KENYA BANKING SECTOR CHARTER

1. Preamble

This Banking Sector Charter (BSC) is issued pursuant to Section 33(4) of the Banking Act and Section 48(2A) of the Microfinance Act, which empowers the Central Bank of Kenya (CBK) to issue directions with respect to the standards to be adhered to by an institution[1] in the conduct of its business in Kenya.

The Charter applies to an institution carrying on banking business[2], financial business[3], the business of a mortgage finance company[4] and microfinance banks and shall be effective from March 1, 2019. The commercial banks, microfinance banks and mortgage finance company will therefore be required to submit their Plans to CBK by May 31, 2019.

The Charter represents a commitment from institutions in the banking sector to entrench a responsible and disciplined banking sector cognizant of, and responsive to, the unique socio-economic realities of the Kenyan populace.

The Charter is premised on the banking sector's vision hinged on four central pillars: -

(i) Adoption of customer-centric business models by banks;
(ii) Risk-based credit pricing;
(iii) Enhanced transparency and information disclosure; and
(iv) Entrenching an ethical culture in banks – doing the right thing.

The Charter should be read together with the provisions of the Banking Act, Microfinance Act, Regulations and Guidelines, Credit Reference Bureau Regulations, 2013 issued by the CBK from time to time.

---

[1] An "institution" means:-
- a bank or financial institution or a mortgage finance company as defined in the Banking Act.
- a microfinance bank licensed under Microfinance Act, 2006.

[2] "banking business" is defined in the Banking Act as: -
(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.

[3] "financial business" means:
(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; and
(b) the employing of money held on deposit 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.

[4] A "mortgage finance company" is defined as a company which accepts, from members of the public, money-
(a) on deposit repayable on demand or at the expiry of a fixed period or after notice; or
(b) on current account and payment on and acceptance of cheques.

2. Background

There have been concerns by the public on the high cost of credit charged by the banking sector and poor customer service. These concerns have led to significant loss of trust in banks by the public. The Government and the Central Bank of Kenya have, in the recent past, introduced several reforms to lower the cost of credit. The reforms include: roll out of mobile phone financial services in 2007, establishment of currency centers in 2009, agency banking in 2010, introduction of the Credit Information Sharing (CIS) mechanism in 2010, and the Kenya Banks Reference Rate in 2014. These initiatives however have not addressed sufficiently these concerns particularly the high cost of credit.

There have been further developments made in the banking sector as a result of the ongoing regulatory reforms aimed at strengthening consumer protection and helping improve transparency and competition in the sector. These include; enhancing the CIS framework, review of the consumer protection framework, implementing the movable collateral registry (Movable Property Security Rights Act, 2017), increasing transparency of the pricing of products through the launch of the total cost of credit website in 2017 and adoption of customer-centric business models by banks. These and other reforms are necessary towards transforming the banking sector to being responsible, disciplined and aligned to the needs of their customers.

3. Kenya Banking Sector Charter

It is in the interest of the Kenyan financial sector and populace that CBK is now issuing this Kenya Banking Sector Charter. The Charter is expected to facilitate a market-driven transformation of the Kenyan banking sector and bring about tangible benefits for Kenyans.

4. Objectives of the proposed Banking Sector Charter

i) To increase access to affordable and appropriate banking services to the unbanked and under-served population in Kenya.

ii) To develop a more resilient, competitive and dynamic financial system based on the four central pillars of the banking sector's vision.

iii) To ensure that institutions proactively engage their customers in financial literacy and consumer education drives, to enhance customers' financial knowledge and skills for them to make informed financial decisions.

iv) To ensure institutions develop and submit a time bound plan approved by the institution's Board in compliance with the Charter for CBK's monitoring purposes.

v) To promote efficiency in lending and acquisition of loanable funds.

In pursuit of these objectives, the Charter commits institutions in the banking sector to transform in the following areas: -

a. **Fairness**

In order to improve the credit risk pricing of loans extended to borrowers as well as implement differential credit pricing, based on a customer credit rating, institutions are henceforth mandated to **implement risk based credit scoring techniques** in their loan screening processes. In order to enhance credit scoring and improve data analytics, a Technical Working Group (TWG)[5] was constituted to facilitate standardization of credit scores among credit reference bureaus (CRBs). Subsequent to this harmonization, institutions will be required to source for credit scoring rating from any of the licensed CRBs with an option of complementing the CRB's rating with their internal credit scores for effective risk management.

CRBs have enriched datasets as compared to individual institutions as they collect credit information from both institutions and other third party data sources; availing comprehensive information for sound decision making.

