

Mobile Money Transfer:

**A CRITIQUE OF THE ANTI-MONEY LAUNDERING LEGAL AND INSTITUTIONAL
FRAMEWORK IN KENYA**

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STUDENT NUMBER: G62/7525/2017

**A Thesis Submitted to the University of Nairobi in Partial Fulfillment of the Requirements
for the Award of the Degree of Master of Laws (LL.M)**

Word Count: 14677

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DECLARATION

I Maina Susan Nyambura hereby declare that this is my original work and has not been presented for the award of a degree or any other award in any other University. Where works by other people have been used, references have been provided.

Student: Maina Susan Nyambura

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Date:

APPROVAL

This thesis titled Mobile Money Transfer: A critique of the Anti-Money Laundering Legal and Institutional framework in Kenya has been done under my supervision and has been submitted to The University of Nairobi, School of Law for examination with my approval as the candidate's supervisor.

Signed: _____ Date: _____

Supervisor: **MS. EVELYN OWIYE ASAALA**

DEDICATION

This thesis is dedicated to the millions of mobile money transfer services users in Kenya. May we strive to enjoy the convenience these services offer with the expectation that their integrity will remain guarded by the law at all times.

ACKNOWLEDGMENT

I wish to appreciate assistance and contribution of those without whom, this thesis would not have materialized. First, I am grateful to God for life, hence the ability to undertake this study. Secondly, my husband Duncan and wonderful sons Jazz and Jozy, my parents, brothers and sisters, for your unwavering support and encouragement during this study. Thirdly, I acknowledge the contribution of my supervisor, Ms. Evelyn Asaala and Dr. Constance Gikonyo for your relentless guidance and insightful comments. Any shortcomings in this thesis are entirely mine.

LIST OF ABBREVIATIONS

AML	Anti-Money Laundering
AMLAB	Anti-Money Laundering Advisory Board
ARA	Assets Recovery Agency
ARN	Asset Recovery Network
BCBS	Basel Committee on Banking Supervision
BFID	Banking Fraud Investigation Department
CAK	Communication Authority of Kenya
CBK	Central Bank of Kenya
CDD	Customer Due Diligence
CMA	Capital Markets Authority
CTF	Counter Terrorist Financing
CTR	Cash Transactions Report
DCI	Directorate of Criminal Investigations
EACC	Ethics and Anti-Corruption Commission
ESAAMLG	Eastern and Southern Africa Anti-Money Laundering Group
FATF	Financial Assets Task Force
FinCEN	Financial Crimes Enforcement Network
FIU	Financial Intelligence Unit
FRC	Financial Reporting Centre
GFPN	Global Focal Point Network
IMF	International Monetary Fund
IVTS	Informal Value Transfer System
KRA	Kenya Revenue Authority

KYC	Know Your Customer
MER	Mutual Evaluation Report
MFS	Mobile Financial Services
ML	Money Laundering
MLA	Mutual Legal Assistance
MM	Mobile Money
MMT	Mobile Money Transfer
MNO	Mobile Network Operator
NIS	National Intelligence Service
NPSA	National Payment Systems Act
NPSR	National Payment Systems Regulations
NRB	National Registration Bureau
OECD	Organization for Economic Co-operation and Development
PEP	Politically Exposed Persons
POC	Proceeds of Crime
POCAMLA	Proceeds of Crime and Anti-Money Laundering Act
POCAMLR	Proceeds of Crime and Anti-Money Laundering Regulations
PSP	Payment Service Provider
P2P	Person to Person
RBA	Risk Based Approach
SAR	Suspicious Activity Reporting
SMS	Short Message Service
SIM	Subscriber Identity Module
STR	Suspicious Transactions Report
UNCITRAL	United Nations Commission on International Trade Law

LIST OF STATUTES

Anti-Corruption and Economic Crimes Act No. 3 of 2003, Laws of Kenya.

Banking Act Chapter 488 Laws of Kenya Laws of Kenya.

Central Bank of Kenya Act, Chapter 491 Laws of Kenya.

Constitution of Kenya, 2010.

Consumer Protection Act, 2012 Laws of Kenya.

National Payment System Act, Chapter 493E Laws of Kenya.

Narcotic Drugs and Psychotropic Substances (Control) Act.

Proceeds of Crime and Anti-Money Laundering Act No. 9 of 2009 Laws of Kenya.

Proceeds of Crime and Anti-Money Laundering (Amendment) Act 2017.

Registration of Persons Act, Chapter 107 Laws of Kenya.

LIST OF REGULATIONS

- Anti-Money Laundering Guidelines for the Provision of Mobile Payment Services, 2013
- Central Bank of Kenya, Prudential Guidelines Reference No. CBK/PG/08 on the Proceeds of Crime and Money Laundering (Prevention).
- Electronic Payment Guidelines, 2011.
- Money Remittance Regulations, 2013.
- Proceeds of Crime and Anti-Money Laundering Regulations, 2013.
- Retail Electronic Transfer Guidelines, 2011.

LIST OF INTERNATIONAL INSTRUMENTS/CONVENTIONS

Financial Action Task Force (FATF) Standards on Combating Money Laundering, Financing or Terrorism & Proliferation 1989 & 2012 – Inter-ministerial standards body.

Financial Action Task Force (FATF), Anti-Money Laundering and Counter-Terrorist Financing Measures, United States of America, Mutual Evaluation Report, December 2016.

Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 20 December 1988, 1582 *UNTS* 95.

Convention against Transnational Organized Crime 9 December 1999, 2225 *UNTS* 209.

Convention against Corruption, 31 October 2003, 2349 *UNTS* 41.

UNCITRAL electronic payment framework for mobile money.

1.0 CHAPTER ONE

1.1 INTRODUCTION AND BACKGROUND TO THE STUDY

Mobile phone penetration¹ is on the rise in Sub-Saharan Africa approximately 76% of the populace owning a mobile phone device.² Consequently, financial inclusion levels in Africa have increased enabling people without an account with any mobile provider or financial institution to access these financial services.³ In the Communication Authority of Kenya (CAK) Statistics Report for the year 2018/2019⁴, the number of mobile subscriptions⁵ stood at Kshs. 46.6 million and the mobile penetration level stood at 100.1% due to most customers having more than one SIM card.⁶ As at the end of the first quarter of the Year 2018/2019, the number of mobile money subscriptions stood at Kshs. 29.7 million.⁷ Impliedly, 64% of the population used mobile money transfer services in the country whose value stood at Kshs. 2.02 trillion.⁸

Mobile money services allow customers without bank accounts to make payments with the mobile phone. Subscribers can reserve real value on their phone and may use phone airtime as

¹ Mobile phone penetration is “the total number of active SIM Cards calculated as a percentage of the total population in the country” see <https://ca.go.ke/wp-content/uploads/2018/12/Sector-Statistics-Report-Q1-2018-2019.pdf> accessed 18 March 2019.

² Sarah Logan, ‘The Benefits of Mobile Money in Kenya’, (2017) <<https://www.usnews.com/news/best-countries/articles/2017-01-05/the-benefits-of-mobile-money-in-kenya>> accessed 15 May 2018.

³*Ibid.*

⁴ Communication Authority of Kenya First Quarter Sector Statistics Report for the Financial Year 2018/2019 available on <https://ca.go.ke/wp-content/uploads/2018/12/Sector-Statistics-Report-Q1-2018-2019.pdf> accessed 18 March 2019.

⁵ Mobile Subscription refers to “a registered SIM card that has generated revenue within the last 90 days” see <https://ca.go.ke/wp-content/uploads/2018/12/Sector-Statistics-Report-Q1-2018-2019.pdf>

⁶*Ibid* note 4.

⁷*Ibid.*

⁸*Ibid.*

tender for payment.⁹ Save as these services guarantee flexibility, they may fall short of efficient supervision and regulation altogether.¹⁰

In Kenya, mobile money services include M-Pesa, Airtel Money, T-Kash, Equitel Money, and Mobile Pay.¹¹ In 2007, Safaricom a telecom company which is a non-banking institution launched Africa's first mobile money service, M-Pesa. This is a short message service (SMS) based money transfer system which allows customers to load, transfer and withdraw funds with their mobile phones.¹² Today, M-Pesa records significant success and widespread adoption in Kenya with 96% of the households in the rural areas having an M-Pesa account.¹³

Operator/ Indicator	July-September 2018						
	Agents	Current Subscriptions	Volume of Transactions	Amount of Transactions (Kshs.)	Total of M-Commerce Transactions	Total of M-Commerce Transactions (Kshs.)	Person to Person Transfers (Kshs.)
M-Pesa	162, 800	24, 206,341	575,660,251	1,585,729,101,317	430,190,383	1,203,392,814,229	590,345,941,145
Airtel Money	27,267	3,434,843	4,628,370	1,153,142,919	3,042,680	2,220,280,505	1,213,897,584
Equitel Money	-	1,992,150	149,463,508	439,188,528,611	92,748,695	347,176,769,388	125,981,207,772
T-Kash	21,538	59,933	104,833	197,106,156	1,009,427	85,656,719	12,820,830
Mobile Pay	6,890	92,122	354,565	1,379,068,293	-	-	729,012,558
Total	218,495	29,785,389	730,211,527	2,027,646,947.296	526,991,185	1,552,875,520,841	718,282,879,889

⁹ FATF Report (2010), 'Money Laundering Using New Payment Methods' <<http://www.fatf-gafi.org/media/fatf/documents/reports/ML%20using%20New%20Payment%20Methods.pdf>> accessed 26 June 2018

¹⁰*Ibid.*

¹¹*Ibid* note 4.

¹²Mercy W. Buka and Michael W. Meredith, 'Safaricom and M-Pesa in Kenya: Financial Inclusion and Financial Integrity' Washington Journal of Law, Technology & Arts (2013) 8 Issue 3 Mobile Money Symposium on <http://digital.law.washington.edu/dspace-law/handle/1773.1/1204> pg. 378 accessed 5 April 2018.

¹³*Ibid.*

Source: Communication Authority of Kenya First Quarter Report for the year 2018/2019 available at <https://ca.go.ke/wp-content/uploads/2018/12/Sector-Statistics-Report-Q1-2018-2019.pdf>, accessed 18 March 2019.

This study is on mobile money as an unconventional transfer method only. The focus is M-Pesa due to its popularity in the country and the fact that it is a reflection of the developments in the country's mobile money transfer (MMT) sector.¹⁴

MMT services in Kenya are regulated by overlapping regulatory frameworks including those of banking, telecommunications, payment service supervisors, Anti-money Laundering (AML) and Counter Terrorism Financing (CTF) such as the National Payment Systems Act (NPSA)¹⁵ (Anti-Money laundering Guidelines for the Provision of Mobile Payment Services) 2013.¹⁶

Mobile phone devices world over are used by billions of people including criminals and terrorists.¹⁷ Thus, inherent financial integrity risks arise in the usage of MMT services which include money laundering (ML) and terrorism financing (TF).¹⁸ This could easily compromise the probity of the financial system. These integrity risks are due to rapidity of transactions, anonymity of persons conducting transactions, cybercrime, poor oversight and compliance mechanisms, weak detection of suspicious transactions and reporting mechanisms.¹⁹

Numerous typologies for money laundering have been employed by money launderers however this study is on mobile money services as an emerging tool for criminals who intend to evade detection.²⁰ Whereas, traditional money laundering methods such as gambling, currency exchanges, wire transfers, cash smugglers or *hawalas*, counterfeiting, creating shell companies,

¹⁴*Ibid* note 11.

¹⁵ No. 39 of 2011 Laws of Kenya.

¹⁶ <https://www.centralbank.go.ke/images/docs/NPS/Regulations%20and%20Guidelines/Guidelines%20-%20Mobile%20money%20AML%20Guidelines.pdf> accessed 29 February 2018.

¹⁷ World Bank Working Paper No. 146 2.

¹⁸ Jane K. Winn and Louis de Koker, 'Introduction to Mobile Money in Developing Countries: Financial Inclusion and Financial Integrity Conference Special Issue' Washington Journal of Law, Technology & Arts (2013) 8 Issue 3 Mobile Money Symposium on <http://digital.law.washington.edu/dspace-law/handle/1773.1/1195> pg. 156 accessed 18 March 2019.

¹⁹ Kersop M and Toit du SF, 'Anti-Money Laundering Regulations and the Effective Use of Mobile Money in South Africa' 18 (2015) 5.

²⁰ FATF (n 9) 36-46.

investing in gems and gold and real estate are still in use,²¹ the rise of MMT services has ridiculed detection of illegal transfer of money particularly integration of the money into the legitimate economy.²² More often than not, the money laundering method to use is dictated by the money markets, AML regime and the economy.²³

Kenya's predisposition to money laundering is on the rise as a result of the increased use and development of complex mobile payment systems. In March 2017, the United States Department of State reported that M-Pesa services in Kenya are impuissant to ML.²⁴

ML is illegal in Kenya pursuant to sections 3, 4 and 7 of the Proceeds of Crime and Anti-Money Laundering Act²⁵ (POCAML). It is utilizing the proceeds of crime (PoC) in any dealing that hides the actual source, location and movement of the property. PoC allows someone who has committed an illegality to evade prosecution and lessens the worth of the property procured either directly or indirectly as a result of the illegality.

