

FSD Insights

FINANCIAL CONSUMER PROTECTION IN KENYA: KEY RESEARCH FINDINGS & POLICY RECOMMENDATIONS

BACKGROUND

The Government of Kenya's (GoK) Vision 2030 Strategy has broad goals that include promoting financial inclusion, improving transparency and affordability of financial services, and increasing competition in the sector to benefit customers and the overall economy. The new Kenya constitution has specific provisions on consumer rights. This agenda has grown out of concerns related to expansion of regulated financial services to large numbers of first-time retail consumers,¹ the large spread between lending and deposit rates, the exposure of consumers to substantial losses through pyramid schemes, the introduction of increasingly complex financial products and the blurring of lines between types of financial service providers.

The Financial Education and Protection Program (FEPP)² formed a Task Force (FEPP TF) to support this agenda. The Ministry of Finance and CPT determined it would be valuable to commission a rapid diagnostic study to identify the main issues and recommend improvements in financial consumer protection and education and support was generously provided by CGAP and FSD Kenya. The focus of the diagnostic study is on 'mass market consumer' who consume basic credit, savings, and payment services provided by banks, mobile financial service providers, savings and credit cooperatives (SACCOs), and microfinance institutions (MFIs).

Mass market financial services are growing at an impressive rate, generating significant benefits for consumers. Evidence from the consumer research outlined herein below suggests that consumer welfare is compromised by lack of effective disclosure of prices and key terms, inadequate dispute resolution mechanisms, and abusive practices. For example, 25% of bank depositors in the survey expressed "surprise" at charges they did not know about. This is not surprising, given that a 2007 CBK survey found that banks had 53 different classes of charges levied on current accounts.

The financial sector regulators provide some, but incomplete and sometimes inconsistent consumer protection to the clients of regulated institutions. In the absence of a market-wide consumer protection law or authority, users of informal financial service providers entirely lack protection. As a result, Kenya falls short in providing comprehensive financial consumer protection and

recourse, in policy and practice. The new Constitution commits the nation to protecting consumers and Vision 2030 proposes policy initiatives.

CONSUMER RESEARCH OBJECTIVES AND METHODOLOGY

The diagnostic process included direct input from consumers through focus group discussions (FGDs) and a national survey, to provide a fuller understanding of consumers' usage of different products and service providers and their experience related to consumer protection issues. Consumer research is an important diagnostic component, as it permits verification or rejection of assumptions regarding the most common or problematic abuses in the market. It also helps assess whether measures currently in place are having the intended effect in protecting consumers or increasing their financial capability.

Consumer experience was measured through two tools

- As a first step, FSDK commissioned FGDs to provide a well-rounded initial scan of consumer protection issues in the mass market. A total of 112 consumers of various socioeconomic backgrounds and from different provinces were selected into a total of 14 FGDs (February-March 2010). This qualitative picture tested consumer protection priorities that had emerged from the early 2010 desk research and key informant interviews. It helped the team determine which questions to ask in the quantitative survey and how to ask them. The FGDs also provided valuable insight into the decision-making processes and knowledge of consumers around financial products and their rights as consumers.
- The second step was an FSDK-commissioned survey of 1548 adult consumers gauging their experiences with savings, loans, insurance, mobile payment, and pyramid schemes. The survey also sought to assess respondents' financial capability and awareness of and response to measures intended to extend protection. The initial sample of 1000 was selected proportionate to population size across provinces and districts. A "booster sample" of 548 additional consumers was added to ensure a minimum of 50 respondents for each financial instrument (since the population-representative sample did not yield sufficient respondents in certain product categories, such as long-term savings). The resulting total sample is more engaged in the formal financial sector than the nationwide population.³

¹ FinAccess 2009 shows an increase from 18.9% to 22.6% between 2006 and 2009 in the share of the adult population accessing finance from formal providers (mainly banks). The M-PESA mobile payments service offered by Safaricom also has brought many new users into the formal system.

