



# Executive Summary

## A Review of East African Debt Policies

**Kenya ♦ Uganda ♦ Tanzania ♦ Burundi**

Digital innovation has made access to credit easier for millions who previously struggled to get loans. This expansion in digital financial services (DFS) can be a boon to development, unlocking the productive potential of large numbers of hard-working, entrepreneurial people who have historically been excluded from market opportunities. However, it also carries the risk that borrowers, especially from the most vulnerable communities, will fall victim to unregulated and predatory lending. Sustainable financial inclusion requires law, policy and good business practice to provide safeguards that protect financial consumers. Accordingly, the United Nation’s Sustainable Development Goal (SDG) 10 requires states to ‘[i]mprove the regulation and monitoring of global financial markets and institutions and strengthen the implementation of such regulations.’

To help measure how well states are doing to protect financial consumers, the Global Alliance for Legal Aid (GALA) and Advocates for International Development (A4ID) are leading multi-country research on consumer debt policies in over 35 (mostly) developing countries. GALA and A4ID have benefited in this collaboration from the pro bono support of law firms and in-house counsel of multinational corporations around the world. The first report in the series that will be issued based on this research focuses on East Africa, where the research was conducted by lawyers from DLA Piper Africa’s offices in Burundi, Kenya, Tanzania, and Uganda.

The legal review undertaken by the research partners sets out to answer the following questions:

- What kinds of laws and policies and regulations are in place to protect financial consumers from predatory lending practices or abusive debt collection practices?
- Whether any financial dispute resolution mechanisms are in place to assist consumers with complaints about financial market conduct?

- Whether a financial regulator monitors levels of consumer or household over-indebtedness?
- What are the consequences of default for the debtor?
- Whether any debt relief mechanisms are available, such as bankruptcy, debt mediation or counseling ?

## Financial Consumer Landscape

Consumer credit has become a significant and growing portion of all lending in many countries, and an important contributor to GDPs. For example, approximately 34% of loans in Tanzania are personal loans, and 28% in Kenya are consumer and household loans. The surge in digital financial services, combined with a global policy push for increased *financial inclusion* has enabled unprecedented access to credit for financial consumers, including the most vulnerable and poor on the planet. Yet, financial consumer protection laws, laws regulating debt relief, and public education to increase debtor awareness have not kept pace. As a result, for those living in or close to poverty, access to short-term and high cost credit may land them in insurmountable debt-traps, or even in prison.

### DEBT IMPRISONMENT

Debtor incarceration is a violation of the *International Covenant on Civil and Political Rights* which, by Article 11, obliges signatory countries to ensure that '[n]o one shall be imprisoned merely on the ground of inability to fulfil a contractual obligation'.<sup>1</sup> Yet, our research found that three countries included in our survey—Kenya, Uganda, and Tanzania--still have laws providing for debtor incarceration on their books.<sup>2</sup> In addition, in these countries, a loan default could result in incarceration not only for the debtor, but also for their loan guarantor or both. In Kenya and Uganda, where data from the prison services was made available, our research found that hundreds of prisoners are serving sentences for debt defaults.

## Debt Entrapment and Financial Exclusion

Unregulated access to consumer lending can result in debt entrapment. For example, even though Kenya has a very high rate of financial inclusion (82% according to World Bank 2017

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<sup>1</sup> *International Covenant of Civil and Political Rights*, ratified on 16 December 1966 and entry into force on 23 March 1976. Available online at <https://www.ohchr.org/en/professionalinterest/pages/ccpr.aspx> Further research is also needed regarding how many of these countries' large populations of pre-trial detainees are awaiting trial for debt default—an important issue given that, although debt defaults typically carry a six-month term, justice system backlogs mean that pretrial detention could ultimately last for years. See, Sarkin, Jeremy, Prisons in Africa: A Human Rights Perspective, *International Journal of Human Rights*, Jan. 2008, available online at <https://sur.conectas.org/en/prisons-in-africa/>.