ML is perpetrated in a cycle which includes "placement", "layering" and "integration".²⁶ Placement is introduction of PoC into the formal financial system.²⁷ Layering occurs when the PoC are 'layered' in a complex web of financial dealings to cover up the origin

²¹ <https://www.investopedia.com/ask/answers/022015/what-methods-are-used-launders-money.asp> accessed 18 March 2019.

²² Constance Gikonyo, (2018) 'Detection Mechanisms under Kenya's anti-money laundering regime: omissions and loopholes' Journal of Money Laundering Control, 21 p.59-70, <http://doi.org/10.1108/JMLC-06-2017-0023> accessed 10 March 2019.

²³ IMF, Anti-Money Laundering/Combating the Financing of Terrorism - Topics <<http://www.imf.org/external/np/leg/amlcft/eng/aml1.htm#moneylaundering>> accessed 24 May 2018.

²⁴ Logan (n 2).

²⁵ No. 9 of 2009 available on <http://kenyalaw.org/lex//actview.xql?actid=No.%209%20of%202009> accessed 9 April 2018.

²⁶ United States Department of the Treasury FinCEN, 'History of Anti Money Laundering Laws' <<https://www.fincen.gov/history-anti-money-laundering-laws>> accessed 4 April 2018.

²⁷ OECD, Money Laundering Awareness Handbook for Tax Examiners and Tax Auditors (2009) <http://www.oecd.org/tax/exchange-of-tax-information/43841099.pdf> accessed 4 April 2018.

and destination of the proceeds.²⁸ Lastly, integration is coalescing funds which are purportedly obtained legitimately into the economy.²⁹



A schematic illustration of stages on money laundering process

Source: United Nations Office on Drugs and Crime available on <https://www.unodc.org/unodc/en/money-laundering/laundrycycle.html> - accessed 14 June 2018.

The rationale for regulating money laundering is due to its potential to promote other crimes like corruption, terrorism and smuggling to name a few which can adversely upset the economy globally.³⁰

Kenya is a member of the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG). This is a regional Financial Assets Task Force (FATF) body that strives to deal with ML through implementation of its Recommendations.³¹ The principal Act on ML in the country is POCAMLA³² which provides for detection and recovery of PoC.³³ It establishes

²⁸*Ibid.*

²⁹*Ibid.*

³⁰Njaramba Gichuki, *Law of Financial Institutions in Kenya*, (2nd edn , Law Africa Publishing (K) Ltd 2013) 286.

³¹These are international standards on combating money laundering, financing of terrorism and proliferation. Adopted by the FATF plenary in February 2012 <<http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf>> accessed 10 May 2018.

³²*Ibid* note 24.

institutions such as the Financial Reporting Centre (FRC)³⁴, the Anti-Money Laundering Advisory Board (AMLAB)³⁵ and the Assets Recovery Agency (ARA)³⁶ which are tasked with among other things recognition, detection, suspension, capture and impounding PoC in Kenya.

In 2017, the Proceeds of Crime and Anti-Money Laundering (Amendment) Act,³⁷ was promulgated to come up with a robust mechanism to combating ML in Kenya. This requires Financial Institutions to establish detection measures and to report suspected ML activities. It adopts the FATF Recommendations and Conventions on AML such as United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances³⁸ (Vienna Convention), United Nations Convention against Transnational Organized Crime³⁹ (Palermo Convention), United Nations Convention on the Suppression of Funding of Terrorism⁴⁰ and the United Nations Convention against Corruption (Merida Convention).⁴¹

Nonetheless, current AML laws strive to expose illegal money as it flows through conventional banks and are unable to detect money laundering in new payment methods such as mobile money. Consequently, money launderers continue to devise ways and means to conceal their approach and stay ahead of the watchful eye of the government, law enforcement agencies and the international community.

³³ Proceeds of Crime defined under Section 2 of POCAMLA to mean “any property or economic advantage derived or realized, directly or indirectly, as a result of or in connection with an offence irrespective of the identity of the offender and includes, on a proportional basis, property into which any property derived or realized directly from the offence was later successively converted, transformed or intermingled, as well as income, capital or other economic gains or benefits derived or realized from such property from the time the offence was committed”

³⁴ POCAMLA s 2.

³⁵ POCAMLA s 49.

³⁶ POCAMLA s 20 and 53.

³⁷ http://kenyalaw.org/kl/fileadmin/pdfdownloads/AmendmentActs/2017/ProceedsofCrimeandAnti-MoneyLaundering_Amendment_Act_2017.pdf accessed 9 April 2018.

³⁸ United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 28 ILM 493; 1582 UNTS 95 (Vienna Convention);

³⁹ United Nations Convention against Transnational Organized Crime (Palermo Convention) November 15, 2001, 2225 UNTS 209.

⁴⁰ United Nations Convention on the Suppression of Funding of Terrorism December 9, 1999 2178 UNTS 197.

⁴¹ United Nations Convention against Corruption (Merida Convention) December 9, 2003 43 ILM 37 (2004).

Therefore, there is need to continuously revise our regulations and policies to keep up with technology and to enhance detection of the vice especially through the MMT service. Appropriate regulatory balance is necessary for the growth of MMT services whilst enhancing financial integrity.

In as much as ML and TF go together,⁴² this study is on ML only. Additionally, MMT regulation in Kenya is on AML measures alongside FATF Recommendations. Also, it will not focus in great detail on the international conventions as they do not bear specific provisions for AML for mobile money services. This study will examine the adequacy or otherwise of the AML regime on mobile money in the country.

1.2 STATEMENT OF THE PROBLEM

ML and TF is eminent in Kenya alongside neighboring Somalia due to the fact that it is a main financial center in East Africa.⁴³ Additionally, the country grapples with illegal and informal financial sectors that government struggles to regulate.⁴⁴ Recently, Kenya was listed by FATF⁴⁵ as one of the “jurisdictions that have not made sufficient progress in addressing sufficient AML/Counter Terrorist Financing (CTF) deficiencies”. This indicates how susceptible the country is regarded to ML by the international community. Further, the fact that Kenya is a cash based economy poses a challenge to the regulation of money laundering in MMT services because of the difficulty in monitoring suspicious transactions and this will be examined in greater detail subsequently.

⁴² As is evident from the FATF Recommendations and various academic works on threats to financial integrity.

⁴³ISSP-CGCC Joint Report, ‘Baseline Study on Anti-Money Laundering and Countering the Financing Terrorism in the IGAD Sub-Region’ pgs 21 & 22 available on http://www.globalct.org/wpcontent/uploads/2012/11/AML_Report.pdf accessed 15 May 2018.

⁴⁴*Ibid.*

⁴⁵FATF (2016) Anti-money laundering and counter-terrorist financing measures – United States, Fourth Round Mutual Evaluation Report, FATF, Paris, available on www.fatf.gafi.org/publications/mutualevaluations/documents/mer-united-states-2016.html accessed 31 March 2018.

The Central Bank of Kenya (CBK) has guidelines to address ML in MMT services in the country which are supplemented by the principal legislation on AML being the POCAMLA. However, the existing legal/regulatory and institutional framework does not adequately address emerging financial integrity risks in the use of MMT services that facilitate money laundering for example loopholes in detection of AML transactions, lack of Customer Due Diligence (CDD) measures that promote sufficient customer identification and verification, smurfing, lack of interoperability of mobile network agents, poor oversight and compliance mechanisms.

Further, MMT services in Kenya are currently regulated by the same AML controls as Banks in Kenya; thus the regulatory framework is inadequate to combat the financial integrity risks and is not sufficiently compliant with the revised FATF recommendations that provide for best practices in detecting and combating the money laundering in MMT services.

1.3 JUSTIFICATION OF THE STUDY

Undoubtedly, there is limited regulatory and legislative experience from other jurisdictions to derive relevant lessons and experiences from when formulating legislation and guidelines on mobile money regulation. Further, there is limited research on money laundering and mobile money. This study is significant for the following reasons:-

First, it is important to the Government of Kenya as it will inform Parliament and policy makers like the CBK on areas to amend existing legal and institutional framework and policy formulation to secure the outlined gaps and omissions in the MMT services AML regulatory landscape. This will align Kenya's AML regime on mobile money services with the revised FATF recommendations that provide for best practices to enhance its capacity to manage potential money laundering risks.

Secondly, the study provides the general public with information pertaining to the benefits of MMT on economic development and likely financial integrity risks posed by usage of the services.

Thirdly, scholars and academicians will benefit from the study as it provides data on MMT and its susceptibility to money laundering. Thus prompts the need for further research.

Lastly, this study further provides valuable lessons to other jurisdictions seeking to promulgate legislation on mobile money regulation that is risk based but also proportionate to enhancing financial inclusion and innovation in the sector.

1.4 STATEMENT OF OBJECTIVE

1.4.1 General Objective

To study the anti-money laundering mechanism for MMT services in Kenya and suggest reforms in the regulatory framework.

1.4.2 Specific Objectives

- (a) To discuss the ML typologies for MMT services.
- (b) To examine the institutional and legal landscape for ML and mobile money in Kenya.
- (c) To study the loopholes and omissions in the existing institutional and legal landscape for combating ML for MMT services.

1.5 RESEARCH QUESTIONS

- (a) What are the ML typologies and risks for MMT services and how can these be mitigated effectively?
- (b) What is the legal and institutional landscape for ML and mobile money in Kenya?
- (c) Is the existing legislative and regulatory framework for AML for MMT services in Kenya adequate?
- (d) Is there an optimal regulatory mechanism for mobile money services that secures financial integrity and promotes financial inclusion?

1.6 THEORETICAL FRAMEWORK

Money laundering is a crime under the law; therefore, the theoretical structures on crimes will apply to a large extent. The following theoretical frameworks which provide rationale for regulation apply to this study.

1.6.1 Market Integrity Theory

It was propounded by Bryan Fodor⁴⁶ and provides that financial markets must be grounded in integrity.⁴⁷ Market integrity is mainly grounded on measures such as law enforcement efficiency and prevention of financial crime, low crime levels and confidence among market actors.⁴⁸ Therefore to combat ML, the law safeguards financial markets, the consumers and providers alike.

1.6.2 Theory of Economic Regulation

It was propounded by George Stigler and is defined as the imposition of rules by a government, backed by penalties intended to change the behavior and actions of individual players in the private sector.⁴⁹ This theory proposes that the central aim of regulation is to safeguard the people; to address interest group and government opportunism.

It emerges from two main theories that is the public interest and the private interest. The former supposes regulators have enough enforcement capacity to promote public interest and that regulators will pursue public interest at all times.⁵⁰

The private or capture interest theory presupposes that individuals form groups to protect their interests in regulation by lobbying.

⁴⁶ Bryan Fodor, 'Measuring market integrity: a proposed Canadian approach', (2008) 3 (15) *Journal of Financial Crime*, pp. 261-268.

⁴⁷*Ibid.*

⁴⁸*Ibid.*

⁴⁹Angela LA, 'Financial Services Regulation in Kenya: A Critical Analysis of the proposed Unified Financial Services Regulator' (LL.M thesis University of Nairobi, 2014).

⁵⁰*Ibid.*

To this end the public interest theory of regulation informs rationale of regulation by the government in developing mobile money ecosystems. This can be attained by developing policy frameworks that will enhance continuous growth, security and stability in the sector.

1.7 RESEARCH METHODOLOGY

The study is largely desktop which includes review of primary sources and secondary research. The primary sources of information will include the Proceeds of Crime and Anti-Money Laundering Act (POCAMLA) No. 9 of 2009, the National Payment System Act (NPSA) (Anti-Money Laundering Guidelines for the Provision of Mobile Payment Services 2013) and international standards such as the revised 2012 FATF recommendations⁵¹ which provide the best practices for governing money laundering and mobile money services.

This study will make anecdotal references to other jurisdictions that have implemented regulatory frameworks to govern MMT services and the manner in which they are combating ML risks in the services. The findings of this study will be disseminated through publication.

1.8 LITERATURE REVIEW

Notably, the available literature on money laundering and its regulation in Kenya is focused mainly on traditional methods of money laundering. There is limited literature on regulation of money laundering for emerging technologies such as MMT services. This section highlights and analyzes relevant material and writings by various scholars. The discussion that ensues identifies gaps emerging from the available literature, which this study seeks to fill.

The literature review adopts a thematic approach by examining the various emerging issues that arise as a result of using MMT services in relation to ML. The said problems include integrity and fraud risks, privacy concerns, money laundering typologies in MMT, regulatory challenges,

⁵¹*Ibid* note 30.

financial inclusion concerns and the mitigation mechanisms for dealing with ML in MMT and will be reviewed below in the context of available literature.

1.8.1 Integrity and Fraud risks

Mercy W. Buka and Michael W. Meredith⁵² focus primarily on M-Pesa due to its popularity and success in the country and note its laudable contribution in deepening financial inclusion. They examine integrity risks for the MMT service with respect to AML and CTF regulations in Kenya. They analyze how AML regulations in Kenya have transformed in their implementation to MMT services in the country.

They note need for development of regulations to safeguard MMT service from money launderers and terrorists. Also, they provide an overview of internal AML policies that have been developed by Safaricom to address money laundering risks. Nonetheless, the authors fail to establish the various detection and reporting mechanisms for AML that Safaricom has adopted. Also, they do not comment on the adequacy of the current legal and institutional landscape for AML in combating MMT fraud, which this study will endeavor to tackle.

