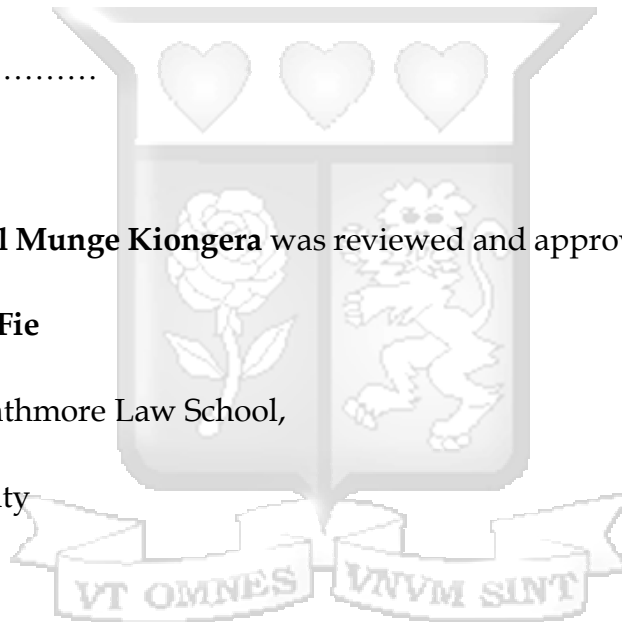
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Abstract

In 2006, the Central Bank of Kenya (CBK) issued the Guideline on Enforcement of Banking Laws and Regulations. The Guideline was subsequently replaced in 2013 by the Prudential Guidelines 2013. Included in Prudential Guidelines 2013 was the Enforcement of Banking Laws and Regulations as Prudential Guideline No.13 (CBK/PG/13). It was expected that with the issuance of the Prudential Guidelines 2013, the quality of the enforcement of banking laws and regulations would improve so as to ensure that banks did not fail. However, within a period of less than three years, the 3 banks were placed under statutory management.

This study examines the enforcement of the Prudential Guideline No.13 by the CBK through a case study of Chase Bank (CB) by making a comparison between the period before and after its being placed under statutory management. This is achieved through making use of qualitative and quantitative data obtained through interviews, with the aid of questionnaires, and from the CBK's Bank Supervision Annual Reports from the year 2008 to 2018.

The study seeks to establish whether the difference in the two periods, the period before and after CB being placed under statutory management, could be attributed to the enforcement mechanisms employed by the CBK in the enforcement of Prudential Guideline No.13 or whether there are other factors responsible for the difference in the two periods, other than the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13. It thereafter makes recommendations based on its findings.

Table of Contents

Chapter 1 INTRODUCTION.....	8
1.1 Definition of key terms	8
1.2 The problem background.....	9
1.3 Statement of the problem.....	11
1.4 Statement of Objectives.....	11
1.5 Research Questions	11
1.6 Hypothesis	12
1.7 Theoretical Framework.....	12
1.8 Justification of the research	13
1.9 Methodology and Approach	14
1.10 Chapter Breakdown	14
Chapter 2 LITERATURE REVIEW	16
2.1 Introduction	16
2.2 Literature review	16
2.3 Conclusion	23
Chapter 3 THE LEGAL BACKGROUND TO CENTRAL BANK SUPERVISION	24
3.1 Introduction	24
3.2 Banking laws and regulations	24
3.2.1 The CBK Act (Cap491).....	25
3.2.2 Prudential Guidelines and Regulations	26
3.3 The enforcement mechanisms	27
3.3.1 Resolutions of the Board	28
3.3.2 Letter of Commitment.....	28
3.3.3 The MOU.....	28
3.3.4 Directives issued.....	29
3.3.5 Discharge of Officers and Withholding of Corporate Approvals.....	30
3.3.6 Intervention of CBK in the running of an institution	31
3.3.7 Dismissal of Directors and Officers and imposition of Penalties	34
3.3.8 Cancellation of Banking License.....	34
3.3.9 Discontinuation of Deposit Protection	35
3.3.10 Corrective Action Guideline (CBK/PG/21)	35
Chapter 4 THE RESEARCH FINDINGS PRESENTATION	39
4.1 Introduction	39
4.2 The regulations and laws that govern the operations of banks in Kenya.....	39

4.3	Mechanisms used by CBK in the implementation of laws and regulations of banking	39
4.4	The on-site and off-site supervision methods used by the CBK in the implementation of laws and regulations of banking.....	39
4.5	The changes in the enforcement mechanisms utilized by CBK since the placing of Chase Bank (now SBM Bank) under statutory management and its re-opening in the year 2016.....	40
4.6	The reforms that would make the CBK more effective in its enforcement of the banking laws and regulations.....	41
4.7	The submission of the auditors' report by the auditors of Chase Bank for each of the years from the year 2013 up to the time of its closure on 7th April, 2016	41
4.8	Whether the Central Bank of Kenya at any one time required Chase Bank, to pass Board Resolutions, to get into an MOU, to take corrective/remedial actions or it issued directives to Chase Bank as per s. 33(1) of the Banking Act in between from the year 2013 up to the time of its closure on 7th April, 2016.....	42
Chapter 5 THE ANALYSIS OF THE FINDINGS OF THE RESEARCH		46
5.1	The introduction.....	46
5.2	The period before the placement of Chase Bank under statutory management ..	46
5.3	The period after the closure and placement of Chase Bank under statutory management.....	48
5.4	A comparison of the period before the placement of Chase Bank on statutory management and the period after the closure and placement of Chase Bank on statutory management.....	52
5.5	Conclusion from the comparison of the period before the putting of Chase Bank in statutory management and the period after the closure and putting of Chase Bank in statutory management.....	62
Chapter 6 THE CONCLUSION AND RECOMMENDATIONS		64
6.1	The study's limitations	64
6.2	The conclusion.....	64
6.3	The recommendations	66
BIBLIOGRAPHY.....		67
ANNEXURES.....		71
Annexure A-	Letter of introduction	71
Annexure B-	Questionnaire	73
Annexure C-	Ethical clearance report	86
Annexure D-	Plagiarism report.....	90

LIST OF STATUTES

The Constitution of Kenya (2010)

The Central Bank of Kenya Act (Cap 491)

The Banking Act (Cap 488)

The Kenya Deposit Insurance Act 2012

The Prudential Guidelines 2013



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Chapter 1 INTRODUCTION

1.1 Definition of key terms

The key terminologies used in this thesis are defined herein under:

Bank is defined by the Kenyan Banking Act as a company which carries on, or proposes to carry on, banking business in Kenya but does not include the Central Bank.¹

Banking business is defined by the Banking Act of Kenya to mean:²

- a) the accepting from members of the public of money on deposit repayable on demand or at the expiry of a fixed period or after notice;
- b) the accepting from members of the public of money on current account and payment on and acceptance of cheques; and
- c) the employing of money held on deposit or on current account, or any part of the money, by lending, investment or in any other manner for the account and at the risk of the person so employing the money;
- d) Such other business activity as the Central Bank may prescribe.

Banking laws and regulations refer to the CBK Act (Cap. 491), the Banking Act (Cap. 488) and Prudential Guidelines and regulations issued therein.

Prudential Guidelines can be defined as a kind of procedures for the government that require banks to comply with specific issues, boundaries and strategies.³

¹Section 2, *Banking Act*

² Section 2, *Banking Act*

³Mohamed S, Mutegi D, and Muriuki M, 'Effects of the Central Bank of Kenya Prudential Guidelines on the performance of Commercial Banks in Kenya' 3 *Imperial Journal of Interdisciplinary Research* 9(2017),613.

1.2 The problem background

In 2006, the (CBK) issued the directive on the implementation of laws and regulations of banking. The directive was later replaced in 2013, exactly seven (7) years later, by the Prudential Guidelines 2013, which included Enforcement of Banking Laws and Regulations as Prudential Guideline No.13 (CBK/PG/13). It was expected that with the issuance of the Prudential Guidelines 2013, the quality of the enforcement of banking laws and regulations would improve so as to ensure that banks did not fail. However, in 2015 and 2016, just within a period of two (2) years, three (3) banks were put within statutory management: Dubai bank, imperial bank, and chase bank.

About four (4) months prior to Imperial Bank being placed under statutory management, Dr. Patrick Ngugi Njoroge was appointed as the new Governor of the CBK on 19 June 2015.⁴ Dr.Haron Sirima, the Deputy Governor, was the acting governor immediately after the retirement of Prof.Njuguna Ndung'u on 4 March 2015.⁵ Following Prof. Ndung'u's retirement, the new governor, Dr. Patrick Njoroge, a strict administrator, on ascertaining the practices that were unethical and which contravened the regulatory rules, put two banks, Dubai Bank Kenya and Imperial Bank into statutory management months after coming into office. This brought Prof. Ndung'u on the limelight, and was blamed of having been compromised when the bank practices that were fraudulent took place. In April 2016, the CBK put Chase Bank, also under statutory management.⁶ Chase Bank (CB) being the third bank to be put under

⁴ 'The real problem with Kenya's banking sector' *Business Daily*, 13 April 2016 <https://www.businessdailyafrica.com/news/539546-3157918-142mvw1z/index.html> on 10 November 2018.

⁵ 'Here are more qualified Kenyans who missed Central Bank Governor job' *Kenya Today*, 3 June 2015 <https://www.kenya-today.com/business/qualified-kenyans-missed-central-bank-governor-job> on 16 January 2020.

⁶ 'Exotic holidays, gifts and the \$ 380 million fraud that brought down a Kenyan bank' *Quartz Africa*, 16 December 2016 <https://qz.com/africa/864182/exotic-holidays-gifts-and-the-380-million-fraud-that-brought-down-a-kenyan-bank/> on 25 January 2020.

statutory management. CB began its life when a number of business men came together in the year 1995 and bought 60% shareholding in United Bank.⁷ During that period, United Bank had been put under statutory administration by the CBK. One year later, the bank was rebranded as CB and it commenced its operations. As at 31st December 2015, CB had assets of about Kshs. 143 billion. Also during the same period, the shareholders' worth was valued at Kshs. 12billion (CBK, 2016).⁸ The CBK put CB in receivership on 7th April, 2016. The principal reasons being non-attainment of the required banking ratios and under-reporting of loans granted internally. The loans granted internally stood at Kshs.13.62 billion in comparison to the Kshs.5.72 billion it had reported.⁹ The main problem at CB was a governance issue. The bank granted huge loans to its directors. KCB being the receiver manager, the bank opened again on the 27th April 2016 (CBK, 2016), twenty (20) days later following it being placed under statutory administration.¹⁰ However, in August 2018 a major portion of CB's assets and liabilities were taken over by the State Bank of Mauritius (SBM) Kenya Limited, the Kenyan subsidiary of State Bank of Mauritius.¹¹

In both the periods before and after CB being placed under statutory management, the Prudential Guideline No.13 was in place and is still in place. However, subsequent to the re-opening of CB no bank has been placed under statutory management or even

⁷ Gathaiya R, 'Analysis of issues affecting collapsed banks in Kenya from year 2015 to 2016' 7 *International Journal of Management & Business Studies* 3(2017), 9.

⁸ Gathaiya R, 'Analysis of issues affecting collapsed banks in Kenya from year 2015 to 2016', 9-10.

⁹ 'Charles Mwaniki: Chase Bank shocks market with Sh8bn secret insider loans' *Business Daily*, 7 April 2016 <https://www.businessdailyafrica.com/Corporate-News/Chase-Bank-shocks-market-with-Sh8bn-secret-insider-loans/-/539550/3149358/-/15aosjsz/-/index.html> on 10 November 2018.

¹⁰ Gathaiya R, 'Analysis of issues affecting collapsed banks in Kenya from year 2015 to 2016', 9-10.

¹¹ 'Otiato Guguyu: Chase Bank officially transforms to SBM Kenya', *The Standard*, 20 August 2018 <https://www.standardmedia.co.ke/business/article/2001292696/chase-bank-is-now-officially-sbm-kenya> on 10 November 2018.

been liquidated. The principal reason of this particular research is to establish whether the difference in the two periods could be attributed to the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13 in each of the two periods or there are other factors responsible for the difference in the two periods.

1.3 Statement of the problem

Before the closure and placement of Chase Bank under statutory management on 7th April, 2016, two other banks, Dubai Bank and Imperial Bank, had also been placed under statutory management. After Chase Bank opened again on the 27th April, 2016 to date no bank has been placed under statutory management. This research seeks to establish whether the difference between the two periods, the period prior to the closure and placement of Chase Bank under statutory management and the period after re-opening of Chase Bank, could be attributed to the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13 or other factors.

1.4 Statement of Objectives

The objectives of this study are:

- a) To establish whether the enforcement mechanisms employed by the CBK in the enforcement of Prudential Guideline No.13 were responsible for the difference in the period before and after the placing of Chase Bank under statutory management;
- b) To establish whether apart from the enforcement mechanisms employed by the CBK there are other factors that could explain the difference in the period before and after the placing of Chase Bank under statutory management.

1.5 Research Questions

- a) Were the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13 responsible for the difference in the period before and after the placing of Chase Bank under statutory management?

- b) Are there other factors responsible for the difference in the period before and after the placing of Chase Bank under statutory management, apart from the enforcement mechanisms employed by the CBK?

1.6 Hypothesis

The enforcement mechanisms employed in the enforcement of Prudential Guideline No.13 is not the only factor to explain the difference between the two period, the period before and after the placing of Chase Bank under statutory management.

1.7 Theoretical Framework

The research is directed by the understanding that the enforcement of banking laws and regulations in Kenya is done by the CBK, established by s. 3 of the CBK Act. The CBK's role is one of oversight over all the banks in Kenya. In order to ensure that banks adhere to all the banking laws and regulations, the CBK employs an enforcement model that has two important aspects incorporated into the design, namely an approach that is based on compliance and an approach that is based on deterrence.¹²

The approach that is based on compliance focuses on ensuring that the rules and guidelines are adhered to through a discussion between the regulator (CBK) and the regulated (all the banks in Kenya). The main characteristics of the approach that is based on compliance is collaboration and persuasion. Education and consultation are also crucial ingredients within this approach, as they boost the communication and provide the regulated with an environment in which they can determine the way regulation is designed to operate in the market place. This is thus regarded as the first way based on the discussion between the regulator and the regulated, as action of first occurrence.

¹² Singh D, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?', *Eur Bus Org Law Rev* (2015), 449.

The approach that is based on deterrence makes use of sanctions to punish those who don't comply with the required rules and codes of behaviour. This is therefore perceived as action of the last recourse.¹³

1.8 Justification of the research

The purpose of this study is to ascertain if the difference in the two periods, the period before and after the placing of Chase Bank under statutory management, could be attributed to the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13 or whether there are other factors responsible for the difference in the two periods, apart from the enforcement mechanisms employed by the CBK. Studies all over the world, especially in South Africa,¹⁴ the US¹⁵ and European Union¹⁶ have been undertaken on the enforcement mechanisms of the regulator (commonly referred to as the Central Bank). However, in Kenya the studies undertaken have mainly focused on regulations, governance within corporations, capital requirements and management of credit risk. This is a justification for undertaking the present study on the enforcement mechanisms of the CBK in the enforcement of Prudential Guideline No.13, with a case study on Chase Bank.

