

**A CRITICAL ANALYSIS OF KENYA'S LEGAL FRAMEWORK FOR DEPOSIT
TAKING SACCOS: TOWARDS A MORE EFFICIENT REGULATORY FRAMEWORK
FOR TRANSPARENCY AND ACCOUNTABILITY**

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G62/7818/2017

**A RESEARCH PROJECT SUBMITTED TO THE UNIVERSITY OF NAIROBI LAW
SCHOOL IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE MASTER OF
LAWS (LL.M) DEGREE PROGRAM**

December, 2019

DECLARATION

I, ALEX ITHUKU, do hereby declare that this is my original work and that it has not been submitted and is not being submitted for the award of a degree or any other academic credit in any other university.

Signed.....

Date.....

Alex Ithuku

This thesis has been submitted for examination with my approval as the University Supervisor

Signed.....

Date.....

Prof. Kiarie Mwaura

DEDICATION

To my dear wife Candy Mwalimu for her love, support and patience.

To my sons, Ian and Paul: They can now unmute the TV.

ACKNOWLEDGEMENT

I am most grateful to *Ngai Mulungu* for good health, grace and unconditional providence.

This thesis would not have been possible without invaluable counsel and guidance of my supervisor, Professor Kiarie Mwaura, from whom I have learnt a lot and developed keen interest in corporate law. I am humbled, honored and privileged to have worked under his supervision.

Finally, I am grateful to all my friends who offered their support and do sincerely thank Fatuma Rashid, Melissa Ng'ania and Rachael Ng'etich for the lengthy group meetings and discussions.

LIST OF STATUTES

Bank of England and Financial Services Act, 2016 (UK).

Companies Ordinance of 1901 (Kenya).

Co-operative and Community Benefit Societies Act, 2014 (UK).

Co-operative Societies (Amendment) Act 2004 No. 2 of 2004.

Cooperative Societies Act, Chapter 490, Laws of Kenya.

Co-operative Societies Ordinance of 1945 (Kenya).

Cooperatives Societies Act 1997, No. 12 of 1997, Laws of Kenya.

Cooperatives Societies Act, 1966, Laws of Kenya.

Cooperatives Societies Registration Ordinance 1931 (Kenya).

Credit Unions Act, 1979 (UK).

Financial Services Act, 2012 (2014) (UK).

Financial Services and Markets Act, 2000 (UK).

Public Officer Ethics Act, Chapter 183, Laws of Kenya.

SACCO Societies Act, Chapter 490B, Laws of Kenya.

Transition to Devolved Governments Act 2012, No. 1 of 2012, Laws of Kenya.

Federal Credit Union Act, 1934 (USA).

LIST OF ABBREVIATIONS

CFPB- Consumer Financial Protection Bureau

DT-SACCOs- Deposit Taking Savings and Credit Cooperative Societies

EACC- Ethics and Anti-Corruption Commission

ECCOS- Ethics Commission for Cooperative Societies

FCA- Financial Conduct Authority

FPC- Financial Policy Committee of the Bank of England

FSA- Financial Services Authority

FTC- Federal Trade Commission

IFRS- International Financial Reporting Standards

NCUA- National Credit Union Administration

NCUSIF- National Credit Union Share Insurance Fund

PRA- Prudential Regulatory Authority

SACCOS- Savings and Credit Cooperative Societies

SAPs- Structural Adjustments Programmes

SASRA- SACCO Societies Regulatory Authority

SDGs- Sustainable Development Goals

UK -United Kingdom

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ABSTRACT

Kenya's legal framework for DT-SACCOs provides for various periodic statutory reporting obligations designed to attain accountability and transparency between the members of a DT-SACCO, the Management Committee, the Commissioner for Cooperative Development and SASRA. However, the SACCO sector is facing a crisis which has seen the collapse or financial distress of major DT-SACCOs. And what is more is that both SASRA and the Commissioner take long to detect fraudulent and wrongful dealings, even where the dealings have continued for a span of years. This study seeks to investigate whether there are legal impediments that make SASRA and the Commissioner take long to detect the fraudulent and wrongful dealings despite their extensive supervisory powers. The study utilizes a combination of qualitative and doctrinal research methodologies to answer the research questions. In addition, interviews on key informants in the SACCO regulatory framework were also utilized.

The study revealed that Kenya's legal framework has been inefficient due to pertinent legal issues occasioned by the devolution of the cooperative function, the intermittent jurisprudence emanating from SASRA's enforcement tendencies, ineffective penalties and sanctions for non-compliance with statutory reporting obligations among others. It also revealed that Kenya has much to emulate from the UK's and the USA's experiences. The study found that the UK's regime is responsive to the financial muscles of the credit unions, with the financially stronger credit unions being subjected to more stringent regulatory requirements. In addition, it has a clear apportionment of duties amongst the regulatory authorities, with no instances of duplication or overlap. Further, the regulatory authorities have a special working relationship characterized by complementarity and partnership. The USA's regime has a dual-regulatory system in which federal credit unions are regulated by a national authority while state-chartered unions are regulated at the state level.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The cooperative societies' movement in Kenya started before independence and has since undergone significant developments to its current state. The first co-operative society was established in 1908, and the first co-operative ordinance was enacted in 1931.¹ The co-operative enterprise has significantly mutated over time. Initially, the enterprise concentrated on traditional areas like agricultural production, processing and marketing. However, co-operatives have now ventured into finance, real estate and manufacturing.²

The Kenyan cooperative sector has turned out to be a key tool of wealth accumulation in terms of assets, savings and its preference amongst Kenyans. By July 2016, the Savings and Credit Cooperative Societies (SACCOS) sector controlled over Kshs. 500 billion in form of assets and savings, and about 63% of the population depended on the co-operatives activities. It had mobilized over 200 billion in savings, which then was over 30% of national savings as well as accounting for 80% of the total accumulated savings.³ By the end of 2016, there were 18,573 registered co-operatives, spread across all the sectors in Kenya.⁴ 177 deposit taking co-operatives⁵

¹ Government Printer, History and organization of cooperative development and marketing sub sector in Kenya, (2014) 2.

² Government Printer, National Co-operative Development Policy: Promoting Co-operative Enterprises for Industrialization (2017) 6.

³ Evans Njoroge Kamau, 'An Investigation into the Causes and Characteristics of Fraud in Kenyan SACCOs and Whether Benford's Law can be used to Detect Fraud in the Accounting Data' (Master of Commerce thesis, Strathmore University 2016) 11.

⁴ Kenya National Bureau of Statistics, 'Economic Survey 2017' (2017) 99
<www.devolutionplanning.go.ke/images/hb/Economic%20Survey%202017.pdf> accessed 26 July 2018.

⁵ SACCO Societies Act, 2008 s 2.

had approximately 3.1 million active members, who had mobilized over Kshs.272 billion in savings and carried loans of Kshs.288 billion.

In addition, the significance of the Kenyan co-operative societies in the national economy and their estimated potential towards achieving vision 2030 cannot be overemphasized. In particular, they form the backbone of rural economies where smallholder agriculture is prevalent. They also finance housing, education and agriculture. In addition, they provide financial intermediation, supply farm inputs and more importantly, they provide storage and marketing of produce.⁶ In terms of their contribution to the national economy, it is estimated that co-operatives societies contribute 31% of Gross Domestic Product (GDP).⁷

The Kenyan cooperative movement has been described as the most successful within the African continent. By 2007, Kenya had the strongest SACCO sector in Africa.⁸ In 2013, an empirical research ranked the Kenyan SACCO sector at the best in Africa and seventh internationally.⁹ The co-operatives enterprise has the potential to spur development in the Kenyan economy.¹⁰ In fact, the co-operatives could prove very instrumental in attaining the fundamental human rights articulated under Chapter 4 of the Constitution of Kenya, especially the right to adequate housing and the right to adequate food of acceptable quality.¹¹

⁶ Government Printer (n 2) 6.

⁷ Ibid 5.

⁸ World Council of Credit Unions, 'Global Regulatory Regime' (WOCCU, 3 June 2017). <https://www.woccu.org/advocacy/global_regulatory?post=1570> accessed 11 July 2018.

⁹ Government Printer, History and Organization of Cooperative Development and Marketing Sub Sector in Kenya, (2014) p. 6.

See also WOCCU - World Council of Credit Unions, 'Kenyan Credit Union Savings Reach a Record US\$5.7 Billion, 33% of National Savings' (WOCCU, 20 February 2018) <<http://www.4-traders.com/news/WOCCU-World-Council-of-Credit-Unions-Kenyan-Credit-Union-Savings-Reach-a-Record-US-5-7-Billion--17421111/>> accessed 11 July 2018.

¹⁰ Government Printer (n 2) 6.

¹¹ Ibid.

However, this economic growth is being threatened by the collapse of major SACCOs and sporadic mismanagement crisis facing cooperative societies in the recent past. Every inquiry into these occurrences seems to develop a disquiet about the efficacy of the Kenyan legal framework on the DT-SACCOs. Specifically, a keen observation of the inquiries boils down to a question of whether the legal framework is efficient with respect to ensuring transparency and accountability between the members, the Commissioner for Cooperatives and SASRA. Given every opportunity, the inquiries demonstrate that there is information asymmetry amongst the key players in the registration, management and supervision of DT-SACCOs. Such was the case in the circumstances surrounding the Harambee SACCO scandal in 2012, where civil servants lost billions of their deposits and savings.¹²

The SACCO had violated almost all SASRA prudence parameters especially with regard to keeping and maintaining financial books of accounts. It had been using accounting tactics to cover up fraud and non-payment of loans by some members. It had operated without an internal audit function and its internal auditor was not registered with the Institute of Certified Public Accountants of Kenya.¹³ In addition, the internal auditor was also the SACCO's front office services activities (FOSA) manager for a considerable duration, the upshot of which was conflict of interest, as he audited the very department he was supervising. There was irregular overdrawing of accounts by directors, the management had understated its bad debt and it disbursed loans without following due process.¹⁴

¹² Matthew K, 'Civil servants to lose billions in Harambee Sacco scandal' *Business Daily* (Nairobi, 4 November 2012) 11.

¹³ Ibid.

¹⁴ Ibid.

The fraudulent and wrongful dealings have detrimental economic and social impacts especially in terms of loss of jobs and decelerating the growth of the economy. These dealings have occasioned tremendous losses of members' funds, liquidation and collapse of financially distressed SACCOs.¹⁵ Members of collapsed or distressed DT-SACCOs have had difficulties in accessing credit facilities,¹⁶ and some of the SACCOs have gone under with substantial amounts of members' life savings.¹⁷ Uncertainty on whether members of a distressed SACCO will ever recover their savings is not good for the sector nor its membership, which draws largely from small-scale traders.¹⁸ Furthermore, these dealings ultimately prejudice the growth of the sector and destabilize the viability of SACCOs as vehicles to achieve financial inclusion, thereby inhibiting the progressive realization of the constitutional social and economic rights and realization of the Sustainable Development Goals (SDGs). A prudential regulatory regime for DT-SACCOs is an effective tool for poverty reduction and promotion of sustained, inclusive and sustainable economic growth.¹⁹

The governance structure for cooperative societies comprises the members at the Annual General Meeting (AGM), Management Committee and a Supervisory Committee. Each member has one vote regardless of their amount of savings.²⁰ The general cooperative societies are regulated by the

¹⁵ Lucy Ngaira, 'The Impact of Sacco Regulatory Authority Guidelines on Sacco Operations in Kenya- The Case of Nairobi Deposit Taking SACCOs' (MBA thesis, University of Nairobi 2011) 14.

¹⁶ Ali Abdi, 'Teachers want Sh100m Sacco cash recovered' *Standard* (Nairobi, 8 December 2017) 8.

¹⁷ Martin Munyi, 'Sacco Regulator Urged To Crack The Whip On Fraudulent Savings' Societies' (*Kenya News Agency*, 26 February 2019) <<http://www.kenyanews.go.ke/sacco-regulator-urged-to-crack-the-whip-on-fraudulent-savings-societies/>>accessed 26 August 2019. (For instance, in 2019, Ekeza SACCO collapsed and thousands of members are staring at losing over Sh. 1 billion of their life savings. A similar occurrence was witnessed in 2014 when Isiolo Teachers SACCO went under).

¹⁸ Leopold Obi, 'Anguish as Ekeza Sacco sinks with Sh1 billion in savings' *Daily Nation* (Nairobi, 23 February 2019) 11.

¹⁹ Government Printer, Implementation of the Agenda 2030 for Sustainable Development in Kenya (2017) 20. See also Constitution of Kenya, 2010 Ar. 43 1 (a-f).

²⁰ Edward K. Mudibo, 'Corporate Governance in Co-Operatives: The East African Experience' (The 3rd Pan-African Consultative Forum on Corporate Governance, Dakar, November 2005) 1-3.

Cooperatives Societies Act,²¹ while the SACCOS are regulated by both the Cooperative Societies Act and the SACCO Societies Act.²² The Cooperative Societies Act generally regulates all the SACCO Societies in Kenya, while the SACCOS Act specifically regulates the Deposit-Taking SACCO Societies (DT-SACCOS). The Cooperative Societies Act is administered by the Commissioner for Cooperatives, while the SACCOS Act is administered by the SACCOS Regulatory Authority (SASRA), a state agency established under the Act.²³

The key players in the SACCO regulatory framework are: the members sitting at the AGM, the management committee, the supervisory management committee, SASRA, and the Commissioner. Each of the players has particular designated reporting obligations. The management committee should report to the members at the AGM and to the Commissioner. In particular, the committee is required to file its audited annual financial statements to the commissioner,²⁴ and to present its reports to the members at the AGM.²⁵ It is obliged to audit its accounts annually.²⁶ The supervisory committee²⁷ is required to present its reports to the members at the AGM and to submit its reports to the Commissioner.²⁸ The management committee of a DT-SACCO is required to file its audited annual financial accounts with SASRA.²⁹

²¹ Cooperatives Societies Act, Chapter 490, Laws of Kenya.

²² SACCO Societies Act, Chapter 490B, Laws of Kenya.

²³ Ibid.

²⁴ Co-operative Societies Act, 2008 s 25 (10).

²⁵ Co-operatives Societies Act, 2008 s 27 (5).

²⁶ Co-operative Societies Act, 2008 s 25 (8). and the auditor is required to submit the audited annual financial accounts to the members at the AGM.

²⁷ Co-operative Societies Act, 2008 s 28. This is a three-member committee elected to oversee the management of the society, but whose duties are distinct and separate from those of the Management Committee.

²⁸ Co-operatives Societies Act, 2008 s 28 (3).

²⁹ SACCO Societies Act s 41.

1.2 Statement of the Problem

In the very recent past, the SACCO sector has experienced collapse or near collapse of major DT-SACCOs, like the Harambee SACCO, Kenya Midland SACCO, Transmara SACCO and Tekangu Farmers' Cooperative Society. For starters, the law imposes annual reporting requirements on the managements committees requiring them to report to SASRA and the Commissioner. However, a critical analysis of the scandals reveal that the two regulators take too long to detect and identify the wrongful transactions within DT-SACCOs. In Harambee SACCO, the wrongful transactions had occurred for a period spread over three years, in Tekangu five years, in Transmara three years while in Kenya Midland SACCO four financial years. Given that the regulators are supplied with annual reports, it is expected that they should be in a position to detect and arrest the situations in good time.

1.3 Objectives of the Research

1. To investigate the efficacy of the Kenya's legal framework in attaining accountability between the board of a SACCO, SASRA and the Commissioner.
2. To examine the legal challenges that impede transparency and accountability between the board, SASRA and Commissioner and how these challenges contribute to financial mismanagement in DT-SACCOs.
3. To examine the extent to which the UK's and the USA's experiences on SACCO regulation provide lessons which Kenya can emulate in the pursuit of a more efficient legal framework.
4. To propose the necessary reforms on the Kenyan legal framework in the pursuit of a sound and prudent regulatory regime.

1.4 Research Questions

1. To what extent is the Kenya's legal framework efficient in attaining accountability between the board of a SACCO, SASRA and the Commissioner?
2. What are the legal challenges that impede transparency and accountability between the board, SASRA and Commissioner and how do these challenges contribute to financial mismanagement in DT-SACCOs?
3. To what extent does the UK's and the USA's experiences on SACCO regulation provide lessons which Kenya can emulate in the pursuit of a more efficient legal framework?
4. What are the necessary amendment/reforms on the Kenyan legal framework in the pursuit of a sound and prudent regulatory regime?