- The use of appropriate credit scoring techniques shall be ascertained by CBK through various avenues, including during on-site examinations and through conducting consumer protection diagnostic exercises like mystery shopping surveys.

To enhance fairness, it is also critical to ensure that transparency and full disclosure of the terms and pricing of products is implemented. In line with the Prudential Guideline on Consumer Protection Guideline and Consumer Protection Act, 2012, institutions are henceforth required to publish in their respective websites and places of business: -

- **Key fact statements (KFS)** of all products to be developed in line with the Risk Management Guideline on Credit Risk Management as well as Prudential Guideline on Consumer Protection. The key features expected to be included in a KFS include: type of product, costs, target clientele, risks, rights and obligations of the parties and legibility of the statement in terms of use of simple language and easy format. For digital products, provision of the abridged version of the terms and conditions to consumers using Unstructured Supplementary Service Data (USSD) format is critical before acceptance of the product. Terms and conditions of their products including, but not limited to, allowance of cooling off period, customer complaint processes, protection of consumer data and privacy should be disclosed. Full disclosures should be included in documentation such as credit agreements, key fact statements and websites. Abridged versions of the salient features to be placed in the places of businesses (outlets, marketing offices, agents, headquarters and branches).

---

[5] The TWG comprises of representatives from selected commercial banks and microfinance banks, Credit Information Sharing Association of Kenya (CIS-Kenya), Kenya Bankers Association (KBA), World Bank, Credit Reference Bureaus (CRBs) and Central Bank of Kenya (CBK).

- **Complaints handling and consumer recourse mechanisms.**

    - An institution, on receiving a complaint, shall provide the complainant with a prompt written acknowledgement[6] within 48 hours and resolve the complaint in 7 working days. For complaints not resolved within 7 working days, written updates should be forwarded to the customer on the progress in resolving the complaint, once in every seven days.

b. Transparency

A joint initiative by the Kenya Bankers Association and the Central Bank of Kenya (CBK), to enhance transparent pricing reporting was launched in June 2017. Some commercial banks are yet to upload their charges and fees to the website which is aimed at enhancing transparency in the pricing of credit.

It is against this backdrop that CBK now mandates **all commercial banks to upload their respective internal and external fees[7] for all products on the cost of credit website** to enable customers make rational financial (product) decisions. The institutions will be held liable on any erroneous or outdated data posted in the website arising from the institutions' errors. Failure to adhere to this clause will result to administrative sanctions as embedded in Section 49 of the Banking Act.

Further the Banking industry should begin to move towards the development of a **Banking Services Pricing Index.** The index will help in: -

- Measuring the weighted average of prices of a basket of banking services, such as direct and intermediation prices. This will be calculated by taking price changes for each banking service in the predetermined basket of banking services and averaging them.
- Comparing between prices of banking services for any two periods.
- Comparing between prices of banking services for any two institutions.

---

[6] Written communication consists of:

- registered mail or certificate of posting;
- e-mail;
- short message service through the customer's registered telephone number; or
- physical delivery of the letter evidenced by acknowledgement of receipt by the customer or his nominee, where the physical address of the customer is known.

[7] External loan-related fees charged by third party service providers (such as legal, valuation, insurance, stamp duty) to be in line with the prescribed Remuneration Orders for the various services offered by the third party service providers.

c. Financial Literacy

As banking services and products become sophisticated and widespread throughout the country, financial literacy[8] will need to be addressed in order to ensure proper use of the available banking services and products offered by institutions. Increases in access to banking services along with rapid growth of the financial sector, will cause more consumers to be exposed to risks that these products/services pose through their normal use. Improved information disclosure may be counterproductive if the information disclosed is not understood by consumers with low level of financial literacy.

In this regard, institutions should:

- Facilitate technical assistance through appropriate financial literacy[9] to potential and existing customers in the Micro, Small and Medium Enterprises (MSMEs) sector in an effort to enhance their financial skills necessary to secure and utilize finances.
- Develop financial literacy initiatives that are distinct from the common product advertising and marketing, and that are more targeted, strengthened and coordinated to have greater impact in terms of effectiveness and efficiency. The financial literacy initiatives will be unique to a bank based on the adopted business model and strategy.

d. Financial Access

The Banking Sector Charter is intended to broaden and hasten the transformation process of the banking industry into a responsible and disciplined industry. This will be through a focus on making banking services accessible to the previously unbanked and under-served through the provision of affordable financing of MSMEs and other underserved segments of the Kenyan economy.