¹³ Singh D, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?', *Eur Bus Org Law Rev* (2015), 449-450.

¹⁴ Schmulow A, 'Financial Regulatory Governance in South Africa: The Move towards Twin Peaks' 25 *African Journal of International and Comparative Law* 3(2017), 393-417.

¹⁵ A research report from the Deloitte Center for Financial Services, 'Enforcement actions in the banking industry (Trends and lessons learned)', 2015; Barry C, Ryan F, 'Overview and Operation of U.S. Financial Sanctions, Including the Example of Iran', *Georgetown Journal of International Law* (2013), 903-913.

¹⁶ Singh D, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?', 339-465.

1.9 Methodology and Approach

This research depends mainly on the review and analysis of primary data and information obtained from interviewing the staff of the CBK, from the Bank Supervision Department (BSD). The directors and employees who had worked for Chase Bank for the two periods were not readily available to be interviewed as they had left the bank, having been taken over by SBM Bank. Moreover, they had cases pending in court and so discussing the matter would be considered subjudice. The persons interviewed from the BSD were allocated to the researcher upon making a request to that effect in writing addressed to the director of that department.

The present research also draws relevant information from the analysis of the CBK's Bank Supervision Annual Reports, CBK's Chase Bank press release and the briefing note by the former board of Chase Bank (Kenya) Limited as submitted to the Kenya National Assembly's Departmental Committee on Finance, Planning & Trade.

In terms of approach, the study is the case study of Chase Bank (now SBM Bank). This is in recognition of the fact that it is nearly impossible to do an in depth study, in a short period of time, of the enforcement mechanisms employed by the CBK to all the banks in Kenya, in the enforcement of the Prudential Guideline No.13.

1.10 Chapter Breakdown

Chapter One: Introduction

The chapter gives an aerial view of the topic in relation to the case study of the application of the Prudential Guideline No.13 to Chase Bank for the period before and after its being placed under statutory management. It also defines the key terminologies used in the thesis. It gives the background to the research problem. It focuses on the study's aim, it states the questions of research and the hypothesis, gives the theoretical framework, the justification of the study, the methodology and approach, and finally the breakdown of the chapters.

Chapter Two: Literature Review

The chapter reviews the studies undertaken in different continents on the enforcement mechanisms of the central banks as regards the enforcement of banking laws and regulations in order to make a case for undertaking the present study to fill the gap that exists in Kenya in that area.

Chapter Three: The legal background to Central Bank supervision

It gives the legal background to the Central Bank Supervision. Specifically, it highlights the different enforcement mechanisms that the Central Bank can use in ensuring that banks adhere to the laws and regulations of banking.

Chapter Four: The research findings presentation

The chapter gives the research findings of the study as per the questionnaire prepared to aid in the collection of the relevant information through interviewing the employees of CBK, specifically those from the Bank Supervision Department(BSD).

Chapter Five: Analysis of the research findings

This chapter analyses the research findings against the backdrop of the events that were happening in the banking sector at the time in the period before and after the placing of Chase Bank under statutory management. Use is made of the CBK's Bank Supervision Annual Reports from the year 2008 to 2018: a comparison of the leadership at the helm of CBK, the number of employees in the Bank Supervision Department and the number of banks detected as having not complied with the banking laws and regulations is made between the two periods.

Chapter Six: Conclusion and recommendations

The chapter focuses on the limitations of the research, answers the research questions and makes recommendations.

Chapter 2 LITERATURE REVIEW

2.1 Introduction

This research seeks to establish whether the difference in the two epochs, the epoch before and the epoch after the placing of Chase Bank under statutory management, could be attributed to the way the enforcement mechanisms were employed by the CBK in the enforcement of the Prudential Guideline No.13 or whether there are other factors responsible for the difference in the two periods. This chapter commences by looking at the different studies undertaken on the banking laws and regulations in Kenya and other jurisdictions.

2.2 Literature review

None of the studies examined below enquired into the matters mentioned above. They are covered in order to illustrate clearly the gap that exists in research carried out to date.

Mwongeli (2016)¹⁷ focused on the effect of regulations, guideline on implementation of banking laws and regulations and the prudential guidelines of the year 2013, on the financial performance of commercial banks in Kenya. The total number of banks that were covered in the study was the 43 Kenyan banks for the duration between 2010 and 2015. Three years before the reviewed Prudential Guidelines for banks of 2013 came into effect and three years after. The secondary data used was collected from the CBK as well as the banks' financial statements. The financial performance was measured by making use of the ratios of finance like return on equity, return on capital, return on assets, credit risk, liquidity ratio, interest coverage ratio, core capital to total risk weighted assets ratio, total capital to total risk weighted assets ratio and core capital to total deposit liabilities ratio. The chi square test of independence was carried out to determine the relationship between the two variables, independent variable-regulations and dependent variable- financial performance. Eight out of the

¹⁷ Mwongeli J, 'The effect of regulations on financial performance of commercial banks in Kenya' Unpublished MBA Thesis, The University of Nairobi, September 2016.

nine ratios analyzed yielded P values that caused her to accept the null hypothesis to the extent there was no correlation between performance of commercial banks in finance and regulations in Kenya. After evaluating capital adequacy, the same conclusion was arrived at as the banking sector's levels of capital had been increasing steadily over the six (6) years that were being studied. It had been expected that there would have been a major increase from 2012 to 2013 when the minimum requirement was increased from 250 million to 1 billion shillings.

Gathaiya R (2017)¹⁸ focused on the analysis of the matters afflicting crumpled banks in Kenya for the years running from 2015 to 2016. The banks that failed within the duration were Dubai Bank (DB), Imperial Bank (IB) and Chase Bank (CB). His study came to a conclusion, being, the main factors that contributed to the crumple of these institutions of banking in Kenya could be attributed to: internal lending, feeble corporate governance practices, deficient strategies of risk management, lack of internal controls, and conflict of interest.

Mohamed S, Mutegi D, and Muriuki M (2017)¹⁹ looked at the ramification of the CBK's Prudential Guidelines 2013 on the performance of commercial banks in Kenya. Specifically, they examined the ramifications of the governance of corporations, capital requirements, credit risk management, and liquidity management, independent variables, on the performance of commercial banks in Kenya, dependent variable. Questionnaires were used in collecting primary data which was done on a one to one basis as well as by way of email and which would allow the respondent to clarify any information that was not clear. The information was collected from the departments dealing with finances; credits; recovery of debts and risks and the department dealing with complying from the 43 commercial banks. Financial

¹⁸ Gathaiya R, 'Analysis of issues affecting collapsed banks in Kenya from year 2015 to 2016' *7 International Journal of Management & Business Studies* 3(2017), 9-15.

¹⁹ Mohamed S, Mutegi D, and Muriuki M, 'Effects of the Central Bank of Kenya Prudential Guidelines on the performance of Commercial Banks in Kenya' *3 Imperial Journal of Interdisciplinary Research* 9(2017), 613-626.

performance, the dependent variable, was depicted by the asset's returns (ROA) and return on equity (ROE) which were proxy indicators of banks' performance. General linear regression model and the analysis of the relationship was adopted to understand the impact and connection of the independent variables in the performance of commercial banks in Kenya. Each variable was regressed against the dependent variable which was performance and it was found that a model of multiple regression was best to establish the ramifications of the variables since they were all affecting the performance of the bank. From the study it was established that all prudential guidelines under the study had a positive correlation with the bank performance. This meant that improvement in each of the prudential guidelines also improved the bank performance.

Schmulow A (2017)²⁰ looked at the governance of regulatory in South Africa dealing with finance following its move towards twin peaks model through the enactment into law on 21st August 2017 of Financial Sector Regulation Act (FSRA). This model creates two (2) independent peak bodies of regulating namely, the Prudential Authority and the Financial Sector Conduct Authority. The Prudential Authority is accommodated within and administered by South African Reserve Bank and ensures soundness and safety in the financial system. However, the Financial Sector Conduct Authority is a separate and independent body and whose task is to stop the misconduct within the market and the consumers being taken advantage of in the financial sector.

Schmulow explored matters relating to that implementation from the point of governance as it is applied in Australia. He commenced with a discussion and an analysis of the historical development of Twin Peaks, followed by a discussion of governance. Thereafter, he analyzed the main difference of the Twin Peaks in Australia and the Twin Peaks in South Africa. Then he concluded with his

²⁰ Schmulow A, 'Financial Regulatory Governance in South Africa: The Move towards Twin Peaks' 25 *African Journal of International and Comparative Law* 3(2017), 393-417.

observations. Amongst the observations he made was that the prosperity of the regime of Twin Peaks in South Africa would depend on the effectiveness of implementation (governance) and that in turn would depend upon the goals that would be set (the principles) and on how those goals would be pursued. That in turn would depend upon market intelligence (the risks) along with the independence and the capacity of the regulators to pursue corrective action, free of interference or industry capture; co-ordination between the peaks; the resources –physical and human – which the regulators would bring to bear, and their willingness, if need be, to take on vested and powerful interests.

About two years down the line after South Africa had adopted the Twin Peaks model, the Reserve Bank of South Africa imposed regulatory sanctions on five banks and directed them to take remedial actions after it found flaws in each of the banks' control measures on money laundering subsequent to the regular inspections carried out in terms of the Financial Intelligence Centre (FIC) Act. The 5 banks were the Standard Bank, GroBank, Ubank, Bank of China, Johannesburg Branch and HBZ Bank.²¹

Deloitte Center for Financial Services (2015)²² carried a study of the Enforcement Actions (EAs) promulgated in US from January 1, 2000 through August 27, 2015. The study concentrated on questions of research: How recent trends in EAs in the banking industry compared with historical norms; How the composition of EAs differed by banking supervisor; How the mix of EAs changed for institutions of different sizes; and what issues led to the issuance of EAs, especially the more severe ones. The findings were that: The statistical numbers of actions of enforcement and strictness were equalizing at historic levels, but the related fines had increased markedly since

²¹ 'Sizwe Dlamini: SA Reserve Bank imposes administrative sanctions on five banks' *Independent Online*, 20 December 2019 <https://www.iol.co.za/business-report/economy/sa-reserve-bank-imposes-administrative-sanctions-on-five-banks-39543889> on 27 April 2020.

²² A research report from the Deloitte Center for Financial Services, '*Enforcement actions in the banking industry (Trends and lessons learned)*', 2015.

2010; The composition of enforcement actions reflects differences in supervisory mandates. The Federal Deposit Insurance Corporation's (FDIC's) style of supervising is more direct than that of other regulators; even though the number of enforcement actions has reduced since 2010, their constitution differs from the years before 2008 for all institution sizes; and failures in the practices of servicing mortgage servicing and Bank Secrecy Act (BSA) adherence triggered many severe EAs for huge institutions. On the other hand, EAs against mid-sized institutions were typically driven by concerns regarding financial safety and soundness of the institution/Bank Holding Company (BHC).

Barry C, Ryan F (2013)²³ looked at the aerial view and operation of United States sanctions that are financial in nature, incorporating Iran as an example. They defined sanctions as the intentional, government-influenced removal, or threat of removal, of customary trade or financial relations for foreign policy or national security goals. They established that financial sanctions of U.S. are established by United States legislations and Executive Orders, and are generally realized through regulations. The Office of Foreign Assets Control (OFAC) in the U.S. Department of the Treasury (Treasury), in consultation with the U.S. Department of State and sometimes other federal agencies, generally has primary responsibility for implementing these financial sanctions. They established that the sanctions on finance focused on the flow of funds and other forms of value to and from a target country, corporation, individual, or other entity. They found that these sanctions could have a wide impact because they could not only freeze financial assets and prohibit or limit financial transactions, but they could also impede trade by making it difficult to pay for the export or import of goods and services. Financial sanctions were often used in tandem with trade and other sanctions to maximize their impact. Barry and Ryan established that from the middle of 1990s, several financial institutions had used as "best practice" advanced OFAC software of screening to buttress their surveilling and reporting

²³ Barry C, Ryan F, 'Overview and Operation of U.S. Financial sanctions, Including the Example of Iran' 44 *Georgetown Journal of International Law* (2013), 903-913.

systems. They also established that over and above institutions reporting themselves, transactions that are illegal are detected during adherence procedures tests, audits done internally, routine physical examinations of banks, investigations by OFAC, and by sources revealing in confidence.

Barry and Ryan established that in the event an illegal transaction comes to the knowledge of OFAC as having been carried out through a financial institution of the United States without being prevented or refused, OFAC may send an administrative subpoena to the particular institution demanding information of how such a transaction was undertaken. Upon ascertainment by OFAC that a contravention has taken place, OFAC may issue a warning letter, levy penalties that are civil in nature, or present the issue to agencies that enforce the law to take it up criminally. Millions of dollars in the range of hundreds have been levied by OFAC as penalties in the civil realm against both financial institutions of the United States and companies and foreign financial institutions for failure to properly stop or refuse or for deceiving the United States financial institutions into carrying out unauthorized transfers including National Specially Designated (SDN) or targeted country.

Singh D (2015)²⁴ in his research on the centralized supervision and financial regulation of, and whether a single handbook of enforcement was, looked at the pertinent features of an enforcement model. He proposes that the way to regulate required looking into how to undertake the job of regulation and how well to see to it that its requirements are adhered to by those who are regulated. He proposes that the generally known way to regulate is the way based on some kind of risk. He proceeds to suggest that the limited resources available to carry out the regulatory and supervisory task means that arrangements need to be made in advance about how the limited resources will be apportioned and how the aims of regulation will be attained. Singh further proposes that the requirement for sufficient resources cannot be

²⁴ Singh D, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?' *Eur Bus Org Law Rev* (2015), 439-465.

disregarded as it will dictate the ability of the regulator to probe and evaluate the scope of the likelihood of contravention of the rules. There is also the need to see to it that regulators are capable of coming up with additional rules and guidelines to include and supervise new kinds of innovations in the industry which go beyond the usual lines of business. These issues will have an impact directly on the manner in which the regulations are implemented. Undoubtedly, the complications of the modern society, and those participating in it, need a more sophisticated approach to implementation that addresses the distinctive nature of the way people and business organizations adhere to the rules. He goes on to say that the extensive effects, economically and socially, of the manner to implement and enforce decisions should also be considered carefully by the regulator. The level of clearness of the decisions to be enforced also requires some consideration with the recognition that exposing all the decisions to be enforced may not yield the desired results. Thus, it is necessary for the regulator to evaluate whether the scope of the available sanctions are appropriate to address the various kinds of nonconformity that can have an impact on the regulator.²⁵

Singh proposes that the model of enforcement has to ensure that it has two important ingredients incorporated into the design, being an approach that is based on compliance and an approach that is based on deterrence. Ensuring adherence to the regulations needs the two kinds of approaches to enforcing abiding by the regulation. The two ways of enforcing can be explained as diametrically opposed sides of continuous compliance. The approach that is based on compliance is centered on ensuring rules and codes are adhered to by way of a discussion involving the regulator and the regulated. The main characteristics of a way that is based on compliance are persuasion and cooperation. Education and consultation are also necessary ingredients within this way, as they boost the exchange of information and afford the regulated with an atmosphere in which they can shape the manner in which

²⁵ Singh D, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?', 449.

regulation is intended to function in the market place. Thus, it is regarded as the first way grounded on a discussion involving the regulated and the regulator, as a response of first occurrence. However, the way that is based on deterrence is to be regarded as making sure regulations are adhered to by negative means at the opposite end of the array of the way that is based on compliance, by means of punishment and sanction. The way of deterrence makes use of the punishments to punish failure to comply with the necessary regulations and codes of conduct. It is thus seen as action of the last recourse.²⁶

Singh's research was centered on the attributes of an enforcement model within the context of the European Union, as applied by the European Central Bank (ECB). The present research also focuses on the enforcement model but within the context of Kenya, as applied by the CBK on CB.

