NR & CO. QUARTERLY

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EDITOR'S NOTE

Dear Reader,

All that is well ends well. We have had such an immaculate year run and indeed from our end, this piece is the icing on the cake. Well, most of you might dispute the 'well' and 'immaculate', one thing is for certain - no matter the highs and lows this year, it is only prudent to hang on to the highs. Doing so, will most definitely claim into being good tidings in the new year.

In this fourth quarter, we shed some light on the innings of the Standard Chartered Marathon. I would like to seize that opportunity and remind you to stay active throughout the festivities.

A man is truly his law, under the legislative updates we highlight activities from the regulatory sector as well as the Kenya Information and Communications (Amendment) Bill, 2022 which seeks to enable persons operating a telecommunication system or providing a telecommunication service to engage in any other business. It also provides for the separation of such other businesses from the telecommunication business.

In the spirit of Christmas, we take time to express our heartfelt gratitude for journeying with us this year and look forward to being of continued stellar service and support in the coming year.

In the Contributor's Platform, Brian Njoroge takes us through digital assets and their regulation in Kenya, while Robert Otieno pens his thoughts on how established organizations can separate the functions of different internal departments but do so in a manner that supports the continued growth and success of the business.

Last but not least, it is my 'Santa' plea that we will enjoy the festivities and give honor to the year that 2022 was. A Merry Christmas to you and your loved ones and a blissful and prosperous 2023!

J. M Kamenju
Editor

The Firm

This quarter members of the Firm took part in the Nairobi Standard Chartered Marathon. This marks the 20th Edition of this event that began in 2003. Since then, it has been a hallmark event in Nairobi athletics and an opportunity to raise funds for worthy causes aimed at tackling inequality and promote economic inclusion, especially for the younger generation. The marathon is the largest single-day sporting event in Kenya attracting thousands of participants.

The Standard Chartered Marathon through the Future Makers Initiative has raised funds for several charities including: contributing to the Women in Technology Incubator Program and supporting efforts to increase literacy in the country through the KipKeino Foundation.

For more information visit https://www.nairobimarathon.com/

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Legislative UPDATE

A number of activities have been undertaken in the legislative and regulatory sector this quarter. From a regulatory viewpoint, we highlight hereunder the crowdfunding regulations as well as the 29th Monetary Policy Committee Report of October, 2022. We also assess the Kenya Information and Communication (Amendment) Bill, 2022.

THE CAPITAL MARKETS (INVESTMENT-BASED CROWDFUNDING) REGULATIONS, 2022

The Capital Market (Investment-based Crowdfunding) Regulations, 2022 (the "Regulations") were formulated pursuant to section 12 (1) (d) of the Capital Markets Act (Cap 485A of the Laws of Kenya) which provides for the power of the Cabinet Secretary for the National Treasury to issue regulations on the operations of body corporates or persons dealing with capital market instruments.

Crowdfunding is defined under the Regulations as 'the act of raising money from many individuals or entities to either finance a project or business through a crowdfunding platform'. It thus involves raising of funds through a platform in exchange for the issuance of an investment instrument.

Accordingly, the Regulations apply to an investment-based crowdfunding platform established, maintained or operated in Kenya. Where a crowdfunding platform operator is located outside Kenya/ where the platform is located outside Kenya, the Regulations would apply to such a person or platform if the operator or their representative promotes crowdfunding activities either directly or indirectly in Kenya.

Crowdfunding platform operators are required to be licensed by the Capital Markets Authority (the "Authority"). In that regard, persons who intend to be licensed as operators are required to apply to the Authority for licensing through lodging of the prescribed application forms together with inter alia:

- evidence of their financial soundness and capital adequacy;
- rules for the operation of their business setting out the planned activities and conduct of its platform users;
- details of the organization structure;
- evidence of adequate human resources with adequate knowledge and competence on crowdfunding business;
- adequate risk management framework that includes details of fraud detection and prevention measures;
- the proposed standard offer document to be used;
- data protection policy; and
- policy on prevention of anti-money laundering and terrorism financing

One is eligible to be licensed as a crowdfunding operator if they: (1) are a company limited by shares, (2) have a minimum paid up share capital of Kenya shillings Five Million (Kshs.5,000,000.00) and (3) have a minimum liquid capital of Kenya shillings Ten Million (Kshs.10,000,000.00) or 8% of their liabilities, whichever is higher.

Below are some of the salient provisions of the Regulations: -

Eligible Issuers

- Micro, small or medium enterprises incorporated in Kenya with a minimum of two years' operating track record and a good corporate governance record; and
- Start-ups with a good operating track record and a good corporate governance record.