1.5 Theoretical Framework

Agency Theory

The agency theory assumes a two-tier form of corporate control; corporate shareholders and corporate management. These two players establish a principal-agent relationship. The principals are the shareholders while the agents are the corporate managers, hired by the shareholders to run the company on their behalf.³⁰ According to the theory, the main aim of a company is to maximize its stock market value, and thus its managers are primarily responsible for maximizing shareholders' wealth.

Ordinarily, the company's aim of maximizing its market value is not compatible with the interests of the corporate managers. This is because the corporate managers will prefer to maximize their

³⁰ Michael C. Jensen and William H. Meckling, 'Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure' (1976) 3 (4) *Journal of Financial Economics* 305, 308.

own personal interests at the expense of the shareholders. The end result of these apparent discrepancy of interests is agency conflicts, which are more pronounced in public companies where there is the separation of ownership and control.³¹

The conflict between shareholders and managers has resulted in the formulation of contracts to mediate the agency relationship. For the principal to limit agency conflicts, the shareholders have to incur agency costs.³² These are the additional costs emanating from the existence of conflict of interest situations among the stakeholders of a company, incurred by the owners of a company when ownership and control of the company are separated.³³ Agency costs are a combination of the monitoring expenditures of the principal, the bonding expenditures by the agent and the residual loss.³⁴

Kim and Nofsinger have suggested two solutions to the agency problems. The use of managerial incentives and managerial monitoring. The use of managerial incentive is made to tie the wealth of the executives to the wealth of shareholders thus aligning the interests of the shareholders with those of the corporate managers. This can be done by giving shares to the executive directors as a way of compensating them.³⁵ The utility of managerial monitoring is made to set up effective mechanisms for monitoring the behavior of corporate managers.

Masulis submits that the conflict of interest between the corporate managers and its shareholders is the most severe. This is the case, despite the fact that the shareholders have the right to appoint and dismiss directors, approve financial statements and appoint auditors rights to sell their shares

³¹ Ibid 353.

³² Kenneth Kim, John Nofsinger and Derek Mohr, *Corporate Governance* (3rd edn, Prentice Hall 2009) 21-23.

³³ Ross S, Westerfield R and Jaffe J, *Corporate Finance* (McGraw-Hill 2005) 41.

³⁴ Residual loss is the reduction in value of the firm that arises when the entrepreneur dilutes his ownership.

³⁵ Kenneth Kim, John Nofsinger and Derek Mohr, *Corporate Governance* (3rd edn, Prentice Hall 2009) 21-23.

eventually put the company at the risk of takeover or even declared insolvent and the right to participate and vote at the AGM.³⁶

Similarly, Jensen advocated for a mechanism of limiting the interest conflict between the directors and shareholders by aligning the interests of both groups. He advances a system which intertwines the managerial remuneration with the firm's performance. Further, he advocates for a system which limits the director's freedom of action, especially through the reduction of free cash flow.³⁷ Such reduction is done through dividend payouts, repurchasing of shares and incurring extra debt. The utility of these three 'free cash flow reduction' tools is to reduce the amount of money under control of the directors. They decrease free cash flow, thus reducing the chances of the directors undertaking unprofitable investments.

The utility and the effectiveness of the three tools have been under considerable scrutiny. Payment of dividends is not very effective, because it is always at the discretion of the directors. On the other hand, the idea of issuing of shares may not be effective: It will eventually dilute the shareholders holdings, to the extent that, if the change grants the shareholders insufficient control, the shareholders will not protect against the wastage of financial resources.³⁸

Continuing research in agency theory attempts to design an appropriate framework for effective corporate control which will force directors to act in the best interests of the company's shareholders. The agency theory operates under the basic assumption that there is non-existence

³⁶ R. Masulis, *The Debt/Equity Choice* (Ballinger 1988) 12.

³⁷ Free cash flow is the surplus of the cash required to fund all the projects that have positive net value.

³⁸ Magdalena Jerzemowska, 'The Main Agency Problems and Their Consequences' (2006) 14 (3) *Acta Oeconomica Pragensia* 9-17.

of a well-developed market for corporate control, occasioning market failures, moral hazards, non-existence of markets and asymmetric information.

Although the agency theory has been extensively used in the context of companies, the theory is equally relevant in the context of cooperatives. The conceptualization of a principal-agent relationship in the nature of companies is replicated in the cooperatives sector, where the members are the principals and the management committees are the agents. The members are the owners of the cooperatives and have the ultimate powers to appoint and remove a member of the management committee. Further, the meeting of the members at the general meeting is the supreme organ of the cooperative, from which the management committee derives its authority.

In the pursuit of solving the agency problems, company law has developed various governance mechanisms, which include, debt, developing an effective board of directors, markets for corporate control, prudent market competition, executive compensation and monitoring by financial institutions. This study advances the mechanism of monitoring by financial institution as a governance mechanism, by advocating for its efficacy and effectiveness in addressing agency problems.

The SACCOs sector is regulated by a financial institution, SASRA. The law regulates the managerial powers of the SACCO directors by requiring the directors to be accountable and transparent to both the members and SASRA. The study will form the basis of analyzing the relationship between the members, the Commissioner and SASRA, in pursuit of accountability and transparency within the DT- SACCOs, and effective managerial monitoring.

1.6 Hypothesis of the Study

The study proceeds on the following hypotheses:

1. That Kenyan legal framework for DT-SACCOs is inherently ineffective with respect to attaining accountability and transparency between the board of a SACCO, SASRA and the Commissioner.
2. That there are legal challenges that impede transparency and accountability between the board, SASRA and Commissioner and that these challenges contribute to financial mismanagement in DT-SACCOs.
3. That these challenges have occasioned information asymmetry between the two institutions with subjects of the law eventually falling through the cracks.
4. That these legal gaps and inadequacy can be cured through legislative intervention and that the UK's and the USA's experiences on SACCO regulation can provide positive lessons which Kenya can emulate in the pursuit of a more efficient legal framework.

1.7 Scope of the Study

The study investigates the effectiveness of the Co-operative Societies Act and the SACCO Societies Act, with respect to attaining transparency and accountability in the SACCO regulatory framework. Given that DT-SACCOs are regulated by SASRA, which was established in 2008 under the SACCO Society Act of 2008, the study will focus on instances of mismanagement which have occurred since 2008.

1.8 Justification of the Study

The significance of the study cannot be overemphasized as it will go a long way towards facilitating and streamlining the achievement of the Government's long term economic-development agenda. A prudent legal framework will be an effective too in realizing the SDGs, especially through poverty reduction and the promotion of sustained, inclusive and sustainable economic growth.³⁹ Under Vision 2030 Blue Print, the Government of Kenya outlined the strategic plans it intends to undertake for the realizing of its long term development agenda. On the financial sector, the government intends to facilitate financial access by strengthening of alternative financial service providers, especially SACCOs.⁴⁰

In addition, the study will assist policy makers to come up with an enabling legal and regulatory environment, which will strengthen the government in monitoring of DT-SACCOs. Under the blue print, the government specifically identified the major constraint to the growth of the SACCOs sector as the lack of effective regulatory framework. Consequently, driven by the need to enhance stability in the financial sector, the government is determined to among other things prepare a targeted supervisory regime for SACCOs.⁴¹

1.9 Research Methodology

The research has taken a mixed approach, which combines comparative and doctrinal research methodologies. The doctrinal research methodology is usually useful when analyzing the legal, institutional and policy framework of a particular jurisdiction. Under this approach, the study has analyzed the Kenyan legal provisions on accountability between the key regulators of DT-

³⁹ Government Printer, Implementation of the Agenda 2030 for Sustainable Development in Kenya (2017) 20.

⁴⁰ Government Printer, Kenya Vision 2030: A Globally Competitive and Prosperous Kenya (2007) 87.

⁴¹ Ibid 89-92.

SACCOs, with a keen emphasis on their source and their eventual implication in the legal framework. Through this methodology, the study has examined the history behind the current legal framework on DT-SACCOs as it appears in the Co-operative Societies Act and the SACCO Societies Act.

Further, the study draws lessons from the UK and the USA with respect to their experiences on regulation of Credit Unions. It has utilized this approach to identify, analyze and explain the differences between their experiences, the lessons which Kenya can emulate and the conditions for the proposed emulation. It is generally agreed amongst legal scholars and Kenya policy makers that the UK and the US are the most advanced jurisdictions with respect to credit unions. The USA's regime for credit unions is very relevant in the Kenyan context, especially with respect to the Kenya's devolved system of governance, which is akin to the USA governance model. On the other hand, Kenya has always looked up to the UK with regard to issues pertaining to SACCOs on policy formulation, regulations and best practices.

Furthermore, the study has utilized primary data-collection methods in which it has employed both questionnaires and interviews. Interviews were conducted on the CEO of SASRA Mr. John Mwaka, CEO of the Cooperative Tribunal Mr. Sirro and the former Commissioner for Cooperative Development, Ms. Mary Mungai. The three persons identified are key informants since they have special knowledge on the regulation of DT-SACCOs by virtue of the office they occupy. In addition, the study utilized secondary sources of data which included government reports, government policies, text books, journals articles, and conference papers and reports.

1.10 Literature Review

The discourse on the regulation of SACCOs is not new internationally, regionally and even in the Kenyan context, as several scholars have variedly written on the subject matter. Most of these writers have addressed the philosophical foundations of a prudent legal regime for SACCOs, and the several attributes of a sound legal framework. While there is general consensus on the importance of accountability and transparency amongst the key players of the regulatory framework, none of the scholars has investigated the efficacy of the Kenya's legal framework in attaining accountability between SASRA, the board and the Commissioner.

Borgia⁴² argues that transparency emanates at the intersection between the public's right to know and the company's right to privacy. He has defined the public's right to know to incorporate the interest of the stakeholders in obtaining information about the corporation's management and strategy. He further defines the corporation's right to privacy to include its right to control the collection and disclosure of its information and management strategies.⁴³ He discusses four key elements of transparency in a corporation; the senior management's commitment and dedication to a culture of openness and transparency, a regulatory regime that ensures openness at every level by rewarding transparent managements while rendering timely punishment for opacity and actions of fraud, a regime that grants corporate managers and employees the confidence and security to do and to report what is right without fear of consequences and the establishment of a regulatory framework that facilitates proactive communication to the corporation's key stakeholders.⁴⁴

⁴² Borgia Fiammetta, 'Corporate Governance & Transparency Role of Disclosure: How to Prevent New Financial Scandals and Crimes?' (2005) Transnational Crime and Corruption Center, 9.

⁴³ Ibid 20.

⁴⁴ Ibid 22.

He places high premium on the facilitative function of disclosure, and concludes that disclosure rules must be designed to objectively facilitate and enable the decision-making of the stakeholders, in exercising their respective oversight role on the corporation.⁴⁵

Davies and Worthington argue that the rationale of the annual reporting requirements of a company is the principle of accountability and transparency in the management of corporate entities. They point out that providing the relevant information to the stakeholders is an effective way of empowering them to exercise oversight over the board and safeguard their interests.⁴⁶ The principle of accountability and transparency plays two fundamental functions. First, it promotes efficient conduct of the company's business because the company's controllers may fear the reputational losses associated with the revelation of incompetence or self-dealing. Second, it informs those who hold legal rights about the company's position, placing them in a better position to enforce both the company's rights against directors for breach of duty and the shareholder's right to remove directors.⁴⁷ They argue that unless the right holders are aware of the company's position, they will have no grounds for exercising their rights.

Kemei and Mweberi⁴⁸ have analyzed the role and the effect of corporate governance practices in financial management of NGOs in Kenya. They establish a positive link between adherence to good governance and success of an organization. They argue the challenge of adhering to accountability and transparency principles is more pronounced in public enterprises than in their private counterpart. They associate this challenge to the governance structure adopted by state-

⁴⁵ Ibid 31.

⁴⁶ Davies P and S Worthington, *Gower's Principles of Modern Company Law* (10th edn, Sweet & Maxwell 2016) 689.

⁴⁷ Ibid 690.

⁴⁸ Felix Kemei and Evans Mweberi, 'Effect of Corporate Governance practices on Financial Management in Non-Governmental Organization, Kenya' (2017) 5 *International Journal of Economics, Commerce and Management* 599, 609.

owned enterprises, under which the government delegates its management responsibilities to a cabinet secretary. They argue that the relationship between the cabinet secretary and the corporate managers is vulnerable to political agendas. They recommended the utilization of independent internal audit mechanisms and effective governance-monitoring regulatory frameworks.⁴⁹

They argue that corporations should be accountable to both themselves and to multiple external stakeholders, by adopting an internal system for checks and balances, through which the stakeholders can restrain and moderate the control of the corporate's management. They opine that an explicit legal framework on corporate governance is a precondition to establishing a stable and predictable framework for accountability and transparency in corporations.⁵⁰

Kamau⁵¹ singles out financial statement fraud as the most lethal form of mismanagement in Kenyan SACCOs. He describes it to entail the manipulation of financial statements. According to him, it can take different forms for instance through manipulation of stock price, increased year-end- bonuses and favorable loan terms. He noted that it was this kind of fraud which informed the several amendments to the Co-operative Societies Act. However, even with the amendments, periodic inspections and supervision by SASRA, he points out that this fraud continues to appear. He goes ahead to recommend new measures on how to detect fraud because the financial statements computed by the SACCOs management may be insufficient, on their own, to detect the fraud. He suggests Benford's Law as the most suitable alternative to detect fraud in fraudulent financial statements in SACCOs.

⁴⁹ Ibid 613.

⁵⁰ Ibid 604.

⁵¹ Evans Njoroge Kamau, 'An Investigation into the Causes and Characteristics of Fraud in Kenyan SACCOs and Whether Benford's Law can be used to Detect Fraud in the Accounting Data' (Master of Commerce thesis, Strathmore University 2016) 10-27.

Mudibo identifies gross mismanagement, misappropriation of funds, illegal and unauthorized investments as the common fraudulent ways through which SACCO Committees violate the regulations.⁵² However, he has not identified even one SACCO where such one incident occurred.

He also examined the relevance of corporate governance within cooperative managements. He found that there were low compliance levels and he attributed this to weak regulations and ineffective supervision of the cooperatives. However, his identification is too general to solve the menace. He does not specify the weak regulations neither does he outline how the supervisions are inadequate.

FSD Kenya investigated SASRA's role and its effectiveness in ensuring SACCOs' compliance with the legal requirements. It established that the Authority has failed to effectively oversee the SACCO sector. However, it never established why the Authority remained toothless, even with the empowering statute provisions.⁵³

1.11 Chapter Breakdown

This study is comprised of five chapters.

Chapter One- Introduction. The chapter outlines the agenda of the study. It begins with a background of the study, followed by a statement of the problem, which articulates the specific legal problem under study. This is followed by an elaborate literature review, which demonstrates the gap in the literature. This is followed by a comprehensive theoretical framework, the

⁵² Edward K. Mudibo (n 20) 2.

⁵³ Brian Ngugi, 'Weak control puts billions of Sacco cash at risk of loss' *Business Daily* (Nairobi, 16 February 2017) 6. (The newspaper cutting discusses a report titled "A Technical Solution to a Political Economy Problem: FSD Kenya's Intervention in the Sacco Sector" which had revealed that Kenya's (Saccos) are operating without effective accounting and control systems, putting billions of savers' funds at risk).

foundation upon which the study rests. Then there is an outline of the objectives of the study and its hypothesis, the basic assumptions upon which the study is taken. The chapter concludes with a discussion on the methodology adopted by the study.

Chapter Two- Historical Development of the Kenya's Legal Framework for DT-SACCOS. This chapter analyzes critically the historical background of the Kenya's legal framework for SACCOS. It does so by giving a detailed outline of the significant legal reforms which have been undertaken in the sector before, and after independence with a keen interest on the reasons behind the particular reforms. This essentially creates a picture of how the legislature has all along attempted to attain accountability between the key players in the sector in the pursuit of a prudent and sound legal regime.

Chapter Three- Kenya's Legal Framework for DT-SACCOS. This chapter examines the efficiency of the Kenya's legal regulatory framework for DT-SACCOS in attaining accountability and transparency amongst the key regulatory authorities. It does this analysis to explain why it is almost impossible for the members, the Commissioner and SASRA to notice or detect fraudulent and wrongful dealings in good time. It brings out the legal challenges which impede transparency and accountability between the board, SASRA and the Commissioner.