2.3 Conclusion

From the literature review above it is evident that studies have been undertaken on the enforcement mechanisms of the central banks in the enforcement of banking laws and regulations in South Africa, US and Europe. Such a study is yet to be undertaken in Kenya. This is a justification for undertaking the present study on the enforcement mechanisms of the CBK in the enforcement of Prudential Guideline No.13, with the case study of Chase Bank.

²⁶ Singh D, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?', 449-450.

Chapter 3 THE LEGAL BACKGROUND TO CENTRAL BANK SUPERVISION

3.1 Introduction

The chapter highlights the regulations and laws of banking, and the different enforcement mechanisms at the disposal of the CBK.

3.2 Banking laws and regulations

One of the mandates of CBK is advancing the liquidity, solvency and suitable operation of a system of finance that is based on a market. The CBK carries out its mandate to check whether the system is working properly. To assist the financial system to operate as it should, the CBK:²⁷

- a) Comes up with guidelines, regulations and laws that are relevant to guide the banking sector players.
- b) Continuously reviews guidelines, regulations and laws in the banking sector to see to it their applicability being relevant to the atmosphere of operation. These comprise the CBK Act (Cap 491), the Banking Act (Cap 488), the Kenyan Deposit Insurance Act 2012, Prudential Guidelines 2013 and the Regulations issued thereunder.
- c) Licenses the banks, the financial institutions that are non-banks, companies that deal in mortgage finance, the bureaus of reference in credit matters, the bureaus of exchanging foreign currencies, the providers of remittance of money and the banks that are microfinance.
- d) Inspects the banks that are commercial in nature, the banks that are microfinance, the financial institutions that are non-bank, the companies that deal in mortgage finance, the building societies, the bureaus of credit reference, the bureaus of foreign exchange, the providers of remittance of money and the offices representing foreign banks to see to it their abiding to all the applicable guidelines,

²⁷<https://www.centralbank.go.ke/bank-supervision/> on 12 April 2019.

regulations, and laws and safeguard the depositors interests and the interests of the banking sector's other users.

- e) Analyses the reports that are financial in nature and the other returns from the players in the banking sector to see to it that they adhere to the applicable guidelines, regulations and laws.
- f) Contributes to initiatives that foster financial inclusion.

The relevant parts of guidelines, regulations and laws of banking directing stakeholders in the sector of banking are summarized below:

3.2.1 The CBK Act (Cap491)

This is the statute that establishes the CBK²⁸ and provides for its operation and establishes the Kenyan currency and for matters akin to and associated thereto.²⁹ The CBK is not subject to Companies Act or the sections of the Banking Act.³⁰

The functions and objects of the CBK are:³¹

- a) To come up with and to actualize the policy of money aimed at realizing and sustaining stability of prices generally.
- b) To advance the liquidity, solvency and suitable operation of a balanced system of finance that is based on market.
- c) To buttress the plan of the government in the area of the economy not to mention its purpose for employing and growing.
- d) To come up with and to actualize the policy for foreign exchange.

²⁸Section 3(1), *Central Bank of Kenya Act (Cap 491)*

²⁹Purpose of the Act of Parliament: *Central Bank of Kenya Act (Cap 491)*

³⁰Section 3(5), *Central Bank of Kenya Act (Cap 491)*

³¹Section 4, 4A, *Central Bank of Kenya Act (Cap 491)*

- e) To manage and hold its reserves for foreign exchange.
- f) To issue license to permitted dealers and to supervise them.
- g) To come up with and to actualize the specific policies that very well promote the institution, supervision and regulation of effective and efficient settlement, payment and systems for clearance.
- h) To act as an adviser and banker to, and the Government's fiscal agent; and
- i) To issue Kenyan currency in the form of notes and coins.

3.2.2 Prudential Guidelines and Regulations

By virtue of s. 33, ss.4³² of the Banking Act, CBK is empowered to provide the directives to be followed by banks so as to realize a financial and system of banking that is steady and efficient.

The Prudential Guidelines and Regulations currently in place is the Prudential Guidelines 2013. The Prudential Guidelines 2013 became operational on 1st January 2013.³³ They replaced Regulations Guidelines and Laws on Enforcement of Banking issued on 1st January 2006.³⁴

The Prudential Guidelines 2013 are for institutions that are licensed under the Banking Act (Cap.488). They provide guidelines on different aspects relating to the said

³² "... (4) The Central Bank may issue directions to institutions generally for the better carrying out of its functions under this Act and in particular, with respect to-

- a) The standards to be adhered to by an institution in the conduct of its business in Kenya or in any country where a branch or subsidiary of the institution is located; and
- b) Guidelines to be adhered to by institutions in order to maintain a stable and efficient banking and financial system".

³³ Prudential Guidelines 2013, 328, para.3.1.

³⁴ Prudential Guidelines 2013, 328, para.3.2.

institutions. The said guidelines are simply referred to as the CBK Prudential Guidelines (CBK/PG) and they range from PG number 1 to PG number 22.

3.3 The enforcement mechanisms

The enforcement mechanisms of the CBK are provided for within the Prudential Guidelines 2013, under the CBK Prudential Guideline No.13.³⁵

As already stated herein above, the directive on the implementation of regulations and laws of banking is issued under s. 33, ss.4 of the Banking Act, which authorizes the CBK to issue directives to be followed by banks so as to realize a financial and system of banking that is steady and efficient.³⁶ The objective of the directive is to avail information and direction to the industry of banking on the way that the CBK will take in releasing corrective orders and prompt supervisory directives to institutions. The actions of supervisory enforcement incorporated in the Guideline have tried to put forward the practices of banking, terms, and contraventions of law giving rise to the specific weaknesses and problems identified, commonly through on- site examinations. The actions of supervisory enforcement are also to be used to avail a lay out of clear-cut remedial/corrective measures, incorporating suitable timelines and goals for the attainment of compliance. The particular ways of action of enforcement which may be taken into consideration for application by the CBK are to be conveyed to every institution at the time of need.³⁷

The succeeding conduct will be used if, generally, the institutions' management liable for such conduct has manifested a neglect for sound and safe practices of banking and/or the unwillingness or ability to make right the problems or weaknesses without the external help. The actions of enforcement contained in the guideline do not cover

³⁵Prudential Guidelines 2013, 323, para.1.1.

³⁶Prudential Guidelines 2013, 323, para.1.2.

³⁷Prudential Guidelines 2013, 323, para.1.3.

everything and CBK is free to suggest any action for correction that it deems proper in view of the failures/contraventions being dealt with:³⁸

3.3.1 Resolutions of the Board

The CBK may demand an institution's Board to pass decisions which are an undertaking or responses from institutions that show supervisory concerns, where such conduct clearly demonstrates the commitment of a board to take quick actions to make right the contraventions or the weaknesses. The aforementioned resolutions should give the period within which adherence will be achieved.³⁹

3.3.2 Letter of Commitment

The CBK can write to the board of directors of an institution laying out particular actions of correction to be followed by the management of the bank which should be acknowledged and executed by the directors of the bank demonstrating their willingness to follow the particular recommendations. The matters brought up will have been established by it through off-site surveillance or on-site inspection. The executed initial write up should be taken back to the Department of Supervision within a period of thirty days and a copy of the same maintained by the institution for record purposes.⁴⁰

3.3.3 The MOU

An agreement in writing can be introduced by the CBK outlining the particular remedial/corrective actions to be carried out by the board of a bank. Failing by the board of directors to abide within the particular period of time specified could lead to a further action which is legal in nature. The flaws that need to be corrected will also have been established by means of either off-site or on-site supervision.⁴¹

³⁸Prudential Guidelines 2013, 323.

³⁹Prudential Guidelines 2013, 323, para.2.1.

⁴⁰Prudential Guidelines 2013, 323-324, para.2.2.

⁴¹Prudential Guidelines 2013, 324, para.2.3.

3.3.4 Directives issued

The following actions of correction are allowed by S. 33 (1) of the Banking Act if the CBK has reason to think that:⁴²

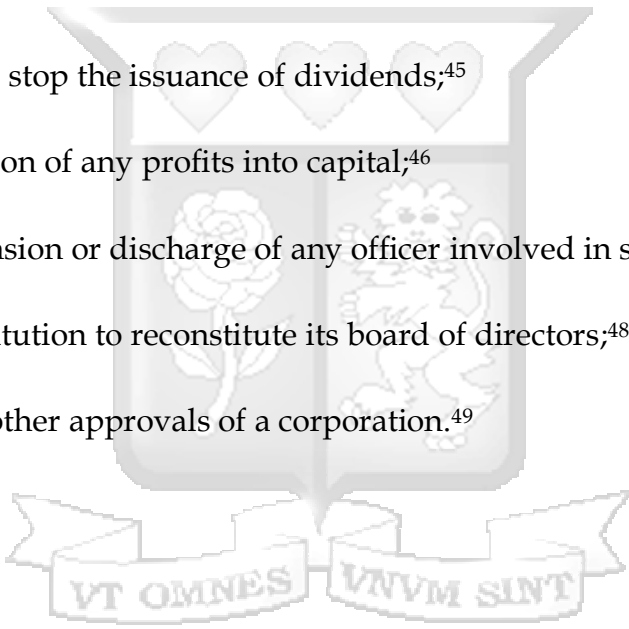
- a) The activities of an institution are being carried out in a way in contravention to or without following the demands of the Act or any guideline made there under or in any way prejudicial to or not in favour of the members of the public or its own; or
- b) If any officers of a bank or other person taking part in the general running of an institution or the institution itself is involved in any conduct that is likely to lead to a violation of particular sections of the Act or any regulations passed pursuant to the Act, the CBK may:
 - i. **Proffer advice** and make propositions to the institution in relation to the way it carries out its business in general;
 - ii. **Provide guidance** in relation to the actions to be employed to better the management or methods of business or to attain or better the adherence with the provisions of the regulations and the law;
 - iii. **Provide guidance**, in S.33, ss. (1) (b), to an officer, institution, or any person to **stop such conduct**;
 - iv. **Nominate an individual** to advise and help the institution in general or with the aim of putting into action any guidance issued within (i) and (ii) above and such person's advice shall have the same force and effect as a guidance and shall be taken to be a guidance issued by CBK.

⁴²Prudential Guidelines 2013, 324, para.2.4.

Nonetheless, before the above action is taken, notice of intention is given to an institution or an officer as the circumstances may be, to justify why such a guidance should not be given.⁴³

3.3.5 Discharge of Officers and Withholding of Corporate Approvals

The ensuing actions of correction are allowed by S.33A of the Banking Act and may be given where an auditor's report, in s.24 (4) of the Banking Act or a report of inspection in Part VII of the Banking Act shows that an institution carries out its affairs in contravention to the sections of the Act or any regulations issued under it or in any way prejudicial to or not in favour to the members of the public or its own depositors:⁴⁴

- 
- a) Limit, hold off or stop the issuance of dividends;⁴⁵
 - b) Stop the conversion of any profits into capital;⁴⁶
 - c) Direct the suspension or discharge of any officer involved in such behaviour;⁴⁷
 - d) Demand the institution to reconstitute its board of directors;⁴⁸
 - e) Deny branch or other approvals of a corporation.⁴⁹

⁴³Prudential Guidelines 2013, 325.

⁴⁴Prudential Guidelines 2013, 325, para.2.5.

⁴⁵ Section 33A (a), *Banking Act* (Cap.488)

⁴⁶ Section 33A (b), *Banking Act* (Cap.488)

⁴⁷ Section 33A (c), *Banking Act* (Cap.488)

⁴⁸ Section 33A (d), *Banking Act* (Cap.488)

⁴⁹ Section 33A (e), *Banking Act* (Cap.488)

3.3.6 Intervention of CBK in the running of an institution

Actions of correction actions are permitted within S. 34 of the Banking Act by the CBK if:⁵⁰

- a) The institution declines to discharge any obligation that is financial in nature, when it becomes due, not to mention payment of an individual who has banked with the institution;
- b) A suit is instituted, or a resolution proposed, for the winding up of the institution or if any receiver or receiver and manager or similar officer is nominated;
- c) The auditor avails a report to CBK under ss.4 of s. 24;⁵¹ or
- d) The CBK finds out or becomes aware of any fact or circumstance which warrants the exercise of the proper power to the benefit of an institution's depositors or other creditors or the institution itself.
- e) If the institution is quite undercapitalized; or

⁵⁰Prudential Guidelines 2013, 325.

⁵¹"... 24 (4) If the auditor of an institution, in the course of the performance of his duties under this Act, is satisfied that: -

- a) There has been a serious breach of or non-compliance with the provisions of this Act, the Central Bank of Kenya Act or the regulations, guidelines or other matters prescribed by the Central Bank;
- b) A criminal offence involving fraud or other dishonesty has been committed by the institution or any of its officers or employees;
- c) Losses have been incurred which reduce the core capital of the institution by fifty per cent or more;
- d) serious irregularities have occurred which may jeopardize the security of depositors or creditors of the institution; or
- e) He is unable to confirm that the claims of depositors and creditors of the institution are capable of being met out of the assets of the institution,
he shall immediately report the matter to the Central Bank."

f) If the institution fails:⁵²

- i. To avail a plan to restore capital or a plan to resolve all the flaws as provide in S.33A;⁵³ or

⁵²Prudential Guidelines 2013, 325-326.

