Analysis of Issues Affecting Collapsed Banks in Kenya From Year 2015 to 2016

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Abstract

The purpose of this study was an analysis of issues affecting collapsed banks in Kenya from the year 2015 to 2016. The stakeholders, creditors, depositors, and other stakeholders will incur huge financial losses in case the banking sector collapses. Furthermore, collapse of the bank may have drastic consequences for the nation's economy. The main bank which has failed in Kenya in that period are: - Dubai Bank, Imperial Bank and Chase Bank. The study used diagnostic research design and also used secondary methods of collecting data. The study adopted content analysis approach. Researchers quantified and analyzed issues affecting collapsed banks in Kenya from year 2015 to 2016 then make inferences about the different scholars work and journals. The study concludes the major issues that contribute to the collapse of most of the banking institutions in Kenya could be related to: insider lending, weak corporate governance practices, weaknesses in regulatory and supervisory systems, poor risk management strategies, lack of internal controls, and conflict of interest. The study recommends the government should reform the management and enforcement activities of central bank of Kenya by promoting transparency and accountability; refine banking laws so as to seal loopholes; banks need take up best practices of corporate governance to ensure stability, the Central Bank of Kenya through enacting rules and regulations can encourage banks to implement corporate governance practices and major shareholders, directors and members of staff should be subjected to normal objective credit assessment before disbursement of loans to them, as they are major contributors of non-performing loans.

Keywords

Corporate Governance, Non-performing Loans and Bank Regulatory Practice

I. Introduction

A financially healthy banking sector is vital prerequisite for economic growth and stability. Therefore, the assessment of banks financial environment is a fundamental goal for many stakeholders. Since the cost of bank fiasco is colossal, the ailing banks require quick action by supervisory authority to salvage them before they collapse (Emmanuel, 2009). Banks play a vital role in any economy through the assembling of savings from surpluses which is followed by funding deficit accounts. This capacitates industries or individual accounts for the purpose of boosting their production capacities (Obiero, 2010).

The financial sector in Kenya has upgraded significantly over the last few years subsequently making it the largest in East Africa. In contrast with other East African economies, the Kenyan banking industry is unique regarding its size and diversification. Despite Kenya having a variety of financial institutions and markets unlike in other regions, the industry has been faced with constraints in terms of growth due to factors such as non-performing loans and weaknesses in corporate governance. Consequently, a number of commercial banks in Kenya has fallen (Brownbridge 2010). The financial sector in Kenya continues to face various challenges including financial distress.

A. Dubai Bank

Dubai Bank Kenya was established in 1982. As of December 2013, the bank's total assets were valued at about US$34.4 million (KES 2.92 billion. In August 2015, the bank was placed under receivership by the Central Bank of Kenya (CBK) which appointed Kenya Deposit Insurance Cooperation (KDIC) as the receiver of Dubai bank. As reported by the CBK, the main contributory factors leading to the collapse of the Dubai bank was capital deficiencies and liquidity. The bank had been breaching its daily cash reserve ratio (CRR) requirement of 5.25 per cent (CBK, 2016).

The bank had failed to honor some of its financial obligations, such as paying off KES 48 million which it owed to the Bank of Africa Kenya. Despite the troubled bank being penalized by the CBK for non- compliance, the situation was not corrected. KDIC made a report to the CBK on August 24, 2015 concerning the financial conditions of Dubai bank. The report indicated that the bank couldn't be salvaged and went on to recommend the bank's liquidation. According to KDIC's report, liquidation was the only feasible option due to the Dubai Bank Kenya Limited's magnitude of weaknesses of (CBK, 2016).

2. Imperial Bank

Imperial Bank Limited was established as a Finance and Securities Company in 1992. In 1996, the bank commenced commercial banking services, after it was issued with a banking license by the Central Bank of Kenya. The bank's stock is privately held. The bank is a medium-sized retail bank that caters to both individuals as well as corporate clients. As of December 2013, its total asset base was valued at about US$498 million (KES 43 billion), with shareholders' equity of approximately US$66.2 million (KES 5.719 billion). At that time, the bank was ranked the 19th largest Kenyan commercial bank, by assets, out of forty-three licensed banks in the country (CBK, 2016).