Chapter Four- A Critical Analysis of the UK's and USA's legal framework for Credit Unions. This chapter analyzes the UK's and USA's legal framework for Credit Unions with a view to identifying any positive lessons that Kenya can emulate. First, it justifies the choice of the two jurisdictions and the relevance of each in the Kenyan context. Additionally, it investigates how their respective legal frameworks have been implemented and how they have enhanced transparency and accountability between the key regulatory authorities.

Chapter Five- Conclusions and Recommendations. The chapter contains a summary of findings of the study and the conclusion taken by the study. Alongside this, it recommends the necessary legislative reforms on Kenyan legal framework with respect to attaining accountability and transparency between SASRA, the Commissioner for cooperatives and the board.

CHAPTER TWO

HISTORICAL DEVELOPMENT OF THE KENYA'S TRANSPARENCY AND ACCOUNTABILITY LEGAL FRAMEWORK FOR DT-SACCOS

2.0 Introduction

The chapter gives an in-depth overview of how the Kenya's legal framework for DT-SACCOs has evolved since the 1900 to 2019. It critically outlines the major legislative amendments which fundamentally shaped the legal landscape from a one-time sketchy legal framework to a world class legal regime. In addition, the chapter explains the reasons behind each particular legislative intervention by outlining the various inadequacies which it sought to cure. It undertakes the discussion under three major periods. The period before independence (1900-1962), the period between 1964 to 2003 and the period between 2004 and 2019. It essentially outlines the legislature's long-standing struggle to attain accountability between the key players in the sector in the pursuit of a prudent and sound legal regime.

2.1 Legislative Interventions in the Period 1900-1962

By 1900, Kenya had a very basic legal framework for cooperative societies under which the government did not directly regulate them, the cooperative societies were entirely on their own. The first Kenyan cooperative societies were formed by European farmers in the early 1900, with the primary objective of marketing agricultural products. In 1908, Lumbwa Farmers' Co-operative Society was registered as the first co-operative society, with the main objective of purchasing of agricultural inputs like fertilizer, chemicals as well as marketing agricultural products.⁵⁴ At that

⁵⁴ Githinji Wairimu, 'The evolution of Co-operative Societies in Nyandarua County, Kenya: The Case of Karagoini Marketing co-operative society in Ndaragwa Sub-County, C. 1965-2000' (MBA thesis, Kenyatta University 2014) 7. See Jeremiah Nyatichi, 'Co-operatives and Employment Creation: The Kenyan Case' (International Co-operative Alliance Seminar, Antalya, November 2015) 5.

time, there were no special legal framework for the establishment and regulation of cooperative societies. In fact, the Lumbwa society was initially not registered as a co-operative society, but under the Companies Ordinance.⁵⁵ In addition, the Government did not directly regulate the cooperative societies, as they were left entirely on their own, managing and operating on the initiatives of members.

Subsequent legislative reforms established a separate legal framework for the formation, registration and regulation of cooperative societies. These reforms were driven by the European Settlers, who sought formal recognition and protection of their cooperative societies. In 1931, the Cooperatives Societies Registration Ordinance was enacted,⁵⁶ and almost immediately, the Kenya Co-operatives Creameries (KCC) was registered, becoming the first cooperative society to be registered under the Ordinance. However, the Ordinance had shortcomings including the fact that it did not allow Africans to participate in the co-operatives movement.⁵⁷

The inadequacies of the 1931 ordinance were fairly addressed through the enactment of the Co-operative Societies Ordinance of 1945. The Ordinance prescribed elaborate mechanisms of ensuring accountability between the management committees, members and government. For instance, the Registrar of co-operative societies could hold an inquiry on the workings and the financial condition of a society.⁵⁸ In addition, the management committee was required to prepare annual accounts showing income and expenditure of the society.⁵⁹ Further, it was made an offence for an officer of the society to fail to provide accurate information.⁶⁰ Noteworthy, the Ordinance

⁵⁵ Ibid 25.

⁵⁶ Government Printer (n 2) 12.

⁵⁷ Co-operative Bank, 'Our History' (*Co-operative Bank*, 12 January 2018) <<https://www.co-opbank.co.ke/info/our-history>> accessed 29 May 2018.

⁵⁸ The Co-operatives Societies Ordinance 1945 s 42.

⁵⁹ The Co-operatives Societies Ordinance 1945 rule 23.

⁶⁰ The Co-operatives Societies Ordinance 1945 s 59.

recognized cooperative societies constituted by Africans with the objective of propelling the development of the movement.⁶¹

2.2 Legislative Interventions in the Period 1964-2003

Immediately after independence, the 1945 Act was considered inefficient with respect to enhancing accountability in the management of the cooperative societies. For instance, it did not provide adequate financial control and their supervision.⁶² In addition, it did not stipulate the manner of holding meetings and there were no channels of removing and replacing an inefficient member of a management committee.⁶³ Further, the management committees had too much unfettered powers such that the members could not effectively play their oversight role.⁶⁴ These inadequacies had overarching effect on the corporate governance. In fact, its regime was dominated by rampant cases of mismanagement and misappropriation of society funds.⁶⁵

The inadequacies of the 1945 Act necessitated legislative reforms, with the view to install accountability mechanisms in the societies sector. The independence Government desired a law under which the Minister and the Commissioner of Co-operative Development would have more supervisory and financial-control powers over the Co-operative Sector.⁶⁶ The felt inadequacies ignited a push for more legislative reforms. These initiatives led to the enactment of the

⁶¹ Government Printer (n 2) 12.

⁶² Kenya National Assembly Official Record (Hansard) 30 November 1966 p. 2184.

⁶³ Ibid 2185.

⁶⁴ Kenya National Assembly Official Record (Hansard) 7 December 1966 p. 2469.

⁶⁵ Kenya National Assembly Official Record (n 62) 2183.

⁶⁶ Ibid 2185.

Cooperative Societies Act 1966,⁶⁷ introducing a single legal framework for the Cooperative sector characterized by strict Government supervision of Cooperatives.⁶⁸

Subsequent legislative reforms on the Cooperative sector were informed by rampant and an unprecedented growth in the sector. For instance, the first SACCO was registered in 1964, and by 1975, approximately one thousand SACCOs were registered.⁶⁹ Within the sector, there were significant developments which ushered in a revolution in the operations of SACCOs. For instance, the SACCOs had developed what was then referred to as ‘bank offices,’ and they could give credit to their members. Simultaneously, rural agricultural marketing SACCOs were developing and farmers created what was referred to as ‘unions banking sections’; a department within the co-operative union of the district that would handle savings and payments to the farmers.⁷⁰

The widespread of these revolutionary developments encountered challenges which necessitated legislative reforms, with a view to redefine accountability in light of the new developments. For instance, members did not understand the nature and intricacies of these new developments and the managers of the SACCOs were not specially trained to undertake their new tasks. It was felt that the SACCOs should be run by accountable persons capable of assuming management positions and that there was a need to separate the main farming activities from the savings and credit activities of the unions.⁷¹ Consequently, a policy was introduced which separated the banking sections from the farming activities of the unions.⁷²

⁶⁷ Cooperative Societies Act 1966, Chapter 490, Laws of Kenya. This followed the operationalization of the Cooperatives Societies Rules of 1966.

⁶⁸ Charles Tibbs and Yegon Reuben, ‘The Effect of Economic Determinants on Performance of Dairy Cooperatives in Kericho County, Kenya’ (2015) 3 (6) International Journal of Economics, Commerce and Management 1497, 1498.

⁶⁹ Kenya National Assembly Official Record (Hansard) October 9, 2008 p. 2636.

⁷⁰ Ibid 2637.

⁷¹ Kenya National Assembly Official Record (Hansard) Sep 28-Dec 9, 1982 p. 544.

⁷² Kenya National Assembly Official Record (n 69) 2637.

Further legislative reforms in the SACCO sector were influenced by the World Bank and the IMF through the Structural Adjustments Programmes (SAPs). In the late 1980s, the World Bank and the IMF initiated the famous SAPs, under which the developing countries were required to loosen their strict control over their economies as a precondition for receiving their financial assistance.⁷³ The institutions felt that the Government was overregulating the sector through the complex monitoring by the Commissioner, inspectors and auditors.

The legislative reforms introduced the 1997 Government policy of Sessional Paper No. 6 of 1997, on *Co-operatives in a Liberalized Economic Environment*, which fundamentally reviewed the Government's involvement in the management of co-operatives. The policy provided a legislative framework under which co-operatives were to survive in a competitive economic environment.⁷⁴ The policy represented a radical shift which redefined the Government's role from strict control to regulatory and facilitative.⁷⁵

The policy framework formed the basis for and influenced the substance of subsequent legislative reforms. For instance, the Cooperatives Act 1997 was enacted,⁷⁶ repealing the Cooperatives Societies Act of 1966. The Act fundamentally reduced Government's involvement in the day to day management of the Cooperatives. For instance, the Act abolished the office of the Commissioner, which had been established under the 1945 Act and there was a reduction in the frequency and the number of audit and inspections. Instead, a registrar was established, whose role was to register the co-operatives and leave them to self-regulate themselves.⁷⁷

⁷³ Kenya Human Rights Commission, 'Robbery Without Violence' (2015) Research Study on the effectiveness of Kenya's Agriculture Co-operatives in Delivering Trade Justice for Farmers of Selected Products p. 18.

⁷⁴ Government Printer (n 2) 5.

⁷⁵ Charles & Yegon, (n 68) 1498.

⁷⁶ Cooperatives Act 1997, Act No. 12 of 1997.

⁷⁷ Government Printer, Kenya National Assembly Official Record (Hansard) 6 May 2004 p. 1000.

The Act brought a radical shift from perceiving cooperatives as subjects of Government control to granting them ‘internal self-rule’ and autonomy. For instance, it transferred management responsibilities from the Commissioner to the management committees. Particularly, they could invest, spend and even borrow, without the permission of the Commissioner.⁷⁸

Matters of accountability in the SACCO sector became more pronounced in the late 1990s as a result of the 1997 policy and legislative reforms. For instance, there was no regulator who could protect the interest of the members against fraudulent managements and members had no avenues of holding their management committees accountable.⁷⁹ Consequently, the newly acquired freedom was abused by the management committees as they had free hand to decide the fate of their membership⁸⁰ as a result of which many co-operatives were mismanaged and run down occasioning the loss of the lustre and glamour that they had.⁸¹

The 1997 legislative reforms did not enhance the concept of accountability in the SACCO regulatory framework. To a great extent, the members did not have mechanisms of holding their directors accountable. For instance, the management committees hardly convened an annual general meeting, especially when the committee was engaging in impropriety. Further, members could only make a request for a meeting to the district co-operative officer who could grant or deny the request as he found appropriate. Furthermore, fraudulent committees were assigning themselves allowances without the approval of the general membership.⁸²

⁷⁸ Wanyama Fredrick, ‘The Impact of Liberalization on the Cooperative Movement in Kenya’ (Strengthening and Building Communities: The Social Economy in a Changing World, Victoria, October 2007) 13.

⁷⁹ Kenya National Assembly Official Record (Hansard) 11 May 2004 p. 1050.

⁸⁰ Wanyama (n 78) 14.

⁸¹ Kenya National Assembly Official Record (Hansard) 6 May 2004 p. 1000. *See* Wanyama (n 78) 14. There were reported cases of gross mismanagement, failure to hold elections, unauthorized investments and illegal payments.

⁸² Kenya National Assembly Official Record (n 81) 1015.

These accountability challenges kindled a call for law reform, with the underlying objective of reinforcing accountability and transparency between the management committees and the general membership. For instance, it was felt that the law should empower the members in order to effectively play their oversight role.⁸³ Further, it was felt that the management committees should come up with budgets and proper estimates with a view to promote clarity in the manner in which they commit their finances. This change was informed by past experiences where management committees took advantage of the illiteracy of their members.⁸⁴

2.3 Legislative Interventions in the Period 2004-2019

These calls for law reforms led to legislative amendments which fundamentally reintroduced the Government's active role in the regulation of SACCOs. The amendments were made through the Co-operative Societies (Amendment) Act 2004,⁸⁵ which amended the Co-operative Societies Act 1997.⁸⁶ The amendment saw the re-invention of the role of the Commissioner, which entailed supervision powers, auditing society reports, routine inspections and general responsibility for the wellbeing of the Co-operative movement.⁸⁷

Considerably, the 2004 amendments illuminated the issues of transparency within the players of the SACCO regulatory framework. To a great extent, the amendments were designed to empower the members to effectively exercise their oversight roles on their management committees. It granted the members the right to requisition for a meeting when they felt it was necessary.⁸⁸ In addition, it prohibited officers and committee members from assigning themselves salaries or

⁸³ Kenya National Assembly Official Record (Hansard) 11 May 2004 p. 1046

⁸⁴ Ibid 1047.

⁸⁵ Co-operative Societies (Amendment) Act 2004, No. 2 of 2004. The Co-operatives Societies (Amendment) Act, 2004 became effective on 5th November 2004.

⁸⁶ Co-operative Societies Act 1997, No. 12 of 1997.

⁸⁷ Kenya National Assembly Official Record (Hansard) 6 May 2004 p. 1001.

⁸⁸ Ibid 1015.

allowances without an approval by the general meeting.⁸⁹ Furthermore, it granted members a right to access committee reports, annual financial statements, minutes of general meetings and supervisory committees.⁹⁰

In equal measures, the 2004 amendments reinforced accountability and transparency between the management committees and the Commissioner for Cooperatives. The management committee is mandated to file its annual audited financial accounts with the Commissioner,⁹¹ and the submitted accounts have to comply with International Financial Reporting Standards (IFRS).⁹² Further, the Commissioner acquired more powers, which included the power to approve the appointed auditors, convene a special general meeting, suspend fraudulent committee members, suspend a non-performing management committee and appoint an interim committee.⁹³

In early 2000s, there was a shared understanding that accountability in the regulatory framework could be enhanced by imposing integrity requirements and codes of ethics on the cooperative officers. For all this time, and with all these major developments in the sector, cooperative officers were not subjected to disciplinary proceedings and integrity requirements. Until 2002, there was no specific administrative body charged with the mandate of imposing discipline and integrity requirements on cooperative public officers. This was the case unlike their counterparts in other sectors, who were subjects of the Public Service Commission, the Judicial Service Commission, the Parliamentary Service Commission, and the Teachers' Service Commission among others.⁹⁴

⁸⁹ Ibid 1016.

⁹⁰ Cooperative Societies Act 1997 s 21.

⁹¹ Cooperatives Societies Act 1997 s 25 (10).

⁹² Cooperatives Societies Act 1997 s 25 (6) (a).

⁹³ Wanyama (n 78) 16.

⁹⁴ Ministry of Industry, Trade and Cooperatives, 'Ethics Commission for Cooperatives Societies (ECCOS)' (*Ministry of Industry, Trade and Cooperatives*, 2018)

<<http://www.industrialization.go.ke/index.php/departments/co-operatives-directorate/ethics-commission-for-cooperative-societies-eccos>> accessed 1 May 2018.

The idea to impose integrity requirements and code of conduct on the cooperative officers led to legislative reforms, with a view to establishing an administrative body, which would impose discipline on the Cooperative Officers. The reforms included the enactment of the Public Officer Ethics Act 2003 which defines a public officer to include cooperative staff and board or management committee.⁹⁵ The Act prompted the establishment of Ethics Commission for Cooperative Societies,⁹⁶ whose mandate is to promote good governance, ethical conduct and financial disclosure within the co-operative sector,⁹⁷ and its jurisdiction covers both officers and employees of cooperative societies.⁹⁸

The most recent 2008-legislative reforms on the SACCO sector were informed by the enormous and unprecedented growth and development within the sector. By 2008, the SACCO sector was the fastest growing sector of the co-operative movement. Indeed, 5000 of the 12,000 registered co-operative societies were SACCOs, which savings worth 170 billion. Out of the 5000 SACCOs, approximately 200 of them had front offices, and were operating like commercial banks. They had savings accounts, they issued debit cards, and people could borrow and deposit money.⁹⁹ With time, the front-office services within the SACCOs grew and the SACCOs were virtually competing with the commercial banks.

The legislative framework which existed pre-2008 legislative reforms could not adequately address accountability and transparency concerns in the regulation of DT-SACCOs. The SACCOs were generally managed and controlled by the Commissioner under the Co-operatives Societies Act, which was primarily meant for marketing agricultural co-operatives, and not to address

⁹⁵ Public Officer Ethics Act 2003 s 2 (e).

⁹⁶ Legal Notice No. 120 of 2003.