⁵³ "Where an auditor's report, under section 24(4) or an inspection report under this Part reveals that an institution conducts its business in a manner contrary to the provisions of this Act, or in any manner detrimental to or not in the best interests of its depositors or members of the public, or that an institution is undercapitalized, the Central Bank may: -

- a) restrict, suspend or prohibit the payment of dividends by the institution;
- b) prohibit the conversion of any profits of the institution into capital;
- c) direct the suspension or removal of any officer involved in such conduct from the service of the institution;
- d) require the institution to reconstitute its board of directors in accordance with the criteria set out in the First Schedule;
- e) withhold branch or other corporate approval with respect to such institution;
- f) undertake more frequent inspections of that institution;
- g) order the institution to submit to the Central Bank, within forty-five days, a capital restoration plan to restore the institution to the capital adequacy prescribed in section 18, or, in the case of issues unrelated to capital, a plan to resolve all deficiencies to the satisfaction of the Central Bank;
- h) prohibit the institution from awarding any bonuses or increments in salary, emoluments or other benefits to the directors and officers of the institution;
- i) at the expense of the institution, appoint a person suitably qualified and competent, in the opinion of the Central Bank, to advise and assist the institution in designing and implementing a capital restoration plan or other corrective action plan under paragraph (g), and the person appointed shall regularly report to the Central Bank on the progress of the plan;
- j) impose restrictions on growth of assets or liabilities of the institution as it deems fit;
- k) restrict the rate of interest on savings and time deposits payable by the institution to such rates as the Central Bank shall determine; or

- ii. To increase capital, and it declines, neglects, or refuses to adhere to an order or to put into action a correction plan.

The following actions of correction may be taken:⁵⁴

- i. **Nomination of a person (Manager)** to take up the management, conduct and control of the affairs and business of an institution without the involvement of its board of directors;
- ii. **Removal of an employee or an officer** that occasioned or contributed to any violation of the Act or any regulations made within the Act or to any decline in the financial stability of the institution or has been guilty of behaviour prejudicial to the depositors' interests or other creditors;
- iii. **Nomination of a qualified person** to the board of directors of the institution to assume office as a director who cannot be removed from office without the approval of CBK; and
- iv. **Revocation or cancellation of current power of attorney**, appointment, mandate or other authority by the institution in favour of any officer or employee or any other person.
- v. **Limitation of the institution** from being involved in new business of foreign exchange;
- vi. **Constraining of the institution** from being involved in new transactions off the balance sheet; and
- vii. **Constraining of the institution** from employing new agents or directing the institution to cancel any agency arrangement.

-
- l) order the institution to do any or take such other actions as it may deem necessary to rectify a capital deficiency or other weaknesses.”

⁵⁴Prudential Guidelines 2013, 326.

3.3.7 Dismissal of Directors and Officers and imposition of Penalties

Where an institution violates any of the sections of the Banking Act, the CBK may exact any of the following conditions/actions:⁵⁵

- a) Joint and several liabilities of officers to compensate the institution against any loss emanating from giving money, loan or credit facility in violation of the applicable section;
- b) Direct the removal of a director and/or direct the suspension of any officer or employee who authorised the advance, loan or credit facility.
- c) Imposition of penalties in line with s. 55, ss.2⁵⁶ of the Banking Act.
- d) Failure to comply may also lead to an action of enforcement as stipulated within the various sections of the Banking Act.

3.3.8 Cancellation of Banking License

By virtue of the Banking Act s.6, the CBK may, by not less than twenty-eight days' notice in writing to the institution, cancel the license of an institution if the institution:⁵⁷

- a) Stops carrying on business in Kenya or goes into liquidation or is wound up or is otherwise dissolved; or

⁵⁵Prudential Guidelines 2013, 326-327, para.2.7.

⁵⁶ "...55(2) Without prejudice to the generality of subsection (1), the Minister may, in regulations, prescribe penalties to be paid by institutions or credit reference bureaus which fail or refuse to comply with any directions of the Central Bank under this Act, which shall not exceed one million shillings in the case of an institution, or credit reference bureau, or one hundred thousand shillings in the case of a natural person, and may prescribe additional penalties not exceeding ten thousand shillings in each case for each day or part thereof during which such failure or refusal continues.

⁵⁷Prudential Guidelines 2013, 327, para.2.8.

- b) Declines to adhere to the Banking Act, the CBK Act, or other regulations, rules, orders or directions given in line with the said Acts or any condition of its license as established by means of off-site surveillance or on-site inspection.

The guideline provides that, as a pragmatic issue, the cancellation of a bank's license should be quickly followed by closure and the initiation of liquidation proceedings.

3.3.9 Discontinuation of Deposit Protection

By virtue of the Banking Act s.38, ss.5, where it becomes apparent to the Kenya Deposit Insurance Corporation (KDIC) that the businesses of a bank are being carried out in a way prejudicial to the bank's own interest or to the interests of the bank's depositors, the KDIC may:⁵⁸

- a) Raise the premiums (to the KDIC) of that institution; or
b) Discontinue the protection of its deposits.

3.3.10 Corrective Action Guideline (CBK/PG/21)

Further to the measures listed above and or sanctions, the CBK may take such action of correction and/or enforcement as it considers essential and as stipulated for in the Guideline for Central Bank on Prompt Corrective Action Guideline.⁵⁹ The Guideline on Prompt Corrective Action is relevant to every institutions that are licensed within the Banking Act (Cap.488)⁶⁰ and is given under Ss. 33 and 34 of the Banking Act, which authorizes the CBK to issue Guidelines to be followed by institutions in order to maintain a financial and banking system that is steady and efficient.⁶¹

Prompt Corrective Action (PCA) is a supervisory action framework of progressively strict actions of enforcement that are used to institutions that frequently contravene

⁵⁸Prudential Guidelines 2013, pg.327, para 2.9.

⁵⁹Prudential Guidelines 2013, pg.327, para.2.10.

⁶⁰Prudential Guidelines 2013, pg.468, para.1.2.

⁶¹Prudential Guidelines 2013, pg.468, para.1.3.

laws and regulations, decline to follow prudential guidelines or regulations or in some other way operate in an unsound and unsafe way. These actions become progressively strict as an institution falls within lower capital categories. Some actions of supervision associated with quick action of correction are compulsory; that is, the actions instantly apply to the institution as it is classified in a particular category. Other actions of supervision associated with prompt corrective action are not compulsory as they are levied by the CBK through a series of remedial actions to be carried out by an institution to deal with problems while they are still of a size that can be managed.⁶²

An institution shall be subject to PCA whenever any or all of the following conditions occur:⁶³

- 1) When it fails to attain the requirements of capital stipulated in s.18⁶⁴ and/or the 2nd schedule (section 7) of the Banking Act;
- 2) The CAMELS system (Capital Adequacy, Asset Quality, Management, Liquidity and Sensitivity to market risk) composite rating is less than “3” and Management component rating of less than “3”;

CAMELS⁶⁵ a system of rating that is internationally recognized as a tool of supervision which was developed in the United States to measure the level of risk of banks or other financial institutions aided by its statements of finance. The criterion used for judgement is made up of capital adequacy, asset quality, management, earnings, liquidity and sensitivity. The CAMELS system of rating

⁶² Prudential Guidelines 2013, 469-470, para.3.1.

⁶³ Prudential Guidelines 2013, 470, para.3.1.

⁶⁴ “The Central Bank may prescribe the minimum ratios which shall be maintained by institutions as between their core capital and total capital on the one hand and their assets (including their total loans and advances) and off balance sheet items on the other and, for that purpose, may also determine the method of classifying and evaluating assets.”

⁶⁵ <https://theinvestorsbook.com/camels-rating-system.html> on 26 January 2020.

is adopted as a tool for establishing the strengths and weaknesses of the various financial institutions and rating their performance in the economy by the supervisory authorities of a country. CAMELS numerical rating explains the financial position of the institutions and marks out the areas of improvement:

1 is “Strong”: The financial institutions that are rated top are those which range between a rating of 1.0 to 1.4; they have the most conducive financial, operational and managerial conditions.

2 is “Satisfactory”: The banks which are suitable but have some established weaknesses and are rated between 1.5 to 2.4.

3 is “Less Than Satisfactory”: These financial institutions are rated between 2.5 to 3.4 and need supervisory concern to surmount several financial, operational and managerial weaknesses.

4 is “Deficient”: The banks or other financial institutions which lie between a range of 3.5 to 4.4 are at an alarming stage. It pertains a lot of economic weaknesses which may result to loss or risk of failure.

5 is “Critically Deficient”: The most inferior rating is between 4.5 to 5. Here, the financial institutions have critical financial weaknesses and need serious attention; otherwise, it will lead to a high degree of failure.

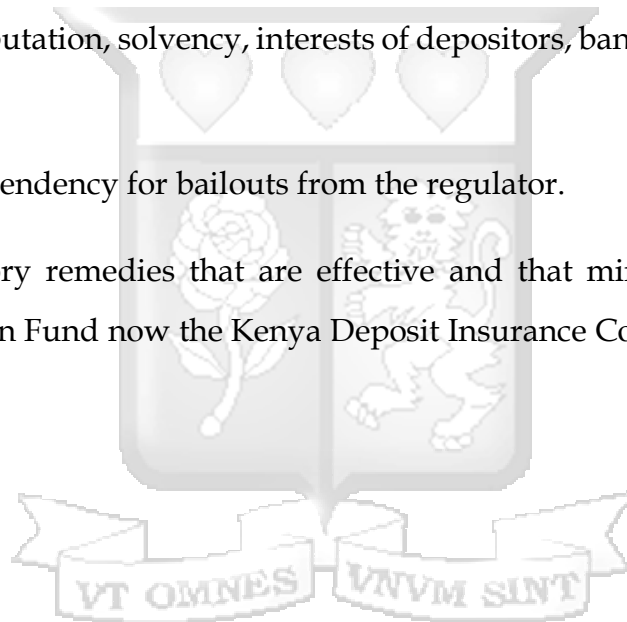
3) A severe supervisory concern has been established that places the institution at more than normal risk of failure in the opinion of the CBK. Such concerns could include, but are not limited, to any one or a combination of the following:

- a) Discovery of unsound and unsafe activities that could negatively affect the depositors’ interest and/or creditors;
- b) A discovery of repetition of violations of law or the continuing failure to adhere to the CBK Directives; and
- c) Serious reporting errors that materially misrepresent the institution’s financial condition.

4) The institution's general composite risk rating is high while the quality of risk management is weak.⁶⁶

The aim of enforcing PCA is to see to it that institutions under the purview of the CBK:⁶⁷

- a) Abide by the Banking Act, regulations and guidelines issued thereunder.
- b) Carry out business in a sound, safe & approved way thus improving the efficiency of the financial sector.
- c) Keep a financial condition that is sound.
- d) Safeguard the reputation, solvency, interests of depositors, banking system, and the public.
- e) Diminish the dependency for bailouts from the regulator.
- f) Afford supervisory remedies that are effective and that minimize losses to the Deposit Protection Fund now the Kenya Deposit Insurance Corporation (KDIC).



⁶⁶ <https://theinvestorsbook.com/camels-rating-system.html> on 26 January 2020.

⁶⁷ Prudential Guidelines 2013, 470, para.3.2.

Chapter 4 THE RESEARCH FINDINGS PRESENTATION

4.1 Introduction

The chapter outlines the research findings of the research undertaken.

4.2 The regulations and laws that govern the operations of banks in Kenya

From the interviews conducted, it emerged that the regulations and laws that govern the operations of banks in Kenya are those stated in **Chapter Three: The legal background to Central Bank Supervision; 3.2 Banking laws and regulations**. These laws and regulations comprise: the CBK Act, the Banking Act, Prudential Guidelines 2013, and Regulations and Guidelines pursuant to the Banking Act. In addition to the above laws, the Consumer Protection Act was also stated as governing the operations of banks in Kenya.

4.3 Mechanisms used by CBK in the implementation of laws and regulations of banking

The interviews revealed that the mechanisms employed by CBK in the implementation of laws and regulations of banking are mainly administrative sanctions such as fines and penalties⁶⁸, Prompt Corrective Action (PCA) and if a banking institution and its officials prove difficult then its license can be revoked and the officials or management disqualified from holding management positions⁶⁹ and sued in a court of law.

4.4 The on-site and off-site supervision methods used by the CBK in the implementation of laws and regulations of banking

It emerged from the interviews that the off-site and on-site supervision methods used by CBK in the implementation of regulations and laws of banking are similar. The methods and tools used are the Prudential Guidelines, monthly returns, quarterly unaudited financial statements and audited annual financial statements, which must

⁶⁸ Sections 49, 50, 55(2), *Banking Act* (Cap.488)

⁶⁹ Section 48, *Banking Act* (Cap.488)

adhere to the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS), forensic audits etc.

4.5 The changes in the enforcement mechanisms utilized by CBK since the placing of Chase Bank (now SBM Bank) under statutory management and its re-opening in the year 2016

The interviewees indicated that the tools, instruments and mechanisms utilized by the CBK in the implementation of regulations and laws of banking since the putting of Chase Bank (now SBM Bank) under statutory management and its re-opening in the year 2016 are the same ones used before its closure and placing under statutory management. The only difference is that the operational rigour has changed following the sagas of Imperial Bank and Chase Bank and this has made the employees of the Supervision Department of CBK (BSD) more effective.

Moreover, there has been strategic hiring of employees of the Supervision Department (BSD) of CBK. People with skills and knowledge in the areas of forensic audit, information and communications technology (ICT), accounting, mathematics etc., that are necessary for the operations in the said department are hired. Furthermore, for the purpose of upskilling, continuous training of the staff members is carried out in the areas that are emerging such as cyber security, money laundering, artificial intelligence etc. This has made the Bank Supervision Department effective in its functions.

Furthermore, the CBK through its Supervision Department (BSD) apart from just ensuring that banks comply with prudential guidelines and the various provisions of the Banking Act by submitting the required quarterly and annual reports, the BSD analyses those reports to ensure that they are in tandem with the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS) and that they reflect a true and fair account of the banks financial position. By doing the aforesaid, the role of the CBK has shifted from just that of oversight to proper supervision of banks and their operations. This has largely contributed to its effectiveness.

4.6 The reforms that would make the CBK more effective in its enforcement of the banking laws and regulations

The persons interviewed stated that the laws and regulations in place are enough for the proper operation of the CBK. Therefore, there is no need for new laws except maybe in the new emerging areas such as cyber security.⁷⁰ The traditional banking can be effectively controlled by CBK using the enforcement mechanisms already in place, to implement the laws and regulations of banking.

The current regime of the CBK has the tools which were available to the previous regimes. However, unlike the previous regimes, the current regime is willing to interpret and enforce the banking laws and regulations fearlessly.⁷¹ This has prevented the moral hazard risk from rising. The moral hazard risk rises when banks know that they can get away with the contravention of the banking laws and regulations.

4.7 The submission of the auditors' report by the auditors of Chase Bank for each of the years from the year 2013 up to the time of its closure on 7th April, 2016

The auditors of Chase Bank were Deloitte. They gave unqualified reports from the years 2013 up to the year 2015. However, in the year 2016 they gave a qualified report because the issue of insider lending had reached a point of materiality and so posed a risk.⁷²

⁷⁰ Singh D, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?', *Eur Bus Org Law Rev* (2015), 449, "...There is also the need to ensure that regulators are able to develop further rules and guidelines to capture and oversee new forms of industry innovations which transcend traditional forms of business lines..."

⁷¹ 'Exotic holidays, gifts and the \$ 380 million fraud that brought down a Kenyan bank' *Quartz Africa*, 16 December 2016 <https://qz.com/africa/864182/exotic-holidays-gifts-and-the-380-million-fraud-that-brought-down-a-kenyan-bank/> on 25 January 2020.