In October 2015 the CBK put imperial bank under statutory management. The main reasons for receivership of imperial banks were unsafe and unsound business conditions and practices of transacting business in the bank. At the time imperial bank was taken over by KDIC the bank had about 53,000 customers with deposit estimated at KES 58 billion. On 21 June 2016, NIC Bank was appointed as asset and liabilities consultant for Imperial Bank (in receivership) by the Central Bank of Kenya. As such, NIC Bank became responsible for returning funds to the failed bank's deposit customers. NIC was also allowed to acquire some of the assets, deposits, and liabilities of Imperial Bank as soon as its receiver manager the Kenya Deposit Insurance Corporation starts liquidating the bank (CBK, 2016).

C. Chase Bank

Several businesses came together in 1995 and acquired a 60% stake in United Bank (Kenya). At that time, United Bank (Kenya) was in receivership and was under statutory administration by the Central Bank of Kenya. In 1996, the bank had been rebranded to Chase bank and it opened its doors once again. As of December 2015, Chase Bank is has an estimated asset valuation of approximately US$1.428 billion (KES 142 billion). At the same time, the shareholders' equity was valued at US$119.7 million (KES 11.9 billion) (CBK, 2016).

The CBK placed the bank under receivership on April 7, 2016. The major causes for placement were associated with failure to meet the statutory banking ratios and under-reporting of insider loans. Chase bank was unable to meet it financial obligation on April 2016 and was put under receivership of CBK. The insider loans stood at 13.62 billion Kenya shillings compared to the 5.72 billion Kenya shillings it reported. The main issue at chase bank was governance problem. The bank made large amount of loan to its directors of about 13.62 billion Kenya shillings. Auditors need to be firm in their opinions so as to mitigate the risks of bank failure as well as collapse as they are related to issues such as fiduciary responsibility and lack of governance of bank directors. With KCB as the receiver manager, the bank would re-open on 27 April 2016 (CBK, 2016).

II. Problem Statement

Banking is the focal part of the financial sector in every economy hence the strength banking system becomes crucial in ensuring growth as well as favorable economic stability. Banks are the main component of financial services sector of for ensuring favorable economic stability and growth Koch and McDonald (2013). Recent collapse of the three commercial banks in Kenya; Chase bank, Dubai bank and imperial bank shows that managers haven't assessed the bank risks or have not dealt with it properly. Therefore, the stakeholders, creditors, depositors, and other stakeholders will incur huge financial losses in case the banking sector collapses. Furthermore, collapse of the bank may have drastic consequences for the nation's economy. The complexity of the modern economy and its sheer size intensifies the importance of this issue hence the need to be carefully considered. This necessitated the study of issues affecting collapsed banks in Kenya from year 2015 to 2016.

III. Purpose of the Study

The purpose of this study was analysis of issues affecting collapsed banks in Kenya from year 2015 to 2016

IV. Objectives

1. To analyze the influence of corporate governance issues the collapsed banks in Kenya
2. To analyze the influence of non-performing loans issues on collapsed banks in Kenya
3. To analyze the influence of regulatory issues on collapsed banks in Kenya

V. Methodology

The study used diagnostic research design and also used secondary methods of collecting data. The study adopted content analysis approach. This is a research tool employed to determine the presence of certain concepts. Researchers quantified and analyzed issues affecting collapsed banks in Kenya from year 2015 to 2016 then make inferences about the different scholars work and journals. Through this method, researchers extend their critique as a positive evaluation of issues affecting collapsed banks in Kenya from year 2015 to 2016 as a healthy judgment but rapidly offer measures through recommendations.

VI. Results of Issues Affecting Collapsed Banks in Kenya

A. Corporate Governance Issues

Apart from the primary goal of profit realization, organizations also have other duties. The Private Initiative for corporate governance defines corporate governance as "the mechanism through which stakeholders (shareholders, creditors, employees, clients, suppliers, the government and the society, in general) monitor the management and insiders to safeguard their own interests" (Kihumba, 2010). In banking, corporate governance revolves around the manner in which banking institutions' affairs and business are managed by the board of administration as well as the top management, which in turn affects how the bank works out its objectives, policies and plans, taking into consideration making appropriate economic returns for founders and other shareholders, day-to-day work management, protection of the rights and interests of recognized stakeholders (shareholders and depositors), companies' commitment to sound and safe professional behaviors and practices which are in conformity with regulations and legislations, (Kihumba, 2010).

