REFORM OF THE SECURED TRANSACTIONS FRAMEWORK IN KENYA

BEATRICE OSICHO
SENIOR STATE COUNSEL, BRS

Presentation Outline

- Introduction
- Need for the Reforms/challenges
- Process of reform
- Reforms undertaken
- Expected Benefits from the Reform

Introduction

- Government of Kenya is committed to improving the business environment in order to support the private sector to promote growth and job creation
- The Vision 2030(Kenya's economic blueprint) outlines improving access to credit by decreasing the share of population without access to finance from 85% to below 70%

Need for Reforms

- Borrowers complain about high interest rates, hidden charges, nondisclosure of pertinent information and unfair denial of access to credit
- Lenders are worried about high default rates, difficulties on foreclosing on collateral through the courts and the misapplication of funds by the borrowers
- With these conflicting views, the Kenyan economy continues to miss out on the huge potential that MSMEs have in driving economic growth

- At the same time there were challenges in the legal and regulatory framework for secured transactions:
- Multiple laws governing different security devices and applying to different types of borrowers e.g Companies Act, Hire Purchase Act, Chattels Transfer Act etc
- Laws were outdated and presented a number of legal risks
- Paper based manual system
- Inefficient and cumbersome registries
- Cumbersome and time consuming registration procedures

Chattels Transfer Act

- Enacted in 1930 but has since been amended to accommodate certain market changes (fees)
- Agreements entered into under this Act required registration, and in the absence of such registration, the instruments are void against third parties
- The Act required submission of the agreement documenting the transaction as well as a schedule of the collateral

- The lender had to register the document within 21 days failing which a court order should be produced.
- Registration is valid for 5 years
- Details of the loan amount, name of borrower and lender were entered in the Register of Chattels which was manual

Companies Act

- Some sections of this Act govern the registration of charges over a company's movable assets.
- A charge on the movable assets of a company had no effect against the liquidator or other creditor if it had not been registered within 30 days (new Act), commencing on the date of the creation of the charge.
- Charges under this Act included floating charges, charges to secure debentures

Hire Purchase Act

- The Act regulates transactions in which the legal ownership of and title to the goods is vested to the hirer upon payment of the hire purchase price in full.
- The Act establishes a transaction registration system in which agreements must be registered at the Registrar of Hire Purchase Agreements.
- Failure to register (within 30 days) results in the legal impossibility to enforce the hire purchase agreement in case of default.

- For a lender to register an agreement, they must first obtain a license to engage in the hire purchase business.
- The feature of hire purchase- the lender retaining ownership until the price is paid in full- makes the product unattractive to many financial institutions.
- Limitation on lenders' enforcement rights – no repossession after payment of 2/3

Process of Reform

- Constitution of Technical Working Group – made up of stakeholders : Central Bank, Kenya Bankers Association, Kenya Law Reform Commission, National Treasury, Office of the Attorney General, Financial Sector Deepening Trust (FSD) and the World Bank
- Scoping mission on current status of the various laws and the registries and presentation to key stakeholders on the results of the scoping mission
- Benchmarking Visits to various jurisdictions that have implemented the reforms successfully

Process of reform….ctd

- Stakeholders workshops were held with sector organizations including: Law Society of Kenya (LSK), Kenya Bankers Association (KBA), Leasing Association of Kenya, Association of Microfinance Institutions (AMFI), Kenya Association of Manufacturers (KAM), Kenya Private Sector Alliance (KEPSA) and the Micro and Small Enterprises Authority (MSEA)
- County stakeholder forums in four Counties - Nakuru, Kisumu, Kakamega and Mombasa. Participants in the Counties were drawn from various MSEs registered by MSEA

Reforms

- The Movable Property Security Rights Act, 2017 was assented to by the President on 10th May 2017. Commenced on 16th May 2017 vide LN No 77
- The key objective of the law is to facilitate the use of movable property as collateral for credit facilities, to establish the Electronic Collateral Registry and to provide for the registration of interests in movable property

- Development and Establishment of the Electronic Collateral Registry in 2017.
- Exclusively electronic and accessible in real time
- Registration is immediate
- Searches by ID numbers of grantors and serial numbers of some assets (e.g., cars)
- Free to register and even minimal search fee

Registry does not verify legality or accuracy of the information in applications (notices) for registration
Registry only ensures that all mandatory information has been provided

- Responsibility for errors remains with the registrant
- Rejection of registration only on limited grounds
  - Missing information
  - Failure to pay a fee

Reforms are seeking to address the following main policies

- Increased access to finance, and overall financial inclusion
- Simplification, modernization and unification of the legal framework
- Less legal complexity - Minimal requirements for agreements and registrations
- Reduced cost of financing - Inexpensive registry
- More transparency that reduces risk - Registration for all property rights in movable assets
- More certainty through clear priority rules

Expected Benefits of the Reform - I

- Greater participation of MSMEs in the economy by enhancing and facilitating access to credit by addressing challenges:
  - inability to capitalize on business opportunities and thus expand their businesses;
  - Lack of bankable collateral which made financial institutions unwilling to extend them credit.
- More attractive and less risky for lenders to give loans to MSMEs due to:
  - Registration of security rights online
  - Clear priority rules for registering security rights
  - Clear and enforceable foreclosure laws in cases of default

Expected Benefits of the Reform - II

- Enhanced transparency in lending, through:
  - Establishment of an electronic register, accessible online to both incorporated and unincorporated entities, and to the members of the public
  - Discharge of collateral once the loan has been fully paid up.

Expected Benefits of the Reform - III

- Supports the achievement of Vision 2030, which seeks to promote the development of a strong and competitive financial sector as a key component of an enabling environment for business.

- In Conclusion we hope that the Movable Property Security Rights Act and the Collateral registry has resulted in significant progress towards creating an enabling environment that facilitates lending on the strength of movable assets as collateral.

Thank You