1.8.2 Regulation concerns

Simone di Castri⁵³ discusses some key policies and regulations governing the mobile industry which according to him do not provide a platform for the industry to succeed, especially ability of MMT services to reach the unbanked population. He recommends enabling regulatory solutions that will promote the mobile industry to reach its full potential at the same time promote financial integrity in the financial services sector.

According to him, cash based transactions are more susceptible to money laundering than mobile money based transactions because the latter transactions can be monitored with ease. This study

⁵² Buka and Meredith (n 12).

⁵³ Di Castri, Simone, Mobile Money: Enabling regulatory solutions (2013) on SSRN: <http://ssrn.com/abstract=2302726> or <http://dx.doi.org/10.2139/ssrn.2302726> accessed 21 April, 2018.

however argues that in as much as MMT transactions are easy to monitor they are still susceptible to money laundering owing to the rapidity of transactions, anonymity risks and omissions in the detection mechanisms currently in place.

The challenge for mobile service providers and regulators he notes, is striking the balance between promoting financial inclusion and ensuring financial integrity. Further, he argues that tailor made Know Your Customer (KYC) and Customer Due Diligence (CDD) Procedures will provide a proportionate risk approach to mitigating risks of ML whilst promoting financial inclusion efforts.

The findings of the author are important in this study as they will inform some of the reforms that ought to be adopted in the sector to enable the industry to thrive without upsetting the integrity of the services. Nonetheless, the author fails to analyze the various money laundering methods that money launderers can use through MMT services which this study will examine.

Jonathan Greenacre⁵⁴ reckons that owing to limited research on mobile money, emerging markets are yet to develop a regulatory framework to regulate the service and tend to use bank regulation which he notes is ineffective. He recommends a functional approach to regulate mobile money as it would entail noting the specific risks created in each component part of the payments process, regardless of the institution providing that part.

⁵⁴Jonathan Greenacre, 'The Rise of Mobile Money: Regulatory Issues for Australia' The Finsia Journal of Applied Finance, (2013) Issue 1 on https://www.finsia.com/docs/default-source/jassa-new/jassa-2013/jassa-2013-issue-1/the-rise-of-mobile-money-regulatory-issues-for-australia.pdf?sfvrsn=e45edd93_5 accessed 15 May 2018.

The findings of the author are important in this study as they will inform the reforms that ought to be adopted in the regulatory framework governing the services which adopt a functional approach as opposed to an overly risk based approach currently in place.

Miriam Goldby⁵⁵ argues that wholesale adoption of Suspicious Activity Reporting (SAR) regime in developing countries as proposed by FATF will impact negatively on financial inclusion by reducing affordability, attractiveness and accessibility to mobile money services. She recommends that FATF should allow developing nations to tailor their SAR regime especially for mobile money service. Nonetheless, the author does not examine the effectiveness or otherwise of SAR regimes in developing countries which gap this study will fill by analyzing the SAR regimes adopted for MMT services in Kenya.

Ross Buckley *et al*⁵⁶ note that mobile money regulatory frameworks should either adopt enabling or proportionate approach. The former provides a platform for growth of mobile money whereas the latter guards against too much regulation that may stifle innovation. They examine the disadvantage of applying proportional control for AML.

These findings enrich our understanding drawing from the Malawian experience on designing regulatory frameworks for mobile money that promote financial inclusion at the same promote financial integrity in the service. This study however will analyze the mobile money regulatory framework in relation to AML using Kenya as a case study and not Malawi.

1.8.3 Security and Privacy Concerns

⁵⁵Miriam Goldby, 'Reporting of suspicious activity by mobile money service providers in accordance with International Standards, how does it impact on Financial Inclusion?' (2013) 8 (3) Washington Journal of Law, Technology & Arts <http://digital.law.washington.edu/dspace-law/handle/1773.1/1205> accessed 14 September 2018.

⁵⁶Ross Buckley, Jonathan Greenacre and Louise Malady, "Regulation of Mobile Money in Malawi" (2015) 14 (3) Washington University Global Studies Law Review http://openscholarship.wustl.edu/law_globalstudies/vol14/iss3/7 accessed 14 September 2018.

Andrew Harris *et al*⁵⁷ examine the risks connected to MMT usage in Africa. They note that the requirement by FATF on clarity by consumer and data collection raise concern on privacy and security of consumers. They assert that users are vulnerable to abuse especially in jurisdictions with limited privacy protections and weak adherence to the rule of law.

They argue that if mobile money platforms have privacy violations and people are likely to distrust the service hence fail to achieve any gains. They recommend we addresses the deficiencies so as to develop a framework that does not infringe on the privacy and security of users but promote financial inclusion by encouraging mobile money usage with integrity.

The authors' findings will provide a benchmark for addressing security and privacy concerns in the regulatory framework governing MMT services in the country.

1.8.4 Money Laundering Typologies and New Payment Methods

Miguel Abel Souto⁵⁸ examines emerging technologies, FATF Standards, Typologies and Spanish penal reform on ML. He notes that the internet, electronic transfers, mobile money services and prepaid card provide potential for money laundering activities. He reckons that money launderers find these new technologies of new payment methods appealing because they pose a challenge in detection of any suspicious activity due to the hardship in tracing movement of funds. This assertion by the author informs the rationale for this study that MMT services are vulnerable to money laundering due to detection challenges.

In his opinion, these new payment methods enable movement of large sums of money, anonymity in the transactions promote the use of false identities and the lack of credit risk curtail service providers from gathering complete and accurate date on a customer. Finally, rapidity of

⁵⁷Andrew Harris, Seymour Goodman and Patrick Traynor, "Privacy and Security concerns associated with Mobile Money applications in Africa" (2013) 8 (3) Washington Journal of Law, Technology & Arts <http://digital.law.washington.edu/dspace-law/handle/1773.1/1198> accessed 14 September 2018.

⁵⁸Miguel A. Souto, "Money laundering, new technologies, FATF and Spanish penal reform" (2013) 16 (3) Journal of Money Laundering Control <https://doi.org/10.1108/JMLC-01-2013-0002> accessed 14 September 2018.

transactions makes it difficult to freeze or control property. Also, that anonymity in the transactions pose a challenge for prosecution of money launderers and recommends development of new payment methods that strike a balance between security and fundamental rights.

He recommends that future AML measures should consider likely dangers that came up as a result of emerging technologies. Additionally, that investigating the true identity of a customer as required by FAFT is evaded through the use of third parties. Ultimately, he finds that emerging technologies are full of dangers that are likely to hinder prevention of ML.

Save as the author identifies the risks posed by usage of new payment methods he does not recommend proposals for managing the said risks and fails to propose a regulatory model that will regulate these new payment methods to combat money laundering activities.

This study examines the identified risks in detail and endeavors to propose recommendations in the context of the AML mechanism in Kenya.

1.9 DELIMITATIONS

Owing to the resources and time constraints, this study will mainly focus on AML regime and its impact on MMT in Kenya. Therefore, this research will make reference to Safaricom's M-Pesa MMT service due to its popularity in the country hence it provides a reflection of what is happening in the mobile MMT sector.⁵⁹ The writer made effort to set up interviews with Safaricom and the Directorate of Criminal Investigations (DCI) officials in charge of the AML unit however due to their unavailability it was not possible to interview them.

1.10 HYPOTHESIS

⁵⁹*Ibid* note 4.

It is hypothesized that, the POCAMLA⁶⁰ and the CBK Prudential Guidelines on Anti-Money Laundering for mobile payment services are inadequate to combat ML for MMT services in Kenya. There is need therefore to reform the existing legal and institutional framework on money laundering for mobile money services in Kenya to enhance compliance and enforcement for economic development.

1.11 CHAPTER BREAKDOWN

Chapter one gives a background and introduction to the area of study. It outlines the statement to the research problem; justification of the research problem; theoretical framework on which the research is founded; literature review; research objectives; research questions; research hypothesis; research methodology; limitations to the study and chapter breakdown.

Chapter two conceptualizes mobile money and financial integrity dangers facing mobile money. It also examines the vulnerability of mobile money to ML particularly the inherent vulnerabilities identified by the World Bank. Also, examines the different mechanisms that criminals use to deal with PoC through MMT services.

Chapter three provides an analysis of the adequacy of Kenya's AML framework from a national legal, regulatory and international context including the FATF Standards and Global Conventions. It will also point out the various mitigation mechanisms that Kenya has adopted to deal with the inherent vulnerabilities that make mobile money vulnerable to ML.

Chapter four examines the institutional bodies that govern AML in Kenya with reference to mobile money. The institutional bodies are divided into national, regional and international agencies that combat AML and their effectiveness or otherwise in combating ML in MMT services.

⁶⁰*Ibid* note 24.

Chapter five summarizes the findings on adequacy of the legal, regulatory and institutional landscape for AML in mobile money in Kenya. Recommendations and policy guidelines are made on the existing regulatory and institutional landscape to ensure MM is regulated effectively.

2.0 CHAPTER TWO

EXAMINING POTENTIAL MONEY LAUNDERING RISKS IN MOBILE MONEY

2.1 INTRODUCTION

Kenya has experienced increased financial inclusion levels due to growth of MM. It has transformed the financial landscape in the country owing to its affordability and convenience. Nonetheless, mobile money faces potential security and integrity risks by virtue of its inherent vulnerabilities which if not mitigated could expose the system to a systemic risk.

The security challenges that mobile money face includes fraud, cybercrime threats, breach of privacy and consumer protection issues.⁶¹ However, the author will examine the potential financial integrity risks that face MM usage and not the aforementioned security risks. This is because the security risks are transaction based and they have not been documented to manifest vulnerability of MMT services to ML unlike the financial integrity dangers which is the focus of this study.

Financial integrity risks that mobile money pose include criminals utilizing the platform to facilitate ML and financing terrorism activities. Accordingly, four major inherent vulnerabilities in mobile money known as anonymity, elusiveness, rapidity and poor oversight have been identified by the World Bank as the reason why mobile money services are vulnerable to ML.⁶²

This chapter is divided into four sections in order to enhance an understanding of how mobile money works and how criminals can manipulate the platform to deal with proceeds of crime.

Section one conceptualizes MM by defining it in general, under the relevant Kenyan law and regulations thereon. Further, it distinguishes the MM from mobile banking which is more often than not misunderstood. It narrows the focus of the study to person to person transfers (P2P)⁶³ due to their likelihood to pose financial integrity risks. Moreover, it highlights the various AML

⁶¹*Ibid* note 9.

⁶²Chatain Pierre-Laurent *et al* (2011), 'Protecting mobile money from financial crimes; global policy challenges and solutions,' World Bank Working Paper 146. Pg. 47 available at <https://openknowledge.worldbank.org/handle/10986/2269> accessed 10 April 2019.

⁶³ P2P also known as domestic money transfer refers to the ability of users in a mobile money system to send money to one another.

measures that have been put in place to guard mobile money from being abused to launder proceeds of crime and the loopholes therewith. Lastly, it provides a brief overview of mobile payment service providers who are tasked with issuing mobile money services and how they are regulated under the law.

Section two provides a conceptual framework of the financial integrity risks that engulf mobile money. The author will rely on the Guidance Note for conducting ML and TF risk assessment developed by the CBK in defining what constitutes a threat, risk and vulnerability. This is informed by the risk factors noted in the World Bank study which was established by the authors that MM has a low risk and limited threat to misuse by criminals.

Section three examines the vulnerability of MM to ML. Here, the author compares the vulnerability of cash transactions and those of mobile money to ML. This is because in many markets cash remains the main type of transaction and are reported to be more susceptible to opportunistic crime. Further, the inherent vulnerabilities in mobile money as noted in the World Bank study being anonymity, elusiveness, rapidity and poor oversight will be examined in detail.

Section four enumerates the various criminal methods used to deal with PoC through mobile money also known as typologies. The typologies are two fold that is those that schemes that criminals use to deal with PoC by manipulating the money laundering cycle using the mobile money platform and the typologies as employed by the various participants or stakeholders in mobile money usage.

2.2 CONCEPTUALIZING MOBILE MONEY

Mobile money in Kenya is a form of e-money.⁶⁴ The National Payments System regulations provide a definition of e-money.⁶⁵ This definition of mobile money comprises either “mobile transfers” or “mobile payments” value that is either transferred from or accumulates in an account that is accessed mainly through a mobile device. The transfer is either domestic or cross border.⁶⁶ Notably, MM is different from mobile banking. The latter allows people access to their bank accounts through a mobile device. MM offers customers great security and benefit than conventional cash and informal funds transfer methods. Customers can access services such as Person to Person Transfers⁶⁷, secure storage of funds, merchant payments like “Lipa Na M-pesa”, payments for utility organizations like Kenya Power, bulk disbursements such as government or private sector payment, airtime top-up and international money transfer services. The focus of this study is P2P transfers because they have been documented to pose integrity risks.⁶⁸

Safaricom recently launched M-Pesa Global which is a Global funds transfer platform that enables people to transfer and receive funds world over.⁶⁹ The platform is acclaimed for boosting international e-commerce and enhancing convenience amongst users. However, it is unregulated under the law and it is presumed that the regulations governing domestic mobile money transfers will be employed to some extent.