⁹⁷ Pursuant to the Public Officer Ethics Regulations 2003.

⁹⁸ Government Printer (n 2) 13.

⁹⁹ Kenya National Assembly Official Record (Hansard) 9 Oct 2008 p. 2637.

delicate issues arising from DT-SACCOs.¹⁰⁰ Further, both the financial reporting and the auditing of SACCOs' financial records were not done in accordance with IFRS. In most instances, the SACCOs' accounts were being audited by either an employee or a manager, inevitably compromising transparent financial reporting.

In addition, the pre-2008 regulatory framework was quiet on the issues transparency between the members and the management committees. There was general uncertainty and lack of uniformity in the manner in which the DT-SACCOs ran their businesses. In some instances, some DT-SACCOs could close their offices during working days, without the knowledge of the members. In addition, there was no regulatory authority for setting prudential guidelines on their management.¹⁰¹ Further, majority of the SACCOs had not made a difference between shares and deposits.

Similarly, the law failed to stipulate how the management committees would discharge their accountability obligations to both the members and the Commissioner. There were no set rules which prescribed how the committee would discharge their mandate. Further, there was a disconnect in the manner of communication between the Commissioner and the management Committees. In most instances, a SACCO would be mismanaged to the extent of collapsing before both the members and the Commissioner could realize that the SACCO was actually collapsing.¹⁰²

These new formation and operations of the DT-SACCOs qualified for legislative reforms to prescribe prudential guidelines and standards for the DT-SACCOs. As early as 2004, there were concerns that DT-SACCOs should be regulated under a separate legislation, owing to their unique

¹⁰⁰ Ibid 2638.

¹⁰¹ Ibid 2650.

¹⁰² Ibid 2651.

nature of being radically different from the ordinary co-operative societies.¹⁰³The idea was to establish an authority that would issue guidelines and prudential standards, as it was happening in the banking world.¹⁰⁴ The main objective of the legislative reforms was to introduce a regulatory authority which would improve governance in the cooperative movement, especially the DT-SACCOs.¹⁰⁵

The second concern was to enact a law which would impose disclosure requirements on the management, and incorporate transparency requirements through which members could monitor the activities of their SACCOs.¹⁰⁶ Alongside this, it was hoped that SACCOs should be regulated and licensed by people who understood finance, credit and savings and this would eventually lead to good governance.¹⁰⁷ Further, it was opined that the law should prescribe how to differentiate between the shares and the deposits with a view to prevent conflicts between the members and the management committees.¹⁰⁸

The intended functions of the proposed SACCO regulatory authority were relatively clear. It would install standards and uniformity in financial reporting and vet the senior members of the management committees.¹⁰⁹To enhance transparency, the SACCOs would be required to file annual reports to the regulatory authority.¹¹⁰ To a large extent, these reforms were designed to empower members to effectively play their oversight role by having a say and control over their

¹⁰³ Kenya National Assembly Official Record (n 87) 1017.

¹⁰⁴ Kenya National Assembly Official Record (n 99) 2650.

¹⁰⁵ Ibid 2639.

¹⁰⁶ Ibid 2640.

¹⁰⁷ Ibid 2639.

¹⁰⁸ Ibid 2654.

¹⁰⁹ Ibid 2651.

¹¹⁰ Ibid.

finances.¹¹¹ In other words, the sector was ripe for an elaborate legal and regulatory framework, which would introduce regulations, controls and standards within the DT-SACCO.¹¹²

Finally, the SACCO Societies Act of 2008 was enacted. The Act establishes SASRA, which is mandated to set prudential standards for the SACCO societies.¹¹³ The Authority is empowered to conduct inspections and inquiries into the financial affairs of the SACCO and it is entitled to receive any inspection reports.¹¹⁴ The Authority is in turn required to submit the report to the Commissioner and also present it to the board of directors.¹¹⁵ The Act provides for financial reporting in compliance with the international financial reporting standards¹¹⁶ and annual submission of audited financial statements to the SASRA.¹¹⁷ The law brought the requirement of an external auditor.¹¹⁸

Other minor legislative reforms have since occurred, with a view to enhance more accountability within the DT-SACCOs. With time, for instance, the structure of the ECCOS Board was criticized for being a purely internal Board and the public agitated for stakeholder participation. Consequently, section 7(2) of the Public Officer Ethics Regulations 2003 was amended, eventually including other stakeholders in the membership of board.¹¹⁹

Further legislative development on issues of transparency and accountability has been informed by the new Constitutional order. Post the 2010, the government has revised its policy to be in conformity with the Constitutional requirements of good governance, transparency and

¹¹¹ Ibid 2654.

¹¹² Ibid 2638.

¹¹³ SACCO Societies Act 2008 s 48 (2) (a).

¹¹⁴ SACCO Societies Act 2008 s 49 (1).

¹¹⁵ SACCO Societies Act 2008 s 49 (6) and (7).

¹¹⁶ SACCO Societies Act 2008 s 40.

¹¹⁷ SACCO Societies Act 2008 s 41.

¹¹⁸ Kenya National Assembly Official Record (Hansard) October 9, 2008 p. 2645.

¹¹⁹ Via Kenya Gazette Supplement No. 28, Legal Notice No. 64 of 2010.

accountability with respect to the leadership standards of cooperative societies.¹²⁰ For instance, the board and management committees are required to publish annual financial statements to their members prior to the convening a general meeting.¹²¹

2.4 Current Management Crises Facing the Sacco Sector

Even under the current legal framework, the SACCO sector continues to encounter challenges in ensuring accountability and transparency between the members and the management committees on one hand, and between cooperatives, SASRA and the Commissioner on the other hand. In 2014, an inquiry into the affairs of Kenya Midland SACCO Society Ltd¹²² revealed how the SACCO had lost Kshs. 1, 653, 950 through unauthorized and irregular issuance of cheques.¹²³ It also lost Kshs. 1, 173, 000 through fraudulent share capital overstatement, which occurred between 2009 and 2012.¹²⁴ Also, between November 2010 and May 2012, two committee directors received about Kshs. 626, 507 for loan repayment from members but failed to remit the same to the society.¹²⁵

Similarly, in 2016, an inquiry into the affairs of Transmara Sugar SACCO Society Limited¹²⁶ revealed that three former committee members could not account for cash amounting to Kshs. 1, 010, 979, for the years 2012, 2013 and 2014.¹²⁷ The three were also implicated in fraudulent transactions which cost the SACCO Society Kshs. 1, 597, 697.¹²⁸

Similar accountability and transparency issues were also evident in 2016, from an inquiry into the affairs of Tekangu Farmers' Cooperative Society Limited which established serious violation of

¹²⁰ Constitution of Kenya 2010, Article 10.

¹²¹ Government Printer (n 2) 29.

¹²² Government Printer, Report on Inquiry into the Affairs of Kenya Midland SACCO Society Ltd, (2015) 1.

¹²³ Ibid 24.

¹²⁴ Ibid 25.

¹²⁵ Ibid 19.

¹²⁶ Government Printer, Report on Inquiry into the Affairs of Transmara Sugar SACCO, (2016) 20.

¹²⁷ Ibid 36.

¹²⁸ Ibid 21.

financial management standards. The inquiry, which covered the period from March 2005 to December 2015, established that a former management committee had failed to apply prudence and diligence while discharging their duties and it could not account for Kshs. 8, 763, 917.¹²⁹ In particular, prior to mid-2014, most payments were done in cash and there was no cash verification done. There was absence of internal control mechanisms and no stock taking had taken place in the history of the society despite huge purchases of farm inputs.¹³⁰

2.5 Conclusion

The chapter reveals that by 1900, Kenya had a very basic legal framework for cooperative societies under which the government did not directly regulate them, the cooperative societies were entirely on their own and they were being managed and operated on the initiatives of members. Ever since then, the once sketchy legal framework has developed into a fully pledged legal framework apportioning different rights and duties to different players in the SACCO sector. To a large extent, the chapter demonstrates that the Kenyan legislative developments in this sector are majorly crisis-driven. In addition, one thing cuts across all these legislative interventions; parliament's attempt to enhance accountability between the board, the members of the DT-SACCO, the Commissioner and SASRA. The need to make the reforms and the urgency of the amendments have been informed by a host of factors; the rapid growth of the sector, technological advancements, introduction of new financial services which were not available in the conventional cooperative society and the ever present attempt to curb white collar crimes and fraud.

¹²⁹ Government Printer, Report on Inquiry into the Affairs of Tekangu Farmers' Co-operative Society Ltd, (2016) 8-11.

¹³⁰ *Ibid.* The report was compiled by Mrs Anne Ochoki and Nancy Muguro.

CHAPTER THREE

KENYA'S TRANSPARENCY AND ACCOUNTABILITY LEGAL FRAMEWORK FOR DT-SACCOS

3.0 Introduction

The chapter examines the efficiency of the Kenya's legal framework for DT-SACCOs in attaining accountability and transparency between the members of the DT-SACCO, the board, the Commissioner and SASRA. It investigates why the two major regulatory authorities, SASRA and the Commissioner, take long to detect, notice or identify instances of prolonged fraud and mismanagement. The chapter seeks to investigate why the legislative provisions of the two major statutes, the SACCOs Act and the Cooperative Societies Act, have failed to attain the initially intended consumer protection. Essentially, it offers a critical overview of the legal, institutional and policy framework with a particular emphasis on the different rights and duties created thereunder. Most importantly, the chapter investigates the efficacy these rights and duties in curing information asymmetry between the key regulatory authorities.

3.1 An Overview of the Nature of the Legal and Policy Framework

Tentatively, Kenya's legal framework for DT-SACCOs sets out certain standards whose adherence are key to underpin transparency in financial reporting. Cooperative societies are required to prepare and keep their accounts in conformity to International Accounting Standards¹³¹ and to ensure accessibility of the financial records for inspection by its supervisory committee.¹³² And what is more about the uniqueness of the framework is that it is not only concerned with the form of the reports, but also the content and quality of the information conveyed in the reports. The

¹³¹ Cooperatives Societies Act, s 25.

¹³² Cooperatives Societies Act, s 25 (2).

accounts should explain the transactions of the society, addressing all sums of money received and paid, all its sales and purchases and its assets and liabilities.¹³³

The framework has a sophisticated structure on reporting mechanisms designed to underscore transparency amongst the three, and which can be summarized as a three-tier reporting requirement. On the first tier, SACCOs are required to adhere to monthly reporting requirements which should state its position in terms of its liquidity, the amount of deposits and the adequacy of its capital. On the second tier, the SACCO is required to make quarterly reporting requirements which should provide elaborate information on its loan loss provisions, its investment returns and its general financial performance. The last tier imposes a duty to make annual reports which comprises of the audited financial statements of the particular SACCO.¹³⁴

More regulation has been enacted to bring into force the otherwise general provisions under the Act. Some of the them impose radical changes to the governance structure, in order to ensure optimal transparency and accountability in the management of SACCOs. For instance, there is a clear division of duties and responsibilities between the board and the management.¹³⁵ Further, the regulation enhanced the role of SASRA, with a view to make it more responsible for the day to day management of the SACCO. SASRA has powers to vet directors and senior management of the SACCOs¹³⁶ and to inspect the premises and the official records of a SACCO.

¹³³ Cooperatives Societies Act, s 25.

¹³⁴ Jared Makori, Charles Muturi and Willy Muturi, 'The Challenges facing Deposit-Taking Savings and credit Cooperative Societies' Regulatory Compliance in Kenya; A case of the Gusii Region' (2013) 4 (12) Interdisciplinary Journal of Contemporary Research in Business 1013, 1036.

¹³⁵ Ibid 1037.

¹³⁶ Ibid.

3.2 Interactions Between the Board, Members and SASRA

The framework has placed high premium on the transparency between the board and members, especially on matters concerning financial affairs of the SACCO and its liquidity. The SACCO's auditor is required to present the audited accounts before the general meeting, within four months after the end of the accounting period.¹³⁷ The members do have a right to receive audited accounts at the general meeting and the auditor has a corresponding duty to present the reports to the members at the AGM.¹³⁸ The board is required to display a copy of its last audited financial statements in a conspicuous position in every place of business and a SACCO which fails to comply is liable to pay penalties.¹³⁹ The published financial statements must disclose certain information which is regarded as key in ascertaining the capital position of the SACCO society. The disclosures in the financial statements must include disclosures on any lending to insiders and any advances or credit facilities which exceed the prescribed limits of its core capital.¹⁴⁰

To a great extent, the framework underpins the theme of transparency and accountability between the board of a DT-SACCO and SASRA through a clear apportionment of rights and obligations between the two. The board is required to keep accounts and records which indicate a true and fair state of affairs in addition to other financial reporting obligations. The board is required to present the financial reports in a manner in which SASRA can determine the extent to which the SACCO has complied with its reporting requirements.¹⁴¹ The Board is required to ensure their financial statements are audited and the audited accounts are submitted to SASRA.¹⁴² The audit must be

¹³⁷ Cooperatives Societies Act, s 25 (8).

¹³⁸ Cooperative Societies Act, s 27 (5). In addition, the auditor of a DT-SACCO presents the reports to the board of directors. See Sacco Societies Act s 43.

¹³⁹ SACCO Societies Act, s 46.

¹⁴⁰ SACCO Societies Act, s 42. In addition, the audited accounts must disclose members of the SACCO society who hold more than 20 percent of the share capital and deposits in the society.

¹⁴¹ SACCO Societies Act, s 40.

¹⁴² Similarly, the external auditor of a DT-SACCO reports to SASRA. See SACCO Societies Act, s 44 (3).

done within three months after the end of the financial year, and the financial statements must contain an audited balance sheet, profit and loss account and a copy of the auditor's report.¹⁴³The board is required to inaugurate an audit and credit committee and in addition, establish appropriate policies on credit, liquidity, risk management and investment.¹⁴⁴

SASRA has wide supervisory powers designed to insulate the members against fraudulent managers, mismanagement and risky trading behaviors. It can undertake inspections on the official records of a SACCO, at any time and from time to time as well as carrying out on-site inspections or off-site surveillance.¹⁴⁵ On-site inspections involve physical visiting of the DT-SACCOs while off-sight inspections are carried out through constant monitoring and analysis of the various statutory reports and returns submitted to the SASRA by the DT-SACCOs without the necessity of making a physical contact with them.¹⁴⁶ In addition, SASRA can require a SACCO to submit reports on its financial affairs of its deposit-taking business to enable it evaluate the society's financial condition.¹⁴⁷ Furthermore, it has advisory powers especially where it has a reasonable belief that the business of a SACCO is being conducted contrary to the law. Through these powers, SASRA can offer recommendations on the proper way of conducting business, and the measures to be taken to achieve compliance.¹⁴⁸

In addition, SASRA has been clothed with extensive powers, essentially made to boost its ability to foresee potential risks in time and effectively discharge its oversight obligations. The regulations

¹⁴³ SACCO Societies Act, s 41. Failure to comply with these requirements is a criminal offence. See SACCO Societies Act, s 41 (2).

¹⁴⁴ Jared Makori, Charles Muturi and Willy Muturi (n 134) 1036.

¹⁴⁵ SASRA, 'The SACCO Supervision Annual Report 2015' (SASRA, 1 June 2015) 65 <<https://www.sasra.go.ke/index.php/resources/publications/category/11-sacco-supervision-reports?download=96:supervision-report-2015>> accessed 12 July 2019.

¹⁴⁶ Interview with John Mwaka, CEO SASRA (Nairobi, UAP Old Mutual Tower, 10 August 2019).

¹⁴⁷ SACCO Societies Act, s 48.

¹⁴⁸ SACCO Societies Act, s 50 (1).

stipulate the different returns expected from a DT-SACCO and the particular time when its submission is due, either monthly, quarterly or annually. On a monthly basis, a DT-SACCO is required to submit a capital adequacy return,¹⁴⁹ a liquidity statement¹⁵⁰ and a statement of Deposit Return.¹⁵¹ Each of the three types of returns has a particular objective which is key to fostering transparency in the financial management of the SACCO.¹⁵² On an annual basis, the SACCO is obliged to submit a statement of financial position, other disclosures, and audited financial statements.¹⁵³

SASRA has a broad class of enforcement actions to sanction its supervisory powers over SACCO societies, especially where it has established that the business of the SACCO has been carried contrary to the prescribed legal requirements. It may require the society to reconstitute its board of directors or restrict, suspend or prohibit the payment of dividends by the society.¹⁵⁴ In addition, SASRA can suspend or remove any board member and officer who has taken part in the unlawful conduct of the SACCO's business¹⁵⁵ as well as imposing financial penalties on the society and issue any administrative directives it deems appropriate. In addition, SASRA can also appoint professionally qualified persons for the purpose of advising, assisting and overseeing the society's restructuring plans.¹⁵⁶

¹⁴⁹ SACCO Societies (Deposit-Taking SACCO Business) Regulation, 2010 s 11 (1).