Prohibited issuers

- Public listed companies;
- Entities with a poor governance record;
- Entities that intend to use the funds raised to provide loans or invest in other entities; and
- Any other entity as may be specified by the Authority

Fund Raising Limits

- Aggregate amount within a twelve months' period is a prescribed maximum amount of Kenya Shillings One Hundred Million (Kshs.100,000,000.00).
- One may however apply for a no—objection letter from the Authority where they wish to raise more than the prescribed maximum within the twelve months' period.

Eligible Investors

- Sophisticated investors (such as banks, insurance companies and collective investment schemes); and
- Retail investors (investors who are not classified as sophisticated investors) subject to investment limits prescribed by the crowdfunding platform operator but up to a maximum of Kenya Shillings One Hundred Thousand (Kshs.100,000.00)

persons operating investment-based crowdfunding platforms prior to commencement of the Regulations are required to obtain a licence within twelve (12) months after the commencement of the Regulations.

To this end, we note the Regulations were published through Legal Notice No. 175 of 2022, Kenya Gazette Supplement No. 148 of 30th September, 2022

THE 29TH BI-ANNUAL REPORT OF THE MONETARY POLICY COMMITTEE

The Monetary Policy Committee of the Central Bank of Kenya is mandated to submit a report of its activities to the Cabinet Secretary of the National Treasury and Planning at least once every six months. The 29th Monetary Policy Committee Report (the "Report") outlines the Committee's activities in the six months to October, 2022.

Below are some of the key economic indicators set out in the Report:

Overall Inflation

Increased to 9.6% in October 2022 from 7.1% in May

Largely owing to increased food and energy prices

Food Inflation

Rose to 15.8% in October, 2022 from 12.4% in May

Largely due to prices of maize and milk [supply reduced owing to depressed rains] & edible oils and wheat products

Fuel Inflation

Increased to 12.6% in October, 2022 from 9.0% in May

Attributed largely to the scaling down of the fuel subsidy, increases in electricity prices & transport costs

Diaspora Remittances

Averaged USD 324.4 Million per month in the 6 months to October, 2022

Compared to USD 341.6 Million per month in the 6 months to April, 2022

CBK Foreign Exchange Reserves

Stood at USD 7,271 Million

Being 4.10 months of import cover

Balance of Payments

Attributed to increase in imports which in turn is largely attributed to an increase in international oil prices

Current account balance in the 12-months to Oct 2022 was a deficit of USD 6,182 million (5.5 % of GDP)

Compared to a deficit of USD 5,739 million (5.3 % of GDP) over a similar period in 2021

Commercial banks liquidity and capital adequacy ratios

Average of 52.3% and 19.0% in October 2022

Above the minimum statutory limits of 14.5% and 20.0% respectively

Ratio of gross non-perfomin g loans to gross loans

13.8% in October 2022

Decreased from 14.1% in April 2022

Main sectors with increased NPLs:
- Manufacturing, energy, water, trade, & agriculture

Weighted average lending rate

Increased to 12.4% in October 2022

From 12.2% in April 2022

Weighted average deposit rate

Increased to 7.0%

From 6.6%

KENYA INFORMATION AND COMMUNICATIONS (AMENDMENT) BILL 2022

The Kenya Information & Communications (Amendment) Bill 2022 (the "Bill") seeks to amend some sections of the Kenya Information and Communications Act, 1998 to the effect of providing for separation of other business (es) from telecommunication business, quality of service to consumers and expansion of the objectives of the Universal Service Fund. The Bill has matured but has yet to undergo the entire legislative process.

Licensee may operate other business

The Bill provides that persons licensed to operate or provide telecommunication services are permitted to engage in any other business provided that they:

1. obtain relevant licences from regulators of the industry or sector ventured into;
2. legally split or separate the telecommunication business from the other businesses; and
3. provide separate accounts and reports in respect of all businesses carried out

Non-compliance with the provisions is an offence which is set out to attract a fine not exceeding Kenya Shillings Ten Million (Kshs.10,000,000.00) or an imprisonment for a term not exceeding two (2) years or both such fine and imprisonment.

Upon assent to and commencement of the provisions of the Bill, persons operating other businesses are required to comply within six (6) months of *the coming into force of the said provisions.

Compensation for Call drops

The Bill also introduces compensation for call-drops meaning that a licensee is liable to credit a consumer, who initiates a call that gets cut out after a connection, by ten (10) shillings worth of airtime for each call drop within its network for a maximum of three (3) call drops per day.

However, if the call gets cut out due to third party interference on the licensee's connection line, then the licensee shall not be liable to compensate a consumer.