To guard against money laundering, all Partners are required to register with their respective regulatory authorities and to undertake due diligence measures on the remitters in line with the respective countries laws and regulations.⁷⁰ Therein lies the challenge of conflict of laws

⁶⁴<https://www.safaricom.co.ke/faqs/faq/278> accessed 13 May 2019.

⁶⁵National Payment Systems Regulations, 2014 s 2.

⁶⁶*Ibid.*

⁶⁷ *Ibid* note 60.

⁶⁸Laurent (n 59).

⁶⁹ <https://www.safaricom.co.ke/faqs/faq/278>[safaricom.co.ke/personal/m-pesa/do-more-with-m-pesa/m-pesa-global](https://www.safaricom.co.ke/personal/m-pesa/do-more-with-m-pesa/m-pesa-global) accessed 13 May 2019.

⁷⁰<https://www.safaricom.co.ke/faqs/faq/278> accessed 13 May 2019.

whereby some countries may have relaxed or no AML laws and may not be in line with FATF standards.

Furthermore, the transactions are monitored to detect any suspicious activity. This may however fail to happen if appropriate detection mechanisms are not in place in either of the partner countries where the transaction is taking place.

MMT services in Kenya are issued by a “mobile payment service provider” defined under the Kenya Information and Communications Act (KICA)⁷¹ and authorized by the CBK to offer MMT services.⁷² The definition of PSPs under NPS Act⁷³ includes agents as PSPs providers thus mandating them to adhere to AML measures established by their principals.

The payment service providers (PSP) are regulated under the NPS Regulations⁷⁴ and the CBK has oversight authority to protect the mobile money platform from criminal abuse such as ML.⁷⁵ With regards to curbing money laundering in mobile money, PSPs should describe their systems for internal control mechanisms established in compliance with POCAMLA⁷⁶ and the relevant Regulations in order to be authorized to carry out business.⁷⁷

Notably, mobile money payment service providers in the country are not categorized as banks. Consequently, they are exempt from prudential regulations and guidelines that regulate banks and guard against systemic risk in the financial system.⁷⁸ This is likely to compromise the integrity of the services by manifesting their susceptibility to ML and TF.

⁷¹ Act No. 2 of 1998, Laws of Kenya available on <http://www.kenyalaw.org/lex/actview.xql?actid=No.%202%20of%201998> accessed on 13 May 2019.

⁷²*Ibid* note 60.

⁷³ Act No. 39 of 2011.

⁷⁴ Part II, 2014.

⁷⁵<https://www.centralbank.go.ke/national-payments-system/> accessed 13 May 2019.

⁷⁶POCAMLA s 47.

⁷⁷NPSR reg (2) g (ii).

⁷⁸https://www.centralbank.go.ke/images/docs/legislation/prudential_guidelines_2006.pdf accessed 13 May 2019.

Recently, the CBK mandated banks to report transactions over Kshs. 1,000,000/- due to the rise in predicate offences in the country such as corruption, drug trafficking among others which have led to increased ML.⁷⁹

These regulations cannot be said to regulate mobile money because one is able to deal with a lot of funds using different SIM cards and at different mobile money agents without notice. This was the case in the recent Dusit terror attack that happened in Nairobi whereby documents presented in court by the Anti-Terrorism police (ATP) unit in a prosecution of suspects linked to the attack indicates one of the suspects dealt with at least Kshs. 100,000,000/- through MM a few months prior.⁸⁰

These points to poor regulatory framework on MM regulation in Kenya occasioning loopholes in the detection mechanisms meant to detect suspicious transactions.

2.3 CONCEPTUALIZING THE FINANCIAL INTEGRITY RISKS IN MOBILE MONEY

Save as MM has advantages such as reducing financial exclusion, concerns have been raised about the soundness of MMT services.⁸¹ In a World Bank study, Pierre Chatain *et al*⁸² assesses the dangers of MM by establishing exposure of the services and the threat of abuse by criminals. In their view “vulnerability + threat=risk”.⁸³

In March 2018, the CBK developed a Guidance Note for conducting ML and TF risk assessment⁸⁴ in line with its Prudential Guidelines⁸⁵, Regulation 6 of the Proceeds of Crime and

⁷⁹ <https://www.businessdailyafrica.com/analysis/ideas/Why-CBK-has-powers-fight-money-laundering/4259414-5072810-11p012r/index.html> accessed 23 May 2019.

⁸⁰ http://www.xinhuanet.com/english/2019-01/30/c_137787614.htm accessed 23 May 2019.

⁸¹ Laurent (n 59) 33.

⁸² *Ibid.*

⁸³ *Ibid.*

⁸⁴ <https://www.centralbank.go.ke/wp-content/uploads/2018/03/Guidance-note-on-ML-TF-risk-assessment.pdf> accessed 14 May 2019.

Anti Money Laundering Regulations (POCAMLRL)⁸⁶ and Recommendations by FATF. The following set of definitions is provided to define what constitutes risk, threat and vulnerability; -

- **“Threat**-it could be a person or group, object that could cause harm. In ML context threat could be criminals or facilitators...;
- **Vulnerabilities**- elements of a business that could be exploited by the identified threat. In ML context vulnerabilities could be weak controls within a reporting entity offering high risk products or services;
- **Risk**-a likelihood of an event and its consequences. In ML context, risk means:

At the national level: threats and vulnerabilities presented by ML that put at risk the integrity of Kenya’s financial system

At the reporting entity level: threats and vulnerabilities that put the reporting entity at risk of being used to facilitate ML.”

The authors of the World Bank establish that MM has low risk and threat to misuse by prospective criminals.⁸⁷This is due to the ability to track and monitor transactions which curb against malefaction and buttresses integrity in the financial system.⁸⁸ This is in comparison to other unconventional value money transfer systems (IVTS) like *hawala* system which sidestep the regulated and traceable channels thus increasing the risk of ML or TF.⁸⁹

2.4 EXAMINING VULNERABILITY OF MOBILE MONEY TO MONEYLAUNDERING

⁸⁵ CBK Prudential Guidelines on Anti-Money Laundering and Combating the Financing of Terrorism (CBK/PG/08) clause 5.5 available on <https://www.centralbank.go.ke/wp-content/uploads/2016/08/PRUDENTIAL-GUIDELINES.pdf> accessed 14 May 2019.

⁸⁶Legal Notice no. 59 of 2013 available on <http://kenyalaw.org/kl/index.php?id=803> accessed 14 May 2019.

⁸⁷Laurent (n 59).

⁸⁸*Ibid.*

⁸⁹ Gikonyo (n 21) 59-70.

Criminals can penetrate any finance system all over the world.⁹⁰ There seems to be no exact and acceptable method to examine the vulnerability of any financial system to ML.⁹¹ Nonetheless, the World Bank conducted a study in which it highlighted four vulnerabilities in mobile money which make it susceptible to ML and these are considered in turn below.

2.4.1 Anonymity

It entails not knowing the real identity of a customer due to a criminal using an MM account in existing by means of theft of a mobile device.⁹²

The vulnerabilities posed by this risk factor include opening or operating different MM accounts by criminals to hide the actual amount of deposits⁹³ and identity fraud in the absence of or weak identification and verification processes.⁹⁴ This could be facilitated by lack of reliable national identification documents and SIM Card registration using forged identity documents which remain a challenge in Kenya. Identity fraud facilitates the withdrawal of proceeds of crime by criminals who are keen to exploit the loophole.

Therefore, this risk factor is said to pose a limited risk to ML compared to cash transactions which are largely anonymous and lack a unique identifier for the user.⁹⁵

2.4.2 Speed

MMT services are fast thus allowing transfer of funds among different accounts to hide the source of funds.⁹⁶ Cash transactions on the other hand move relatively slow making it difficult for

⁹⁰ <https://pdfs.semanticscholar.org/7fa1/4907c2e67442979a31bef1bd061e805f0c4b.pdf> accessed 27 September 2019.

⁹¹ *Ibid.*

⁹² World Bank (n 16) 71.

⁹³ Marina Solin and Andrew Zerzan, 'Mobile Money: Methodology for Assessing Money Laundering Risks and Terrorist Financing Risks' GSMA discussion paper p.14 available at <https://www.gsma.com/mobilefordevelopment/wp-content/uploads/2012/03/amlfinal35.pdf> accessed 27 October 2018.

⁹⁴ *Ibid.*

⁹⁵ *Ibid.*

transaction layering as in the case of MMT services. Save as the transactions are traceable in the system, criminals are still able to manipulate the platform and launder money or finance terrorism activities. Mobile money agents for instance have been said to facilitate SIM card registrations and bulk withdrawal and deposit of funds beyond the approved limits due to failure to comply with know your customer (KYC) requirements like requesting for the profile of the customer.

This is by far the highest degree of vulnerability to ML. Further, the fact that criminals can engage in suspicious transactions in mobile money points to loopholes in the detection mechanisms.

2.4.3 Elusiveness

It refers to the ability to disguise the origin, destination and value of a mobile money transaction.⁹⁷ Money launderers or criminals are able to engage in smurfing which entails using minimal dealings to hide huge amounts of money under transfer.

Recently, Safaricom called upon the CBK to increase the maximum daily transaction amount because of the rising adoption of e-commerce in the country.⁹⁸ However, the CBK is said to be reluctant to review the limit due to fears that the platform may be used for ML and finance terrorist activities in the country.⁹⁹

In Kenya, there is no limitation on the number of accounts that an individual can hold which is a challenge to monitoring and detecting source of illicit funds.

2.4.4. Poor Oversight

⁹⁶*Ibid.*

⁹⁷*Ibid*; World Bank Working Paper No. 146 xiv.

⁹⁸ <https://www.businessdailyafrica.com/corporate/companies/Safaricom-wants-Sh140-000-daily-M-Pesa-limit-increased/4003102-4840694-mm2h2hpz/index.html> accessed 15 May 2019.

⁹⁹*Ibid.*

This is not an inherent risk as compared to the risks discussed above however it can aggravate existing inherent risks.¹⁰⁰ The lack of co-ordination among authorities, exclusion of MMT services from AML requirements applicable to traditional financial institutions such as banks and absence of fit and proper checks bring about this risk.¹⁰¹

Additionally, mobile money services are undertaken by registered agents on behalf of PSPs albeit under weak controls. In so far as PSPs are liable for the actions of their agents as contained in their agency agreement¹⁰²; they may fail to follow through the known policies and to scrutinize transactions they handle especially because the agency agreement is not exclusive.¹⁰³

Monitoring transactions is a challenge in mobile money because criminals smurf their funds within the approved thresholds.¹⁰⁴ In this regard monitoring and follow through becomes a challenge.¹⁰⁵ Notably, there are limited cases, if any, on money laundering through MMT and the few suspicious activity reports that have been filed are fraud related.¹⁰⁶ In Kenya, the same Customer Due Diligence measures apply to all accounts despite value held or transferred through these accounts.

2.5 TYPOLOGIES OF MONEY LAUNDERING IN MOBILE MONEY

This section will examine how mobile money vulnerabilities discussed above are used to deal with PoC. Typologies refer to “typical criminal schemes that have been associated with a particular financial service”.¹⁰⁷ In the mobile money context typologies refer to the various methods that criminals abuse the system to deal with proceeds of crime. In MM context the

¹⁰⁰*Ibid.*

¹⁰¹*Ibid.*

¹⁰²NPSR regulations 14 (4) (5).

¹⁰³ FATF Guidance for a Risk-Based approach para 2; NPSR regulation 15 (2).

¹⁰⁴*Ibid.*

¹⁰⁵*Ibid.*

¹⁰⁶*Ibid.*

¹⁰⁷ <https://www.gsma.com/mobilefordevelopment/wp-content/uploads/2012/03/amlfinal35.pdf> accessed 15 May 2019.

typologies are broken down into two. That is those criminal schemes that are facilitated *vide* known ML cycle and those typologies or schemes employed by participants in the mobile money system such as customers and agents among others.

Typologies are important as they assist in detecting abuse and assessing the robustness of the PSPs systems.¹⁰⁸ Further, in terms of method, they guide on how to measure risk posed by an MMT service which in turn informs the appropriate mitigation measures to adopt.¹⁰⁹

Notably, criminals can misuse MM through the same methods used to abuse other systems like hacking.¹¹⁰ Exploitation of mobile money to launder money can occur in any of the stages in the ML cycle discussed in the preceding chapter. It is either during loading money into the mobile money account, transferring or withdrawal of funds. Additionally, participants in the mobile money system such as customers, merchants and agents can exploit the platform to launder money.¹¹¹

The ensuing section will discuss the various typologies that criminals use to launder money through MMT. These schemes are divided into two categories that is the methods that can be used by criminals using the money laundering cycle and the mechanisms used by the various participants in the mobile money cycle.

2.5.1 Typologies based on the mobile money transaction cycle

¹⁰⁸*Ibid.*

¹⁰⁹*Ibid.*

¹¹⁰ Laurent (n 59) 24.

¹¹¹*Ibid.*

The typologies are categorized in three (3) stages, depositing money into the account (placement), sending the money (layering) and removing the same (integration).¹¹² An illustration of how criminals can abuse the mobile money system for money laundering purposes is discussed below.