⁷² "...Chase Bank's restated figures showed it had under-reported insider loans by a whopping sh8 billion, casting doubts over the financial health of the lender, which also reported a surprise sh743 million loss..." 'How Deloitte audit row caused a run on Chase Bank' *Business*

4.8 Whether the Central Bank of Kenya at any one time required Chase Bank, to pass Board Resolutions, to get into an MOU, to take corrective/remedial actions or it issued directives to Chase Bank as per s. 33(1) of the Banking Act in between from the year 2013 up to the time of its closure on 7th April, 2016

The persons interviewed stated that the Central Bank of Kenya did not require Chase Bank at any one time in between the year 2013 up to the time of its closure on 7th April, 2016 to pass Board Resolutions, to get into a Memorandum of Understanding, to take corrective/remedial actions or issue directives to Chase Bank under s. 33(1) of Banking Act which provides:

“ If, at any time, the Central Bank has reason to believe that –

- (a) the business of an institution is being conducted in a manner contrary to or not in compliance with the requirements of this Act or of any regulations made thereunder or in any manner detrimental to or not in the best interests of its depositors or members of the public; or
- (b) an institution, any of its officers or other person participating in the general management of the institution is engaged in any practice likely to occasion a contravention of any of the provisions of this Act or any regulations made thereunder,

the Central Bank may –

- (i) give advice and make recommendations to the institution with regard to the conduct of its business generally;
- (ii) issue directions regarding measures to be taken to improve the management or business methods of the institution or to secure or improve compliance with the

Daily, 14 April 2016 <https://www.businessdailyafrica.com/corporate/How-Deloitte-audit-row-caused-a-run-on-Chase-Bank/539550-3158416-7k4ijn/index.html> on 26 January 2019.

requirements of this Act, any regulations made thereunder or any other written law or regulations;

(iii) in any case to which paragraph (b) applies, issue directions to the institution, officer or other person to cease such practice;

(iv) appoint a person, suitably qualified and competent in the opinion of the Central Bank, to advise and assist the institution generally or for the purposes of implementing any directions under subparagraphs (ii) and (iii) and the advice of a person so appointed shall have the same force and effect as a direction made under subparagraphs (ii) and (iii) and shall be deemed to be a direction of the Central Bank under this section.”

Moreover, Chase Bank had good loan books and good deposit books. The case of the fall of Chase Bank they said could just be summarized as one of simple fraud influenced by greed. The issue of Musharakah⁷³ products they said was just an excuse. The directors of Chase Bank lend themselves colossal sums of money which could not be secured by their salaries and allowances, as would be expected in insider loans under s. 11(1)(c)(d) and (e) of the Banking Act which provide:

(1) An institution shall not in Kenya –

...

(c) grant or permit to be outstanding any unsecured advances in respect of any of its employees or their associates; or

⁷³ The financier and the client get into a contractually designed joint ownership of a property or undertake a joint commercial enterprise. The profits and losses are shared in an agreed ratio. 'Jaafar S Abdulkadir: Kenya can use Islamic finance to unlock mortgage market' *Business Daily*, 24 July 2016 <https://www.businessdailyafrica.com/analysis/539548-3308676-6yvdxqz/index.html> on 8 December 2019.

(d) grant or permit to be outstanding any advances, loans or credit facilities which are unsecured or advances, loans or credit facilities which are not fully secured –

(i) to any of its officers or significant shareholders or their associates; or

(ii) to any person of whom or of which any of its officers or significant shareholders has an interest as an agent, Director, manager or shareholder; or

(iii) to any person of whom or of which any of its officers or significant shareholders is a guarantor; or

(e) grant or permit to be outstanding any advance, loan or credit facility to any of its directors or other person participating in the general management of the institution unless such advance, loan or credit facility –

(i) is approved by the full board of directors of the institution upon being satisfied that it is viable;

(ii) is made in the normal course of business and on terms similar to those offered to ordinary customers of the institution, and the institution shall notify the Central Bank of every approval given pursuant to subparagraph (i) of this paragraph, within seven days of such approval; or...”

The insider loans were used to purchase properties which were registered in the names of the directors and their companies instead of being jointly owned with the bank as is always the case when it comes to Musharakah products. The income and proceeds from those properties purchased using the insider loans never found their way back into the bank to service the loans. Instead they went to the personal accounts of the directors.

Despite the aforesaid, the situation of Chase Bank could have been salvaged. However, due to the bank run which was occasioned by the information in the social media which painted a picture of the bank being in financial distress, the customers did massive withdrawals that resulted in the depletion of the bank's core capital. This

made it difficult for the bank to meet its financial obligations when they arose and this resulted to it being placed under statutory management.



Chapter 5 THE ANALYSIS OF THE FINDINGS OF THE RESEARCH

5.1 The introduction

The chapter analyses the findings of the research on the backdrop of the events that were happening in the banking sector at the time in the period before the placement of Chase Bank into statutory management and the period after. This is also achieved by making use of the CBK's Bank Supervision Annual Reports from the year 2008 to 2018 from which a comparison is made between the leadership at the helm of CBK, the number of employees in the Bank Supervision Department (BSD) and the number of banks detected as having not complied with the banking laws and regulations.

5.2 The period before the placement of Chase Bank under statutory management

Imperial Bank was the immediate bank to be placed under statutory management prior to Chase Bank being placed under statutory management. The placement of Imperial Bank under statutory management on the 13th October 2015 is said to have caused liquidity pressures in the banking sector with customers of various tier 2, 3 and 4 banks including Chase Bank losing confidence and moving their deposits to the larger banks, compounded by a tightening of the inter-bank lending market as some tier 1 banks cut their credit lines to lower tiered banks.⁷⁴

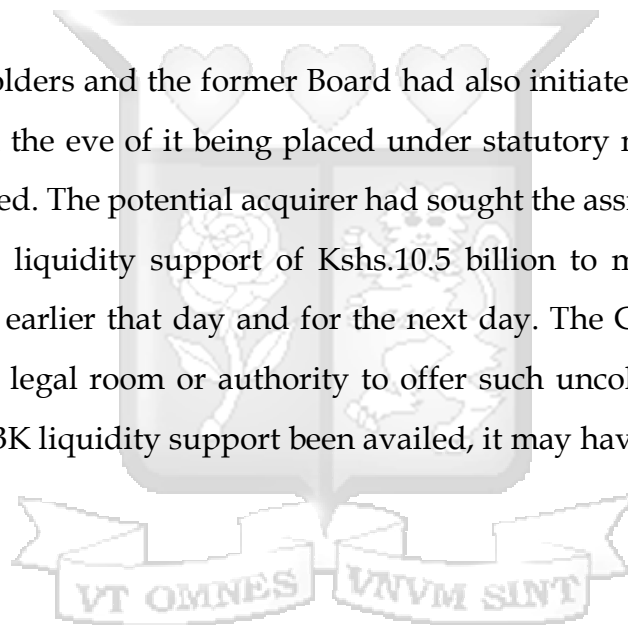
The subsequent trigger for Chase Bank being placed under statutory management by the CBK on April 7th, 2016 was due to its inability to meet its financial obligations on April 6th, 2016, following a panic run of withdrawals amounting to approximately Kshs.8 billion as a result of: (i) re-publication of the financial statements of the bank as they were on December 31st, 2015 showing a disclaimer of opinion by the auditor; and (ii) publication of the notice by the bank's board that Mr.Zafrullah Khan and Mr. Duncan Kabui, Group Chairman and Managing Director respectively, had stepped down. The deposit withdrawals were then fueled by social media reports that started

⁷⁴ The former board of Chase Bank (Kenya) Limited, *Briefing note to the Kenya National Assembly's Departmental Committee on Finance, Planning and Trade*, 9 June 2016, 7, para.1.

in October 2015 and heightened in the days leading up to and on the date of publication of the notice.⁷⁵

During the years 2015 and 2016, in which the market faced sustained liquidity pressures, the CBK provided REPO (repurchase agreement)⁷⁶ facilities which offered some liquidity support to Chase Bank and other banks. However, deposit outflows continued into the first quarter of the year 2016. Chase Bank shareholders therefore agreed a further rights issue for Kshs.2.5bn, and agreed to fast-track the previously agreed private placement interrupted by the Imperial Bank Limited crisis, to shore-up capital and liquidity. Both these actions were halted following the closure of Chase Bank.⁷⁷

Chase Bank shareholders and the former Board had also initiated discussions with a third party bank on the eve of it being placed under statutory management but the negotiations collapsed. The potential acquirer had sought the assistance of the CBK to offer an emergency liquidity support of Kshs.10.5 billion to manage the liquidity crunch experienced earlier that day and for the next day. The CBK informed Chase Bank that it had no legal room or authority to offer such uncollateralized liquidity support. Had the CBK liquidity support been availed, it may have stemmed the crisis



⁷⁵ The former board of Chase Bank (Kenya) Limited, *Briefing note*, 9 June 2016, 7, para.1.

⁷⁶ An agreement of repurchase (repo) is a kind of short-term borrowing for those who deal in the securities of the government. In the instance of a repo, a dealer will sell the securities of the government to investors, normally over a night, and buy them again the day after at a slightly higher price. That little difference in the price is regarded as an overnight interest rate. The repos are commonly used to raise short-term capital. They are also a tool common for open market operations of central bank <https://www.investopedia.com/terms/r/repurchaseagreement.asp> on 21 November 2019.

⁷⁷ The former board of Chase Bank (Kenya) Limited, *Briefing note*, 9 June 2016, 7, para.2.

and allowed the merger/acquisition transaction to proceed.⁷⁸ As a result and despite the Board's best efforts and attempts to find an adequate solution, with the proposed merger with a local bank failing at the last minute at 4.00 am on April 7th, 2016 due to the lack of liquidity support, Chase Bank could not meet its obligations and CBK placed the Bank under statutory management.⁷⁹

5.3 The period after the closure and placement of Chase Bank under statutory management

CBK on 7th April, 2016 by virtue of Ss. 43(1), 43 (2) and 53 (1) of the Kenya Deposit Insurance Act 2012 (KDI Act), for a period of 12 months, appointed the Kenya Deposit Insurance Corporation (KDIC) as a receiver for Chase Bank.⁸⁰ The KDIC appointment as a receiver for Chase Bank was done taking into consideration its depositors' interests, its creditors' interests and the interests of the members of the public.⁸¹

Section 43 (2) of KDI Act provides that CBK is to nominate the KDIC as a receiver of a bank, if the following conditions, among others exist, unsound or unsafe condition to transact; the likelihood of a bank to fail to meet its obligations that are financial in nature; a bank has considerably inadequate capital or if there is a contravention of any regulation or law.⁸²

Amongst the primary roles of CBK as a regulator is the role to advance the liquidity, solvency and proper functioning of a market-based financial system that is stable. Chase Bank underwent through liquidity difficulties, as a consequence of information

⁷⁸ 'Emmanuel Wanjala: Lawyers hit at CBK over failure to save collapsed banks, depositors' *The Star*, 27 June 2017 <https://www.the-star.co.ke/news/2017-06-27-lawyers-hit-at-cbk-over-failure-to-save-collapsed-banks-depositors/> on 16 January 2020.

⁷⁹ The former board of Chase Bank (Kenya) Limited, *Briefing note*, 9 June 2016, 7, para.3.

⁸⁰The Central Bank of Kenya Press Release, *Chase Bank Limited*, 7 April 2016, para.1.

⁸¹ The former board of Chase Bank (Kenya) Limited, *Briefing note*, 9 June 2016, 7, para.2.

⁸²The Central Bank of Kenya Press Release, *Chase Bank Limited*, 7 April 2016, para.3.

that was circulated on social media that it would receive a qualified opinion regarding its financial status, and the stepping aside of its two directors. As a result, the bank could not meet its obligations of a financial nature on April 7, 2016.⁸³

It is following the preceding that CBK appointed the KDIC to take over the management, conduct and control of the affairs and business of Chase Bank and to assume all the powers of the bank without the involvement of its Board of Directors and to advise CBK of a proper resolution strategy as soon as it was pragmatic and not beyond twelve (12) months from their appointment date. KDIC was required to avail information on the development progressively.⁸⁴

On 20th April, 2016, with the endorsement of the CBK, the KDIC came to an agreement with Kenya Commercial Bank (KCB) on the manner to reopen Chase Bank after some days and the ultimate acquisition of a majority shareholding in the bank.⁸⁵ This involved KDIC, “the Receiver”, appointing KCB, as “the Manager”, by virtue of sections 44(2)(b) and 44(3) of the Kenya Deposit Insurance Act, 2012 to undertake the business and manage the assets and the liabilities of Chase Bank. The appointment of KCB as “the Manager” was based on its reputation as a stable bank with a solid brand, sufficient human resources, and extensive experience in the country would help in safeguarding the interests of the depositors and creditors of Chase Bank, and the interests of the public at large. The CBK would go on to follow closely the developments in Chase Bank. KCB being the receiver manager, the bank would re-

⁸³The Central Bank of Kenya Press Release, *Chase Bank Limited*, 7 April 2016, para.4.

⁸⁴The Central Bank of Kenya Press Release, *Chase Bank Limited*, 7 April 2016, para.5.

⁸⁵ The Central Bank of Kenya Press Release, *Chase Bank Limited (In receivership)*, 20 April 2016, para.1.

open on 27th April 2016 (CBK, 2016), exactly twenty (20) days later following it being placed under statutory administration.⁸⁶ Accordingly:⁸⁷

- a) Every branch of Chase Bank would open on Wednesday, 27th April 2016. The mobile banking services and other online services would also be resume. Nonetheless, the branches would begin by offering limited banking services.
- b) Customers of Chase Bank would have instant access to their deposits at most up to Kenya shillings one million. On that ground, one hundred and sixty-seven thousand two hundred and ninety accounts (equal to 97% of accounts or 6% of all deposits) would have access to all their money. Subsequent deposits would be instantly available.
- c) The deposits exceeding Kenya shillings one million would be made available in a certain order, the details of which would be conveyed after that.
- d) The deferment of payments to the creditors and the lenders would continue to subsist. Nonetheless, the manager would get in touch with them after that and provide them with details on how their payments would be made.
- e) The continuing endeavour to obtain security of the existing loans and to recover monies that had been obtained without following the due process or were not being paid up would be intensified. The current borrowers were required to continue paying their loans.
- f) CBK together with KCB would see to it that Chase Bank Ltd would have sufficient liquidity for its operations.
- g) KCB would avail a management team that would give a helping hand in the receivership.

⁸⁶ Gathaiya N, 'Analysis of issues affecting collapsed banks in Kenya from year 2015 to 2016' *7 International Journal of Management & Business Studies* 3(2017) 9-10.

⁸⁷The Central Bank of Kenya Press Release, *Chase Bank Limited (In receivership)*, 20 April, 2016, 1-2.