The subject of corporate governance is multi-faceted. A vital theme of corporate governance is associated with issues related to fiduciary duty as well as accountability. This revolves around advocating the implementation of mechanisms and guidelines necessary to ensure correct behavior and protection of shareholders. Another primary focus is the economic efficiency view. This view points towards the fact that corporate governance system need to aim at optimizing economic results, while placing great emphasis on the welfare of shareholders (Kihumba, 2010).

The stakeholders in the banking sector who play key roles regarding corporate governance range from shareholders, the management, the board of directors, the Central Bank of Kenya, external auditors to the Capital Markets Authority (CCG, 2004). Despite the numerous efforts made to streamline the banking sector, issues have persisted as many banks have been put under receivership or liquidated. Such collapse was linked to weak internal controls as well as poor governance and management practices.

There have been reasons put forward in an attempt to explain the collapse of some of Kenya's banking institutions. The Centre for Corporate Governance, (2004) enumerated the following reasons as being the central contributors to this undesirable phenomenon; poor risk management strategies, insider lending and conflict of interest, lack of internal controls, weak corporate governance practices and weaknesses in regulatory and supervisory systems.

The Board of directors of an organization is an essential mechanism to monitor manager's behavior and to advise them. To improve the performance of a firm at the various levels, it is crucial to limit the board size to a certain level. It has been observed that the benefits that arise from increased monitoring by large boards can be outweighed by the issue of poorer communication and cumbersome decision–making. Dubai bank by the time it was collapsing had just three directors which compromised its monitoring. In this case, the size of the Board plays a significant role on the performance of every prospering organization. BODs are the highest and main decision-making body of bank and they are primarily responsible for the fate of their organizations

Another corporate governance issues that caused the collapse of banks in Kenya was the structure and type of a bank's ownership. There are two ownership structure types; concentrated ownership, and dispersed ownership to outside investors (Surya 2005). If ownership is concentrated in some families or business group, the majority shareholder has more control. This may lead to a different treatment between shareholders as harm is likely to come to the minority shareholders. Ownership concentration is determined by the number of share that is held by three biggest shareholders (Goldstein and Turner, 2016). Collapsed banks had a high ownership concentration which led the interests of minority shareholders not been taken care of. As such, ownership concentration factor is among the determinants of collapsed banks.

Other issues that affected the collapsed banks were transparency and disclosure issues. Transparency is an integral component of corporate governance. Since higher transparency reduces the information asymmetry between a firm's management and financial stakeholder's (equity and bondholders) there is mitigation of the agency problem in corporate governance (Sandeep 2012). The concept of Bank transparency is quite broad in its scope as it refers to the quality as well as quantity of public information available on a bank's risk profile and to the timing of its disclosure, including the bank's decisions both past and current and the actions as well as its future plans (Sandeep 2012). Chase bank underreported its non-performing loans, had fishy special purpose vehicle accounts which siphoned billions of money from the bank. Chase bank chairman, chief executive officer and four senior managers used several special purpose vehicles (SPVs) (Riverside Mews Limited got fake Islamic lending contracts) to defraud the bank of $149 million, leading to its collapse. The amalgamation of the purported personal or private properties in these third party SPVs indicates that the entities were not necessarily set up for a 'special purpose' but apparently intended to defraud the bank. Mr. Khan, through the SPVs, bought luxury properties in the US, the Kenya Coast and Dubai. He also purchased luxurious vintage vehicles. Furthermore, there was lack of clear demarcation between properties belonging to Mr. Khan and the ones that belong to the Chase Bank which points towards poor corporate governance. Dubai bank did not disclose its safety net operations as required by central bank until it collapsed.

The board of the directors of the bank brought to the attention of the central bank the improper banking practices plaguing it that warranted immediate remedial action so as to safeguard the interest of creditors and depositors. The imperial bank shareholders were negligent and reckless in their fiduciary duty. They had been awarding themselves dividends amounting to millions of dollars regardless of the precarious financial situation of the bank. Forensic investigations by FTI Consulting revealed several breaches of financial duty on the directors' part leading to massive losses.