Loading of funds (“placement phase”)

It entails loading or placement of proceeds of crime into the mobile money account. It involves huge money transactions. Therefore, criminals engage in smurfing which allows for a huge sum of money to be tacked as small inconspicuous amounts below the AML reporting threshold with the intention of evading detection.¹¹³ Additionally, various remitters may divert money to a singular mobile account.¹¹⁴ Transferring funds (“layering phase”)

Criminals can use MMT services to “layer” funds by converting PoC to a different form and hiding source and ownership of funds for instance dealing in stock.¹¹⁵ The intention is to distinguish the proceeds of crime from their source.

This is made possible through “pooling and delegation”.¹¹⁶ Pooling takes place when mobile phones are shared among many individuals particularly in poor communities.¹¹⁷ Delegation on the other hand occurs among wealthy individuals wherein a delegate handles the mobile device on the owner’s behalf.¹¹⁸ These practices disguise the originator of a transaction as the initiator’s identity is concealed by the person who was registered as the owner.¹¹⁹

¹¹²*Ibid.*

¹¹³Kersop and Toit (n 18); World Bank Working Paper No. 146 27.

¹¹⁴*Ibid.*

¹¹⁵<http://www.fintrac-canafe.gc.ca/fintrac-canafe/definitions/money-argent-eng.asp> accessed 15 May 2019.

¹¹⁶ Laurent (n 59).

¹¹⁷*Ibid.*

¹¹⁸*Ibid.*

¹¹⁹*Ibid.*

Furthermore, cross border transfers provide an opportunity for criminals to layer transactions due to complexity of the transfers which can conceal either the origin or destination of funds.¹²⁰

Criminals may take advantage of the structural limitations on international law enforcement coordination, detection and monitoring mechanisms to render funds less traceable.¹²¹

Withdrawing of funds (“integration phase”)

It entails putting back the proceeds of crime back into the system as if it is emanating from a reputable source.¹²² Criminals find this stage useful due to the inherent vulnerability of mobile money known as rapidity. It enables real time transfer of money combined with uncertainty from the initial deposit of money and ultimately withdrawing the same.

2.5.2 Typologies based on mobile money stakeholders/participants

Notably, typologies are not limited to the different stages of the payment system but also the different stakeholders involved such as customers, merchants and agents as discussed below.¹²³

Customers

This can occur as legal transfer of illicit funds or funds intended to commit a crime.¹²⁴ Whereas true credentials may be used for registration, false information can be presented. In practice, Kenyan MMT services customers are required to present their original Identification Card for purposes of registration of a mobile money account and also for verification purposes while sending or transferring money using the mobile phone. The Registration of Persons Act¹²⁵ provides for the mandatory identification, registration and issuance of identity cards to all Kenyan citizens who are 18 years and above. It established the Department of National

¹²⁰*Ibid.*

¹²¹*Ibid.*

¹²²*Ibid.*

¹²³ Laurent (n 59).

¹²⁴*Ibid.*

¹²⁵ Chapter 107 Laws of Kenya.

Registration Bureau (NRB) which is tasked with implementation of the Act. The Department is still issuing 2nd generation ID cards which were introduced in 1995 to address the challenges of fraudulent issuance and acquisition of ID cards, duplicate identity card numbers and the cumbersome manual process associated with the issuance of ID cards.¹²⁶ Further, the NRB has digitized registration services by installing live capture systems in 43 Huduma Centres to enhance the quality of applications and drastically reduce the time taken to issue identity cards.¹²⁷

This is good news for the financial system as many Kenyan citizens will be able to secure an MM account. Nonetheless, the Bureau needs to introduce an electronic identity system compliant with best global standards and regional trends. This entails among other things a centralized database which is crucial for verification of persons purposes in consonance with CDD requirements. It will address emerging challenges in the issuance of 2nd generation ID Cards such as forgery, fraud and slow labour intensive processes experienced in issuance of the cards.¹²⁸

Further, dealings are used to move funds amongst people who are conspiring or to move them cross border to jurisdictions where AML regulation is less onerous.¹²⁹ Cross border remittances have been found to pose a higher ML risk than domestic remittances due to difficulties in identifying the financial details of the sender and recipient and the actual purpose of transferring the funds. It is subsequently coalesced with exchange of such monies for cash and subsequent utility or transfer by other methods.

¹²⁶ <http://www.immigration.go.ke/national-registration-bureau/> accessed 27 September 2019.

¹²⁷ *Ibid.*

¹²⁸ *Ibid.*

¹²⁹ *Ibid.*

Customers can also engage in multiple registrations, deposits or transfers owing to multiple SIM ownership challenging tracing of transactions meant to launder money.¹³⁰ In addition, customers can load their mobile money account with proceeds of crime by engaging in smurfing. The use of proceeds of crime by customers to purchase goods or services that fail to align with expected transaction modes point to how ML can take place.

Merchants

These persons pose a huge danger as they often can and actually do receive huge amounts of payments and deduct the same as legal business profit (“integration” of money). Further, they may not only be fraudsters but may provide an avenue for laundering of proceeds of crime other people posing as customers.¹³¹

POCAML A provides that anyone with knowledge or ought to know that the property they are transacting with constitutes PoC is guilty of ML.¹³²

Employees of PSPs

Internal staff of PSPs can facilitate ML through mobile money by colluding with criminals to facilitate fraudulent registration of non-existent accounts and failure to comply with KYC procedures.¹³³ Further, employees may allow known proceeds of crime to be loaded or withdrawn from a criminal’s account for instance the transfer of funds to dormant accounts.¹³⁴

Employees can also allow customers to exceed loading or withdrawing limits and this is established by reviewing audit trails which point to internal approval to exceed capped

¹³⁰*Ibid.*

¹³¹*Ibid.*

¹³²POCAML A s 3.

¹³³ Laurent (n 59).

¹³⁴*Ibid.*

limits.¹³⁵ In the absence of effective internal controls, employees can use their position to conceal their tracks thus heightening the degree of risk to conduct money laundering for this specific typology.

Agents

They play a crucial role in mobile services payment cycle which include depositing money, redeeming the money and even selling the handsets that are used to facilitate the payments and transfer of funds. They can falsify records, ignore suspicions of ML or simply act as compliance barriers by absconding their duties in a careful manner.¹³⁶ They can also allow customers to exceed their loading and withdrawing limits which facilitate abuse of the system to facilitate ML.¹³⁷

PSPs should invest greatly in agent training to ensure that their agents understand the importance of complying with KYC procedures, conducting due diligence on customers and reporting suspicious transactions. Also, PSPs can conduct onsite visits to ensure that their agents are compliant with their AML policies.

2.6 CONCLUSION

Mobile Money Transfer services potentially pose a risk to money laundering and the inherent vulnerabilities that the services pose ought to be sufficiently mitigated against in order to secure the integrity of the services. This will encourage greater use of the services which will ensure that many people is in the legal financial system to boost monitoring economic transaction with a view to averting the ML risk. There is also need to create awareness on the various typologies/methods that money launderers can use to evade detection by laundering money

¹³⁵*Ibid.*

¹³⁶*Ibid.*

¹³⁷*Ibid.*

through MMT services. This will ensure that the various participants and stakeholders are well versed and are able to detect and monitor suspicious transactions.

Effective risk mitigation measures should be put in place to guard mobile money from potential abuse at the same time promote its ability to increase financial inclusion. PSPs must develop compliance procedures that align with AML policies to safeguard sustainability of MM. Kenya should therefore thrive to develop regulation that is proportional to AML as this will guard integrity of MMT services and increase financial inclusion levels in the country.

3.0 CHAPTER THREE

OVERVIEW OF ANTI-MONEY LAUNDERING LAW FOR MOBILE MONEY IN KENYA

3.1 INTRODUCTION

Kenya has promulgated legislation and regulations to govern mobile money usage including the anti-money laundering framework. For mobile money to thrive there needs to be regulation that is proportional not only to curbing risk but also to promoting financial inclusion. Since mobile money is a product of technology which is dynamic in nature there is need to review the law constantly to ensure that it's abreast with changes in the sector. The recent launch of M-Pesa Global as noted previously points to the changing face of mobile money and the need to constantly review the legal framework to capture the dynamic nature of these services.

Having examined the nature of mobile money and its vulnerability to money laundering in the previous chapter, herein we will discuss the legal landscape governing mobile money in the country. An assessment of its effectiveness to deal with these vulnerabilities will follow thereafter to determine viability. Further, Kenya's AML regime is studied within the broader global landscape owing to its growth being necessitated by events at the global sphere.¹³⁸ Accordingly, international development regarding AML strategies has pursued both the preventative and prohibitory strategies.¹³⁹ This is through the enactment of conventions¹⁴⁰ and establishment of specific organizations¹⁴¹. These conventions will be discussed in detail below

¹³⁸ Gikonyo (n. 21) 59-70.

¹³⁹ *Ibid.*

¹⁴⁰ FATF (n 41).

¹⁴¹ Financial Action Task Force (FATF) which is an intergovernmental organization established in 1989 by the G7 to effectively deal with AML initiatives world over. Regional organizations are tasked with implementing FATF Recommendations such as the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG).

however the emphasis will be on the FATF Recommendations as they contain standards that provide for the AML framework governing proper utility of MM.

Having discussed the dangers that expose MM to ML in the previous chapter, the author will endeavor to examine the various mitigation measures under the legal framework in Kenya and whether the said measures conform to the international standards on AML for mobile money.

3.2 LEGAL AND REGULATORY LANDSCAPE FOR MOBILE MONEY IN KENYA

During inauguration of M-Pesa in 2007, which was Kenya's pioneer MM service, the country attempted to regulate mobile money services through a dilation of pre-existing regulations governing banks.¹⁴² Before 1990, the measures taken to control ML in MM were contained in general criminal statutes such as the Anti-Corruption and Economic Crimes Act¹⁴³ and the guidelines by CBK¹⁴⁴. The guidelines sought to implement the Recommendations by FATF which included KYC regulations, CDD procedures, monitoring transaction requirements, screening measures, SAR and record keeping.¹⁴⁵

In 2009, the POCAMLA was promulgated to introduce more stringent measures as it sought to explicitly make ML an illegality in the country. The Act equipped the Government with enforcement capacity to trace and capture PoC and valuables and provided for harsh penalties for criminals.¹⁴⁶ Furthermore, the Recommendations by FATF implemented prior through CBK's prudential guidelines became compulsory for MM service providers.¹⁴⁷ Through the enactment of this Act, Kenya has implemented AML preventive measures which are mandatory and failure to comply amounts to an offence.

¹⁴²Buka (n 12).

¹⁴³ Act No 3 of 2003 Laws of Kenya available on <http://www.kenyalaw.org/lex//actview.xql?actid=No.%203%20of%202003> accessed 27 March 2019.

¹⁴⁴ Chapter 488 Laws of Kenya available on <http://www.kenyalaw.org/lex//actview.xql?actid=CAP.%20488> accessed 27 March 2019.

¹⁴⁵ Buka (n 12) 395.

¹⁴⁶*Ibid.*

¹⁴⁷*Ibid.*

In April 2010, the CBK by virtue of the authority granted by section 4A of the CBK Act¹⁴⁸ issued Guidelines for Agents.¹⁴⁹

In 2011, CBK in consultation with stakeholders like Safaricom came up with sector-specific regulations for MM.¹⁵⁰ These included the Electronic Payment Guidelines of 2011 and the Retail Electronic Transfer Guidelines of 2011.¹⁵¹ They required electronic money issuers such as Safaricom's M-PESA holding company to maintain a capital of Kshs. 10M or 1% of one-twelfth of the previous year's total turnover.¹⁵²

Pursuant to these guidelines and constant lobbying by the banking sector, Parliament started to debate on a robust payment law that would govern payments done electronically and put MM on the same playing field as other money transfer services provided by banks.¹⁵³ This led to the promulgation of the National Payment Systems Act (NPSA) in December 2011¹⁵⁴ which statute converged all PSPs including mobile phone service providers into a singular regulatory framework. It also gave CBK supervisory powers over these PSPs to ensure their effectiveness in the market.¹⁵⁵

In 2014, the NPS Regulations (NPSR) were promulgated to operationalize the NPSA. They provide for the supervision of PSPs, creation of payment systems, payment instruments and AML measures.¹⁵⁶ CBK in 2013 issued the NPS (AML Guidelines for the provision of mobile

¹⁴⁸ Chapter 491 Laws of Kenya.

¹⁴⁹ <https://www.centralbank.go.ke/images/docs/legislation/GUIDELINE%20ON%20AGENT%20BANKING-CBK%20PG%2015.pdf> accessed 10 April 2019.

¹⁵⁰ *Ibid.*

¹⁵¹ *Ibid.*

¹⁵² *Ibid.*

¹⁵³ *Ibid.*

¹⁵⁴ Act No. 39 of 2011 available at <http://www.kenyalaw.org/lex//actview.xq!?actid=No.%2039%20of%202011> accessed 27 March 2019.

¹⁵⁵ Buka (n12) 396.

¹⁵⁶ <https://www.centralbank.go.ke/national-payments-system> accessed 02 January 2019.

payment services) 2013¹⁵⁷ to aid in combating ML in MMT services. However, these guidelines fail to address the vulnerabilities that MMT services face, the manner in which these vulnerabilities can be identified and the mitigating mechanisms that payment service providers can adopt. Further, the guidelines maintain the reporting threshold for suspicious transactions at USD. 10,000/- which is unlikely to be met by the PSPs due to the transaction threshold provided. The regulations therefore warrant amendment to provide for adequate AML regulation of MMT services.