KCB would carry out a comprehensive due diligence review of Chase Bank. That would inform decisions relating to KCB's interest in a majority stake.⁸⁸

Prior to KCB being appointed "the Manager" by KDIC, on 16th April 2016, the nominees of the Shareholders Committee of Chase Bank had made a presentation to the CBK on what they viewed, as a credible, reasonable and expedient way to open Chase Bank and ensure that all the primary objectives were achieved.⁸⁹ The primary objectives being to ensure job security for all the Bank's employees; to restore stability and confidence in the Banking sector; and to safeguard Kenya's international image as one of the premier investment destinations in Africa.⁹⁰

On 17th April 2018, CBK and KDIC disclosed the execution of an agreement between the State Bank of Mauritius Bank (Kenya) Ltd (SBM Kenya), and KDIC for the purchase by SBM Kenya of specific assets and the taking over of specific deposits with respect to Chase Bank (Kenya) Ltd (In Receivership). That concluded the dialogue between SBM, KDIC and CBK on Chase Bank transaction that had been disclosed on 5th January, 2018.⁹¹

The agreement between SBM and KDIC provided that there would be a transfer of 75% of the amount of the deposits that were then on moratorium at Chase Bank, and the transfer of the majority of the employees and branches of the current Chase Bank operations. 25% of the amount of moratorium deposits would remain in Chase Bank (Kenya) Ltd (In Receivership).⁹²

⁸⁸The Central Bank of Kenya Press Release, *Chase Bank Limited (In receivership)*, 20 April, 2016, 2, para.2.

⁸⁹ The former board of Chase Bank (Kenya) Limited, *Briefing note*, 9 June 2016, 18, para.4.

⁹⁰ The former board of Chase Bank (Kenya) Limited, *Briefing note*, 9 June 2016, 18, para.2.

⁹¹The Central Bank of Kenya Press Release, *Chase Bank Limited (In receivership)*, 17 April 2018, 1, para.1.

⁹²The Central Bank of Kenya Press Release, *Chase Bank Limited (In receivership)*, 17 April 2018, 1, para.2.

For the 75% of the moratorium deposits to be transferred to SBM, the conditions of the transferred deposits were destined as follows:⁹³

- a) 25% of every transferred deposit was going to be held in a current account with SBM Kenya, with unlimited usage and with no interest being payable thereon; and
- b) A further 25% of every transferred deposit would be held in a savings account with SBM Kenya at an annual interest rate of 6.65%, with unlimited usage; and
- c) The remainder of every transferred deposit would be held on a fixed term deposit with SBM Kenya at an annual interest rate of 6.65%, such deposits (and the interest thereon) were to mature, as to 1/3 of such remainder, on the 1st, 2nd and 3rd anniversaries of the transfer respectively.

In August 2018 the 75% mentioned above and a number of branches of Chase Bank's assets and liabilities were taken over by the State Bank of Mauritius (SBM) Kenya.⁹⁴

5.4 A comparison of the period before the placement of Chase Bank on statutory management and the period after the closure and placement of Chase Bank on statutory management

The persons interviewed in the course of the current research indicated that the tools, instruments and mechanisms used by the CBK in the enforcement of Prudential Guideline No.13 after the closure and placement of Chase Bank (now SBM Bank) under statutory management in the year 2016 are the same ones used for the period before the placement of Chase Bank under statutory management. The only difference was that the operational rigour had changed and that made the employees of the Supervision Department of CBK (BSD) more effective.

⁹³The Central Bank of Kenya Press Release, *Chase Bank Limited (In receivership)*, 17 April 2018, 1, para.3.

⁹⁴ 'Otiato Guguyu: Chase Bank officially transforms to SBM Kenya', *The Standard*, 20 August 2018 <https://www.standardmedia.co.ke/business/article/2001292696/chase-bank-is-now-officially-sbm-kenya> on 10 November 2018.

Moreover, there had been strategic hiring of employees of the Supervision Department of CBK (BSD). People with skills and knowledge in the areas of forensic audit, information and communications technology (ICT), accounting, mathematics etc., that are necessary for the operations in the said department were hired. Furthermore, for the purpose of up-skilling, continuous training of the staff members was carried out in areas that were emerging such as cyber security, money laundering, artificial intelligence etc. This had made the Bank Supervision Department effective in its functions.

Additionally, the CBK through its Supervision Department (BSD) apart from just ensuring that banks comply with Prudential Guidelines and the various provisions of the Banking Act by submitting the required quarterly and annual reports, the BSD analyses those reports to ensure that they adhered to the International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS) and that they reflected a true and fair account of the banks financial position. By doing the aforesaid, the CBK's role has shifted from just that of oversight to proper supervision of banks and their operations. This has largely contributed to its effectiveness. This is demonstrated by the table below, which indicates the number of banks detected as having not complied with the relevant banking laws and regulations in different years by the CBK's Supervision Department (BSD):

**SUMMARY FROM THE CBK'S ANNUAL SUPERVISION REPORTS FROM THE
YEAR 2008 TO THE YEAR 2018**

Year	The governor	Total No.of employe es in the BSD	No.of technical employees	No. of support staff	No. of non- compl ying banks	Non- perfor ming loans (Kshs.
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						Millions)
2008 ⁹⁵	Prof.N.Ndung'u	68	59	9	8	22,655
2009 ⁹⁶	Prof.N.Ndung'u	55	47	8	7	24,596
2010 ⁹⁷	Prof.N.Ndung'u	70	61	9	5	19,084
2011 ⁹⁸	Prof.N.Ndung'u	70	60	10	3	13,983
2012 ⁹⁹	Prof.N.Ndung'u	78	68	10	6	22,937
2013 ¹⁰⁰	Prof.N.Ndung'u	73	63	10	4	35,476
2014 ¹⁰¹	Prof.N.Ndung'u	84	74	10	5	48,544
2015 ¹⁰²	Dr.H.Sirima(Ag) (March4,2015) Dr.P.Njoroge(Ju ne 19, 2015)	79	69	10	4	73,363
2016 ¹⁰³	Dr.P.Njoroge	79	69	10	12	103,815
2017 ¹⁰⁴	Dr.P.Njoroge	79	69	10	15	119,698

⁹⁵ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2008, 3, 34, 50.

⁹⁶ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2009, 2, 28, 44.

⁹⁷ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2010, 2, 25, 40.

⁹⁸ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2011, 3, 32, 57.

⁹⁹ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2012, 3, 37, 69.

¹⁰⁰ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2013, 3, 34, 73.

¹⁰¹ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2014, 3, 37, 61.

¹⁰² The Central Bank of Kenya, *Bank Supervision Annual Report*, 2015, 2, 34, 54.

¹⁰³ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2016, 3, 32, 52.

¹⁰⁴ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2017, 3, 32, 55.

2018 ¹⁰⁵	Dr.P.Njoroge	79	69	10	11	146,666
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A quick overview of the aforesaid table reveals the following:

a) The period before the placing of Chase Bank (2008-April 6, 2016) under statutory management:

- i. The Governor of CBK was Prof.Njuguna Ndung'u (2008-March 4, 2015). Thereafter, the Deputy Governor Dr. Haron Sirima took charge from 4th March, 2015 until the appointment of Dr. Patrick Njoroge on 19th June, 2015.
- ii. The number of employees at the CBK (BSD) was approximately 72.
- iii. The number of non-complying institutions was approximately 5.
- iv. The number of non-performing loans have been increasing steadily (22,655; 24,596; 19,084; 13,983; 22,937; 35,476; 48,544; 73,363) with the exception of the years 2010 to 2011 where they declined to 19,084 and 13,983 respectively.

b) The period after the closure and placement of Chase Bank (April 7, 2016-2018) under statutory management:

- i. The Governor of CBK has been Dr. Patrick Njoroge.
- ii. The number of employees at the CBK (BSD) has been approximately 79.
- iii. The number of non-complying institutions has been approximately 12.
- iv. The number of non-performing loans increased very steadily (73,363; 103,815; 119,698; 146,666).

From the above summary it is clearly evident that for the period after the closure and putting of Chase Bank under statutory management (April 7, 2016-2018) the number of institutions (banks) that were detected as having not complied with the banking laws and regulations were found to be approximately 12, which is more than double the number of institutions (banks) that were detected as having not complied with laws and regulations of banking for the period before the placement of Chase Bank under statutory management (2008-2015), which were approximately 5.

¹⁰⁵ The Central Bank of Kenya, *Bank Supervision Annual Report*, 2018, 3, 40, 67.

The number of non-performing loans for the period before the putting of Chase Bank under statutory management (2008-April 6, 2016) increased steadily from 22,655 to 73,363 for a period of eight (8) years whereas for the period after the closure and putting of Chase Bank under statutory management (April 7, 2016-2018) the number of non-performing loans increased very steadily from 73,363 to 146,666 for a period of four (4) years. The approximate difference in the increase between the two periods being that the non-performing loans in the period after the closure and placement of Chase Bank under statutory management were about one and a half times the period before the placement of Chase Bank under statutory management.

The number of employees at the CBK (BSD) for the period before the placement of Chase Bank under statutory management (2008-April 6, 2016) was approximately 72 whereas for the period after the closure and putting of Chase Bank under statutory management (April 7, 2016-2018) has been approximately 79. The approximate difference of the number of employees for the two periods is seven (7).

The Governor of CBK for the period before the placement of Chase Bank under statutory management (2008-April 6, 2016) was Prof. Njuguna Ndung'u (2008-March 4, 2015). Thereafter, the Deputy Governor Dr. Haron Sirima took charge from 4th March, 2015 until the appointment of Dr. Patrick Njoroge on 19th June, 2015. Four (4) months following the appointment of Dr. Patrick Njoroge, Imperial Bank was placed under statutory management on 13th October, 2015, which was about a month following the demise of the Imperial Bank Group Managing Director, Mr. Abdulmalek Janmohamed which occurred on 15th September, 2015. The Governor of CBK for the period immediately after the closure and putting of Chase Bank under statutory management (April 7, 2016-2018) has been Dr. Patrick Njoroge.

As already stated herein before, in both the period before putting Chase Bank on statutory management and the period after the closure and putting Chase Bank on statutory management, Prudential Guidelines 2013 were in place and are still in place.

The question that arises therefore is what could explain the more than double the number of institutions (banks) that were detected as having not complied with the

laws and regulations of banking for the period after the closure and putting Chase Bank on statutory management in comparison to the period before putting Chase Bank on statutory management? Is it the change in the number of employees at the CBK (BSD) for the two periods, the change of leadership at the helm of CBK for the two periods or the sagas of Imperial Bank and Chase Bank?

The answers to the preceding questions can be found from the interviewees interviewed for the present research and summarized at **paragraphs 4.5 and 4.6** herein before in chapter four (**The research findings presentation**).

Paragraph 4.5 provides that:

The interviewees indicated that the tools, instruments and mechanisms utilized by CBK in the enforcement of the laws and regulations of banking since the placing of Chase Bank (now SBM Bank) under statutory management and its re- opening in the year 2016 are the same ones used before its closure and placing under statutory management. The only difference is that the operational rigour has changed following the sagas of Imperial Bank and Chase Bank and this has made the employees of the Supervision Department of CBK (BSD) more effective.

Moreover, there has been strategic hiring of employees of the Supervision Department (BSD) of CBK. People with skills and knowledge in the areas of forensic audit, information and communications technology (ICT), accounting, mathematics etc., that are necessary for the operations in the said department are hired. Furthermore, for the purpose of upskilling, continuous training of the staff members is carried out in areas that are emerging such as cyber security, money laundering, artificial intelligence etc. This has made the Bank Supervision Department effective in its functions.

Additionally, the CBK through its Supervision Department

(BSD) apart from just ensuring that banks comply with prudential guidelines and the various sections of the Banking Act by submitting the required quarterly and

annual reports, the BSD analyses those reports to ensure that they adhere to the International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS) and that they reflect a true and fair account of the banks financial position. By doing the aforesaid, the role of the CBK has shifted from just that of oversight to proper supervision of banks and their operations. This has largely contributed to its effectiveness.

Paragraph 4.6 provides that:

The persons interviewed stated that the laws and regulations in place are enough for the proper operation of the CBK. Therefore, there is no need for new laws except maybe in the new emerging areas such as cyber security. Traditional banking can be effectively controlled by CBK using the enforcement mechanisms already in place, to implement laws and regulations of banking.

The current regime of the Central Bank of Kenya has the tools which were available to the previous regimes. However, unlike the previous regimes, the current regime is willing to interpret and enforce the banking laws and regulations fearlessly. This has prevented the moral hazard risk from rising. The moral hazard risk rises when banks know that they can get away with the contravention of the laws and regulations of banking.

The CBK current regime's willingness to interpret and implement the laws and regulations of banking fearlessly was evident during the CBK's investigation of the banks that were made use of by persons who were suspected of transacting illegally with National Youth Service (NYS). This came after the serious concerns that emerged in May 2018, linked to the transmission of monies stolen from NYS.¹⁰⁶

The CBK announced on 12th September 2018, the completion of the 1st phase of the investigation of the banks that were used by the said persons in transmitting the NYS monies. The investigations gave priority to banks that handled the biggest

¹⁰⁶ The Central Bank of Kenya Press Release, *Investigations of banks related to National Youth Service transactions*, 12 September 2018, 1, para.1.

transmissions, namely: Standard Chartered Bank Kenya Ltd, Equity Bank Kenya Ltd, KCB Bank Kenya Ltd, Co-operative Bank of Kenya Ltd, and Diamond Trust Bank Kenya Ltd.¹⁰⁷

The main purpose of the investigations was to probe the operations of the bank accounts and transactions related to NYS, and in each case check the compliance of the bank with the requirements of Anti-Money Laundering/Combating Financing of Terrorism (AML/CFT) laws and regulations in Kenya. The contraventions identified were mainly related to the following:¹⁰⁸

- a) Declining to report substantial transactions in cash;
- b) Declining to carry out sufficient due diligence on customer.
- c) Absence of documents to support the substantial transactions; and
- d) Deterioration in the preparation of Reports on Suspicious Transaction (STRs) to the Centre for Financial Reporting (FRC).

The CBK determined the penalties for each of the five banks in monetary terms corresponding to the level of the contraventions that were identified and by virtue of the powers of the CBK as provided for in the Banking Act and the Central Bank of Kenya Act. The penalties imposed were as below:¹⁰⁹

Bank	Total sums received from NYS (Ksh. Million)	Penalty imposed (Ksh. Million)	Penalty determined as a % of

¹⁰⁷ The Central Bank of Kenya Press Release, *Investigations of banks related to National Youth Service transactions*, 12 September 2018, 1, para.2.

¹⁰⁸ The Central Bank of Kenya Press Release, *Investigations of banks related to National Youth Service transactions*, 12 September 2018, 1, para.3.