Finally reliability of financial reporting affected the collapsed banks in Kenya. The accuracy and reliability of the financial reports issued by management impacts the perception of the firm by all other stakeholders as well as prospective investors. The financial reporting of the collapsed banks was less transparent and credible. This therefore makes the financial reporting element of corporate governance harder to be assured in privately held firms. Audit committees and external auditors are the most important instruments available for ensuring this corporate governance variable. Hassan Zubeidi the founder and chairman of Dubai bank had accumulated substantial wealth through what was termed as irregular insider lending deals that he had covered up by manipulating books of accounts. This could have been exposed by auditors and saved the bank from collapse. A forensic report by Deloitte and Touche who was Chase Bank's auditors for more than 20 years revealed that Mr. Khan (Chairman) and Mr. Kabui (managing director) were drawing funds from the lender and directing them to entities they co-owned. Such funds were then utilized in the purchase of prime real estate and the construction of properties in Nairobi and abroad. The CBK forcefully seized properties worth Sh7.9 billion camouflaged as Islamic joint ventures by Mr. Khan and Mr. Kabui, and charged them to the bank, paving the way for the re-opening of Chase Bank.

While Chase blamed the accounting surrounding the bank's Islamic banking assets, more grave consequences point towards governance problems. To illustrate the severity of these management issues, we are told that the bank made a staggeringly large amount of loans to its directors, an average of KES 1.35 billion per director (USD 13.5 million which is not a routine staff and associate credit. Chase had a loan program for staff. Its average loan size was KES 1.9 million (USD 19,000). How could an SME bank, a financial inclusion flag bearer, allow its directors to lend tens of millions of dollars to themselves?! In a recent interview, three leading Kenya bank executives decried the lack of governance and fiduciary responsibility of bank directors in the country and called upon auditors to be firm in their opinions to mitigate the risk of bank failures and avoid panic. Deloitte and Touche gave a qualified opinion of the banks financial records in 2015.

Chase Bank's chairman Mr. Zafrullah Khan and the group managing director Mr. Duncan Kabui stepped aside as the concerns over the credibility of the bank's financials become more widespread. The lender restated its financial results revealing that it had under-reported the insider loans by Sh8 billion. The restated financial results published showed that insider loans money advanced to directors, shareholders, associates and employees of the bank stood at KES 13.62 billion.

Separation of office of board chair from that of CEO seeks to reduce agency costs for a firm. Kajola (2008) found a positive and statistically significant relationship between performance and separation of the CEO and the office of board chair. Yermack (1996) equally found that firms are more valuable when different persons occupy the positions of board chairman and CEO. The results of the study of Klein (2002) suggests that boards structured to be more independent of the CEO are likely to be more efficient in the monitoring the corporate financial accounting process and therefore more valuable. This was not the case with the Imperial Bank. Abdulamek Janmohamed was the founder, managing director, chairman and principal shareholder of the Imperial Bank. Abdulamek Janmohamed had on many occasions started and authorized irregular disbursements of large amounts of money that belong to the bank, which was concealed from the Board. Together with other managers, it is claimed he carried out the fraud worth KES 45 billion. Mr. Janmohamed had been running a scheme of fraudulent and illegal disbursements with certain accomplices, within and outside the Bank, without the knowledge or consent of the Board.

The fallout between the Chairman of Dubai Bank of Kenya, Zubeidi and managing director Ms. Said revealed the rot that had been present at the bank. She had been fired in November 2012 and went on to claim that weak governance structures nurtured by the chairman Mr. Zubeidi had exposed the bank to extensive fraud and theft of funds.

B. Non-Performing Loans

There is no set global standard to define NPL uniformly at the practical level. A non-performing loan is a loan that is in default or close to being in default. A loan is nonperforming when payments of interests and principal are past due by 90 days or more, or at least 90 days of interest payment have been capitalized, refinanced or delayed by agreement, or payments are less than 90 days overdue, but there are other good reasons to doubt that payment will be made in full (IMF, 2009). NPLs are often treated as undesirable outputs or costs to loaning banks which decrease the bank's performance.

The central bank of Kenya defines NPLs as those loans that are not being serviced as per loan contracts and expose the financial institutions to potential losses (CBK, 2016). It is important to note that non-performing loans refer to accounts whose principal or interest remains unpaid 90 days or more after due date. According to the Central Bank of Kenya Supervision Report (CBK, 2016), the level of non-performing loans has been increasing steadily in Kenya. The high level of non-performing loans persists as an issue of primary supervisory concern in the country.