¹⁵⁰ *Ibid* s 14 (2).

¹⁵¹ *Ibid* s 24.

¹⁵² The Capital Adequacy Return helps monitor whether the DT-SACCO is maintaining at minimum the prescribed minimum capital and associated ratios. The liquidity statement monitors if the SACCO is able to meet its short term obligations, particularly to depositors. The statement of Deposit Return monitors the deposits and the trend in deposit within the DT-SACCO. *See also*, SASRA (n 145) 66.

¹⁵³ SACCO Societies (Deposit-Taking SACCO Business) Regulation, 2010 ss 41, 52 (3) and 55.

¹⁵⁴ SACCO Societies Act, s 51 (a).

¹⁵⁵ *Ibid* s 51 (c).

¹⁵⁶ *Ibid* s 51 (i).

Recently, related state agencies have shown a tendency to collaborate, pool together their resources in the pursuit of a more stringent regulatory framework for accountability and effective law enforcement in the SACCO sector. Such a move was seen in 2019, where the Ethics and Anti-Corruption Commission came together with the State Department for Cooperative Societies and Ethics Commission for Cooperative Societies through a MOA which essentially sought to empower and cure SASRA's incapacity to prosecute culpable managers.¹⁵⁷

3.3 The Efficacy of the Penalties and Sanctions for Non-Compliance

To a great extent, the Kenyan regime offers insufficient sanctions for non-compliance with the reporting requirements through lenient sanctions which cannot deliver the necessary deterrence function. When a general cooperative society fails to comply with the reporting standards, members of its committee automatically lose their positions at the next general meeting and are not eligible for re-election for three years, unless the commissioner is satisfied that the failure to comply in time was due to circumstances beyond their control.¹⁵⁸ For DT-SACCOs, the law is more lenient and the sanctions are a mere slap on the wrist. Although the Act criminalizes the failure of a SACCO to submit its audited accounts to SASRA, it does not prescribe a specific penalty for the offence.¹⁵⁹ In addition, although the Act criminalizes the act of opening a branch or changing the place of business without the approval of SASRA, a person convicted for the offence is liable to pay a maximum penalty of one hundred thousand shillings.¹⁶⁰

¹⁵⁷ Ethics and Anti-Corruption Commission, 'MOU to Strengthen Anti-Graft Fight in Cooperative Sector' (*Ethics and Anti-Corruption Commission*, 6 August 2019) <<https://www.eacc.go.ke/mou-to-strengthen-anti-graft-fight-in-cooperative-sector/>>accessed 20 August 2019.

¹⁵⁸ Cooperative Societies Act, s 25 (11).

¹⁵⁹ SACCO Societies Act, s 41 (2).

¹⁶⁰ *Ibid* s 32 (2).

Similarly, the law has failed to adopt a very severe view of wrongful activities which hinder transparency in the preparation and presentation of the financial reports. Even though the law has criminalized activities like falsifying the books of accounts, forging signatures in the process of preparing the accounts, destroying the books or engaging in transactions in which he has a conflict of interest negate the concept of transparency in the financial reporting,¹⁶¹ these criminal offences have, however, received a rather lenient treatment with respect to penalties. Anyone found guilty of any of them is liable to be prohibited from holding office in any SACCO society. In addition, the person is liable to a maximum fine of one hundred thousand shilling or to imprisonment for a term not less than twelve months or both.¹⁶² Arguably, these criminal sanctions are not sufficient to meet their deterrence objective and this observation has been collaborated by earlier studies which have argued that the current penalties are not enough to sanction the statutory compliance requirements.¹⁶³

3.4 The Quality of Institutional Oversight by Key Players

Both the legal framework and the internal mechanisms of corporate control within the SACCOs have failed to exercise their oversight role effectively and in a manner to insulate the SACCOs against fraud and misappropriation of their funds. It has been argued that the inadequacy of the financial management systems has been characterized by weak watch dog systems and unsound management and accounting models.¹⁶⁴ It has been observed that internal politics in most SACCOs have blurred the relationship between the Supervisory Committee and the Management

¹⁶¹ Ibid s 65 (a-e).

¹⁶² Ibid s 66.

¹⁶³ Leonard Baka, 'The Challenges Facing Co-operative Societies in Kenya a Case Study: Kenya Planter Co-operative Union (KPCU)' (2013) 3 (11) Public Policy and Administration Research 32, 42.

¹⁶⁴ Ibid.

Committee, essentially insulating the management committee against the supervisory jurisdiction and the oversight mandate of the supervisory committee.¹⁶⁵

To a great extent, the members of the DT-SACCOs have not been adequately empowered to exercise their oversight role over the board. This has been attributed to the non-availability of the financial statements on regular basis.¹⁶⁶ The members do not have a right to access the audited financial accounts except of course during the AGM. Instead, only the members of the supervisory committee and the auditor have the right to access the books of accounts at the registered office.¹⁶⁷ The members of a DT-SACCO have a somewhat limited right with respect to accessing and inspecting account books. Although a SACCO society is obliged to display the audited financial statements in a conspicuous position in their place of business,¹⁶⁸ the audited accounts do not offer an opportunity to inspect the real books. Furthermore, the audited accounts must be prepared in conformity with specified standards, which are not very friendly to majority of the members.

The SASRA's current structure, form and mode of operation is characterized by lapses, inefficiency and unstructured jurisprudence, making its efficacy debatable. It has been observed that even though the establishment of SASRA was done with good intentions, its current structure and form does not deliver its very intended purpose. It does not have capacity and its penalties are very limited in scope since they chiefly suspend and cancel licenses. The Act establishing SASRA largely took the structure of the CBK model of regulation while actually the powers of SASRA should be more than just being licensing.¹⁶⁹

¹⁶⁵ Interview with Sirro, CEO Cooperative Tribunal (Nairobi, Reinsurance Plaza, 9 August 2019).

¹⁶⁶ Richard Kivuvo and Tobias Olweny, 'Financial Performance Analysis of Kenya's SACCO Sector Using the Altman Z Score Model of Corporate Bankruptcy' (2014) 5 (9) International Journal of Business and Social Science 34, 34.

¹⁶⁷ Cooperatives Societies Act, s 25 (2).

¹⁶⁸ Sacco Societies Act, s 46.

¹⁶⁹ Interview with Mr. Sirro (n 165).

In addition, there is a general agreement amongst scholars that the efficacy of the legal framework has been impaired by several other internal challenges which have cumulatively aggravated the information asymmetry between the board and the members. There are weak and inadequate communication systems between the members and the board since majority of SACCOs lack a structured communication system between the board members and management.¹⁷⁰ Majority of the members of the SACCOs are uninformed and are easily manipulated when exercising their voting rights.¹⁷¹ It has been argued that many SACCOs encounter transparency challenges especially during the election of its officials, who are elected politically in total disregard of the statutory professional requirements necessary for efficient management of the SACCOs.¹⁷² Other internal challenges include poor leadership, characterized by lack of transparency¹⁷³ and limited accountability in management of SACCOs.¹⁷⁴

Furthermore, the role of the ICT in the preparation, submission and compliance with the financial reporting requirements cannot be overemphasized. The absence of ICT initiatives within the SACCOS has hindered the SACCOS's ability to meet their reporting requirements in time. Majority of SACCOs are yet to embrace ICT in their financial departments, leading the manual generation of their reports, which in turn hinders efficacy, transparency and accuracy in the preparation and submission of the financial statements.¹⁷⁵

¹⁷⁰ Samuel Ngugi and Francis Ofunya, 'Challenges Facing Deposit Taking Savings and Credit Co-Operatives' Compliance with the Sacco Societies' Act Number 14 (2008) in Nyeri' (2015) 11 *Journal of Poverty, Investment and Development* 1, 15.

¹⁷¹ Leonard Baka (n 163) 42.

¹⁷² James Miriti, 'Factors Influencing Financial performance of savings and credit cooperative societies, A case of Capital SACCO, Meru County, Kenya' (MBA thesis, University of Nairobi 2014) 14.

¹⁷³ Faith Ngugi Nkuru, 'Factors Affecting Growth of SACCOs Within the Agricultural Sector in Kenya: A Case of Meru Farmers SACCOs' (2015) 4 (1) *Global Journal of Commerce & Management Perspective* 34, 38.

¹⁷⁴ Jared Makori, Charles Muturi and Willy Muturi (n 134) 1039.

¹⁷⁵ Samuel Ngugi (n 170) 15.

Studies have shown that most SACCOs lack adequate transparency in conducting SACCO affairs in terms of cash transactions, loan disbursements, payments and, member statements within the organization structure.¹⁷⁶ In addition, a majority of SACCOs do not educate their members and create awareness on their role in the SACCO operations and hence obstructing their ability to make informed decisions with respect to their participatory role.¹⁷⁷ It has been established that most SACCOs have not incorporated a clear and transparent communication about the internal control policies and procedures within the organization structure.¹⁷⁸ Other failures of the SACCO can be attributed to their failure to adhere to the regulations prescribed in the SACCO Societies Act and its accompanying regulations.¹⁷⁹

3.5 Devolution of the Cooperative Development Function: Pertinent Legal Hurdles

Even before the ink of the Constitution dried up in 2010, there were contests as to the implementation of the Fourth Schedule to the Constitution, especially on the transmission of the cooperative function from the national government to the county governments. Unlike the other functions which the two levels have a concurrent jurisdiction, the cooperative development was wholly devolved exclusively to the county governments.¹⁸⁰ All since then, administrative bodies, the public and legal scholars have dived into an ever-green discourse seeking to address several issues namely; whether the office of the Commissioner of Cooperative Development is still relevant, whether the county commissioner for cooperatives of a particular county has any powers and functions under the Cooperative Societies Act, who between the two has powers to regulate

¹⁷⁶ Makau Mathuku, 'An investigation of cash management practices of savings and credit cooperative societies in Nairobi County' (MBA thesis, Unites States International University 2017) 33.

¹⁷⁷ Ibid 36.

¹⁷⁸ Ibid 38.

¹⁷⁹ Ibid.

¹⁸⁰ Constitution of Kenya, 2010 Fourth Schedule.

cooperative societies and whether for the county governments to exercise the function, there is a need for a statute to give specific powers in this regard.

The legal and policy framework on DT-SACCOs does not reflect the devolved governance system under the new constitutional order. The two substantive statutes do not provide for the functions of the devolved system of government, thereby leaving critical gaps which hinder transparency between the two systems of governance with respect to the regulation of DT-SACCOs.¹⁸¹ In this regard, it has been recommended that the two statutes should be amended in order to align them with the dictates of the constitutional order and particularly outline the distinct roles of the national and the county governments in the regulation and monitoring of SACCO affairs.¹⁸²

3.6 The Mandate of the Commissioner for Cooperative Development and the County Commissioner for Cooperatives

There has been push and pull between the national government and the county government as the two contest on who between them has exclusive and the ultimate say on regulation of cooperatives in Kenya. This sort of commotion featured very conspicuously in the *Republic v Commissioner for Co-operative Development*,¹⁸³ in which the County Cooperative Commissioner for Machakos county had suspended an entire management committee of Katelembo Athiani Farming and Ranching Co-operative Society Limited.¹⁸⁴ When the suspension was challenged in court, one of the issues for determination was whether who among the two had the power to remove or suspend

¹⁸¹ Government Printer, Co-operative Development Policy: Promoting Co-operative Enterprises for Industrialization, (2017) 50.

¹⁸² Ibid 51.

¹⁸³ *Republic v Commissioner for Co-operative Development & 69 others Ex Parte Katelembo Athiani Maputi Ranching & Farming Co-operative Society Limited* [2016] eKLR. It is worth to note that this particular case has essentially settled the applicability of section 15 of the Sixth Schedule to the Constitution, and sections 23 and 24 of the Transition to Devolved Act.

¹⁸⁴ *Republic v Commissioner for Co-operative Development & 69 others* (n 183) 12.

an elected management committee.¹⁸⁵ This was a pertinent issue given that the Co-operative Societies Act does not provide for the office of the County Cooperative Commissioner vis a vis the general rule that a holder of an office unrecognized in law cannot purport to enjoy duties not given to him by statute.¹⁸⁶ And what was making the matter more complicated was the fact that the function of co-operative societies had then been wholly and exclusively transferred to the Machakos County government.¹⁸⁷

To some extent, the rule in *Republic v Commissioner for Co-operative Development* clearly demarcated the respective spheres of the Commissioner for Cooperatives and the County Cooperative Commissioner by outlining their special relationship and their respective territorial coverage. The relevance of, and the continued existence of the powers and functions of the Commissioner for Cooperative Development is only in two special circumstances. One, in those counties where the function of cooperative societies has not been transferred. Two, in those counties where there is an agreement between a county government and national government that the Commissioner for Cooperative Development shall continue to exercise the functions and powers conferred on it under the Co-operative Societies Act in relation to that particular county government.¹⁸⁸ In the absence of these two circumstances, the powers of the Commissioner for Cooperative Development are to be exercised by the county governments and officers of the county government.¹⁸⁹

¹⁸⁵ The applicant was of the view that the power to suspend an elected management committee lies with the Commissioner of Cooperative Development and in the AGM.

¹⁸⁶ *Republic v Commissioner for Co-operative Development & 69 others* (n 183) 4.

¹⁸⁷ The transfer was pursuant to a Legal Notice 168 published on 9th August 2013, in which the Transition Authority approved the transfer of the functions to the county government of Machakos, with effect from the 9th August 2013. The notice was pursuant to section 15 of the Sixth Schedule to the Constitution as read with sections 23 and 24 of the Transition to Devolved Governments Act, 2012.

¹⁸⁸ *Republic v Commissioner for Co-operative Development & 69 others* (n 183) 14.

¹⁸⁹ The Constitution of Kenya, Sixth Schedule s 7 (2).

The court in *Republic v Commissioner for Co-operative Development* made significant contribution in the Kenyan jurisprudence on the devolution of the cooperative development function. It established that cooperative development is wholly a function of county governments, and there is no allocation of any aspect of regulation of co-operative societies assigned to the national level.¹⁹⁰ It also clarified that the powers and functions set out in the Co-operatives Societies Act, including those of Commissioner of Cooperatives, are exercisable by the county government through its officers, and especially through the County Co-operative Commissioner.¹⁹¹

Courts have attempted to interpret the Cooperative Societies Act with a view to bringing it in conformity with the dictates of the Constitution, and especially where the respective County Government is yet to enact an empowering legislation to exercise functions previously exercised by national government. The Courts have held that since the function of the co-operative societies is no longer a function of the national government, the Co-operative Societies Act which is still in force consequently has to be construed as applying to the regulation of co-operative societies at the county governments, until a county government has enacted its own law regulating co-operative societies.¹⁹² The jurisprudence emanating from the courts indicate that pending the enactment of a county legislation to regulate co-operative societies by any County Assembly, the Co-operative Societies Act continues to regulate co-operative societies in the particular county with the necessary alterations, modifications and exceptions.¹⁹³

¹⁹⁰ The Court in *Republic v Commissioner for Co-operative Development & 69 others* (n 183) 11 contrasted this with the concurrent jurisdiction which exists in other functions such as health, agriculture and transport, where the aspects of policy and standard setting of these functions are allocated to national government.

¹⁹¹ *Republic v Commissioner for Co-operative Development & 69 others* (n 183) 14.

¹⁹² *Ibid* (n 183) 16.

¹⁹³ *Ibid*.

To some extent, the transfer of the cooperative function from the national government to the county governments has occasioned some uncertainty on the exact extent to which the two should relate with regard to the regulation of cooperative societies. Several cooperative managers have taken advantage of the current state of affairs to approach different levels of government in pursuit of their personal interests and commonly at the expense of accountability.¹⁹⁴ It has been felt that cooperatives are being directed by two conflicting authorities namely the Commissioner for Cooperative Development and the County Cooperative Commissioner, and hence finding it difficult to comply with their orders and directions.¹⁹⁵ While some counties are still relying on the national legislation on cooperatives, some county governments have already gone further to legislate on cooperative societies.¹⁹⁶

The upshot of this uncertainty on the interplay between the national and the county government has seen subjects of the law fall through the cracks and especially where a cooperative society is operating from more than one county. Such was the case in the Ekeza SACCO, which was initially incorporated in Nairobi County, through the Starehe Sub-County Commissioner for Cooperatives. Immediately after its incorporation, Ekeza SACCO moved to Thika town in Kiambu County whereupon it operated without the knowledge of the relevant sub-county cooperative commissioner. The SACCO later moved to Nakuru County, whereby it too operated without the knowledge of the relevant sub-county commissioner for cooperatives.