<sup>2</sup>

Findex data), 4 million Kenyans have effectively been 'black listed' on the credit registry<sup>3</sup>. Their negative credit listing results from having defaulted, often on loans valued at less than 10 USD. As a result they are barred from further access to credit, and may be at risk of losing a job, or not being retained for future employment. To have their names removed from these adverse credit listings, debtors in these circumstances must pay their debt in full, as well as late fees and an additional 20 USD for a clearance certificate, costs that are often out of reach for the poorest borrowers.

## HARASSMENT AND VIOLATIONS OF PRIVACY

Debt default in the countries reviewed can have other serious consequences for individuals who have revealed their personal information in the course of getting a loan. For instance, defaulting consumers in Kenya are frequently subjected to harassment via text messaging and calls to friends, relatives and employers through unauthorized use of their personal information.<sup>4</sup>

## Lack of Adequate Debt Relief

It is important that distressed debtors who cannot pay their loans have a way to start afresh so that they can restart their economic lives. However, whereas, insolvency or bankruptcy legislation exist in all four of the countries reviewed, with the exception of Kenya, the laws not provide for debt write-offs for a low income person with no assets and only debts.<sup>5</sup>

Further, bankruptcy proceedings are costly and complex, making them inaccessible to the vast majority of debtors. Extra judicial debt mediation or counseling services would make debt management and relief available to greater numbers of debtors, however none of the four countries reviewed have any such services available.

## Inadequate Financial Markets Monitoring

Monitoring of over-indebtedness among consumer borrower is particularly important function of public financial sector risk management, especially where (i) consumer lending is a large component of all lending, ii) consumer lending is marketed to vulnerable members of the population who do not have access to financial education, and iii) there is evidence of high

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<sup>4</sup> Unpublished Interviews with Over indebted Consumers in the Toi Market by GALA affiliate MicroJustice Kenya, May, 2021; whereby 68% of the consumers surveyed indicated they had received menacing calls/texts due to being late with a loan repayment. See also, BBC, *Kenya Outrage Over Debt Collectors' Shaming Tactics*, 5 August 2021 at <https://www.bbc.co.uk/news/world-africa-57985667>

<sup>5</sup> See the Republic of Tanzania, Bankruptcy Act Cap. 25 R.E.2019; The Uganda Insolvency Act , Section 20(1)of 2011; Kenya, Insolvency Act, 2015, and The Republic of Burundi, Bankruptcy Act, Law No. 1/05 of January 23, 2018.

rates of default and multiple lending in the market. However, none of the countries reviewed systematically monitors over indebtedness rates of consumers or households, though the Central Bank of Kenya does have a definition of over indebtedness.<sup>6</sup>

In addition, we could find no evidence that non-performing loan rates of the micro and digital lending sector; those financial services likely to be targeting the poor consumer are tracked or disaggregated from the general category of consumer/household lending by any public agencies in Uganda, Tanzania nor Burundi. In Kenya, where digital and microfinance lenders do report defaults to the credit registry, at peak there were recently as many as 4 million Kenyans with a negative credit listing.<sup>7</sup>

## Access to Redress Mechanisms

Given the ease of access to credit, and the strong incentives for lenders to engage in predatory practices, it is essential that countries establish efficient and fair financial complaints handling mechanisms, and then clearly promote and educate consumers on how to use them. Financial consumer protection (FCP) is a relatively new area of law and policy. The Organization for Economic Co-operation and Development, citing the importance of financial consumer protection to the financial stability of nations, published its *High Level Principles on Financial Consumer Protection in 2011*.<sup>8</sup> Many countries have yet to put in place the laws, policies and institutions to effectively protect their financial consumers from abusive . Our survey found that, only Tanzania and Burundi have financial consumer protection (FCP) regulations. Uganda

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<sup>6</sup> Clause **3.2.1 (e) of the Central Bank of Kenya Prudential Guideline on Consumer Protection (CBK/PG/22)** provides that a consumer is **over-indebted** if the available information at the time a determination is made indicates that the consumer is or will be unable to satisfy in a timely manner all the obligations under all the credit agreements to which the consumer is a party, having regard to that consumer's:

- i. financial means, prospects and obligations; and
- ii. probable propensity to satisfy in a timely manner all the obligations under all the credit agreements to which the consumer is a party, as indicated by the consumer's history of debt repayment and other relevant factors prevailing at the time of credit assessment.