In 2017, the POCAMLA was amended by Parliament through the promulgation of the POCAMLA¹⁵⁸ to provide a robust mechanism for dealing with ML in the country. Financial bodies like MM service providers are now mandated to develop measures to report and identify suspected ML activities. Subsequently, the provisions of the POCAMLA will be analyzed in greater detail to determine its effectiveness in curbing money laundering in MM in Kenya.

Further, Kenya has adopted the International AML standards/recommendations by FATF requiring adoption of KYC procedures to detect suspicious transactions.

The recent Dusit terrorist attack that happened in Kenya's capital city, Nairobi is an example of swift movement of large amounts of funds through mobile money using different SIM cards to disguise the source of funds.¹⁵⁹ The case is currently in court with the suspects having been charged pursuant to the provisions of the Prevention of Terrorism Act.¹⁶⁰

3.3 INTERNATIONAL REACTIONS TO MOBILE MONEY ML: THE RECOMMENDATIONS BY FATF

¹⁵⁷ <https://www.centralbank.go.ke/images/docs/NPS/Regulations%20and%20Guidelines/Guidelines%20-%20Mobile%20money%20AML%20Guidelines.pdf> accessed 27 September 2019.

¹⁵⁸ POCAMLA (n 36).

¹⁵⁹ *Ibid* note 76.

¹⁶⁰ No. 30 of 2012 Laws of Kenya.

The Recommendations or standards by FATF¹⁶¹ are known as the international best practices on ML and provide a benchmark for AML. They outline actions that countries should criminalize to comply with the objectives by FAFT. The 2012 Recommendations are revised form of the AML global standards originally assumed in 1990 and revised in 2003.¹⁶² The existing Recommendations were revised in February 2012 to deal with affected adherence of countries and to strengthen their consistency.¹⁶³

The foregoing discussion will examine the ramifications of these new recommendations on MM highlighting the positive aspects of the same and the challenges they pose to mobile money.

3.4. Assessing the effectiveness of THE 2012 FATF Recommendations on mobile Money Transfer

3.4.1. FATF Recommendation 1-The Risk Based Approach (RBA)

Countries and financial organizations are mandated to adopt the RBA however its usefulness is on particular aspects of AML.¹⁶⁴ The RBA should be used to develop the appropriate regulatory framework or determine the CDD measures to apply on specific customers, products or services. Under this recommendation, countries should undertake a risk assessment which will include “identifying, assessing and understanding” their ML risks so as to adopt the appropriate risk mitigation measures. This is expected to offer countries flexibility so as to encourage widest form of participation in the regulated financial sector.¹⁶⁵

¹⁶¹FATF (2012), International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation, The FATF Recommendations, FATF, Paris.

¹⁶²Louis de Koker, ‘*The 2012 Revised FATF Recommendations: Assessing and Mitigating Mobile Money Integrity Risks within the New Standards Framework*’ in Jane K. Winn and Louis de Koker, ‘*Introduction to Mobile Money in Developing Countries*’ Financial Inclusion and Financial Integrity Conference Special Issue, Washington Journal of Law, Technology & Arts (2013) 8 Issue 3 Mobile Money Symposium on <http://digital.law.washington.edu/dspace-law/handle/1773.1/1204> pg. 172 accessed 27 March 2019.

¹⁶³*Ibid.*

¹⁶⁴*Ibid.*

¹⁶⁵ Laurent (n 59).

Countries are therefore encouraged to adopt this approach so that their risk alleviation measures are in line to the noted dangers. For instance, where higher AML risks are identified, enhanced risk mitigation measures ought to be applied.¹⁶⁶ Similarly, where low AML risks are established countries may fail to impose AML obligations on organizations that should otherwise be regulated.¹⁶⁷ Further, simple CDD mechanisms may be adopted for customers and services posing a low danger.

However, where simplified CDD measures are implemented it is difficult to get a complete client account.¹⁶⁸ Consequently, detection of an activity that is suspicious will be a challenge since the PSP will not be sure of the customer's background and what is unusual activity.¹⁶⁹ Further, the capacity to file reports that are meaningful will lessen since the reason for suspicion is not included to help gather information for investigation purposes.¹⁷⁰

Notably, FATF has established specific CDD measures for particular clients, activities and relationships that it considers posing universally high risk.¹⁷¹ These include Politically Exposed Persons¹⁷² (PEP) and MMT services.

Kenya seems to be non-compliant with this requirement, since all reporting institutions are subject to the same CDD measures irrespective of risks involved. This puts MMT transactions which are usually high volume and low risk in nature at the same level with high risk reporting institutions such as banks.

Section 45A of POCAMLA provides for adoption of enhanced CDD measures when reporting institutions enter into business relationships with people and financial bodies with countries noted by FATF as posing higher ML risks. This is in line with Recommendation 19 by FATF.

¹⁶⁶*Ibid* p. 174.

¹⁶⁷*Ibid*.

¹⁶⁸ Goldby (n 52).

¹⁶⁹*Ibid*.

¹⁷⁰*Ibid*.

¹⁷¹*Ibid*.

¹⁷² PEPs are usually defined as persons who have great public duties by a foreign country such as government officials.

3.4.2 FATF Recommendation 10: Requirements for CDD and KYC

Financial bodies are prohibited from maintaining accounts that are anonymous. They should undertake CDD measures while developing business relations, doing transactions above USD 15,000/-, there is likelihood of ML or there is doubt about the veracity of customer profile obtained before.

POCAMLA¹⁷³ mandates financial bodies to confirm their customer's profile implement CDD measures for new and existing customers'. Further section 45A¹⁷⁴ mandates financial bodies to implement CDD policies on business dealings and relations with any person or financial organization emanating from countries noted by FATF as being a greater ML danger. The challenge in this guideline is in the lack of identification documents especially where the national identity card systems are underdeveloped.¹⁷⁵ Also, failure to confirm the profile of the customer identity based on dependable sources may result to mobile money providers running the danger of customers having various accounts at the same time undetected by the PSP.¹⁷⁶

3.4.3 FATF Recommendation 11: Keeping records

Financial bodies are mandated to keep customers' records for at least five (5) years to allow compliance with requests for information from authorities. They are required to keep transaction records procured through CDD.

Section 46 of POCAMLA and section 12 and 29 of NPSA mandates reporting institutions to establish and maintain customer records. These records include transaction records and information obtained through CDD measures as required by FATF guidelines.¹⁷⁷ However, financial bodies are required to keep customer records for seven (7) years or such duration as the

¹⁷³ Section 45.

¹⁷⁴ POCAMLA.

¹⁷⁵ FATF (n 98).

¹⁷⁶ Kersop and Toit (n 18).

¹⁷⁷ POCAMLA s 45 and 46 (3).

Financial Reporting Centre (FRC) demands.¹⁷⁸ This is an extended record keeping period than that which is prescribed by FATF.

3.4.4 FATF Recommendation 14: money or value transfer services

FATF has established additional measures for specific customers and activities as is the case with MMT services. Countries are expected to ensure mobile money operators and providers are registered or licensed. Further that they are supposed to have monitoring and compliance systems that are adequate and comply with the Recommendations by FATF.

Similarly, agents working with MMT service providers should be registered and the provider to have a record of its agents which should be available to the authorities.¹⁷⁹ The MMT PSPs should add their agents in their AML programs and follow up with them for compliance.

3.4.5 FATF Recommendation 20: Reporting of Suspicious Transactions

Suspicious Activity Reporting (SAR) Regimes are established in line with this standard in that if a reporting body suspects or has knowledge that funds are proceeds of an illegality they are supposed to report immediately to the Financial Intelligence Unit (FIU).¹⁸⁰ Arguably, successful implementation of such a regime requires investment of time and resources which many developing countries such as Kenya may grapple with.¹⁸¹ Notably, the genesis of any SAR regime is legal provisions that provide for punitive measures for financial bodies failing to report transactions that are suspicious and which may constitute ML.

In Kenya, PSPs are reporting institutions under POCAMLA¹⁸² and are mandated to monitor dealings so as to note and report any suspicious dealings to the Financial Reporting Centre¹⁸³.

Financial bodies should also maintain internal mechanisms for reporting suspicious dealings.

Nonetheless, monitoring suspicious transactions remains a challenge. Attributably due to

¹⁷⁸ POCAMLA s 46 (4).

¹⁷⁹ NPSA s 19.

¹⁸⁰ Koker (n 156).

¹⁸¹ Goldby (n 52).

¹⁸² POCAMLA s 2.

¹⁸³ POCAMLA s 21.

criminals engaging in smurfing wherein they ensure transfer of funds fall within approved thresholds. Also, MMT services are provided by registered agents albeit under weak controls. They may fail to follow approved regulations thus failing to monitor dealings in their care. This becomes a problem when it comes to detection and follow through.¹⁸⁴

Further, compliance with reporting obligations is resource intensive, in Kenya for instance financial bodies are required to come up with adequate internal monitoring structures to detect likely ML activity.¹⁸⁵ Not to mention staff training and human resource requirements to ensure monitoring and compliance in line with FATF recommendation 18.

3.4.6 FATF Recommendation 21: Confidentiality and Tipping off

This guideline requires that financial bodies and their agents should be:

(a) “Safeguarded by law from either criminal and civil accountability for violation of any limitations on divulgence of data either by agreement, legislative, administrative requirement, if they proclaim their suspicions to the FIU, regardless of whether they were unaware of any illegality criminal activity or whether it really happened. (b) Forbidden by law from “tipping off” that an STR is being filed with the FIU.”

Compliance with this standard is seen under section 8 of the POCAMLA which prohibits tipping off. The current FATF Recommendations have been critiqued for being unsuitable for application in economies that are cash based hence need for additional recommendations that offer guidance on combating ML in cash based economies especially because of MVT services.¹⁸⁶

¹⁸⁴Gikonyo (n 21).

¹⁸⁵ POCAMLA s 47.

¹⁸⁶ <https://pdfs.semanticscholar.org/7fa1/4907c2e67442979a31bef1bd061e805f0c4b.pdf> accessed 27 September 2019.

3.5 United Nations Convention against illicit Traffic in Narcotic Drugs and Psychotropic Substances (Vienna Convention)

It was assumed in Vienna on 19th December, 1998 and has since been ratified in Kenya. This was the first global convention to address PoC and to mandate countries to declare ML an illegality.¹⁸⁷ Consequently, countries have developed detection systems to note movement of PoC.¹⁸⁸

Kenya's substantive law on money laundering, the POCAMLA has embodied the said objectives of the convention in its text. For instance, the property definition in the POCAMLA addresses all assets in or outside the country and is in line with the property definition in Vienna and Palermo Conventions and the FATF glossary.

3.6 United Nations Convention against Transnational Organized Crime (Palermo Convention)

This global convention on ML was assumed by the General Assembly on 15th November, 2000.¹⁸⁹ Also known as the Palermo Convention, the scope of the ML in the instrument includes funds deriving from major offences.¹⁹⁰ The instrument requires countries to co-operate to detect, investigate and prosecute ML.¹⁹¹ Further, States are obliged to fortify demands for customer profiling, keeping records and STR alongside the setting up of FIUs to gather, examine and spread information.¹⁹²

¹⁸⁷ UNODC, 'Global Programme against Money Laundering' available on <https://www.imolin.org/pdf/imolin/UNres03e.pdf> accessed 5 April 2019.

¹⁸⁸*Ibid.*

¹⁸⁹*Ibid.*

¹⁹⁰*Ibid.*

¹⁹¹*Ibid.*

¹⁹²*Ibid.*

The terms of the convention have been captured in Kenya's AML regime including the POCAMLA as seen in the establishment of FRC.¹⁹³ Also, the criminalization of ML in Kenya is broadly in line with provisions of the Vienna and Palermo Instruments.

3.7 Mitigation Measures adopted in Kenya for the inherent vulnerabilities in mobile money as classified by the World Bank

3.7.1 Anonymity

This is mitigated by implementing enhanced KYC and CDD measures such as confirmation of customer's profile pursuant to regulation 12 of POCAMLR. Also, other factors in practice that aid in mitigating this risk factor include¹⁹⁴ firstly, allocation of a unique mobile number to the transactions thus enhancing ease of tracing the same. Secondly, transaction details are recorded that is the sender's and recipient's mobile number, amount and date of transaction. Thirdly, SIM card registration records provide crucial information that can help identify a customer and lastly law enforcement officials who intend to identify a particular customer can request for details from the provider for instance voice recordings and transaction patterns.¹⁹⁵

In South Africa for instance customer information is verified in third party databases and in the Republic of Korea electronic signatures are required for mobile money payment services above a certain threshold.¹⁹⁶

3.7.2 Rapidity

In practice the transactions are traceable in the mobile network system hence making it easy to flag off certain type of transactions as being suspicious and managing risks posed by third party providers. This Integrated system of internal controls is one of the ways in which this risk can be

¹⁹³ POCAMLA s 21.

¹⁹⁴ Laurent (n 59).

¹⁹⁵ Louis de Koker (2009), "Anonymous Clients, Identified Clients and the Shades In Between: Perspectives on the FATF AML/CFT Standards and Mobile Banking." Paper presented at the 27th Cambridge International Symposium On Economic Crime, Jesus College, Cambridge, UK.