To broaden the outreach of banking services, there is need for institutions to embrace new business models deploying technologies and risk management systems to serve all consumer segments, particularly the un-banked and under-banked. Therefore, the business models of banks should be innovative, responsive and dynamic to address the specific needs of their customers.

In this regard, institutions should demonstrate:

- Consumers input towards the development of the product are considered;
- Strategic benefit of the product to the consumer is evidenced;
- Required resources and competences to offer the products sustainably are available; and

[8] The Organization for Economic Cooperation and Development (OECD) has **defined financial literacy** as follows: 'A combination of awareness, knowledge, skill, attitude and behavior necessary to make sound **financial** decisions and ultimately achieve individual **financial** wellbeing.'

[9] Financial literacy helps in empowering and educating MSMEs so that they are knowledgeable about finance in a way that is relevant to their business and enables them to use this knowledge to evaluate products and make informed decisions. (Source: International Journal of Economics, Finance and Management Sciences 2017; 5(3): 173-181)

- Innovative and dynamic business models and channels are employed.

Similarly, for the consumers who are perceived to be risky and thus barred from accessing banking services optimally, credit risk reduction mechanisms such as insurance products, collateralization of transactions and risk-sharing and transfer arrangements should be considered and adopted.

In this regard, to achieve the desired penetration of affordable and appropriate banking services, institutions should promote enterprise development. In this regard, each institution to evaluate its existing processes to promote lending to MSMEs, as well as document the initiatives that the institution is undertaking to promote access to finance for MSMEs. December 2018 will be used as a baseline.

5. Compliance with Charter

Banks should develop and submit to CBK a time bound plan approved by the institution's Board to comply with the Charter that is approved by the Board by May 31, 2019. The plan is to be signed by both the Chairman and Chief Executive Officer of the institution.

The plan will be used by CBK to monitor compliance and should focus on the new banking sector vision hinged on the four key pillars: transparency, responsible pricing, customer-centric models and ethical culture.

6. Reporting Mechanism

Each institution shall submit a quarterly report to CBK on the progress of its implementation of the Charter within 10 days after the end of every calendar quarter.

7. Remedial Measures

CBK may assess and levy monetary penalties as provided for under the Banking Act and Microfinance Act against any institution that violates, contravenes or otherwise fails to comply with the Charter. In addition, CBK may pursue any or all remedial actions and take such other administrative actions as it may deem appropriate in the circumstances.

8. Effective Date

The Charter is effective from March 1, 2019.

CENTRAL BANK OF KENYA
FEBRUARY 2019

Glossary of Terms

1. **Agent banking** is an alternative delivery channel for offering banking services in a cost effective manner using entities contracted by an institution to provide specified banking services on its behalf.
2. **Banking Services Pricing Index –** is a measure that examines the weighted average of financial services and products prices over time.
3. **Cooling off Period** refers to the time allowed under law to enable a consumer to cancel an agreement without incurring any penalty.
4. **Credit risk reduction mechanisms** – refers to risk management techniques used by financial institutions to mitigate their credit risks exposures.
5. **Customer Centricity** is a deliberate strategy by financial institutions that seeks to re-orient their entire operating business model around the customer, increasing customer satisfaction and their own profitability in the process.
6. **Credit Information Sharing** refers to a process where credit providers (such as banks, microfinance institutions, Saccos, etc.) exchange information on their outstanding loans and advances through licensed Credit Reference Bureaus (CRBs).
7. **Credit scoring** entails use of judgment, statistics or both in predicting the customers' ability to repay a loan.
8. **Micro, Small and Medium Enterprises (MSMEs) -** Under the Micro and Small Enterprises (MSE) Act, 2012;

   Micro enterprises refer to any firm, trade, service, industry or a business activity, whether formal or informal, that has an annual turnover that does not exceed **Ksh. 500,000** and employing (or rather engaging) **1- 9 people**. The total assets and financial investment or the registered capital of the enterprise does not exceed **Ksh. 10 million** in the manufacturing sector and does not exceed **Ksh. 5 million** in the service and farming sector.

Small enterprises are those firms, trade, service, industry or business activities that post an annual turnover of between **Ksh. 500,000** and **Ksh. 5 million** and have **10-49**

employees. In the manufacturing sector, investment in plant and machinery should be between **Ksh. 10 million** and **Ksh. 50 million** and registered capital of the enterprise between **Ksh. 5 million** and **Ksh. 25 million** in the service and farming sector.

9. **Mystery Shopping Survey -** Mystery shopping survey is a research approach that is used to amongst others, test customer experience in obtaining services; evaluate compliance with regulation or to gather specific information about products and services.