Non-Performing loans are widely associated with bank failure as well as financial crises for commercial banks. Due to the nature of their business, commercial banks expose themselves to the risks of default from borrowers. The eradication of NPL's is a necessary condition to improve the economic status and stability of the banking sector. If the Non-Performing loans are kept existing and continuously rolled over the resources are locked up in an unprofitable sector; thus hindering the economic growth and impairing the economic efficiency.

Bank failures in Kenya can also be attributed to NPLs which is due to the interest rate spread. According to (Fafack 2005), controlling NPLs is very important for both the performance of an individual bank and the economy's financial environment. Due to the nature of their business, commercial banks expose themselves to the risks of default from borrowers. Prudent credit risk assessment and creation of adequate provisions for bad and doubtful debts can cushion the bank's risk.

According to Kioko (2008), non-performing loans are closely associated with banking crises. Fafack (2005) also links the Japanese financial commercial banks expose themselves to the risks of default from borrowers. Prudent credit risk assessment and creation of adequate provisions for bad and doubtful debts can cushion the bank's risk. However, when the level of non- performing loans (NPLs) is very high, the provisions are not adequate protection.

During the past few years, the collapsed Kenyan banks have struggled in the red, with business profits swallowed by the disposal of NPLs. Chase Bank reports showed that the Bank ran a loss of KES 742 million. This happened even though it had made a profit of KES 2.3 billion the previous year. The statements also revealed that non-performing loans had risen from KES 3 billion in 2014 to KES 11 billion in 2015. The bank's problems were mostly related to KES 16.6 billion "problematic" insider loans whose chances of recovery were doubtful at the time. The unsecured loans comprised KES 8.7 billion suspicious loans to companies owned or related to some directors and KES 1 billion personal loans to some directors.

The KES 742 million loss of the Chase Bank was attributed to non-performing loans and this, in turn, has been blamed on weak lending policies and management failure. To strengthen the lending policies, CBK Governor Dr. Patrick Njoroge said that CBK would implement stringent checks including IT audits that will ensure a reduction in the non-performing loans.

In 2013, after several capital injections from investors, Chase bank embarked on luring Kenyans and corporates with easy to get loans to the extent that one would get a KES 1 million (USD 10,000) loan with only six-month bank statement from another bank. No other collateral was necessary. This led the bank to issue many unsecured loans, and the rate of loan repayment default began to bite. Chase bank began to collapse.

According to a study by Waweru and Kalani (2009), most of the bank failures were caused by non-performing loans. Arrears affecting more than half the loan portfolios were typical of the failed banks. Many of the bad debts were attributable to moral hazard: the adverse incentives on bank owners to adopt imprudent lending strategies, in particular, insider lending and lending at high-interest rates to borrowers in the riskiest segments of the credit markets.

According to Kiayai (2003), the single biggest contributor to the bad loans of many of the failed local banks was insider lending. In at least half of the bank failures, insider loans accounted for a substantial proportion of the bad debts. Most of the larger local bank failures in Kenya, such as the Chase Bank, Imperial Bank and Dubai Bank, involved extensive insider lending, often to directors and directors associates.
Chase Bank by the time it collapsed its financial results published showed that insider loans money advanced to directors, shareholders, associates and employees of the bank stood at KES 13.62 billion. The companies which siphoned Chase bank are owned by the bank chairman, over 90 percent of the ownership of these enterprises was the chairman, and 10 per cent was the Bank managing director.

Imperial Bank chairman Abdulmalek Jamohamed incorporated companies such as WE Tilley Ltd, Metro Petroleum Ltd, Jade Petroleum Ltd and Adra International Ltd through proxies. These companies benefited from fraudulent inside lending from the imperial bank up to a tune of KES 45 billion. The companies acquired assets using money that was fraudulently or unlawfully obtained from the bank.
The threat posed by insider lending to the soundness of the banks was exacerbated because many of the insider loans were invested in speculative projects such as real estate development, breached large loan exposure limits, and were extended to projects which could not generate short-term returns, with the result that the maturities of the bank's assets and liabilities were imprudently mismatched.