The **CBK/PG/22** can be accessed on the CBK website under the link <https://www.centralbank.go.ke/wp-content/uploads/2016/08/PRUDENTIAL-GUIDELINES.pdf>.

<sup>7</sup> Mito, Washington, *CBK Orders Millions of Kenyans to Be Removed from CRB Blacklist*, Kenyans.Co.KE, 8 Nov. 2021. Available online at <https://www.kenyans.co.ke/news/70316-cbk-orders-millions-kenyans-be-removed-crb-blacklist>

<sup>8</sup> *High Level Principles of Financial Consumer Protection*, OECD, Nov, 2011. Available online at <https://www.oecd.org/daf/fin/financial-markets/48892010.pdf>

has FCP guidelines<sup>9</sup> which do not have the force of law, and the Central Bank of Kenya has some FCP provisions included in its prudential guidelines which are applicable only to licensed banks<sup>10</sup>. However, digital lending regulations are expected soon.

In the four countries reviewed in East Africa some progress has been made to make it possible for consumers to complain about financial providers' bad conduct, though in none was there a financial consumer protection regulator with a full suite of supervisory and enforcement powers. The Bank of Uganda, has a financial complaints handling mechanism in its *Financial Consumer Empowerment Mechanism (FCEM)*, In Tanzania and Burundi, where an aggrieved consumer can file a complaint with the central bank, after first complaining to the services provider. However, there is no data published by Tanzania, Burundi nor Kenya on the volume/type of financial complaints received by Central Banks (or other regulators). In 2020, the Bank of Uganda FCEM reported over 260,000 complaints it received against financial services providers.<sup>11</sup> Data on the volume and type of complaints can provide regulators with a keen insight to both market conduct as well as consumers' financial capacity; both of which are relevant for evidence based policy making.

This research reveals that despite the push for and relative success of countries to improve access to financial services for the poor, much more work needs to be done on the legal frameworks to ensure financial consumer protection, fair treatment and debt relief is available for them. Legal reform needs to address the very real probability of consumer over-indebtedness and default when credit is easily accessible to debtors who are ill-informed about the risks of credit and/or have no savings to draw from if they become ill, lose their job, or suffer other adverse financial reversal. Laws and policies must monitor and prevent over-lending, must prohibit and remedy abusive lending practices, and must eliminate debt imprisonment and offer distressed borrowers the means to escape debt traps.

Financial inclusion is an admirable goal if financial consumers are duly protected, including the most vulnerable, who are the most likely to fall into debt difficulty. As one microfinance employee handbook noted 'The poor live on the edge of disaster and frequently fall into it.' The law serves many purposes but, in this instance, it should be there to provide a safety net.

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<sup>9</sup> <https://bou.or.ug/bou/bouwebsite/bouwebsitecontent/FinancialInclusion/Financial-Consumer-Protection-Guidelines-2011.pdf>

<sup>10</sup> <https://www.centralbank.go.ke/wp-content/uploads/2016/08/PRUDENTIAL-GUIDELINES.pdf>

<sup>11</sup> Ssonko, George Wilson, *Central Banks, Consumer Protection and Covid 19 in Uganda*, Bank of Uganda Working Paper No. 1/2021, June, 2021. Available online at [https://www.bou.or.ug/bou/bouwebsite/bouwebsitecontent/research/BoUworkingPapers/research/BouWorkingPapers/2021/Central-Banks-Consumer-Protection-and-COVID-19-in-Uganda\\_WP-01-2021.pdf](https://www.bou.or.ug/bou/bouwebsite/bouwebsitecontent/research/BoUworkingPapers/research/BouWorkingPapers/2021/Central-Banks-Consumer-Protection-and-COVID-19-in-Uganda_WP-01-2021.pdf)