² FEPP is a public-private partnership that comprises those public bodies and private stakeholders that are most relevant to improving financial education and consumer protection. The Governor of the CBK is the official champion of the FEPP, and the Financial Sector Deepening Trust-Kenya (FSDK) provides secretariat support.

³ Based on data from FSDK's FinAccess 2009 report. In the survey, for instance, only 12% of respondents are dependent upon financial remittances, compared to 21% in the national sample. Similarly, the survey contains an urban bias, with a rural-urban split of 63%-37%, compared to 79%-21% in the national sample.

KEY FINDINGS

1. Consumer information and knowledge

Obtaining information about many different types of financial instruments appeared to be relatively easy for consumers. On average, 66% of survey respondents found it “very easy” to find information on different types of products and their charges and penalties across a range of financial institutions. Informal instruments such as ROSCAs and ASCAs were considered easier to get information from than banks, MFIs and SACCOs. Overall, focus groups revealed a surprisingly high awareness of issues such as the Central Bank issuing licenses, knowledge about the banking act and use of correct financial terms.

There was some lack of clarity about practices in banking. FGDs revealed some doubts amongst users about whether their money was really safe in financial institutions, even in banks and SACCOs. Respondents were also uncertain about available options for recourse, and were often unsure whether the problems they were dealing with had a legal basis or not. Furthermore, the recourse systems in place did not appear to be easy to use or timely, as many FGD participants recounted stories about seeking redress that ultimately required their having to hire a lawyer. Together, these focus groups reveal some weakness in both transparency and financial capability.

2. Savings

According to the consumer protection survey, 59% of the sample had a bank savings account, 20% had a SACCO account, 15% an MFI account, 17% an ASCA account and 47% a ROSCA merry-go round. These numbers are higher than those in the FinAccess 2009 survey, indicating that the consumer protection survey covered a population with more access to different types of savings products than the overall Kenyan population.⁴

Table 2: Respondents who say that they trust their savings instrument to keep their money safe

Type of institution	Bank savings account	SACCO	MFI	ASCA	ROSCA/ Merry go round
% responding yes	97%	93%	93%	92%	92%

Of those that had a savings account, between 7% and 11% of respondents said that they had lost money in them. Of those that had lost money, 33% blamed the charges and penalties for “eating away” their money, although many also claim to have lost money when the institution closed down (21%), when money was misappropriated (12%) or there were errors in records (27%). Misappropriation of money was more prevalent with informal instruments such as ASCAs (56%) and ROSCAs (51%) than formal financial institutions. Similarly, banks (7%) had lower levels of loss than informal instruments (9%–11%), which could explain why banks were the most trusted vehicle for savings among respondents (see Table 2.)

Table 3: Were the charges, interest and penalties explained clearly?

Type of institution	Bank savings account	SACCO	MFI	ASCA	ROSCA/ Merry go round
% responding yes	97%	93%	93%	92%	92%

Interestingly, while banks are the most trusted option, they are also the instrument where users felt that charges, interest and penalties were least clearly explained. As Table 3 shows, nearly 12% of bank users felt that this

Table 1: How easy is it to get information about charges or penalties for each of these different savings products? (1 = very easy; 5=very difficult)

Difficulty rankings:	Bank savings	MFI	Sacco	ASCA	Rosca	Across all financial institutions
1 (very easy)	54%	61%	63%	79%	81%	66%
2	28%	29%	28%	16%	15%	23%
3	9%	6%	7%	3%	2%	6%
4	6%	3%	2%	0%	0%	3%
5 (very difficult)	1%	1%	0%	0%	0%	0%
Refused/ did not know	2%	0%	1%	2%	2%	2%
Number of respondents	949	238	303	266	723	2479

⁴ In the FinAccess 2009 Survey, only 24% of respondents said they had a bank account, with 9% for SACCOs, 3% for MFIs, 8% for ASCAs and 32% for ROSCA merry-go round.

was the case. When questions or concerns did arise, 91%-93% of all users had their issue resolved after contacting the institution. However, between 5%-7% of users did not receive a satisfactory response after contacting the institution. This and the percentage of users who felt that charges, interest and penalties were not sufficiently explained, suggest that there could still be room for improvement in transparency and information.