¹⁰⁹ The Central Bank of Kenya Press Release, *Investigations of banks related to National Youth Service transactions*, 12 September 2018, 1, para.4.

			the sum received from NYS.
Standard Chartered	1,628	77.5	4.76%
Equity	886	89.5	10.10%
KCB	639	149.5	23.40%
Co-operative	263	20.0	7.60%
Diamond Trust	162	56.0	34.57%

The CBK deliberated the comprehensive outcome of the investigation with each of the banks' senior management and boards of directors. Each indicated their firm commitment to adhere to all aspects of the law fully, and to address the gaps that had been established through actions to be undertaken within a certain period of time. The plan of the actions to be undertaken it was agreed that they would be availed to CBK within 14 days and CBK would closely follow their discharge. In general, CBK would cooperate with all other banks to ensure that the outcome of the investigations is again used to strengthen all the frameworks of AML/CFT.¹¹⁰ From the time the aforesaid penalties were imposed, the banks have taken very seriously the application of the laws and regulations on AML/CFT particularly, carrying out sufficient due diligence on customer and ensuring that transactions involving huge sums of money have the relevant documents in support.

The CBK indicated that the 2nd phase of the investigations would entail the use of the outcome of the investigation by other agencies, among other things, appraisal of criminal culpability by the Criminal Investigations Directorate (DCI) and the Director of Public Prosecution's Office (ODPP). CBK had shared the outcome of the

¹¹⁰ The Central Bank of Kenya Press Release, *Investigations of banks related to National Youth Service transactions*, 12 September 2018, 2, para.1.

investigations with the proper investigative agencies for their fitting action. Moreover, other banks would also be singled out for the purpose of investigation.¹¹¹

The CBK indicated that the actions that it had taken and those that had been taken thereafter by other agencies were intended to protect the interests of all the collaborators and to maintaining a robust financial sector. CBK indicated that it would go on to see to it that the legal and regulatory framework of the banking sector, including for AML/CFT, was in line with the best practices. The CBK indicated that it would also go on to implement the firm compliance with the relevant regulations and laws, as the interests of the investors, the public, and other stakeholders would be safeguarded only in an environment that was directed by the rule of law.¹¹²

At the beginning of April 2020, the CBK took action of a regulatory nature against Absa Bank, due to Absa's failure to avail information regarding some certain foreign exchange trades that it had undertaken in March 2020.¹¹³ Following the investigation of CBK of these transactions and others undertaken earlier on, CBK found that Absa Kenya did not have adequate assurance of the hidden commercial transactions aiding these trades, as is needed, nor did the bank see to it that the standard checks on AML/CFT and the requirement to know-your-customer were enforced. The CBK therefore needed Absa to carry out the following:

- a. By Wednesday, April 15, 2020, to put in place a sound framework that would see to it that all the proper documents for such foreign exchange transactions were accessible as prescribed, and ensure that the requirements of AML/CFT and those of knowing your customer were followed.

¹¹¹ The Central Bank of Kenya Press Release, *Investigations of banks related to National Youth Service transactions*, 12 September 2018, 2, para.2.

¹¹² The Central Bank of Kenya Press Release, *Investigations of banks related to National Youth Service transactions*, 12 September 2018, 2, para.3.

¹¹³ The Central Bank of Kenya Press Release, *Regulatory action against Absa Bank Kenya PLC*, 9 April 2020.

- b. Overturn the market positions that were created as a consequence of the highlighted transactions.
- c. Cease to transact as a dealer authorised to deal in foreign exchange in the market in Kenya from Thursday, April 9, 2020, to Wednesday, April 15, 2020. Throughout that time Absa would not engage, among other things, in the market of interbank foreign exchange. Nonetheless, all the pledged transactions as at April 8, 2020, could be completed.

While taking the aforesaid regulatory action against Absa Kenya, the CBK noted Absa's acceptance of its duties as a dealer licensed to deal in foreign exchange and its guarantee to deal with the issues underlying. The CBK also reiterated the purpose of building robust, fair and transparent financial markets, grounded in the law and according to the best practices in the world.

5.5 Conclusion from the comparison of the period before the putting of Chase Bank in statutory management and the period after the closure and putting of Chase Bank in statutory management

The more than double the number of institutions (banks) that were detected as having not complied with the laws and regulations of banking for the period after the closure and putting of Chase Bank in statutory management in comparison to the period before the putting of Chase Bank under statutory management is attributed to the preceding sagas of the Imperial Bank and Chase Bank and also the change of leadership at the helm of CBK for the two periods.

As already indicated herein above the persons interviewed indicated that the tools, instruments and mechanisms used by CBK in the enforcement of banking laws and regulations since the re-opening of Chase Bank (now SBM Bank) in the year 2016 were the same ones used prior to its closure. The only difference being that the operational rigour had changed following the sagas of Imperial Bank and Chase Bank and this had made the employees of the Supervision Department of CBK (BSD) more effective.

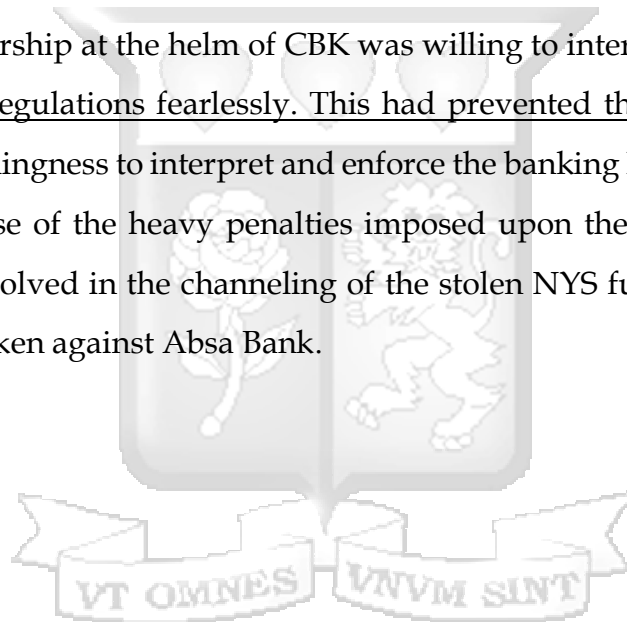
The change in the leadership at the helm of the CBK between the two periods had also influenced the strategic hiring of employees of the Supervision Department of CBK

(BSD). People with certain skills that are deemed necessary for the operations in the said department are hired.

Furthermore, the leadership at the helm of CBK had also influenced the continuous training of the staff members in particular areas of interest carried out for the purpose of up- skilling. This has made the Bank Supervision Department effective in its functions.

Additionally, the leadership at the helm of CBK had influenced the Bank Supervision Department to shift its role from just that of oversight to proper supervision of banks and their operations. This has largely contributed to its effectiveness.

Moreover, the leadership at the helm of CBK was willing to interpret and enforce the banking laws and regulations fearlessly. This had prevented the moral hazard risk from rising. The willingness to interpret and enforce the banking laws and regulations is evident in the case of the heavy penalties imposed upon the five (5) commercial banks that were involved in the channeling of the stolen NYS funds and also on the regulatory action taken against Absa Bank.



Chapter 6 THE CONCLUSION AND RECOMMENDATIONS

6.1 The study's limitations

The following are the study's main limitations:

- a) The directors and employees who had worked for Chase Bank for the two periods were not readily available to be interviewed as they had left the bank, having been taken over by SBM Bank. Moreover, they had cases pending in court and so discussing the matter would be considered subjudice.
- b) There was limited time to allow the study of all the banks within Kenya. This resulted into adopting an approach of case study of Chase Bank.
- c) Only a few individuals from the Supervision Department of CBK (BSD) who had in one way or another been involved in Chase Bank investigation were interviewed.
- d) Certain crucial documents like the Forensic Audit Report of Chase Bank by Deloitte Kenya could not be availed as they were regarded as very confidential. This could have shade more light on the issues that resulted into Chase Bank being placed under statutory management.
- e) There was limited human resource, the researcher being one, to critically analyse all the materials available in relation to the topic of research from all the possible perspectives.

6.2 The conclusion

The study's purpose was to find out whether the difference in the two periods, the period before and after the placement of Chase Bank under statutory management, could be attributed to the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13 or whether there were other factors that were responsible for the difference in the two periods, other than the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13.

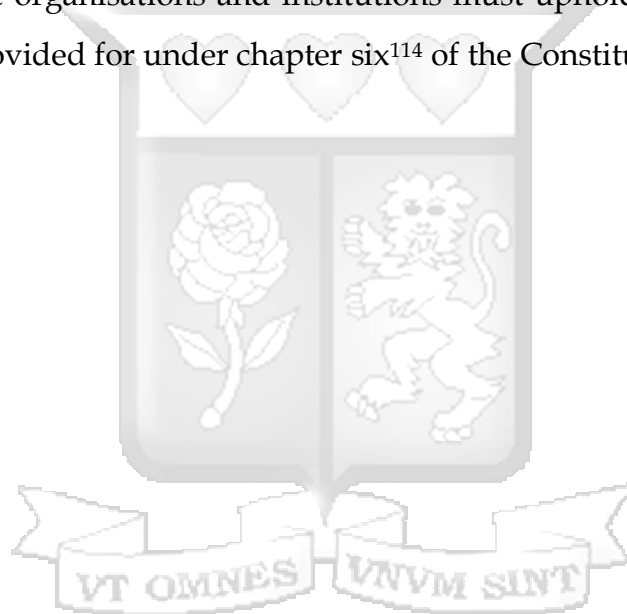
The study established that the tools, instruments and mechanisms used by the CBK in the banking laws and regulations enforcement after the placement of Chase Bank (now SBM Bank) under statutory management in the year 2016 were the same ones used before it being placed under statutory management. Therefore, the difference in the two periods, could not be attributed to the enforcement mechanisms employed by the CBK in the enforcement of the Prudential Guideline No.13. Instead, the study established that there were other factors that were responsible for the difference in the two periods, these being:

- a) After the Imperial Bank and Chase Bank sagas this had made the staff members of the Supervision Department of CBK (BSD) more effective in the performance of their duties. This meant strict enforcement of the applicable laws and regulations with strict penalties for non-adherence. Consequently, the banks have taken the implementation of the laws and regulations, which include the Prudential Guideline No.13, more seriously.
- b) The change of leadership at the helm of CBK influenced the change in the operational rigour that made the staff members of the Supervision Department of CBK (BSD) more effective.
- c) The change of leadership at the helm of CBK also influenced the change in the strategic hiring of staff members of the Supervision Department of CBK (BSD). This means that people with certain skills that are deemed necessary for the operations in the said department are hired.
- d) Moreover, the change of leadership at the helm of CBK also influenced the continuous training of the staff members in particular areas of interest carried out for the purpose of up skilling. This has made the Bank Supervision Department effective in its functions.
- e) Also the Imperial Bank and Chase Bank sagas and the change of leadership at the helm of CBK also influenced its Supervision Department to shift its role from just that of oversight to proper supervision of banks and their operations. This has largely contributed to its effectiveness.

f) Lastly, the change of leadership at the helm of CBK also influenced the willingness to interpret and enforce the banking laws and regulations, which include Prudential Guideline No.13, fearlessly. This has prevented the moral hazard risk from rising. The willingness to interpret and enforce the banking laws and regulations is evident in the case of the heavy penalties imposed upon the five (5) commercial banks that were involved in the channeling of the stolen NYS funds and also on the regulatory action taken against Absa Bank Kenya PLC.

6.3 The recommendations

In order for organisations and institutions to be effective in their functions, the leaders at the helm of those organisations and institutions must uphold leadership imbued with integrity as provided for under chapter six¹¹⁴ of the Constitution of Kenya, 2010.



¹¹⁴ Articles 73-80, *Constitution of Kenya* (2010).

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ANNEXURES

Annexure A- Letter of introduction

Samuel Munge Kiongera

P.O. Box 28491-00200,

Nairobi.

Email: samuelkiongera@gmail.com

21st March, 2019

The Director,
Bank Supervision Department,
Central Bank of Kenya,
Haile Selassie Avenue,
P.O. Box 60000-00200,
Nairobi.

Dear Sirs/Mesdames,

RE: AUTHORITY TO CARRY OUT RESEARCH IN YOUR DEPARTMENT

My name is Samuel Munge Kiongera, a student at Strathmore Law School, currently undertaking Masters of Laws in the area of International Financial Law and Regulation.

My thesis is on **'Enforcement of the Prudential Guideline No.13 by the Central Bank of Kenya (CBK): A case study of Chase Bank (now SBM Bank), for the period before and after its being placed under statutory management'**.

In order to write on the aforesaid topic, I would like to conduct research in your department by way of a questionnaire **(copy enclosed herein)**.

I confirm that any information given will be very strictly for academic research purposes only.

By this letter I therefore request to be granted the permission to conduct the research at your department.

I look forward to your positive response.

Yours faithfully,

Samuel Munge Kiongera



Annexure B- Questionnaire

QUESTIONNAIRE

(This is strictly confidential)

This questionnaire has been issued by a Master of Laws student at Strathmore University. The purpose of the questionnaire is to enable the student collect the necessary information for the research he is carrying on, on the enforcement of the Prudential Guideline No.13 by the CBK, with a specific case study on Chase Bank (now SBM Bank) for the period before and after its being placed under statutory management.

1. What are your full names?.....
2. Where do you work, and in which department, if any?.....
3. When did you start working there?.....
4. What is your job description?.....
5. What does your job entail?.....
6. Have there been any changes in the enforcement mechanisms employed by CBK in the enforcement of Prudential Guideline No.13, since the re-opening of Chase Bank (now SBM Bank) in the year 2016? If yes, please state them.....
7. What enforcement mechanisms were employed by the CBK on Chase Bank, for the period before its closure and placement under statutory management, to

ensure that it complied with the banking laws and regulations?.....

8. What enforcement mechanisms have been employed by the CBK on Chase Bank (now SBM Bank) in its enforcement of the laws and regulations of banking after its re-opening?.....
.....
.....
.....
.....

9. What enforcement mechanisms employed by the Central Bank of Kenya in the enforcement of the banking laws and regulations on Chase Bank (now SBM Bank), after its re-opening can be attributed to its adherence with laws and regulations of banking in comparison to the period prior to its closure?.....

10. Are there reforms that you think would make CBK more effective in its enforcement of the banking laws and regulations? If yes, please state them.....

11. Was Chase Bank submitting audited accounts to Central Bank of Kenya (CBK) every year since the year 2013 up to the time of its closure on 7th April, 2016, as required under section 23 of the Banking Act?.....

12. Did auditors of Chase Bank submit auditors' report for each of the years from the year 2013 up to the time of its closure on 7th April, 2016? If so what did the auditors' report state about the financial condition of Chase Bank in each of those years?.....

13. Has SBM Bank been submitting audited accounts to CBK every year since August 2018 up to date?.....

14. Who have been the auditors of SBM Bank since August 2018 up to date?.....
15. Have the auditors of SBM Bank been submitting the auditors' report for every year since August 2018 to date? If so what have been the auditors' report on the state of the financial condition of SBM Bank in each of those years?.....
16. Did the CBK at any one time require Chase Bank to pass Board Resolutions, in between from the year 2013 up to the time of its closure on 7th April, 2016?

If so:

- a) What were the Board Resolutions to be passed?.....
- b) What was the timeline for passing those Board Resolutions?.....
.....
.....
- c) Did Chase Bank pass those Board Resolutions? If not, what action did CBK take?.....
.....
.....