The Universal Service Fund

The Bill proposes to expand the object and purpose of the Universal Service Fund to include, inter alia, promotion of the availability of quality services at just, reasonable and affordable rates

case Highlights

This quarter we highlight the following cases:

Omondi Justus Ranga'nga & 28 Others vs KCB Bank Kenya Ltd & Banking, Insurance and Finance Union (BIFU) ***(Judgment delivered on 30th November, 2022)***

Employers are mandated by law to treat permanent and contractual employees performing similar work fairly - "equal pay for equal work done"

Omondi & 28 Others ("Claimants"), all former employees of KCB Bank Kenya Ltd (the "Respondent"), moved to Court to seek, inter alia: a declaration that work practices by the Respondent were discriminatory towards contract clerks, a declaration that the Respondent violated the principle of equal pay for equal work as well as a tabulation and compensation of lost income which included underpaid salary, underpaid overtime, lack of pension and annual leave not taken.

The background to the matter is that on different dates between the years 2013-2016, the Claimants entered into a contract with the Respondent as contract clerks and were deployed to work at the Contact Centre [Kencom House] under the Customer Experience Department. The Department later on in 2018 became a division.

The Claimants were tasked to carry out clerical tasks at the front office and back office and this, they were to do together with the permanent clerks in their assigned division. Despite them being contract clerks, their job description was similar to that of permanent clerks. Additionally, the two groups of clerks were issued and evaluated with a similar Balanced Score Card (BSC) for similar job responsibilities. Unlike permanent clerks, contract clerks did not enjoy terms and conditions incorporated in the negotiated Collective Bargaining Agreement ("CBA").

The claim on discrimination was based on numerous factors including:

	Contract Clerks	Permanent Clerks
Monthly Gross Wage/ Min. starting basic salary	Kshs. 32,481.00	Kshs. 67,157.00
Annual Salary Increment	N/A	At least 5%
Overtime	About Kshs.274.22 per hour – Normal rate	About Kshs.614.00 per hour – Normal rate
	About Kshs.365.63 -Double hourly rate	About Kshs.820.00 -Double hourly rate
Overtime Increment	N/A	Rate subject to annual increment
Annual Leave Days	24 days	28 days
Annual Leave Allowance	N/A	Kshs.10,500.00
House Allowance	Exempted	Kshs.11,800.00
Medical Cover Limits	Kshs.300,000.00 - Inpatient	Kshs.650,000.00 - Inpatient
	Kshs.50,000.00 – Outpatient	Kshs.130,000.00 – outpatient
	• No medical cover in their pre-vious engagements – 2014, 2015 and 2016; • Until 2019, contract clerk spouses were not allowed to use medical cover	
Pension Scheme	No contributions made	Contributions made

In February 2019, the Claimants raised complaints about the ongoing discrimination with their employer but their claims were dismissed.

Alongside the discrimination claims was the claim that the Respondent failed to remit deductions to BIFU despite express requests and interest from the Claimants. According to the Respondent, the Claimants were not unionisable.

The Respondent, on the other hand, submitted that: -

- The Claimants agreed to the contractual terms as well as the benefits provided therein
- The Claimants were engaged on the Respondent's terms of service for casual and temporary employees
- Fixed term contracts carry no right or obligations beyond their date of expiry
- The Claimants failed to discharge their obligation by not producing the job description or payslips of any permanent employee to prove similarity in the job descriptions/ job groups
- The Court ought not to convert fixed term contracts to permanent employment contracts as to do so would be to interfere with the freedom and rights of the parties

Lady Justice M. Mbaru held that: -

1. Fixed term contracts are legitimate and lawful. However, an employer is not permitted to have unfavourable employment terms for any employee where the basic minimum terms and conditions have been negotiated for a unionisable cadre.
2. Once terms and conditions of employment are negotiated and secured under a CBA, such terms are enforceable and applicable to all unionisable employees.
3. The obligation to disclose an existing CBA to an employee rests on the employer.

"Where the employer....proceeds to issue a fixed term contract and blind-sides the employee on the terms and conditions negotiated under a CBA....despite any consent given by the employee....such is direct fraud, it is misrepresentation of facts of the existence of the CBA regulating employment and this being contrary to the law regulating basic terms and conditions of employment is illegal....The lack of knowledge of the existing CBA negates the consent given at the point of signing..."