The second major factor contributing to bank failure was the high-interest rates charged to borrowers operating in the high-risk segments of the credit market. There were weak loaning controls being deployed by banks despite their aggressive selling of bank loan known as "loan hawking" thus resulting in high non-performing loans. This involved elements of moral hazard on the part of both the banks and their borrowers. In Kenya by the time these banks were collapsing the interest rate was a high as 28% per annum. High-interest rate has resulted to increase non-performing loans which translated to the bank problem. In 2016 the Kenya government capped the interest rate at 14% due to public outcry.

According to Fafack (2005), non-performing loans are mainly caused by an inevitable number of wrong economic decisions by individuals and plain bad luck (inclement weather, unexpected price changes for certain products, etc.). Under such circumstances, the holders of loans can make an allowance for a normal share of nonperformance in the form of bad loan provisions, or they may spread the risk by taking out insurance. The problem of NPL's is widespread.

In their study, Kiayai, (2003) state that the growth of bank credit in Kenya and its prudential implications are an ever-present item on the agenda of banking supervisors since most banking crises have had as a direct cause the inadequate management of credit risk by institutions. They further assert that even though bank supervisors are well aware of this problem, it is however very difficult to persuade bank managers to follow more prudent credit policies during an economic upturn, especially in a highly competitive environment. They claim that even conservative managers might find market pressure for higher profits very difficult to overcome.

C. Regulatory Issues

As the definition proposes, organizations have a broad spectrum of entities to be accountable to, concerning their mission, and as such, they need supervision and regulation. In Kenya, the banking sector is regulated and supervised by the Central Bank of Kenya, which ensures that banks are governed according to the Banking Act (Chapter 488 of Kenya constitution). Other constitutional acts that provide governance regulations applicable to banks are; The Companies Act, The Capital Markets Authority Act and Nairobi Stock Exchange (NSE) Regulations and the Penal Code.

The regulation of banks is the responsibility of the Central Bank of Kenya. The Banking Supervision department carries out the function of supervising banks to ensure the following; liquidity, solvency, and proper functioning of a stable market based banking system. Further to this, audited performance of the banking sector is measured in terms of capital adequacy, asset quality, liquidity, and earnings based on the Central Bank internal rating system. Under section 19 of the Banking Act in Kenya, an institution shall maintain a minimum holding of liquid assets as the Central Bank may from time to time determine. Currently, an institution is required to maintain a statutory minimum of 20% of its deposit liabilities with the Central Bank.

Without adequate regulation, financial systems can become unstable, triggering crises that can devastate the real economy (Spratt 2013). Given the main purpose of finance is to facilitate productive economic activity the aim of regulation is to maintain financial stability and to promote economic growth. This is a delicate balancing act, as too great a focus on security could stifle growth, while a dash for growth is likely to sow the seeds of future crises.

Section 43(2) of the Kenya Deposit Insurance Act, 2012 requires CBK to appoint the KDIC as a receiver of a bank if, among other reasons, it is in an unsafe or unsound condition to transact, a bank is likely to fail to meet its financial obligations, a bank has substantially insufficient capital or if there is a violation of any law or regulation.

In 1988, the Basel Committee issued the Basel I Accord which assesses banks capital adequacy requirements in the context of the credit risk they face and advocates risk-based supervision. Basel I, therefore, emphasized a set of minimum capital requirements for banks to address credit risk. In 2004, the Committee issued the Basel II Accord which contained further recommendations on banking laws and regulations. The Committee attempted to accomplish this by setting up severe risk and capital management requirements designed to ensure that a bank holds capital reserves appropriate to the risk the bank exposes itself to through its lending and investment practices. The Accord was to be implemented from 2007 by G10 countries, with more time given to developing countries, as they were yet to satisfy the prerequisites for the new accord. Basel II has three pillars: Pillar I on minimum capital requirements; Pillar II on the supervisory review process; and Pillar III on market discipline. In December 2010, the Committee announced proposals dubbed Basel III which is currently being reviewed for regulatory and supervisory suitability to financial systems (Centre for Corporate Governance 2014). These proposals include the strengthening of capital adequacy and liquidity requirements as well as countercyclical macro prudential measures.