3. Loans

Respondents received loans from a variety of formal and informal institutions, including banks (10%), SACCOs (9%), MFIs (11%), ASCAs (8%), informal lenders (2%), employers (1%), through hire purchase (3%) and from local shop keeper credit (22%). These numbers again reflect greater access to loans among the sample group than the FinAccess 2009 results would suggest.⁵

As Table 4 shows, not all users received a written loan agreement. While this is expected from informal lenders, only 93% of bank borrowers and 95% of SACCO borrowers said they had received a written agreement. Of those that did receive one, most but not all were able to take it away to study it before signing. However, many were still pressured to sign the agreement immediately, even in formal institutions such as banks (10%), MFIs (10%), SACCOs (14%) and hire purchase (10%).

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immediately, even in formal institutions such as banks (10%), MFIs (10%), SACCOs (14%) and hire purchase (10%).

Those who had taken a loan or credit often were required to offer some type of collateral. In 42% of cases, this involved the rights to a home or other asset; in 45%, this involved someone signing surety (i.e., providing a guarantee); and in 7%, the lender withheld the borrower's ATM card and pin number, which is a highly improper lending practice that warrants further investigation. As Table 5 shows, most respondents also reported that loan terms were explained to them and many seemed aware in focus groups about what hidden charges could arise in loans, mentioning insurance, registration fees, standing order fees, negotiation fees, stamp charges and loan processing fees. Practically speaking, however, many respondents still found it difficult to completely understand loan documents and many were surprised by how much is actually charged for loans. About 6-9% of those surveyed reported that they were surprised after the fact by how long and how much they needed to pay after taking out a loan. Finally, FGD evidence suggests that repossession and auctioning off of goods appear to be the norm in instances where the user defaults on a loan. This was consistent across semi-formal and formal lenders.

4. Insurance

According to the consumer protection survey, 26% of respondents held life insurance, 3% medical insurance, 6% house-building or contents insurance and a negligible percentage auto insurance. The share of 2010 survey respondents with life insurance was significantly higher than in the FinAccess 2009 results.⁶

Table 4: Did someone explain the terms of the loan before you signed?

	Bank loan	SACCO	MFI	ASCA	Shylock, money lender, or shopkeeper	Employer	Hire purchase
% of those with loan that responded yes	94%	93%	97%	97%	97%	83%	100%

Table 5: Experiences of insurance users

	Were the details explained to you in writing?	Did you understand the details of the insurance?	Were you able to take the agreement away with you before	Have you made a claim?	In your opinion, was the claim processed quickly?
Yes	87%	89%	74%	19%	74%
No	13%	11%	17%	81%	26%
Total	194	190	191	457	86

⁵ In the FinAccess 2009 Survey, loans were received from banks (2.6%), SACCOs (3%), MFIs (1.8%), ASCAs (1.8%), informal lenders (0.4%), from employers (0.5%), through hire purchase (0.1%) and from local shop keeper credit (24.3%).

⁶ FinAccess 2009 reports that 1% of respondents had life insurance, 4.9% had medical insurance, 0.2% had house-building or contents insurance and 1.1% had auto insurance.

Most FGD respondents did not have experience with insurance. Among those that did, the experience was often not positive. Most complaints that surfaced in the FGDs centred on salespeople not clearly explaining the products, resulting in users not receiving the package they had envisioned. As Table 6 shows, 13% of insurance users said the details were not explained in writing and 11% said they did not understand the details of the insurance, in terms of how much would be paid and what was and wasn't covered by the policy. 17% reported that they felt pressured to sign right away. In one case, a man from Mombasa reported in a FGD that an insurance agent managed to sign him up for a policy he did not authorize and that he was only able to have the debit order reversed and his money refunded after hiring a lawyer. Finally, insurance users also reported that making claims was far from easy, with 26% of survey respondents saying that their claims were not processed quickly.