17. Has the CBK at any one time since August 2018 to date required SBM Bank to pass Board Resolutions?.....

If so:

- a) What Board Resolutions were to be passed?.....
.....

b) What was the timeline for passing those Board Resolutions?.....
.....

c) Has SBM Bank passed those Board Resolutions? If not, what action has CBK taken?.....
.....

18. Did the CBK at any one time write a commitment letter to Chase Bank's Board of Directors, in between from the year 2013 up to the time of its closure on 7th April, 2016?.....

If so:

a) What were its recommendations to Chase Bank's Board of Directors?.....
.....
.....

b) Did Chase Bank's Board of Directors sign the letter of recommendation and return the original to CBK within 30 days?
?.....

c) Did Chase Bank's Board of Directors comply with the recommendations of CBK? If not, what action did CBK take?.....

19. Has the CBK at any one time since August 2018 to date written a commitment letter to SBM Bank's board of directors?.....

If so:

a) What have been its recommendations to the board of directors of SBM Bank?.....

b) Did SBM Bank's board of directors sign the letter of recommendation and return the original to CBK within 30 days?.....

c) Has SBM Bank's board of directors complied with the recommendations of CBK? If not, what action has CBK taken?.....

20. Did the CBK at any one time get into a Memorandum of Understanding with Chase Bank's board of directors, in between from the year 2013 up to the time of its closure on 7th April, 2016?.....

If so:

a) What corrective/remedial actions was the board of Chase Bank required to take?.....

b) If not what legal action did the CBK take?.....

21. Has the CBK at any one time since August 2018 to date gotten into a Memorandum of Understanding with SBM Bank's board of directors?.....

If so:

a) What corrective/remedial actions has the board of SBM Bank been required to take?.....
.....

b) Has the board of directors of SBM Bank taken those corrective/remedial actions? If not what legal action has the CBK taken?.....
.....
.....

22. Did the CBK at any one-time issue directives as per s. 33(1) of the Banking Act to Chase Bank's board of directors, in between from the year 2013 up to the time of its closure on 7th April, 2016?.....
.....
.....

If so:

a) What specific directive(s) did the CBK issue?.....
.....

b) Did Chase Bank's board of directors comply with the directives issued by CBK? If not what action did CBK take?.....
.....

c) Prior to the issuance of the directive(s) in a) herein above, did the CBK issue a notice of intention for Chase Bank's board of directors to show cause why such directive(s) should not be issued? If not,

why?.....
.....

23. Has the CBK at any one time since August 2018 to date issued any directives as per s. 33(1) of the Banking Act to SBM Bank's board of directors?.....
.....
.....

If so:

a) What specific directive(s) has the CBK issued?.....
.....

b) Has the board of directors of SBM Bank complied with the directives issued by CBK? If not what action has the CBK taken?.....
.....

c) Prior to the issuance of the directive(s) in a) herein above, did the CBK issue a notice of intention for the board of directors of SBM Bank to show cause why such directive(s) should not be issued? If not, why?.....
.....

24. Did the CBK at any one time deny corporate approvals to Chase Bank in between from the year 2013 up to the time of its closure on 7th April, 2016?.....
.....
.....

If so:

a) What was the nature of the corporate approval denied?.....
.....

b) What was the reason for the corporate approval denial?.....
.....

25. Has the CBK at any one time since August 2018 to date denied SBM Bank any corporate approvals?.....

If so:

a) What was the nature of the corporate approval denied?.....
.....

b) What was the reason for the corporate approval denial?.....
.....
.....

26. Did the CBK at any one time intervene in the management of Chase Bank in between from the year 2013 up to the time of its closure on 7th April, 2016?.....
.....
.....

If so:

a) Was it occasioned by the failure of Chase Bank to avail a plan for capital restoration or a plan to address all deficiencies as directed under S. 33A; or failure to increase

capital?.....
.....

b) What corrective action did the CBK take?.....
.....

27. Has the CBK at any one time since August 2018 to date intervened in the management of SBM Bank?.....
.....
.....

If so:

a) What occasioned the intervention?.....
.....

b) What corrective action did the CBK take thereafter?.....
.....

28. Did the CBK at any one time direct the removal of directors and officers of Chase Bank and also impose penalties on them and it, in between from the year 2013 up to the time of its closure on 7th April, 2016?.....
.....

If so:

a) Was the directive effected?.....
.....
.....

b) Which category of directors (executive or non-executive) and officers were removed?.....
.....
.....

c) How many directors and officers were removed?.....
.....
.....

d) How much was the penalty imposed on the directors and officers (if any) and why?.....
.....
.....

e) How much was the penalty imposed on Chase Bank (if any) and why?.....
.....
.....

29. Has the CBK at any one time since August 2018 to date directed the removal of directors and officers of SBM Bank and also imposed penalties on them and it?.....
.....

If so:

a) Was the directive effected?.....
.....
.....

b) Which category of directors (executive or non-executive) and officers were removed?.....

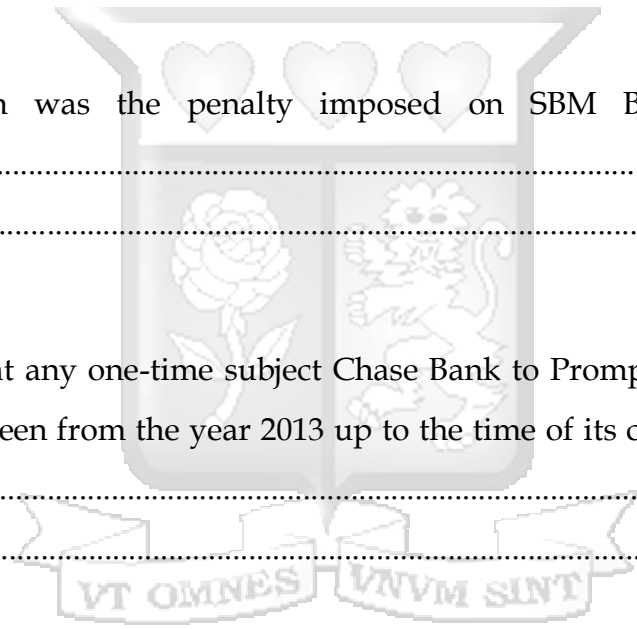
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c) How many directors and officers were removed?.....
.....
.....

d) How much was the penalty imposed on the directors and officers (if any) and why?.....
.....
.....

e) How much was the penalty imposed on SBM Bank (if any) and why?.....
.....
.....

30. Did the CBK at any one-time subject Chase Bank to Prompt Corrective Action (PCA) in between from the year 2013 up to the time of its closure on 7th April, 2016?.....
.....
.....



If so:

a) Was the subjection to Prompt Corrective Action occasioned by the large errors of reporting that materially misrepresented the financial condition of Chase Bank?.....
.....
.....

b) What was the specific large error of reporting that materially misrepresented the financial condition of Chase

Bank?.....
.....
.....

c) Was the reporting error corrected? If so, what was the outcome of the correction?.....
.....
.....

31. Has the CBK at any one time since August 2018 to date subjected SBM Bank to any Prompt Corrective Action (PCA)?.....
.....
.....

If so:

a) What occasioned the subjection of SBM Bank to Prompt Corrective Action (PCA)?.....
.....

b) Was the cause of the subjection of SBM Bank to Prompt Corrective Action (PCA) corrected? If not, what action has the CBK taken?.....
.....
.....

32. Did the CBK at any one time enter into a final agreement with Chase Bank in between from the year 2013 up to the time of its closure on 7th April, 2016?.....
.....
.....

If so:

a) Was the reason for entering into a final agreement occasioned by failure to avail a capital restoration plan?.....
.....
.....

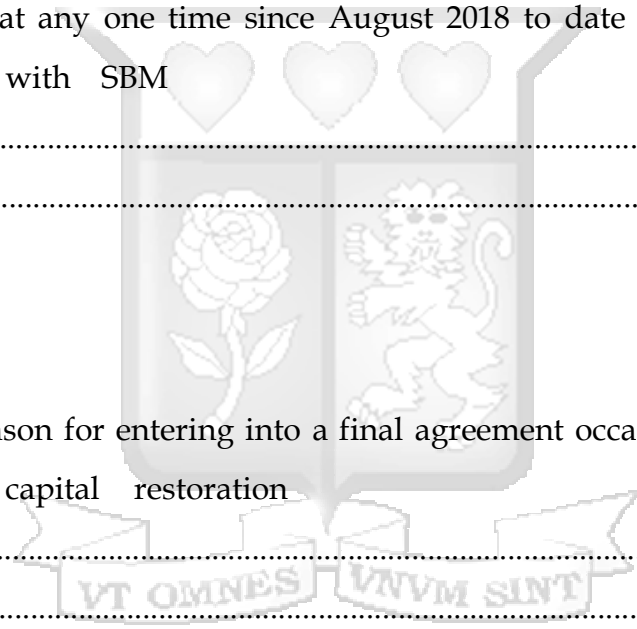
b) Did Chase Bank comply with terms of the final agreement?.....
.....
.....

33. Has the CBK at any one time since August 2018 to date entered into a final agreement with SBM Bank?.....
.....
.....

If so:

a) Was the reason for entering into a final agreement occasioned by failure to avail a capital restoration plan?.....
.....
.....

b) Did SBM Bank comply with terms of the final agreement?.....
.....
.....



**THIS IS TO CERTIFY THAT:
MR. SAMUEL MUNGE KIONGERA
of STRATHMORE UNIVERSITY,
50199-100 NAIROBI, has been permitted
to conduct research in Nairobi County**

**Permit No : NACOSTI/P/19/25593/29271
Date Of Issue : 23rd April,2019
Fee Recieved :Ksh 1000**

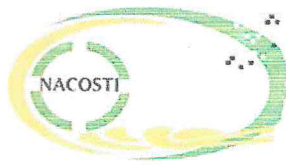
**on the topic: ENFORCEMENT
MECHANISMS OF THE CENTRAL BANK OF
KENYA (CBK): A CASE STUDY OF CHASE
BANK (NOW SBM BANK), FOR THE
PERIOD PRIOR TO ITS CLOSURE AND THE
PERIOD AFTER ITS RE-OPENING**

**for the period ending:
23rd April,2020**



Samuel Munge Kiongera
.....
**Applicant's
Signature**

Glenn
.....
**Director General
National Commission for Science,
Technology & Innovation**



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TECHNOLOGY AND INNOVATION**

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NAIROBI-KENYA

Ref. No. **NACOSTI/P/19/25593/29271**

Date: **23rd April, 2019**

Samuel Munge Kiongera
Strathmore University
P.O. Box 59857-00200
NAIROBI.

RE: RESEARCH AUTHORIZATION

Following your application for authority to carry out research on *“Enforcement mechanisms of the Central Bank of Kenya (CBK): A case study of Chase Bank (now SBM Bank), for the period prior to its closure and the period after its re-opening”* I am pleased to inform you that you have been authorized to undertake research in **Nairobi County** for the period ending **23rd April, 2020**.

You are advised to report to **the County Commissioner and the County Director of Education, Nairobi County** before embarking on the research project.

Kindly note that, as an applicant who has been licensed under the Science, Technology and Innovation Act, 2013 to conduct research in Kenya, you shall deposit a **copy** of the final research report to the Commission within **one year** of completion. The soft copy of the same should be submitted through the Online Research Information System.

GODFREY P. KALERWA MSc., MBA, MKIM
FOR: DIRECTOR-GENERAL/CEO

Copy to:

The County Commissioner
Nairobi County.

The County Director of Education
Nairobi County.



23rd April 2019

Mr. Kiongera, Samuel
P.O. Box 60531, 00200
Nairobi.
samuelkiongera@gmail.com

Dear Mr. Kiongera,

REF Protocol ID: SU-IERC0398/19

ENFORCEMENT MECHANISMS OF CENTRAL BANK OF KENYA (CBK): A CASE STUDY OF CHASE BANK (NOW SBM BANK), FOR THE PERIOD PRIOR TO ITS CLOSURE AND THE PERIOD AFTER ITS RE-OPENING.

We acknowledge receipt of your application documents to the Strathmore University Institutional Ethics Review Committee (SU-IERC) which includes:

1. Study Protocol submitted 11th March 2019
2. Cover letter listing all submitted documents 11th March 2019
3. Proposal declaration Page signed by supervisors 11th March 2019

The committee has reviewed your application, and your study "*Enforcement mechanisms of the Central Bank of Kenya (CBK): A case study of Chase Bank (now SBM Bank), for the period prior to its closure and the period after its re-opening*" has been granted **approval**.

This approval is valid for one year beginning **23rd April 2019** until **23rd April 2020**

In case the study extends beyond one year, you are required to seek an extension of the Ethics approval prior to its expiry. You are required to submit any proposed changes to this proposal to SU-IERC for review and approval prior to implementation of any change.

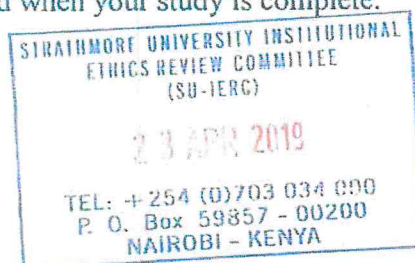
SU-IERC should be notified when your study is complete.

Thank you

Sincerely,

Prof. Florence Oloo
Secretary

Strathmore University Institutional Ethics Review Committee





BSD/GEN/16

Halle Salasie Avenue
P.O. Box 60000 - 00200 Nairobi, Kenya
Telephone: 2540000, Fax: 340192

June 12, 2019

Mr. Samuel Munge Kiongera
Strathmore University
P.O. Box 59857 - 00200
Nairobi

Mobile: +254723281558
Email: samuelkiongera@gmail.com

Dear Sir,

PERMISSION TO CONDUCT RESEARCH IN BANK SUPERVISION


This is in reference to your letter dated February 28, 2019 requesting for permission to conduct research in Bank Supervision Department. We note that your research focuses on the laws and regulations that govern the operations of banks in Kenya and the enforcement mechanisms of the Central Bank of Kenya (CBK).

We have reviewed your request and advice that the primary laws and regulations governing the Kenyan banking sector are mainly Central Bank of Kenya Act, Banking Act, Microfinance Act, National Payment System Act and Kenya Deposit Insurance Act together with the attendant regulations and guidelines. These banking sector laws, regulations and guidelines are available on the CBK website under the link: <https://www.centralbank.go.ke/policy-procedures/legislation-and-guidelines/>.

As regards the enforcement mechanisms of the Central Bank of Kenya (CBK), these are contained in the above banking sector laws and regulations. Examples include sections 48, 49, 50, 51 and 55(2) of the Banking Act and the clauses on Remedial Measures and Administrative Sanctions under the CBK Prudential Guidelines.

For any further clarification, you may contact Bank Supervision Department through the email: fin@centralbank.go.ke.

Yours faithfully,


GERALD NYAOMA
DIRECTOR, BANK SUPERVISION

Thesis final copy 4

by Kiongera Samuel

Submission date: 18-Nov-2020 09:45AM (UTC+0300)

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