¹⁹⁶ Laurent (n 59).

mitigated as is the case in the Philippines wherein Telecommunication companies enhance manual controls with automated ones in the computer systems.¹⁹⁷

3.7.3 Elusiveness

Currently in Kenya transaction and the maximum account balance limits are set to control the amount customers can transact and account balance they can maintain to mitigate this risk. For instance, the maximum daily transaction value for M-pesa is Kshs. 140,000/- whereas the most value per dealing is Kshs. 70,000/- and the highest account balance is Kshs. 100,000/-.¹⁹⁸

Additional mitigation measures that Kenya has adopted include enhanced customer profiling, monitoring and reporting however these measures have challenges under the law as previously pointed out hence inadequate in curbing the risk.

3.7.4 Poor Oversight

Practically, Kenya has the same CDD requirements for all its customers and is yet to adopt an RBA approach to CDD for various account holders. Additionally, sector specific guidelines are set up to govern money laundering in MM however they are inadequate. There is need to develop tailor made customer due diligence requirements for mobile money to enhance compliance and come up with clear guidelines regarding regulation of PSPs and risk supervision.

3.8 CONCLUSION

Evidently Kenya has an AML regime to deal with ML but the same is inadequate for addressing ML in mobile money especially because Kenya is an economy that is cash oriented and also due to the inherent vulnerabilities that lie in the usage of MMT services which are not contemplated in the law. The country continues to grapple with implementation challenges, poor verification

¹⁹⁷*Ibid.*

¹⁹⁸<https://www.safaricom.co.ke/personal/m-pesa/getting-started/m-pesa-rates> accessed 15 May 2019.

and KYC procedures, lack of technical expertise to detect and monitor ML in new payment methods such as MMT services. Limiting cash use in the economy and enhancing governance of money laundering risks in MMT services will boost the fight against ML and promote financial deepening in the country.

4.0 CHAPTER FOUR

INSTITUTIONAL FRAMEWORK GOVERNING ML IN MOBILE MONEY IN KENYA

4.1 INTRODUCTION

Kenya's anti-money laundering legal framework establishes various institutional bodies mandated to combat ML. This chapter will highlight these institutional bodies and examine their efficacy or otherwise to combat ML in MMT services in Kenya. Notably, Kenya not only has national organs to combat ML but enjoys membership of regional and international bodies like the East and Southern Africa Anti-Money Laundering Group (ESAAMLG) whose mandate is to combat money laundering. This chapter will discuss these institutions in detail and assess the impact of Kenya's membership in reference to mobile money AML regulation in the country. In order to enhance the discussion on the adequacy of these institutional bodies the writer will categorize the institutions into national, regional and international bodies.

4.2 NATIONAL AML INSTITUTIONAL FRAMEWORK ON MOBILE MONEY

4.2.1 CENTRAL BANK OF KENYA (CBK)

CBK has supervisory authority over all financial institutions and national payment systems in the country. Notably, for ML purposes the CBK only has supervisory authority over mobile service providers and not trust companies or trust account holders entrusted with customers' deposits. This has been considered a serious omission as it puts customers' funds under risk.

4.2.2 THE FINANCIAL REPORTING CENTRE (FRC)

It is a functionally independent State Corporation that administratively falls under the National Treasury.¹⁹⁹ It is established under section 21 of POCAMLA as a state financial intelligence unit and its principal duty is to spot PoC and to deal with ML.²⁰⁰ It is the overseer of execution of AML schemes in Kenya pursuant to the POCAMLA and the national center for Suspicious Transaction Reporting (STR).

Before POCAMLA, the AML policies in the Banking Act²⁰¹ required both financial and non-financial bodies authorized under the Act to send STRs to Central Bank of Kenya. The reports would then be forwarded to the Banking Fraud Investigations Department (BFID) for Investigations. Currently, FRC analyses STR, Cash Transaction Reports and cross border conveyancing of monetary instruments and disseminates intelligence to institutions like the Ethics and Anti-Corruption Commission (EACC), Directorate of Criminal Investigation (DCI), National Intelligence Service (NIS) amongst other authorities like the Kenya Revenue Authority (KRA), Capital Markets Authority (CMA) and supervisory bodies.

Financial institutions including PSPs should document Suspicious Transactions Report with FRC for dealings whose amount exceed USD 10,000/-.²⁰² Failure by financial institutions to abide by this rule is an offence.²⁰³ In practice PSPs are unlikely to be charged with this offence because they have transaction limits which fall below the required reporting threshold of USD. 10,000/-.

Also, neither is the mandate of the FRC with regard to detection of ML transactions in MMT services nor the provision of what constitutes a suspicious transaction for MMT clearly spelt out under the POCAMLA. Hence the vacuum in the law means that it is at the discretion of the PSP to define what constitutes a suspicious transaction for its purposes.

¹⁹⁹<http://frc.go.ke/faq.html> accessed 10 June 2019.

²⁰⁰ POCAMLA s 24.

²⁰¹ Chapter 488 Laws of Kenya.

²⁰² POCAMLR reg. 32 (1) and 34 (1).

²⁰³ POCAMLR reg 42.

Further, FRC lacks powers to investigate or prosecute offenders and is only required to report to agencies established by the law to enable them investigate independently prior to taking action. This process occasions delays on the part of the Centre in achieving its objectives.

In so far as the POCAMLA allows the Centre to co-operate and collaborate with other jurisdictions in combating money laundering, the act does not contemplate overlap of jurisdiction and sovereignty and this may pose a challenge to enforcement. Therefore, countries may be required to negotiate separate agreements on jurisdiction to facilitate enforcement. Also, Kenya lacks a comprehensive legislation on Mutual Legal Assistance (MLA) authorities rely on bilateral agreements, Instrument governing Extradition and Harare Scheme to which it is a member. POCAMLA under part XII contains some provisions relating to MLA however they are only limited to investigations and proceedings.

Further, the Centre is considering joining the Egmont Group of FIUs which will enable it benefit from the Egmont Group Statement of Purpose and its objectives for exchanging information between FIUs for ML cases. Failure to join the Egmont Group has affected Kenya's compliance with FAFT Recommendation 38 on freezing and confiscation mutual legal assistance.

4.2.3 THE ASSET RECOVERY AGENCY (ARA)

FRC shares intelligence with ARA which is set up pursuant to section 52 of POCAMLA as a semi-independent institution under the AGs office. ARA is mandated with recovering PoC however so as to carry out its mandate effectively there needs to be inter-agency co-operation with the Financial Reporting Centre. The agency also works in partnership with other state agencies such as the Kenya Revenue Authority and the EACC to seize proceeds of crime and freeze accounts bearing proceeds of crime.

ARA can move to court for a restraint order to prohibit dealing in property that is subject to investigations. Further, under Part VIII of POCAMLA, the Agency can apply to court for preservation and recovery of assets emanating from PoC. For instance in the matter of *Asset Recovery Agency v Stephen Vicker Mangira & 2 Others*²⁰⁴ the Agency sought preservation orders seeking to freeze property belonging to four suspected drug traffickers including eight vehicles and Kshs. 21 Million. Proceeds of crime derived pursuant to confiscation and forfeiture orders and any funds or valuables recovered under the Anti-Corruption Act, 2003²⁰⁵ shall be deposited in the Criminal Asset Recovery Fund established under section 109 POCAMLA. In recent times, the agency has succeeded in confiscating properties purchased using proceeds of crime for corrupt individuals in the public sector as was seen in the Nation Youth Service scandal case of *Asset Recovery Agency v Josephine Kabura Irungu & 7 Others*²⁰⁶

Nonetheless, the agency needs to also pursue criminals laundering money using mobile money to avert loss of public funds and deter criminals from engaging in the vice. This is especially as a result of slow prosecution and conviction of ML offences in our courts. In addition, the agency officials ought to be coached on the latest methods for laundering money particularly in mobile money to enhance recovery of PoC. Further, to use enhance technology to recover PoC is something that ARA should consider going forward.

Pursuant to the adoption of the United Nations Convention against Corruption (UNCAC), asset recovery gained prominence due to emergence of asset recovery networks (ARN).²⁰⁷ ARNs

²⁰⁴ Misc Civil Application No. 195 of 2017.

²⁰⁵ <https://www.eacc.go.ke/wp-content/uploads/2018/06/aceca.pdf> accessed 26 September 2019

²⁰⁶ Misc. Civil Application No. 524 of 2015.

²⁰⁷ <https://www.unodc.org/documents/treaties/UNCAC/WorkingGroups/workinggroup2/2018-June-6-7/V1803851e.pdf> accessed 24 September 2019.

enable countries to establish systems that seek to obtain data on the source, destination and beneficiary of PoC thus aiding the battle against ML and corruption.²⁰⁸

Kenya is a member of INTERPOL/StAR Global Focal Point Network (GFPN) which was launched in 2009 to aid asset recovery officials to overcome operational barriers related to international asset recovery.²⁰⁹ This is by setting up a safe information exchange platform for criminal asset recovery.²¹⁰

4.2.4 THE ANTI MONEY LAUNDERING ADVISORY BOARD

It is set up pursuant to section 49 of POCAMLA to advice on framework, standards and related functions to detect PoC and to combat money laundering.

It is inadequate to combat ML because their mandate is limited to PSPs since the trust companies that hold customer funds are not reporting institutions under POCAMLA and hence not subject to AML mechanisms. Further, such entities cannot be prosecuted for failure to meet reporting obligations under the Act.

Also the POCAMLA does not provide for intra agency co-operation of the various bodies and this can lead to overlap of duties. These institutions also lack adequate funding and sufficient training especially on MMT services which is a developing phenomenon.

4.3 REGIONAL AML INSTITUTIONAL FRAMEWORK FOR MOBILE MONEY

4.3.1 EAST AND SOUTHERN AFRICA ANTI-MONEY LAUNDERING GROUP (ESAAMLG)

As a global network of FIUs, the Egmont Group's membership is made up of eight regional groups.²¹¹ The East and Southern Africa Region comprises jurisdictions that are part of the

²⁰⁸ *Ibid.*

²⁰⁹ *Ibid.*

²¹⁰ *Ibid.*

²¹¹ <https://egmontgroup.org/en/content/regional-groups> accessed 24 September 2019.

ESAAMLG, Kenya included. The ESAAMLG is aligned with the FATF regional groups and assist Egmont Group to achieve its goals of co-operation, development and sharing expertise on a regional level.²¹² Kenya stands to benefit in detecting and preventing money laundering by joining the Egmont Group of FIUs through sharing of financial knowledge and investigative techniques which is crucial for mobile money due to advancement in technology. Also due to the fact that criminals continue to devise techniques that evade detection of movement of proceeds of crime.

4.4 INTERNATIONAL AML INSTITUTIONAL FRAMEWORK FOR MMT IN KENYA

4.4.1 FINANCIAL ACTION TASK FORCE (FATF)

The FATF established in 1989 during the G7 summit as an inter-governmental organization.²¹³ It develops standards and promotes application of legal, regulatory and operational mechanisms for combating ML, TF and other related threats to the integrity of the international financial structure.²¹⁴ It seeks to develop national legislative and regulatory reforms in these areas.

It has come up with Recommendations that are noted as the international standard for combating ML.²¹⁵ In addition to monitoring the development of countries in implementing required mechanisms, it examines ML techniques and encourages application of adequate mechanisms worldwide²¹⁶. Together with other global stakeholders, FATF identifies vulnerabilities from a national level to safeguard the international financial structure from abuse.

²¹² *Ibid.*

²¹³ <https://www.fatf-gafi.org/about/> accessed 24 September 2019.

²¹⁴ *Ibid.*

²¹⁵ *Ibid.*

²¹⁶ *Ibid.*

In 2014, FATF established that Kenya's AML regime had improved including regulating mobile money by establishing laws in response to strategic deficiencies it had noted in its Mutual Evaluation Report (MER) of 2010.²¹⁷

4.4.2 THE EGMONT GROUP

The Egmont Group is an international organization comprising of 164 FIUs.²¹⁸ It provides a platform for member FIUs to securely exchange operational financial intelligence (Egmont Secure Web) and expertise to deal with ML.²¹⁹ It is crucial since FIUs are in a better position to support national and global attempts to deal with ML and TF. In addition, because FIUs are trusted avenues for apportioning data locally and globally in line with international AML regime such as the Recommendations by FATF. The Egmont Group also supports the endeavours of its member FIUs and global members such as the G20 Finance Ministers, United Nations and FATF in dealing with ML and TF.²²⁰ This is through enhancing comprehension of ML and TF dangers and the provision of a secure platform to exchange financial intelligence information mentioned earlier.²²¹ In so doing, the organization is able to derive operational experience that informs domestic and international AML policy.²²²

Notably, Kenya's FRC does not belong to the Egmont Group of FIUs.²²³ It is imperative that Kenya joins the Egmont Group to benefit from capacity building, understanding the typologies and methodologies used by money launderers and exchange of financial intelligence information especially because money laundering is a global vice.

4.4.3 THE INTERNATIONAL MONETARY FUND (IMF) AND THE WORLD BANK

²¹⁷ <http://www.fatf-gafi.org/publications/mutualevaluations/documents/mutualevaluationofkenya.html> accessed 24 September 2019.

²¹⁸ *Ibid.*

²¹⁹ *Ibid.*

²²⁰ *Ibid.*

²²¹ *Ibid.*

²²² *Ibid.*

²²³ <https://egmontgroup.org/en/content/east-and-southern-africa-region> accessed 24 September 2019.