5. Long term savings: Investments, pensions, retirement annuities

As shown in Table 7, very few respondents had long term investments, reflecting similar results from FinAccess 2009.⁷ Of those that did have investments, many respondents reported that they were promised a certain return from a salesperson (25%), pressured to make an investment (14%), or were left without written documentation on the terms of the product (32%).

Table 7: Respondents with various forms of long term savings

	Education Savings policy	Retirement annuity	Pension or provident fund	Investment portfolio, shares, or bonds
Number of respondents	63	52	46	113
% of respondents	4%	3%	3%	7%

Qualitative and quantitative data also show that there is a lack of adequate information about pensions. In FGDs, many respondents reported that they were unsure of whether or not they were receiving pensions. As Table 8 shows, 17% of the sample said they would receive a pension when they retired, but 12% were unsure and 69% said they would not. Of those that think they are receiving pensions, 21% felt uncomfortable asking their employers about it. This lack of clarity carries through to retirement payments. Of those who were receiving pensions at the time of the survey, 12% said they received less than they had expected and 4% said they were unsure whether they had received the right amount.

⁷ FinAccess 2009 recorded that 1% of the population has an education savings plan and 2% have a pension or retirement plan.

6. Mobile payment services

Mobile money services like M-Pesa, Zain/Zap and Yu have become central in people's financial lives. The survey revealed that 84% of respondents have used a mobile money service, significantly higher than the 40% reported by FinAccess 2009. Quantitative data from the consumer protection survey shows just how popular mobile payment services are – 5% of all respondents claimed to use a mobile payment service every day, 33% at least once per week, 38% at least once per month and 24% once in a while. FGD participants also reported feeling safer using M-Pesa than having to walk around with cash.

Table 8: Respondents who have used a mobile payments service

	Have you used a money transfer service like M-Pesa, Zain, etc?	Whose phone did you use?		
		My own phone	Phone of family or friend	Agent's phone
Number of respondents	1,293	1137	131	33
% of respondents	84%	73%	8%	2%

While FGD findings suggest that M-Pesa charges were quite clear – for example, most respondents knew what it cost to send and receive money – this contrasted somewhat with survey data, where 16% of users felt that the charges were not clearly explained before starting to use the service. Moreover, although mobile payments are widely used, over 36% of users reported problems when using mobile payment services. As Table 9 shows, 22% have had a problem when there was no cash at the agent, 11% of users have made a mistake and sent money to the wrong account and 3% of users have had problems with either receiving money or having their recipient not receive money.

When experiencing these problems, however, M-Pesa users were very clear about what to do when problems arose and overwhelmingly stated that problems were resolved quickly when reported. FGD participants were even able to recite the telephone number of customer care at M-Pesa, and many respondents noted that even when money was sent to the wrong person, it was often easy to recover the money. Table 10 shows the length of time it took to resolve problems.

7. Pyramid Schemes

A very large number of respondents were approached about joining a pyramid scheme. At least one participant in every focus group had been a victim of a pyramid scheme, or had someone close who had fallen victim. Forty four percent (44%) of survey respondents reported that they had been approached

Table 9: Problems users have had with mobile payment service

Problem (n=1,293 who've used mobile payment services)	No.	Percent
No problem	792	61%
You made a mistake; Sent to wrong account	136	11%
Payment you made wasn't received (no error)	39	3%
Never received money	45	3%
Money not in MP account	7	1%
Robbed	7	1%
No cash at agent	279	22%
Network failure	99	8%
Couldn't directly deposit money into another's account	1	0%
I don't have an account, so agent didn't transact	2	0%
Entered wrong agents' number when withdrawing money	1	0%

Table 10: How long did it take to resolve the problem?

	Percent
Right away	61%
Within a day	11%
Within one month	3%
Total	3%

to invest in a pyramid scheme. While only 9% of those who reported being solicited invested in the pyramid schemes, this figure may be low as the diagnostic team believes participants might have been unwilling to self-report not to have been deeded as having been fooled. The survey established that the average amount invested and lost was Kshs. 37,013, quite a sizable sum.