The CBK continues to regulate banks mainly based on Basel I but was in the process of formulating a policy position on Basel II implementation (KPMG 2012). New guidelines that came into force in January 2013 contain some features of Basel II and Basel III on capital adequacy requirements (Obiero 2010). Overall, Kenya has endeavored to implement the Basel accords for ensuring the financial stability of the country's financial sector. The Kenyan banking system has continued to record compliance with the minimum capital and liquidity prudential requirements.

CBK has focused more on macroprudential regulation which relates to factors that affect the stability of individual banks and less so on macroprudential regulation which relates to factors which affect the stability of the financial system as a whole. In the latter case, changes in the business cycles may influence the performance of banks, hence the Basel III proposal for countercyclical capital changes to provide the way forward for future macroprudential regulation, which should take into account the growth of credit and leverage as well as the mismatch in the maturity of assets and liabilities. Murinde (2012) however argues that review of macroprudential regulations should encompass the broader aspects of financial services regulation, such as depositor protection or deposit insurance and the safety of the payments system which has received attention from CBK.

The receivership of Dubai Bank was due to several reasons. First, they were deteriorating cash reserve ratio. The second was the failure of the bank to honor its financial obligations. The third was violation of banking laws and regulations such as maintaining adequate capital and liquidity ratios as well as provisions for non-performing loans and weak corporate governance structure. Dubai Bank was also cited for failing to honor customer instructions to complete transactions totaling KES 41 million and owed the Bank of Africa KES 48 million from a forex transaction. The CBK officials have since been implicated in aiding top administrators of both lenders to conceal the scams.

The regulator had been closely monitoring Dubai Bank's daily cash reserve ratio from July 14, 2015, when the bank began breaching its daily cash reserve ratio requirements. The regulator also said its attempt to get the small lender to redress the situation had failed. Instead, there had been "no compliance by the bank, and its cash reserve ratios have continued to deteriorate". "The non-compliance with the cash reserve ratios has to date attracted a total penalty of KES 5,395,721.03. Owing to the consistently deteriorating cash reserve ratio position of Dubai Bank and its failure to honor financial obligations, including KES 48.18 million due to Bank of Africa Kenya Limited, the CBK is of the considered opinion that the bank will most likely fail to meet its financial obligations in the normal course of business," the regulator said in its decision to put the lender under receivership.

Imperial Bank Limited was a piggy bank for Central Bank employees who benefited by allowing the bank to carry on years and years of suspicious transactions. To hide this, the regulator's team worked with the management team at Imperial Bank Limited on doctoring the exit reports in ways that led to the fraud being undetected for long. Rogue central bank officials conspired with Imperial Bank Limited officials to steal from depositors. CBK officers were compromised not to inspect books the central bank officials who are the regulator of the banking industry in Kenya's conspired in a multi-year fraud that cost the Imperial Bank Limited $380 million in bad loans and customer deposits.

The funds were swindled from the Imperial Bank by the late Abdulamek Janmohamed, the principal shareholder of the bank he started in 1992 and served as managing director until his demise in September 2015. Together with other managers, he carried out the fraud in collusion with among others, former governor of central bank of Kenya, Prof. Njuguna Ndung'u. The governor of central bank Prof. Ndung'u and other officials in the central bank was given assorted favors by top management of the bank to aid in circumventing industry regulations in their dealings. The Imperial Bank provided gifts to central bank officials as well as loans that were often never repaid. The said officials also dangled favors for employment for relatives or acquaintances. Prof. Ndung'u was said to have had visas sponsored for visits to Dubai while his wife was sponsored for personal holidays to exclusive resorts in Thailand. The relationship between senior managers of the collapsed Imperial Bank and Central Bank of Kenya (CBK) officials was too intimate to allow proper regulation of the bank

In 2012, a whistleblower notified central bank about funds that were being moved from Imperial Bank into fictitious accounts on a monthly basis, asking the regulator to "act with speed" but no action was taken. The central bank failed to act on whistleblower reports of unethical practices at the Imperial Bank gave the perpetrators greater leeway to continue stealing from depositors.

Imperial Bank top leadership and central bank staff conspired to ensure that Imperial Bank MD Abdulmalek Janmohamed remained the sole executive director by blocking the application of Anwar Hajee after the board expressed the concerns that perhaps the late Janmohamed had too much latitude at the bank, which was risky. According to the CBK prudential guidelines, non-executive directors are not allowed access to core banking system to facilitate self-verification.