(WB)

The IMF is a global institution that was established in 1945 and boasts of a near global membership of 189 Countries, Kenya included.²²⁴ It mainly secures solidity of the global fund system of remittances made globally and exchange rates and allow states and their people to deal with one another.²²⁵ It provides technical assistance to its signatories on a discretionary co-operative premise on how to apply AML measures. Kenya will benefit by being a member of the Fund from the technical know-how in application of its AML obligations with regards to MMT services.

The World Bank through its Group that oversees integrity of the Financial Market seeks to provide aid to countries regarding AML. This assistance is in the form of review and development of policy, technical expertise of country's statutes, applying institutional laws, developing financial know how capability and enabling the Judiciary to prosecute ML.²²⁶ These reviews are crucial as they identify the flaws in a country AML regime and provides training where training is necessary.²²⁷ This is beneficial to Kenya especially for MMT services as the country will stand to benefit from enforcement of its AML regime and enhance capacity building to mitigate ML risks in MMT services in the country.

4.5 CONCLUSION

Kenya has a robust institutional framework on AML however the national bodies struggle to a large extent with unqualified and trained workforce, financial capacity and other resources to enable them fulfill the AML duties under the law. To boost regulation of ML in MMT services Kenya should consider joining the Egmont Group to benefit from technical assistance amongst

²²⁴ <https://www.imf.org/en/About> accessed 27 September 2019

²²⁵ *Ibid.*

²²⁶ <https://pdfs.semanticscholar.org/7fa1/4907c2e67442979a31bef1bd061e805f0c4b.pdf> accessed 27 September 2019

²²⁷ *Ibid.*

other AML initiatives. Further, by joining these regional and global institutions Kenya will benefit from assessment and evaluation of its AML regime as seen in the Mutual Evaluation Report by ESAAMLG. This is important as it informs the omissions and the loopholes in the existing framework and proposes amendment. The absence of data by the requisite national bodies particularly for MMT services hinders examination of the AML framework in the country.

5.0 CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1 INTRODUCTION

The burgeoning and uptake of MM is to a large extent influenced by the legal, regulatory and institutional framework within which it operates. Indeed, a relaxed and overlapped framework bears the risk of regulatory failure and threatens the growth of MM. As illustrated in previous chapters, MM has potential to boost financial integrity in the financial system by eradicating financial exclusion through erosion of informal remittance channels. However, it also has potential to challenge the integrity of the financial system particularly money laundering if not adequately governed. Accordingly, proportional regulation that guards against ML and hinders against financial exclusion should be put in place.

This chapter provides a summary of the findings on the adequacy of the AML legal and institutional framework on MMT services in the country. It concludes on the way forward and makes recommendations on the various omissions and loopholes in the legal and institutional frameworks that warrant amendment by Parliament for adequate AML governance of MMT services in Kenya.

5.2 SUMMARY OF FINDINGS

This study has attempted to critique the adequacy of the AML legal and institutional landscape governing MMT services in the country. The research in chapter one has established that majority of the population in the country own an MM account hence use of MMT services is on the rise. Further, that these MMT services face inherent financial integrity risks that criminals are prone to abuse so as to deal with their proceeds of crime. Notably, mobile money is vulnerable to money laundering and if not adequately regulated may compromise the financial integrity of the services. It provides a conceptual framework of money laundering to foster an understanding of how proceeds of crime are legitimized. It was found as a result of unique status and characteristic of MM criminals who are keen to evade detection while conducting suspicious transactions are likely to misuse the platform. This is because it is a new payment system that is continuously developing thus criminals who are looking for new avenues to launder money may opt to use the services. Despite Kenya promulgating various pieces of legislation to deal with ML, it was established that MMT services are put on the same AML mechanisms as those of banking institutions hence making the regulatory frameworks inadequate to combat ML.

Chapter two examined the potential money laundering risks in mobile money. The findings of this chapter establish that mobile money has inherent vulnerabilities that make the services susceptible to money laundering. The writer relied on the four major inherent vulnerabilities comprising of anonymity, elusiveness, rapidity and poor oversight which have been documented by the World Bank to manifest the vulnerability of MMT to money laundering. It is established that despite Kenya having regulations and institutions to combat money laundering in mobile money they do not adequately mitigate against these inherent vulnerabilities.

It was established that monitoring of suspicious transactions, inadequate reporting mechanisms, customer identification and profiling remain a challenge. The findings in this chapter also note

the different typologies criminals launder funds using the mobile money platform. It was noted that this can be done through the mobile money transaction cycle or facilitated by the various stakeholders and actors in the transaction. It is therefore crucial for the law to address these inherent vulnerabilities in MM and the typologies criminals use to explore whilst using MMT services to launder money.

Chapter three provided an assessment of the AML regime for MM in Kenya. Herein various national and international laws that are promulgated to regulate money laundering particularly in mobile money are examined. It is found that Kenya's legal regime is inadequate and not fully compliant with FATF recommendations which provide for best practices for combating ML in mobile money. For instance, it was established that the country is yet to adopt an RBA approach for due diligence on the customer as recommended by FATF. Similarly, the mitigation mechanisms for dealing with ML in mobile money are not adequate as they do not envision the inherent vulnerabilities in MMT services usage and warrants revision to adequately mitigate ML risk in mobile money.

Chapter four examines the institutional framework on AML for MM in Kenya. National, regional and global organizations that form the framework of the AML institutional framework are examined. It is established that national, regional and global cooperation is crucial to deal with ML and that Kenya stands to benefit from its membership in these bodies by gaining technical assistance and evaluation and assessment of its AML regime. This important especially for mobile money which is now global service. The country thus seeks to benefit from mutual legal assistance in terms of technical expertise, sharing information and knowledge on the increasing number of trends and methodologies for laundering money using this platform.

5.3 CONCLUSION

In view of the foregoing findings it is evident that the AML institutional and legal regime for mobile money in Kenya is inadequate. In so far as MM is classified as a monetary institution like banks it is supposed to be uniquely regulated given its inherent vulnerabilities. Therefore, there is need to amend the AML legal regime for MM in Kenya to address loopholes which include lack of a harmonized framework to deal with money laundering in mobile money, poor implementation and oversight frameworks, poor detection mechanisms, ambiguous reporting thresholds and lack of compliance with AML measures by PSPs and agents. Also, there is need to address the investigative challenges that arise due to Mutual Legal Assistance (MLA) which include stringent and elaborate MLA procedures, conflict of laws and the cost of financial expertise which may hinder successful investigations of ML.

Further, mobile money has established itself as a pivotal tool in effecting international remittances due to its affordability and convenience. Nonetheless, lack of an enabling regulation to govern global money transfer remains a challenge in many developing countries and Kenya is no exception. Other challenges facing international mobile money transfer services include lack of a harmonized and transparent licensing or partnership criteria, lack of standard KYC and CDD procedures for AML purposes, low transaction and balance limits, data privacy and cyber security.

5.4 RECOMMENDATIONS

In view of the analysis on various inherent vulnerabilities in MM and the legal and institutional regime on ML for mobile money. The following recommendations are made: -

5.4.1 Risk Based Approach to CDD for Mobile Money

CBK should implement policies that provide for a ‘categorical’ approach which is risk based for different CDD measures applicable to the various needs pursuant to FATF Recommendation 10.

It is imperative that MMT services be declared a low risk service hence simplified CDD measures apply to it as recommended by FATF so as to encourage increased usage of MM and minimize cash based transactions.

Kenya's economy is made up of a combination of credit based and cash based economies. Credit histories are established as a matter of time when people use credit to purchase services and goods. A cash based economy on the other hand can be said to be "an economy in which more than 50 percent of the economic transactions in all sectors are made in cash and in which majority of the population are unbankable".²²⁸ Kenya is largely a cash based economy which amplifies its susceptibility to ML. Arguably, increased cash dealings combined with limited levels of financial inclusion makes it easy for PoC to gain access into the legitimate system.²²⁹ The three staged money laundering cycle of layering, placement and integration barely apply in an economy that is cash based save for integration hence facilitating ML faster and easier than in an economy that is not cash based.²³⁰ Cash dealings which are unmonitored and which are legal in many countries, Kenya included, pose a threat to ML due to inability to detect suspicious transactions.²³¹ Notably, cash based economies pose a challenge to the application of the Recommendations by FATF this is because unbanked population do not use formal financial institutions to effect payments or any other monetary transactions.²³² The risk based approach guards against disproportionate and unwarranted AML obligations which may discourage the unbanked population to use mobile money.

5.4.2. Granting investigative and prosecutorial powers to the Financial Reporting Centre (FRC)

²²⁸ <https://issafrica.s3.amazonaws.com/site/uploads/SitRep2012Oct.pdf> accessed 27 September 2019.

²²⁹ *Ibid.*

²³⁰ *Ibid.*

²³¹ <https://pdfs.semanticscholar.org/7fa1/4907c2e67442979a31bef1bd061e805f0c4b.pdf> accessed 27 September 2019

²³² *Ibid.*

Parliament should further amend the substantive law on AML in the country, POCAMLA to enhance the capacity of FRC to carry out simple inquiries and partner with other local and international investigative agencies to combat money laundering. Further, it should amend the law to clearly spell out the mandate of FRC regarding combating ML in MMT services.

Currently, the FRC is an administrative Financial Intelligence Unit (FIU) with no independent investigative or prosecutorial powers. This will ensure that money laundering cases particularly in mobile money are investigated and prosecuted independently and with the requisite expertise.

5.4.3 Enhanced detection mechanisms for ML through MMT

The Central Bank of Kenya should develop guidelines in collaboration with the various PSP providers on detection mechanisms that will enhance monitoring and detection of suspicious transactions in MMT services. This is including the requirement for training of PSPs, their agents and staff on detection mechanisms for purposes of reporting suspicious transactions in mobile money both for domestic and international money transfer services.

5.4.4 Reporting threshold for MMT services

Parliament should amend POCAMLA and the NPSR to provide for a reporting threshold that is reasonable to MMT services to do away with the vacuum in the law. This is because the reporting threshold for all financial institutions including PSPs as provided by is Kshs. 1M. PSPs are unlikely to reach this limit given that they have transaction limits which fall way below the required threshold.

5.4.5 Suspicious Transaction Reporting for MMT

Parliament should revise the law to define what constitutes a suspicious transaction for purposes of MMT services. This is because of the unique nature of the services offered this will enhance compliance by PSPs and their agents in reporting and monitoring suspicious transactions as it

will be specific on MMT services. Also, it will facilitate filing of suspicious transaction reports that are not defensive but meaningful for purposes of detecting movement of proceeds of crime.

5.4.6 Limitation on number of accounts

The CBK and Parliament should amend the legal regime on MM in Kenya that is NPSA and NPSR to provide for a limitation on the mobile accounts that an individual can open for purposes of receiving or transferring funds. This will aid to mitigate against multiple registrations and elusiveness.

5.4.7 Enhanced customer profiling and identification.

The Government of Kenya should develop a centralized database for identification purposes to avoid criminals using forged identity documents or those belonging to deceased persons. Reconciliation of identification records is crucial to enable proper verification of customers for due diligence purposes. Parliament should also come up with regulatory guidelines on mandatory SIM card registration to reinforce verification of customer's identity.

5.4.8 AML Training for MMT services

Parliament and CBK should provide policy guidelines for AML training for PSPs and enforcement agencies to boost enforcement and compliance. For instance, the requirement for exchange programs to benchmark with countries that have established an AML framework for MMT. This will enhance effectiveness of the various bodies tasked with combating money laundering.

5.4.9 Harmonized AML laws on MMT and consolidated supervisory body

Parliament should harmonize and the various pieces of legislation and guidelines promulgated to combat money laundering in financial institutions including PSPs. This will enhance

implementation and provide clarity in the law by getting rid of any grey areas that may create loopholes for criminals to take advantage of.

Further, CBK should establish a supervisory body that is mandated to oversee MMT transactions and to monitor any suspicious transactions that may arise thereon.

5.4.10 Create guidelines on the provision of international remittances through mobile money

CBK should develop guidelines specific to global money transfer through mobile money that will address customer identification management systems, due diligence procedures, licensing and partnership requirements, transaction and account balance limits, consumer protection, data privacy and AML frameworks on suspicious transaction reporting, detection mechanisms and enforcement mechanisms.

5.4.11 Assessment of effectiveness of AML systems

Government agencies in Kenya should establish mechanisms to not only record but to also keep detailed data on ML inquiries, execution and convictions, MLA and extraditions will aid in assessment of AML systems and procedures especially for mobile money transfers services.

5.4.12 Develop comprehensive MLA law

Parliament should come up with a comprehensive domestic law on MLA to assist not only in investigations and proceedings as is the case under POCAMLA but to also seek assistance on matters, detection mechanisms and training for AML to boost fight against money laundering.

5.4.13 Joining the Egmont Group of FIUs

Kenya's FIU, the FRC should consider joining the Egmont Group of FIUs in order to benefit from benefit from capacity building, understanding the typologies and methodologies used by

money launderers and exchange of financial intelligence information especially because money laundering is a global vice.

5.4.14 Create awareness on potential ML risks in MMT usage

The Central Bank of Kenya should come up with a sensitization programme to educate the mobile money stakeholders, participants and the general public on the ML risks that MMT services pose and the various mitigation mechanisms.

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