Table 11: Number of respondents approached about a pyramid scheme and invested

	Approached about entering a pyramid scheme	Investing money in a scheme
Number of respondents	685	144
Percent	44%	9%

Table 12: Did you complain to anyone, if you lost money?

Response	Number	Percent
Yes	50	41%
No - wouldn't know who to complain to	31	25%
No - it wouldn't do any good	42	34%
Total	123	100%

There was little recourse for those who lost money in pyramid schemes. Of those that lost money, 25% did not complain because they did not know who to complain to and 34% did not complain because they did not think it would do any good. Most FGD participants who had been taken advantage of reported that they were too ashamed to admit having participated in a pyramid scheme.

8. Policy recommendations

The consumer research evidence suggests that current consumer protection problems merit attention. Kenya needs to develop a strategy for strengthening consumer protection grounded on pragmatic solutions to problems that affect the larger majority of consumers. The lack of comprehensive consumer protection legislation lends urgency to the finalization of the Consumer Protection bill and the implementation of the Competition bill. However, gradual but continual progress is recommended as a more prudent strategy than relying on future legislation and the capacity of a brand-new regulator.

An incremental approach is therefore recommended as offering the best way to build effective financial consumer protection. The financial sector regulators, responsible for oversight of mass-market services – particularly the Central Bank of Kenya, the Insurance Regulatory Authority, SASRA and the Ministry of Finance – have adequate authority to improve financial consumer protection through making incremental improvements in regulation. The revisions set to occur to the various financial sector regulations, aligning them to the provisions in the new constitution provide a good opportunity to enhance consumer protection. A coordinated approach to issuing and enforcing consistent rules governing disclosure, recourse and fair treatment may also be considered.

Jointly, the regulators are positioned to launch this strategy by establishing a basic protection regime that would cover 40% of the adult population who are clients of banks, foreign exchange bureaus, deposit-taking microfinance institutions, mobile financial services, insurance companies, pension plans, investment brokers and advisors, and larger SACCOs.⁸ Each sector regulator already has similar legal mandates to safeguard consumer interests. It is noteworthy that some regulators have put in place rules that can be adapted

⁸ Finaccess 2009

by their counterparts to create a harmonized protective regime related to the following core areas:

- **Minimum disclosure requirements for pricing and plain language in contracts.** The CBK is well advanced in reviewing credit price disclosure guide-lines, and the IRA is engaged with the insurance industry in the development of standardized, plain language policy wording for various insurance products.
- **Minimum requirements for provider-level dispute resolution mechanisms and independent third-party recourse.** The Credit Reference Bureau regulations, for example, establish clear guidelines for providers. The IRA and CMA are mandated to, and in practice provide recourse to consumers unable to resolve grievances through provider dispute channels. The other regulators may – with good reason – choose to delegate this function to a future entity with a market-wide recourse mandate.
- **Regulations that clarify provider liability and responsibility for oversight of third-party agents who play a role in service delivery.** The recent Agent Banking Guidelines serve as a model for other sectors in this respect. Ensuring clear provider liability for agents is particularly important in the insurance sector and with the mobile financial service providers. Where liability is limited for practical reasons, it is important that consumers are aware of that limitation.
- **Public reporting of provider performance in basic areas.** The regulators should ensure public disclosure including:
 - A list of providers that are subject to prudential and consumer protection regulations;
 - A description of the regulations including, specifically, the obligations of the providers; and,
 - Periodic reporting on individual provider performance against the transparency and internal dispute mechanism rules to which they are subject.

Mobile financial services deserve particular attention, since users number over ten million Kenyans or 54% of the adult population. Formalising regulation of mobile service providers is now timely and prudent, to control risks to consumers while ensuring a solid foundation for the industry. For now, the 27% of the population that use unregulated providers must rely mainly on their own financial capability to assess providers and products and protect themselves against abusive or unfair practices. Extrapolating from the national survey conducted as part of the diagnostic, for example, just under 1 million adults lost roughly Kshs. 31 billion in pyramid schemes.