¹⁹⁴ Government Printer, Promoting Co-operative Societies for Industrialization Cooperative policy, (2019) 11.

¹⁹⁵ *Republic v Commissioner for Co-operative Development & 69 others* (n 183) 3.

¹⁹⁶ For Instance, the Meru County; Meru SACCO Act.

3.7 Conclusion

The chapter reveals that, to some extent, the Kenya's legal framework for DT-SACCOs has certain positive attributes which enhance transparency in financial reporting. However, the regime offers insufficient sanctions for non-compliance with the reporting requirements. In addition, both the legal framework and the internal mechanisms of corporate control have failed to exercise their oversight in a manner to insulate the SACCOs against fraud and misappropriation of their funds. Further, the members of the DT-SACCOs have not been adequately empowered to exercise their oversight role over the board. Furthermore, the SASRA's current structure, form and mode of operation is characterized by lapses, inefficiency and unstructured jurisprudence, making its efficacy debatable. In the same vein, there is a general agreement amongst scholars that the efficacy of the legal framework has been impaired by several other internal challenges which have cumulatively worsened the information asymmetry between the board and the members.

The study also revealed that these inefficiencies have been aggravated by the devolution of the cooperative development function. It established that the statutory framework on DT-SACCOs does not reflect the devolved system of governance, thereby occasioning uncertainty as to who between the national government and the county government has exclusive and the ultimate say on the regulation of cooperatives. Even though the courts attempted to interpret the Cooperative Societies Act, with a view to bringing it into conformity with the dictates of the Constitution and solve the stalemate, the uncertainty still persists on the exact extent to which the two level of government should relate with regard to the regulation of cooperative societies. The upshot of this persisting and recurring uncertainty on the interplay between the two levels of governments has seen subjects of the law fall through the cracks and especially where a cooperative society is operating from more than one county.

CHAPTER FOUR

ANALYSIS OF THE UK'S AND USA'S TRANSPARENCY AND ACCOUNTABILITY LEGAL FRAMEWORK FOR CREDIT UNIONS

4.0 Introduction

The chapter offers a critical analysis of the UK's and USA's legal framework for credit unions with a view to investigating any positive lessons which Kenya can draw from their experience. First, it offers an explanation as to the suitability and the choice of the two jurisdictions for the purposes of this study by demonstrating their relevance to the Kenyan context. It outlines the positive attributes of the said legal frameworks in terms of the efficacy of their institutional framework in attaining accountability between the relevant financial regulators. It also investigates the apportionment of rights, duties and responsibilities under the legal framework and how the enforcement of these rights has contributed to enhance accountability and transparency amongst the several players in the sector.

4.1 The Suitability of the UK's and the USA's Jurisdiction for Best Practices

There are striking similarities between the Kenyan, USA's and UK's financial system in terms of the nature, the structure and the operation of SACCOs as financial services providers. In the UK and USA, the term credit union is used to refer to financial institutions that are the equivalent of the Kenyan SACCOs.¹⁹⁷ In the UK context, credit unions are mutual financial institutions that offer savings and loan facilities to their membership at an interest rate and are owned and controlled by their members.¹⁹⁸ In all the three jurisdictions, these financial institutions have

¹⁹⁷ In the USA, UK and Canada, the term Credit Unions is used while in India the term used is financial cooperatives.

¹⁹⁸ Tischer Daniel, Packman Carl & Montgomerie Johnna, 'Gaining Interest: A New Deal for Sustained Credit Union Expansion in the UK' (2015) Political Economy Research Centre, 6.

played a key role and have been effective tools of ensuring financial inclusion. No wonder then that strengthening the SACCO sector has been at the top of the priority list of the three jurisdictions.¹⁹⁹

The choice of the two jurisdictions for the critical analysis of their legal framework is based on principle. It is generally agreed amongst legal scholars and Kenya policy makers that the two are the most advanced jurisdictions with respect to credit unions.²⁰⁰ The USA's regime for credit unions is very relevant to the Kenyan context, especially with respect to the devolved governance system, which is similar to the USA governance model. The USA's regime for credit unions dates back to 1909,²⁰¹ while the UK's 1893.²⁰² Ever since, the respective legal regimes have evolved overtime to become strong financial services providers that are similar to commercial banks as demonstrated by the wide range of the financial services they offer.²⁰³ And what is more is that Kenya has always looked up to the UK with regard to issues pertaining SACCOs on policy formulation, regulations and best practices.²⁰⁴ In addition, since Kenya has the most advanced SACCOs in Africa, it is reasonable to compare its system with the best in the world.

¹⁹⁹ Alan Weaver, 'Financial Exclusion and Credit Unions: Recent developments' (LGiU, 13 July 2015) 2 <<https://www.lgiu.org.uk/wp-content/uploads/2015/07/Financial-Exclusion-and-Credit-Unions-recent-developments-.pdf>> accessed 28 September 2019.

See also Tonny Omwansa and Timothy Waema, 'Deepening financial inclusion through collaboration to create innovative and appropriate financial products for the poor' (2014) KBA Centre for Research on Financial Markets and Policy Working Paper Series 01/2014, 4-6.

²⁰⁰ Interview with John Mwaka, CEO SASRA (Nairobi, UAP Old Mutual Tower, 10 August 2019). John Mwaka admitted that the UK and Germany are more advanced than Kenya and that Kenya has a tendency to borrow from their practice and experience.

²⁰¹ Patrick Sauer, 'A brief history of American credit unions and banks' *The Liberty Project* (1 March 2018) 7.

²⁰² Mark Lyonette, 'Celebrating our past, looking forward to our future' (2014) 16 (1) *Credit Unions News* 4.

²⁰³ Paul A Jones, 'The Role of Credit Unions in Promoting Financial Inclusion in Rural Communities in Britain' (*Rural Cooperation in the 21st Century: Lessons from the Past, Pathways to the Future*, The Hebrew University of Jerusalem, June 2009) 25.

In the UK, credit unions can offer a current account, benefit direct accounts, savings accounts with variable interest rates, loan accounts with variable interest rates, multiple insurance products, bill payment accounts among others.

²⁰⁴ John Mwaka (n 200).

Mr John Mwaka has over 20 years' experience in institutional development and is an expert in cooperative development, planning & change management.

4.2 An Overview of the UK's Transparency and Accountability Legal Framework for Credit Unions

The UK regime has a sophisticated legal framework comprised of powerful institutions and a comprehensive legislative and policy framework designed to deliver maximum consumer protection.²⁰⁵ The discourse on the efficacy of the UK's regime brings to center the role played by two leading institutions; Financial Conduct Authority (FCA) and the Prudential Regulatory Authority (PRA). PRA is a department of the Bank of England, it is responsible for the prudential regulation and supervision of credit unions²⁰⁶ and the lead regulator thanks to its primary responsibility on verification, scrutiny and authorization of credit unions.²⁰⁷ FCA is a financial regulator mandated to ensure consumer protection, the integrity of the UK financial system and promotion of healthy competition amongst various financial services providers.²⁰⁸

The institutional framework has a clear division of duties amongst the relevant institutions, with no instances of duplication or overlap. The two leading regulatory authorities have clearly demarcated spheres of influence with respect to the prudential regulation of credit unions. The FCA is responsible for the prudential regulation of those financial service firms not supervised by

²⁰⁵ The legislative framework is comprising of the Credit Unions Act 1979, the Co-operative and Community Benefits Act and the Financial Services and Markets Act 2000. The Credit Unions Act 1979 is the enabling statute with respect to the registration of Credit Unions and their regulation and taxation. In addition, credit unions in Northern Ireland are regulated by one additional piece of legislation; The Credit Unions (Northern Ireland) Order 1985. The regime under this legislation is very identical to the one regulating other credit unions from England, Scotland and Wales in terms of the registration and regulation of credit unions and more particularly the role of PRA and FCA. The Credit Unions Act 1979 applies to the Great Britain while the Credit Unions (Northern Ireland) Order 1985 applies to the Northern Ireland only. *See also* Bank of England, 'Supervision: Credit unions' (*Bank of England*, 4 July 2019) <<https://www.bankofengland.co.uk/prudential-regulation/supervision/credit-unions>> accessed 30 August 2019.

²⁰⁶ It is also responsible for the prudential regulation and supervision of banks, building societies, insurers and major investment firms.

²⁰⁷ Association of British Credit Unions Limited, 'Reform of the legacy Credit Unions sourcebook' (2015) Response from the Association of British Credit Unions Limited (ABCUL) CP 22/15, 16.

²⁰⁸ Will Kenton, 'Financial Conduct Authority (UK) (FCA)' (*Law & Regulations* 3 May 2019) <<https://www.investopedia.com/terms/f/financial-conduct-authority-uk-fca.asp>> accessed 30 August 2019.

the PRA.²⁰⁹ In addition, each institution has its own exclusive jurisdiction when it comes to authorizing deposit taking activities of the credit unions. While as PRA is the appropriate authorizer in cases where the regulated activities²¹⁰ to which the application relates consist of or include a PRA-Regulated activity, FCA is the appropriate regulator in any other case.²¹¹

4.3 The Efficacy of the UK's Legal Framework

The leading state agencies have a special working relationship characterized by complementarity and dominated by collaboration on matters of authorizing, registering and regulating credit unions. The registration of a credit union must be approved by both the FCA and PRA.²¹² In addition, such complementarity is also manifested when seeking authorization to accept deposits. Even though each authority has an exclusive jurisdiction with respect to authorization of the deposit taking activities, they are mandated to communicate their approvals to one another. Once PRA is satisfied that the credit union will satisfy and continue to satisfy the threshold conditions in relation to accepting deposits, it must notify FCA and vice versa.²¹³ Both the FCA and the PRA have powers to appoint an inspector and call a meeting when either of them is of the opinion that an investigation should be held into the affairs of the credit union.²¹⁴

²⁰⁹ These include asset managers and independent financial advisers.

²¹⁰ Financial Services and Markets Act, 2000 schedule 2. 'Regulated activities' is a generic term used in the statutes to refer to activities like deposit taking, dealing in investments, arranging deals in investments, safekeeping and administration of assets among others. *See also* The Financial Services and Markets Act, 2000 (Regulated Activities) Order 2001 for a finer description of the regulated activities.

²¹¹ Financial Services and Markets Act, 2000 s. 55A (2).

²¹² Credit Unions Act, 1979 s. 1 (a).

²¹³ Credit Unions Act, 1979 s. 1 (a), (e) and (f). *See also* Financial Services and Markets Act, 2000 s. 1B (a); 55E 1-5. Under the latter Act, the FCA must not register a society as a credit union unless it has proposed to give that society permission to accept deposits in cases where it is the appropriate regulator. Also, the FCA must not register a society as a credit union unless the PRA has proposed to give that society permission to accept deposits in cases where PRA is the appropriate regulator.

²¹⁴ Credit Unions Act, 1979 s. 18 (1). They can also exercise these powers if they are of the opinion that the affairs of the credit union call for consideration by a meeting of members. The meeting and the investigation can be done on the same or on different occasions.

To some extent, the UK's legal framework has established a form of oversight in which the two institutions can exercise healthy oversight in the regulation of the credit unions. For starters, credit unions are required to apply to the Bank of England for authorization and approvals, after which they are required to register with the FCA, which is solely responsible for the registration of credit unions. Further, the FCA cannot register a credit union unless the PRA has proposed to give that society permission to accept deposits in cases where PRA is the appropriate regulator.²¹⁵ In addition, even though the two institutions have powers to appoint an inspector or call a meeting, the two must each notify the other before exercising these powers.²¹⁶

The relevant institutions have established structures for efficient dissemination of information amongst themselves and the credit unions. Both the FCA and PRA have powers to require information about the books and accounts relating to the credit union's business as is necessary for the exercise of their functions.²¹⁷ The two have signed a memorandum of understanding in the pursuit of an efficient reporting process for dual-regulated firms. The arrangement obliges the two to consult each other on changes of data which is submitted periodically, and efficient sharing of data whereby the credit unions are only required to submit data sets once and then leave the institutions to share it where appropriate.²¹⁸ The duo has employed this high-level framework to co-operate and co-ordinate in discharging their statutory mandates.²¹⁹

²¹⁵ Financial Services and Markets Act, 2000 s. 1B (b), 1C, and 55F 1-5.

²¹⁶ Credit Unions Act, 1979 s. 18 (4).

²¹⁷ Credit Unions Act, 1979 s. 17.

²¹⁸ Bank of England, 'Regulatory reporting banking sector' (*Bank of England*, 24 August 2019) <<https://www.bankofengland.co.uk/prudential-regulation/regulatory-reporting/regulatory-reporting-banking-sector>> accessed 26 September 2019.

²¹⁹ Bank of England, 'Memorandum of Understanding between The Financial Conduct Authority and The Bank of England (exercising its prudential regulation functions)' (*Bank of England*, July 2019) 10 <<https://www.bankofengland.co.uk/-/media/boe/files/memoranda-of-understanding/fca-and-bank-prudential-july-2019.pdf>> accessed 26 August 2019.

The UK prudential regulation regime is comprehensive, objective and responsive in terms of the financial muscles of particular credit unions, with the stronger credit unions being subjected to more regulatory requirements. The regime has grouped the credit unions into several categories in terms of their financial capabilities and their worth, prescribing different regulatory requirements to the respective categories.²²⁰ The PRA in consultation with FCA has come up with various regulations for the respective categories.²²¹ In conclusion, the UK legal framework treats credit unions more or less like commercial banks with respect to prudential regulation. UK credit unions are regulated by the PRA which is a department of the Bank of England, and which is also the chief regulator for commercial banks.

The UK's regime has been designed to promote transparency between the members of a credit union and the management committees. Credit unions are required to submit audited accounts to the FCA.²²² They are also required to avail to every member, upon request and free of charge, a copy of the latest audited accounts.²²³ At the end of the year, also, credit unions are required to file a report with FCA indicating the number of complaints raised against it and the response to the particular complaint.²²⁴

The regime has embraced and incorporated modern technological advancements into the data collection and dissemination mechanisms. Credit unions can deliver their audited accounts through

²²⁰ The first category comprises of credit unions with total assets above £15 million or with more than 10, 000 members, the second category comprises of credit unions with total assets below £15 million and fewer than 10,000 members. The third category is made up of credit unions with total assets of less than £15 million, and whose assets have grown by more than 30% and/or whose members have grown by more than 50% in the last financial year. The Last category comprises of all credit unions with assets above £40 million.

²²¹ Bank of England, 'PRA Annual Assessment of the Credit Union sector' (*Bank of England*, 28 August 2018) <<https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervision/credit-unions/2018-assessment-category-5-plus-credit-unions-above-15m.pdf>> accessed 26 August 2019.

²²² Co-operative and Community Benefit Societies Act, 2014 s 82.

²²³ Credit Unions sourcebook, (Para 8.2.6.R) 8.

²²⁴ Ibid (Para 9.2.1.R) 9.

email.²²⁵ FCA has introduced an online data submission and reporting system, which is very efficient in terms of collecting and storing regulatory data from firms.²²⁶ These online platforms have reduced the regulatory burdens for the government agencies and reporting-obligations for the firms in equal measures, as firms are only required to submit data sets once and the two regulatory agencies have mechanisms on sharing the data where necessary.²²⁷ This automated reporting system is a big win for the regulatory framework as it gives the authorities a better and overall view of the market.

Both the FCA and PRA play a central role in the appointment of professionals whose services are key in the management of the credit union. The outsourced professional of any credit union must first secure approval of the governing regulatory organ. The credit union is obliged to first seek the approval of FCA or PRA, before which approval the credit union cannot allow the outsourced professional to perform the function.²²⁸ In addition, the regime is efficient in circumstances where the professional is being sought to execute several functions at the same time for the same credit union, some of which functions are regulated by FCA and others by the PRA. In these scenario, the credit union does not have the burden to seek double approval as a single approval will be sufficient.²²⁹

The UK regime has evolved overtime through periodic restructuring of the financial regulation systems in an attempt to address the felt necessities of the time. In 2000 and 2003, legislative reforms were made to accelerate the success of the credit unions in the UK by providing a

²²⁵ Ibid 49.