Furthermore aided by central bank officials, it is claimed, Janmohamed founder of Imperial bank deployed a software reporting program which ensured fictitious, unlawful and fraudulent accounts were created and used to defraud depositors. These were not reflected in the financial statements, and the bank's true financial position was understated. There was also the issue of falsifying bank accounts to meet the recommended non-performing loans and provisioning figures. Bank reports were falsified, data was deleted or heavily edited on Central Bank of Kenya report and board papers, sometimes surpassing between KES 8 billion to KES 5 billion per quarter by deleting between 20-25 accounts from the list of top 50 borrowers and presenting cooked loan balances for other accounts.

On April 7, 2016, Chase Bank was placed under receivership by the Central Bank of Kenya. Central Bank of Kenya placed Chase Bank under receivership following liquidity problems even as the Chairman Zafrullah Khan and Managing Director Duncan Kabui were forced to resign after giving conflicts accounts of the financial state of the bank within a week. This was mainly due under-reporting of insider loans and not meeting the statutory banking ratios. Chase Bank had under-reported insider loans by a whopping KES 8 billion. The financial results showed that insider loans money advanced to directors, shareholders, associates and employees of the bank stood at KES 13.62 billion. CBK appointed the Kenya Deposit Insurance Corporation to assume the management, control and conduct of the affairs and business of the institution. Later on, the Chase Bank re-opened on 27 April 2016 with KCB as the receiver manager.

VII. Conclusion

The research focused on the determinants that led to the collapse of banking institutions in Kenya. The study concludes that on the whole, these are attributed to or related to weak corporate governance practices, poor risk management strategies, lack of internal controls, and weaknesses in regulatory and supervisory systems, insider lending, ineffective laws, poor financial sector oversight, a base sector culture and overbearing political and executive corruption and conflict of interest among others.

The study concludes that corporate governance plays a vital role in the success and prosperity of the banks. Weak corporate governance has resulted in the failure of the banks in Kenya. Banking supervision cannot function properly if there is no correct corporate governance. Improving governance is an important way to promote financial stability. The effectiveness of bank's internal governance arrangements has very substantial effect on the ability of a bank to identify, monitor and control its risks

The study concludes that the main factors affecting non-performing loans include the speedy process of evaluating loans mainly due to external pressure, the high-interest rates charged, insider lending and owner concentration among others. The quality of bank's loan has more to do with risk and safety in banking system than any other aspect of the banking business. Many borrowers in collaboration with bank management are involved in non-performing loans leading to financial theft of banks which ended up collapsing.

The study concludes that the Central Bank of Kenya, besides regulating the banking sector is charged with the responsibility of supervising banks and raising the red flag at first sight of danger. The bank's supervision department of the Central Bank has not discharged this mandate effectively. A corollary of this objective requires bank supervisors to minimize moral hazard behavior, connected lending, conflicts of interest, fraud and mismanagement through effective regulation backed by a good legal regulation framework. Despite the existence of this banking act Banks continue to lend more than this percentage of directors and insider lending which involves giving loans to bank officers without adhering to the rules as per the Central Bank regulations.

VIII. Recommendations

1. The government should promote transparency and accountability in the management and enforcement activities

of the central bank of Kenya. Governments must make enforcement more transparent and accountable by publicly reporting this information.

2. Governments should work to continuously refine laws so that loopholes cannot be exploited. This will lead to close loopholes, address new challenges and promote global coherence.
3. For banks to have the stability, they should embrace best practices of corporate governance which will ensure that shareholders wealth is looked after in the best way possible, that adequate risk management measures are put in place and that standards are not only in writing but that they are practiced on a day to day basis.
4. The central bank of Kenya has to encourage banks to implement corporate governance practices through enacting rules and regulations.
5. The Central Bank of Kenya being the regulator of banking sector should ask from individual commercial banks on a quarterly basis a calculation of loans that have migrated from good book to bad book to avoid a situation where a commercial bank can have a compounding effect huge bad loan.
6. Major shareholders, directors and members of staff should be subjected to normal objective credit assessment before disbursement of loans to them, as they are major contributors of non-performing loans.

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