Building the nation's financial capabilities is a formidable challenge. The Financial Education and Consumer Protection Partnership (FEPP) already

convenes most key public and private sector players and provides a strong vehicle for implementing a credible strategy. Promising pilots are underway. The diagnostic identifies a number of key short-term awareness and education priorities directly related to the proposed transparency, fair treatment and effective recourse measures. Although this will be a long-term process, successful pilot project approaches can be scaled up rapidly to support core protection issues in the short to medium term. The financial sector regulators have also created the Joint Regulators' Task Force with a memorandum of understanding for collective action on consumer awareness and financial education. This taskforce could collaborate with the FEPP to support the implementation of financial education campaigns and in the development of a comprehensive national strategy. For now, the 27% of the population that use unregulated providers must rely mainly on their own financial capability to assess providers and products and protect themselves against abusive or unfair practices. Extrapolating from the national survey conducted as part of the diagnostic, for example, just under 1 million adults lost roughly Kshs. 31 billion in pyramid schemes.

These first-phase incremental efforts will be to cultivate the critical mass of political will and practical experience needed to drive the development of a comprehensive financial consumer protection legal framework and a dedicated enforcement authority. A new authority of this type would complement the financial sector efforts in three important ways:

- An enforcement agency with a market-wide protection mandate could enforce consumer protection regulation across the entire financial market and thereby cover the clients of otherwise unregulated providers.
- It could address specific practices and products in ways that the more risk-based, prudential regulators typically do not.
- And finally, it could establish a recourse mechanism to function as a check and balance on providers' internal dispute resolution. The authority could also cooperate with the financial sector regulators for consistent market monitoring.

As for implementation, this proposal for incremental improvements leverages the existing capacity of established financial-sector regulatory entities, in advance of creating a new cross-market authority. It mitigates the high risk of regulatory dysfunction when a new regulatory agency is set up to enforce a new law. The sector regulators can lend capacity and credibility to the early stages of this incremental process. And their early success can create impetus for an eventual comprehensive consumer protection regime.

This strategy contemplates a pivotal role for the Ministry of Finance, which is best positioned to engage the financial sector regulators, monitor progress, and guide the policy dialogue. The Ministry is also uniquely positioned to secure the public sector resources required to sustain this effort over time.

About the Financial Education and Consumer Protection Partnership (FEPP)

The FEPP is a public-private sector partnership driving the development of a comprehensive national financial education strategy for Kenya. Together, the partnership aims to build a strategy that finds effective ways to improve the nation's knowledge and understanding of personal finances.

FEPP offers the prospect of strengthening the development of financial markets and enhancing the impact of expanded services on the livelihoods of Kenyans, especially among poorer groups. If this potential is to be realised then the long-term vision needs to be bold and the ambition from the outset should be the creation of a comprehensive, national programme. There are some encouraging initiatives already underway and a credible route to achieving major impact has been defined.

Work has been ongoing to understand practically what works and doesn't work in Kenya and to motivate the key stakeholders who can drive the longer-term programme. The objective for this project will therefore be to establish the foundations for a comprehensive and sustainable programme of financial education in Kenya. FEPP is supported and coordinated by the Financial Sector Deepening (FSD) Kenya, a multi-donor financial sector development programme.

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The Kenya Financial Sector Deepening (FSD) programme was established in early 2005 to support the development of financial markets in Kenya as a means to stimulate wealth creation and reduce poverty. Working in partnership with the financial services industry, the programme's goal is to expand access to financial services among lower income households and smaller enterprises. It operates as an independent trust under the supervision of professional trustees, KPMG Kenya, with policy guidance from a Programme Investment Committee (PIC). In addition to the Government of Kenya, funders include the UK's Department for International Development (DFID), the World Bank, the Swedish International Development Agency (SIDA), Agence Française de Développement (AFD) and the Bill and Melinda Gates Foundation.