²²⁶ Financial Conduct Authority, 'Gabriel' (*Financial Conduct Authority*, 5 May 2016) <<https://www.fca.org.uk/firms/gabriel>> accessed 3 September 2019.

²²⁷ Bank of England (n 219) 11.

²²⁸ Credit Unions sourcebook, (Para 8.3.3.G) 8. *See also* Co-operative and Community Benefit Societies Act, 2014 s. 59.

²²⁹ Credit Unions sourcebook, (Para 8.3.6.R) 52.

framework through which credit unions could borrow from one another and the banks, access hirer loans and charge for ancillary services.²³⁰ The same reforms saw major alterations in the regulatory framework in the pursuit of more efficient institutions while at the same professionalizing the sector.²³¹ The aftermath of the 2007-2008 financial crisis and the felt need to reform the then financial regulatory structures occasioned the abolishment of the FSA, which was succeeded by the FCA and PRA.²³² More changes were done in 2018, which essentially increased the number of potential members of a credit union and eliminating restrictive elements of the previous regime.²³³

The UK's legislative developments and reforms are well founded on public participation, constructive consultation and a comprehensive policy framework. Major changes to the 1979 Act were first proposed by a credit union taskforce and a Policy Action Team, which made fundamental proposals that were reflected in the Financial Services and Markets Act 2000.²³⁴ Before the 2012 and 2013 legislative reforms, extensive consultations were carried out in which major regulatory institutions expressed their views on why UK credit unions were failing.²³⁵ The consultative process established that much of financial loss was attributed to inadequate financial control, financial indiscipline and lack of effective governance.²³⁶

²³⁰ The 2000 Financial Services and Markets Act and 2003 Regulatory Reform (Credit Union) Order. *See also* Government of United Kingdom, House of Commons Regulatory Reform Committee, *Draft Legislative Reform (Industrial and Provident Societies and Credit Unions) Order 2011* (HC 2010–12, 151-1) paras 173-75, p. 16.

²³¹ The 2000 and 2003 legislative reforms saw the transfer of regulatory authority from the registry of Friendly Societies to the FSA, which further widened the ability of credit unions to lend, yet professionalized the sector. *See also* Tischer Daniel, Packman Carl and Montgomerie Johnna (n 198) 14.

²³² These changes were effected by the Financial Services Act, 2014.

²³³ The Credit Unions Act, 1979 (Locality Common Bond Conditions) Order 2017 (SI 2017/1144) ss 4-11.

²³⁴ The proposed changes removed some of the legislative restrictions which credit unions then faced. They included: further consultation on increasing the sources from which credit unions can obtain credit and allowing credit unions to charge for ancillary services.

²³⁵ Paul A Jones, 'Stabilising British Credit Unions' (2010) Liverpool John Moores University Research Paper 1/2010, 11. This process involved consultations with the FSA, the FSCS, and the DWP.

²³⁶ *Ibid* 14. This included lack of board competence due to inadequate financial and business competency among directors.

The UK's credit unions and the commercial banks receive equal treatment with respect to prudential regulation and supervision under the Bank of England. The Bank is the most central figure in the regulation of the commercial banks and credit unions as it has macro-prudential responsibility for oversight of the financial system.²³⁷ In addition, the Bank of England is responsible for the day to day supervision of the major financial services providers especially those that are managing noteworthy balance-sheet risk.²³⁸ Both banks and credit unions have higher disclosure requirements made to reduce information asymmetry between them and licensed third party businesses.²³⁹

The UK regulatory architecture has been designed to protect and enhance the resilience of the UK financial system against financial crises. Fundamental regulatory restructuring since the 2007 financial crisis has brought forth the establishment of new financial regulators, fully equipped to prevent similar occurrences in the future. The new regulators are the FCA, PRA and the Financial Policy Committee of the Bank of England (FPC).²⁴⁰ FPC identifies, monitors and takes action to remove and reduce systemic risks.²⁴¹ The FCA has been clothed with extensive powers, which enable it to step in earlier, act faster and timely before the risk occurs to the consumers or the

²³⁷ Noam Noked, 'Financial Services Act 2012: A New UK Financial Regulatory Framework' (*Harvard Law School Forum on Corporate Governance and Financial Regulation*, 24 March 2013) <<https://corpgov.law.harvard.edu/2013/03/24/financial-services-act-2012-a-new-uk-financial-regulatory-framework/>> accessed 4 September 2019.

²³⁸ *Ibid.*

²³⁹ The Payment Services Regulations, 2017 ss 40-62. It directs banks and credit unions to give open access to their customer data and account information to licensed third party businesses, though with the caveat that the supplied data can only be provided with their customer's explicit consent.

²⁴⁰ Financial Services Act, 2012 s 6, 12 and 18.

²⁴¹ Bank of England, 'Financial Policy Committee' (*Bank of England*, 6 August 2019) <<https://www.bankofengland.co.uk/about/people/financial-policy-committee>> accessed 4 September 2019. The FPC was established in 2013 as part of the new system of regulation brought in to improve financial stability after the 2008 financial crisis.

market.²⁴² Taken wholesomely, the regulators are mandated to prevent, identify and respond quickly to financial stability issues.²⁴³

4.4 USA's Transparency and Accountability Legal Framework for Credit Unions

The USA's regime for credit unions is very relevant to the Kenyan context for a host of reasons. The USA has a federal government of the united states, which is very much akin to the Kenyan devolved system of governance in several aspects. To that extent, scrutinizing her experience is very helpful as it illuminates pertinent issues on regulating credit unions in a system comprised of shared governance between national and state governments, where both have exclusive and concurrent powers. This analysis goes a long way in explaining the negotiation over the balance of power between the two levels of governance.

The USA's regime on credit unions is chiefly informed by interaction between the federal government and the united states in the exercise of their exclusive and concurrent powers. Credit unions chartered by the federal government are referred to as 'federal credit unions' while those chartered by state government are referred to as 'state-chartered unions.' Federally chartered credit unions are regulated by the National Credit Union Administration (NCUA) while state-chartered credit unions are regulated at the state level.²⁴⁴ Some states do not have set procedures for establishing and regulating credit unions at the state level and persons intending to register a credit union under these states are required to obtain authorization from the federal government.²⁴⁵

²⁴² Bank of England and Financial Services Act, 2016 ss 18-37. The FCA has powers to ban financial products, publish details of misleading financial promotions and publish information about taking disciplinary actions.

²⁴³ Claude Lopez and Elham Saeidinezhad, 'UK Financial Reforms: Bank of England 2.0' (*Milken Institute*, 5 December 2016) 4 <<https://www.milkeninstitute.org/sites/default/files/reports-pdf/Milken-Institute-UK-Financial-Reform.pdf>> accessed 4 September 2019.

²⁴⁴ Dr. Econ, 'Are credit unions regulated or supervised by the Federal Reserve System?' (*Federal Reserve Bank of SAN Francisco*, March 2005) <<https://www.frbsf.org/education/publications/doctor-econ/2005/march/credit-unions-regulation-supervision/>> accessed 28 August 2019.

²⁴⁵ This is the case for states like South Dakota, Delaware and the state of Wyoming.

The USA has a well-defined institutional framework with clear distribution of mandates amongst regulators and less overlap in the regulatory framework for credit unions. While as the Federal Reserve makes consumer protection rules that all lenders, including credit unions, must follow,²⁴⁶ the enforcement of these rules is done by the NCUA for federally chartered credit unions and by the Federal Trade Commission (FTC) and state regulators for state-chartered credit unions. In addition, the Federal Reserve does not supervise or regulate credit unions, with its role being restricted to overall policy formulation.

The USA's legal framework places more premium on the soundness of the financial system, consumer protection and safety of members' deposits and savings. NCUA protects members of credit unions and consumers by raising awareness of potential frauds and by examining credit unions for the compliance with consumer financial laws and regulations.²⁴⁷ It also administers the National Credit Union Share Insurance Fund (NCUSIF) which insures deposits and savings in all federal and state-chartered unions.²⁴⁸ In addition, it promotes safety and soundness in the credit union system through providing confidence in the national structures and consumer protection.²⁴⁹ And more importantly is the role of the Consumer Financial Protection Bureau (CFPB), which has supervisory and enforcement powers over credit unions with assets over \$ 10 billion.²⁵⁰

These achievements notwithstanding, the USA's regulatory framework has been criticized as being fragmented, occasioning multiple overlaps on the mandates of the regulating institutions. It has been argued that there are regulatory overlaps between the CFPB, the NCUA and state

²⁴⁶ Dr. Econ (n 244).

²⁴⁷ National Credit Union Administration, 'Commemorating the 85th Anniversary of the Federal Credit Union Act' (*National Credit Union Administration*, 14 August 2019) <<https://www.ncua.gov/>> accessed 28 August 2019.

²⁴⁸ Lee Hudson Teslik, 'The U.S. Financial Regulatory System' (*Council on Foreign Relations*, 1 October 2018) <<https://www.cfr.org/backgrounder/us-financial-regulatory-system>> accessed 28 August 2019.

²⁴⁹ U.S. Department of the Treasury, *A Financial System That Creates Economic Opportunities: Banks and Credit Unions* (Cmd 13772, 2017) 25.

²⁵⁰ *Ibid* 26.

regulators.²⁵¹ CFPB, which came in later to address issues of regulatory fragmentation with respect to consumer financial protection has to the contrary proven to be duplicative with the supervisory actions of other regulators.²⁵² The fragmented framework has had overreaching negative effects on the efficacy of the entire regime with in terms of increased costs for supervised credit unions, while on the other hand accumulating burdens for the regulatory agencies themselves.²⁵³

4.5 Conclusion

The chapter reveals that there are striking similarities between the Kenyan, the USA's and the UK's financial system in terms of the nature, the structure and the operation of SACCOs or credit unions. It also establishes that the UK and the USA are the most advanced jurisdictions with respect to credit unions.

The UK's legal framework has several positive attributes, which are fundamental in attaining the efficacy of the framework and accountability amongst key regulatory authorities. For starters, the institutional framework has a clear division of duties, rights and responsibilities amongst the relevant regulatory authorities, with no instances of duplication or overlap. In addition, the leading regulatory agencies have a special working relationship characterized by complementarity and partnership on matters of authorizing, registering and regulating credit unions. To some extent, the UK's legal framework has established a form of oversight in which the major regulators, FCA and PRA, can exercise healthy oversight in the execution of their mandates.

²⁵¹ Ibid 30.

²⁵² These include the Federal Reserve, OCC, FDIC, NCUA and state regulators.

²⁵³ U.S. Department of the Treasury (n 249) 30.

The UK prudential regulation regime is comprehensive, objective and responsive in terms of the financial muscles of the credit unions, with the stronger credit unions being subjected to more stringent regulatory requirements. In addition, the regime has embraced and incorporated modern technological advancements into data collection and dissemination mechanisms and that the two chief authorities have established structures for efficient dissemination of information amongst themselves and the credit unions. Further, both the FCA and PRA play a central role in the appointment and approval of professionals whose services are key to a credit union.

The study reveals that the UK's legal regime has evolved overtime through periodic restructuring of the financial regulation systems in an attempt to address the felt necessities of the time. And what sets the UK's experience aside is that her legislative interventions and reforms are well founded on public participation, constructive consultation and a comprehensive policy framework. The study further observed that the UK's credit unions and the commercial banks receive equal treatment with respect to prudential regulation and supervision as they are both regulated by the Bank of England. Lastly, the study demonstrates that the UK's regulatory architecture has been designed to protect and enhance the resilience of the UK's financial system against financial crises.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATIONS

5.0 Introduction

The study sought to investigate the efficacy of the Kenya's legal framework for DT-SACCOs in attaining transparency and accountability between the members of a DT-SACCO, the Management Committee of the SACCO, the Commissioner for Cooperative Development and SASRA. The legal framework creates a host of duties and rights with respect to information disclosure and reporting requirements in the pursuit of accountability between the key stakeholders in the SACCO sector. This notwithstanding, the sector has recently been rocked by major financial scandals which have occasioned great loss of members' life savings and deposits and the collapse of giant DT-SACCOs. And what is more is that both the Commissioner, the members and SASRA have taken long to discover these instances, even where the fraudulent and wrongful dealings have been happening for several years.

The study sought to investigate why the legal framework has not been efficient in attaining accountability between the board of a SACCO, SASRA and the Commissioner. In particular, the study sought to examine the legal challenges that impede transparency and accountability between the board, SASRA and Commissioner and how these challenges contribute to financial mismanagement in DT-SACCOs. Further, it sought to inspect the extent to which the UK's and the USA's experiences on SACCO regulation provide lessons which Kenya can emulate in the pursuit of a more efficient legal framework. Lastly, the study sought to propose any necessary reforms or amendments on the legal framework in the pursuit of a prudent regulatory regime.

The study made three hypotheses. First, that the Kenyan legal framework for DT-SACCOs is inherently ineffective in attaining accountability and transparency between the board of a SACCO, SASRA and the Commissioner. In addition, the study hypothesized that there are legal challenges that impede transparency and accountability between the board, SASRA and Commissioner and that these challenges contribute to financial mismanagement in DT-SACCOs. It also makes an assumption that these challenges have occasioned information asymmetry between the two institutions with subjects of the law eventually falling through the cracks. Lastly, it assumes that this inadequacy is curable through legislative intervention and that the UK's and the USA's experiences on SACCO regulation can provide positive lessons which Kenya can emulate in the pursuit of a more efficient legal framework.

The study utilized a mixture of doctrinal and qualitative research methodologies to prove or disprove the three hypotheses. It did a critical analysis of the UK's and the USA's legal framework for credit unions with a view to identify any positive lessons which Kenya can emulate from their experiences. It conducted interviews on the CEO for Cooperative Tribunal, the former Commissioner for Cooperatives and the CEO for SASRA.

5.1 Findings

The study has proved the three hypotheses. First, it has established that the Kenyan legal framework for DT-SACCOs is inherently ineffective in attaining accountability and transparency between the board of a SACCO, SASRA and the Commissioner. In addition, it has proved that there are legal challenges that impede transparency and accountability between the board, SASRA and Commissioner and that these challenges contribute to financial mismanagement in DT-SACCOs. It has also been confirmed that these challenges have occasioned information asymmetry between the two institutions with subjects of the law eventually falling through the

cracks. Lastly, it has confirmed that the UK's and the USA's experiences on SACCO regulation can provide positive lessons which Kenya can emulate in the pursuit of a more efficient legal framework.

The study revealed that the inefficacy of the Kenya's legal framework for DT-SACCOs has been occasioned by a host of factors. One, the members of the DT-SACCOs have not been adequately empowered to exercise their oversight role over the board. Secondly, the regime offers insufficient sanctions for non-compliance with the reporting and disclosure requirements. In addition, the SASRA's current structure, form and mode of operation is characterized by lapses, inefficiency and unstructured jurisprudence, eventually compromising its efficacy. And what is more is that there are several instances of duplication or overlap between the mandate of the Commissioner and that of SASRA. Further, other internal challenges have cumulatively aggravated the information asymmetry between the board and the members.

Furthermore, these inefficacies have been aggravated by the devolution of the cooperative development function. The statutory framework on DT-SACCOs does not reflect the devolved system of governance, thereby occasioning uncertainty as to who between the national government and the county government has exclusive and the ultimate say on the regulation of cooperatives. Even though the courts have attempted to interpret the Cooperative Societies Act, with a view to bringing it into conformity with the dictates of the Constitution and solve the stalemate, the uncertainty still persists on the exact extent to which the two level of government should relate with regard to the regulation of cooperative societies. The upshot of this persisting and recurring uncertainty on the interplay between the two levels of governments has seen subjects of the law fall through the cracks and especially where a cooperative society is operating from more than one county.

The study revealed that Kenya has a lot to learn from the UK's experience on the regulation of credit unions. The UK's institutional framework has a clear division of duties, rights and responsibilities amongst the relevant regulatory authorities, with no instances of duplication or overlap. In addition, the leading regulatory agencies have a special working relationship characterized by complementarity and partnership on matters of authorizing, registering and regulating credit unions. At the same time, the UK's legal framework has established a form of oversight in which the major regulators, FCA and PRA, can exercise healthy oversight in the execution of their mandates.

The UK prudential regulation regime is comprehensive, objective and responsive to the financial muscles of the credit unions, with the stronger credit unions being subjected to more stringent regulatory requirements. In addition, the regime has embraced and incorporated modern technological advancements into data collection and dissemination mechanisms and that the two chief authorities have established structures for efficient dissemination of information amongst themselves and the credit unions. Further, both the FCA and PRA play a central role in the appointment and approval of professionals whose services are key to a credit union.

The study reveals that the UK's legal regime has evolved overtime through periodic restructuring of the financial regulation systems in an attempt to address the felt necessities of the time. And what sets the UK's experience aside is that her legislative interventions and reforms are well founded on public participation, constructive consultation and a comprehensive policy framework. Further, the UK's credit unions and the commercial banks receive equal treatment with respect to prudential regulation and supervision as they are both regulated by the Bank of England. Lastly, the UK's regulatory architecture has been designed to protect and enhance the resilience of the UK's financial system against financial crises.

With respect to the USA, her regime is chiefly informed by interaction between the federal government and the united states in the exercise of their exclusive and concurrent powers. The study revealed that the USA's legal framework has several positive features which are fundamental in attaining accountability and transparency amongst key regulatory authorities. To some extent, USA has a well-defined institutional framework with clear distribution of mandates amongst regulators and less overlap in the regulatory framework. In addition, the USA's legal framework places more premium on the soundness of the financial system, consumer protection and safety of members' deposits and savings. However, the regulatory framework has to some extent been criticized as being fragmented, occasioning multiple overlaps on the mandates of the regulating institutions.

5.2 Conclusion

The study reaches the conclusion that the Kenya's legal framework on DT-SACCOs is inherently ineffective in attaining transparency within the sector and that these legal challenges have impeded transparency and accountability between that managements committee, SASRA and the Commissioner. In addition, most uncertainty has been occasioned by the role of the County Cooperative Commissioner whose presence, duties and rights have not been provided under the relevant statutes, bringing into focus the interaction between him and the Commissioner for Cooperatives recognized by the Cooperatives Societies Act. Also linked to this is the issue of devolution of the cooperative function, on whether the national government has any role in the regulation of the cooperative movement. The study concludes that while the regulation of the cooperatives has been wholly devolved, the national government has a critical role in that it has the exclusive mandate to generate a monetary policy for the purposes of uniformity and monitoring of the huge sums of monies held by the DT-SACCOs.

Lastly, the framework does not impose on the two regulators the duty to effectively complement each other, mutually coexist and there is much overlap in their duties. It is the considered view of the study that the remedy lies in amending the relevant statutes with a view to establishing the office of the County Cooperative Commissioner, and outlining how he should interact with the national Cooperative Commissioner. Furthermore, there should be a clearer apportionment of responsibilities between the key players to curb overlaps, while sanctioning necessary complementarity to arrest information asymmetry between the regulators.

5.3 Recommendations

Amending the current statutes to conform to the Constitution.

The study revealed that the Cooperative Societies Act 1997 does not conform to the constitutional dispensation, with respect to the devolution of the cooperative function. It is recommended that the Act should be amended in order to reflect the devolved system of governance. In addition, the Sacco Societies Act should be amended to provide for the matter of interaction between the county government and SASRA in the regulation of DT-SACCOs.

A national policy standardizing all county-government SACCO legislations

The study revealed that there is lack of uniformity on the SACCO legislations enacted by various county governments, thereby eroding predictability and quality standards in the sector. It is recommended that parliament should come up with a national policy outlining the bare minimum parameters and threshold, which shall be pre-requisites for any SACCO registration, irrespective of the county in which registration is sought.

Providing a clearer division of duties between SASRA and the Commissioner.

The study revealed that in some instances, there is no clear demarcation and apportionment of mandates between SASRA and the Commissioner, thereby occasioning overlap or duplication. It is recommended that the Sacco Societies Act should be amended in order to introduce a clearer apportionment of rights and duties between the two.

Providing more severe penalties for non-compliance with reporting requirements.

The study revealed that the Kenyan regime offers insufficient sanctions for non-compliance with reporting requirements thanks to lenient sanctions which do not serve the necessary deterrence

function. It is recommended that both the Cooperative Societies Act and the Sacco Societies Act should be amended to incorporate more severe penalties which can deter the fraudulent and wrongful dealing.

Incorporating complementarity and partnership between SASRA and the Commissioner.

The study revealed that there are some instances where the two regulatory authorities appear to have parallel regulatory systems, occasioning overlaps and regulatory gaps in their intersections. It is recommended that the law should be amended to provide mechanisms which foster transparency between the two and which establish a complementarity relationship and coordination in the exercise of their statutory mandates. In particular, both SASRA and the Commissioner should be required to inform the other whenever either of them is about to exercise any of their supervisory powers.

Prudential regulation in accordance with the financial strength of DT-SACCOs.

Chapter four revealed that the UK's regime is objective and responsive in terms of the financial muscles of particular credit unions, with stronger credit unions being subjected to more regulatory requirements. It is recommended that the Kenyan regime should group the DT-SACCOs into several categories in terms of their financial capabilities and their worth, prescribing different regulatory requirements to the respective categories.

Provision of a national regulatory authority for cross-county DT-SACCOs.

Chapter four revealed that the USA's regime on credit unions is chiefly informed by interaction between the federal government and the states in the exercise of their exclusive and concurrent powers. It was showed that there is a body which regulates federally-chartered credit unions while state-chartered credit unions are being regulated at the state level. It is recommended that

parliament should enact a law establishing a national authority whose mandate shall be to regulate DT-SACCOs operating in more than one county. It is also recommended that the new legislation should in addition cover the county governments which are yet to legislate on the SACCO sector. In the circumstances where a particular county government has not enacted the relevant law, persons intending to register a DT-SACCO in that specific county will be required to obtain authorization from the national authority.

Basing the legal framework on solid policy framework.

The study revealed that the UK's regime is founded on public participation, constructive consultation and a comprehensive policy framework. It is recommended that any attempts to amend the current Kenyan law on DT-SACCOs should be informed by extensive consultation amongst stakeholders, taskforces and reports by parliamentary committees. Through this way, the resulting legislation will very much reflect the felt necessities of the time.

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APPENDICES

7.1 Appendix 1: Questionnaire for CEO for SASRA

APPENDIX I

The questionnaire administered to the CEO, SASRA

This open-ended questionnaire is intended to collect information related to the implementation of the law on DT-SACCOs in Kenya, with a particular focus on issues of transparency between the members of the DT-SACCO, the Board of Directors and SASRA. Be assured that the information you provide will be solely for academic purposes and will be treated in confidence.

Section A: Periodic Filling of financial reports

The Sacco Societies Act requires that Sacco Societies submit their audited financial statements within three months after the end of each financial year.

In your opinion:

1. To what extent does the DT-SACCOs meet their reporting requirements on time?
2. What sanctions do you have for DT-SACCOs which do not submit their reports in time?
3. Are the above named sanctions anchored in law or are they based on practice?
4. How effective are the sanctions in ensuring timely compliance of the reporting requirements?
5. What legal reforms would you suggest with a view to streamline the efficacy of the filing requirements?

Section B: The form and Substance of the Financial reports

The Cooperatives Societies Act is equally concerned by the form of the submitted reports as the substance of the forms. On the formality aspect of the reports, they must conform to International Accounting Standards and on the substance of the reports, the accounts should explain certain things, including the transactions of the society, the sums received and paid, all its sales and purchase and its assets and liabilities.

In your opinion:

1. To what extent do the DT-SACCOs comply with the substantive aspects of the reporting requirements?
2. To what extent do the DT-SACCOs comply with the International Accounting Standards?
3. In cases of non-compliance with the reporting standards, what causes the non-compliance?
4. What sanctions does SASRA has in enforcing compliance with the International Accounting Reporting Standards?
5. Are the above named sanctions based in law or are based on practice?
6. How effective are the above named sanctions in enforcing compliance with the international Accounting Standards?
7. What legal reforms would you suggest with a view to enhance compliance with the procedural and substantive aspects of the reporting requirements?

Section C: Powers of SASRA in cases of Non-compliance

The Sacco Societies Act empowers SASRA to undertake either on-site inspections or off-site surveillance or both in its supervisory role over DT-SACCOs. In addition, the Act empowers SASRA to offer advisory opinions and recommendations to those SACCOs which she has a reasonable belief that their business is being conducted contrary to the law. Further, the Act empowers SASRA to summon and require a SACCO to submit reports on its financial affairs to enable SASRA evaluate the SACCO's financial condition.

In your opinion:

1. To what extent has SASRA utilized these supervisory powers?
2. Of the three powers listed above, which ones are least utilized?
3. Why does the Authority forgo invoking these powers?
4. How effective are these supervisory powers in ensuring compliance with the reporting requirements of DT-SACCOs?
5. What legal reforms would you suggest with a view to streamline the efficacy of these supervisory powers?

Section D: Penalties and Sanctions imposed on SACCOs for Non-compliance

The Sacco Societies Act provides several civil and criminal penalties and sanctions which might be utilized by SASRA where it has established that the business of the SACCO has been carried contrary to the prescribed legal requirements. The civil sanctions include reconstituting the SACCO's board of directors, suspending or removing any board member or officer implicated in the wrongful transaction, imposing financial penalties and administrative directives.

Under the criminal sanctions an officer who is convicted for the criminal offences is liable to a variety of liabilities including imprisonment, payment of fines and prohibition from holding office in any SACCO society.

In your opinion:

1. To what extent has SASRA utilized these remedies and sanctions?
2. Of the four mentioned penalties, which ones are least utilized?
3. Why does the Authority forgo invoking these sanctions?
4. How often have the police charged and successfully prosecuted a member or an officer under the criminal provisions in the Act?
5. How effective have these penalties in ensuring compliance with the reporting requirements and attaining transparency in the DT-SACCOs?
6. What legal reforms would you suggest with a view to enhance the efficacy of the above sanctions and penalties?

Summary of the Responses got from the CEO, SASRA

To a large extent, majority of DT-SACCOS meet their reporting requirements on time and those that miss the timelines usually have reasonable justifications for their failure to meet the statutory filing requirements. The CEO hinted that SASRA is in the process of creating an online filing system, whereby DT-SACCOs will no longer be required to submit physical documentations at the SASRA offices. In addition, the new system will enable the SACCOs conduct self-assessment,

even before they submit their returns to the regulator. Furthermore, SASRA has employed both on-site inspections and off-site surveillance in its supervisory role over DT-SACCOs.

More often, SASRA summons and requires a SACCO to submit reports on its financial affairs to enable them evaluate the SACCO's financial condition. It was his opinion that DT-SACCOs have underutilized some of the regulator's special powers, especially advisory opinions and recommendations. Lastly, SASRA has to a large extent utilized penalties and sanctions imposed on SACCOs for non-compliance. In some instances, the police have charged and successfully prosecuted officers under the criminal provisions of the Sacco Societies Act 2004, especially where an officer has committed forgery. The CEO was of the opinion that the current law is sufficient with respect to attaining transparency and accountability in the legal framework for DT-SACCOs.

7.2 Appendix 3: Questionnaire for former Commissioner for Cooperative Development.

APPENDIX III

The questionnaire administered to the Commissioner of the Cooperatives Development in Kenya

This open-ended questionnaire is intended to collect information related to the implementation of the law on DT-SACCOs in Kenya, with a particular focus on issues of transparency between the members of the DT-SACCO, the Board of Directors and SASRA. Be assured that the information you provide will be solely for academic purposes and will be treated in confidence.

Section A: Periodic Filling of financial reports

The Co-operatives Societies Act requires Sacco societies to submit to the Commissioner, their annual audited financial statements within a certain prescribed period.

In your opinion:

6. To what extent has the DT- SACCOs been meeting this reporting requirements on time?
7. What sanctions have you imposed on those DT-SACCOs which have failed to submit the audited accounts in time?
8. Are the above named sanctions anchored in law or are they based on practice?
9. How effective were the sanctions in ensuring timely compliance of the reporting requirements?
10. What legal reforms would you suggest with a view to ensure that DT-SACCOs comply with this requirement in time?

Section B: The Powers of the Commissioner to Call for a Special Meeting

The Cooperative Societies Act empowers the commissioner to convene a special meeting of a DT-SACCO at which the Commissioner may direct the matters to be discussed at the meeting. The Commissioner may preside at the meeting.

In your opinion:

1. To what extent has the office of the commissioner utilized these powers?

2. On what occasions has the office of the commissioner invoked these powers?
3. How effective has the invocation of these powers been with respect to fostering transparency in the DT-SACCOs?
4. What legal reforms would you suggest with a view to enhance the efficacy of these powers in attaining transparency within DT-SACCOs?

Section C: The powers of the Commissioner to hold an inquiry into the financial conditions of any DT-SACCO.

The Cooperatives Societies Act empowers the commissioner to hold an inquiry into the by-laws, working and financial conditions of any DT-SACCO. The commissioner can exercise these powers of his own accord, or upon the direction of the Cabinet Secretary, or on the application of members of the DT-SACCO. If the report of the inquiry indicates that the committee of the DT-SACCO is not performing its duties properly, the Commissioner may dissolve the Committee and appoint an interim committee for a maximum period of ninety days.

In your opinion:

8. To what extent has the office of the Commissioner invoked these powers?
9. On the various occasions where the Commissioner has invoked these powers in the past, who provoked his action? (the CS, the members or on own accord or a combination)?
10. Are there occasions where the Commissioner invoked the powers on his own accord?
11. If the above question is answered in the affirmative, what informed his suspicion for the commissioner to invoke these powers on his own accord?
12. Are there occasions where the Inquiry conformed that a committee of a DT-SACCO was not performing their duties properly?
13. If the above question is answered in the affirmative, how effective was the consequential dissolving of the non-functioning Committee in ensuring a more diligent performance from the subsequent committees?
14. What legal reforms would you suggest with a view to enhance the efficacy of the commissioner's powers in attaining transparency in the DT-SACCOs?

Section D: Powers of the Commissioner to conduct routine inspection

Under section 60A, the Cooperative Societies Act empowers the commissioner to carry out impromptu inspection into the affairs of a DT-SACCCO.

In your opinion:

6. How many times has the Commissioner invoked these powers?
7. What are the usefulness of the impromptu inspections with respect to enhancing transparency in DT-SACCOs?
8. What legal reforms would you suggest with a view to enhance the efficacy of the impromptu inspections in attaining transparency in DT-SACCOs?

Section E: The automatic dissolution of a Committee which fails to audit their financial accounts within the prescribed period.

According to section 25 (11) of the Cooperatives Societies Act, members of a committee which has failed to audit its accounts within the prescribed period shall automatically lose their positions at the next general meeting. The ousted committee members are not eligible for re-election for three years unless the Commissioner is satisfied that the failure was due to circumstances beyond their control.

In your opinion:

1. To what extent has this provision been operationalized?
2. How many committees have been automatically dissolved in line with this provision?
3. On exercising his discretion under the provision, what factors does the commissioner consider in determining whether the failure to audit within time was due to circumstances beyond the committee's control?
4. How effective has this provision been with respect to sanctioning timely auditing of financial accounts?
5. What legal reforms would you suggest with a view to enhance the efficacy of this provision in attaining timely auditing of the financial statements?

Summary of the Responses got from the former Commissioner for Cooperative Development

The former commissioner illuminated the study in a material way, especially on the manner in which the Commissioner is interacting with the county governments in discharging mandates under the new constitutional dispensation. Her contribution brought on the surface the debate on the role of the national government in the regulation of DT-SACCOs, given that the Constitution entirely devolves the cooperative function to the County Governments. Generally, the former commissioner was of the view that the office has effectively utilized the power to call for a special meeting, power to hold an inquiry into the financial condition of any DT-SACCO, the power to conduct routine inspection, and the automatic dissolution of a committee which fails to audit their financial accounts within the prescribed period.

More importantly, she pointed out the real legal challenges countering the powers of the commissioner as provided for under the Cooperative Societies Act 1997 and the Sacco Societies Act 2004. She revealed that the powers and the supervisory role of the commissioner is under siege, thanks to the Constitution 2010 which has devolved the cooperative function. And what is more is that the current statutes do not recognize the role of the county cooperative commissioners, who are the actual persons running the SACCO sector. As a result, there is much uncertainty on the nature of interaction between the commissioner and the county cooperative commissioner, eventually eroding transparency and accountability in the regulation of DT-SACCOs. She was of the opinion that parliament should enact a legislation stipulating the manner of interaction between the national government and the county governments, with respect to regulation of DT-SACCOs, especially for those DT-SACCOs operating in more than one county.