4. The Court held that indeed the Respondent applied unfair employment practices against the Claimants and that the Claimants were discriminated against on account of employment terms and conditions contrary to the CBA rates that apply to unionisable employees. Besides, the Claimants were paid an unequal wage for equal work and work of equal value with permanent clerks. The Claimants were also awarded general damages, pension and the difference in salary that had led to them to be underpaid. The Respondent was also ordered to pay house, leave and meals allowances that it had denied the Claimants and to issue Certificates of Service for the years it had failed to issue.
5. Failure by the Respondent to treat all clerks equally where no reasonable distinction could be found was direct discrimination against the Claimants.
6. The recognition of fixed term contract in law is not a justification to pay low wages and create a disparity that is not justified. The right to issue a term contract should not negate the application of the law in its entirety with regard to payment of a basic minimum wage based on a negotiated CBA.

Judgement was thus entered in favour of the Claimants and orders issued accordingly including an order for general damages of Kshs.2,000,000.00 for each Claimant.

Momentum Credit Limited vs Teresia Kabuiya Nduta [2022] eKLR *(Judgment delivered on 7th Day of October 2022)*

The in duplum rule (Section 44 of the Banking Act [CAP 488]) held not to apply to institutions that are neither banks nor financial institutions

This case was first filed in the Small Claim's Court in which judgment was declared in favour of Teresia Kabuiya Nduta (the "Respondent"). Dissatisfied with the judgment, Momentum Credit Limited ("Appellant") filed an appeal in the High Court.

The matter involved disbursement of a loan of Kshs.1,300,000.00 to the Respondent which loan was secured by the Respondent's motor vehicle as collateral. Upon default, the Appellant repossessed the motor vehicle and sold it for Kshs.1,500,000.00 against an outstanding amount of Kshs. 2,050,328.00. The Appellant thus sought the difference of Kshs. 731,722.00 being the principal, interest, penalties and legal costs.

The Respondent, on the other hand, claimed that: (1) there was no evidence of sale of the motor vehicle; (2) in the instance there was such a sale, the same was without her knowledge and/ or consent; (3) the motor vehicle was sold at an undervalue; (4) the Appellant changed the interest rate from 14% per annum to 10% per month without notice; and (5) the interest charged was high and unconscionable

The Adjudicator at the Small Claims Court held that the provisions of the Banking Act and the Central Bank of Kenya Act (CAP 491) applied to the Appellant and as such the interest rates charged were found to be above those set by law. The Small Claims Court further held that the Kshs.1,500,000.00 recovered was sufficient to offset the loan.

In the appeal, Justice Majanja held that for Section 44 of the Banking Act to apply, 'it must be established that the Appellant is a bank or financial institution'. He averred that: -

"It is not in dispute that the Appellant is neither a bank nor mortgage finance company. In order to qualify as a financial institution, the Appellant must either be gazetted as such by the Minister or be one that carries on or proposes to carry on financial business as defined under the Banking Act. In order to qualify as a financial institution, it must accept money on deposit from members of the public and employ that money or part of it for lending or investment as contemplated under the Act. The Appellant's witness clearly stated on cross-examination that the Appellant was not a deposit taking institution while the Respondent did not provide evidence to the contrary or show that it is gazetted under the law in order for it to fall under the ambit of the Act."

Noting that the Respondent relied on section 44 of the Banking Act in her claim of unconscionability of the interest rate, it was held that the aforesaid section 44 did not apply to the Appellant and further that the rate of interest was governed by the provisions of the contract between the Appellant and Respondent. The appeal was allowed and judgement entered in favour of the Appellant to the tune of Kshs.731,722.00.

Kenya Tea Growers Association & another v Attorney General & the National Social Security Fund Board of Trustees [Petition 38 of 2014 (Consolidated) with Petition 34, 35, 49 and 50 of 2014] *(Judgment Delivered on 19th September 2022)*

Mandatory Contributions to the National Social Security Fund declared Unconstitutional

The Petition was a consolidation of five Petitions brought by various bodies against the National Social Security Fund Board of Trustees, the Cabinet Secretary of Labour, the Retirement Benefits Authority, the Competition Authority and the Attorney General.

The basis of the Petition was the unconstitutionality of certain provisions of the National Social Security Fund Act, 2013 **("NSSF Act")** in so far as it obligated employers to register employees for pension and making certain percentage deductions from salaries and wages. The reason given for the same was that the provisions they had were sufficient, and registration in the mandatory pension scheme was unconstitutional and would overburden employees. In addition to that, the issue of lack of public participation was contested

The Court found that the Act was inconsistent with **Article 10** of the Constitution as read with **Section 3** of the Competition Act as it gave the National Social Security Fund a monopoly over the provision of pension and security services in the country. It further found that the requirement for mandatory registration and contribution interfered with the free choice of employers and employees. The Court thereafter ordered that the NSSF Act would only apply to those that opted in.

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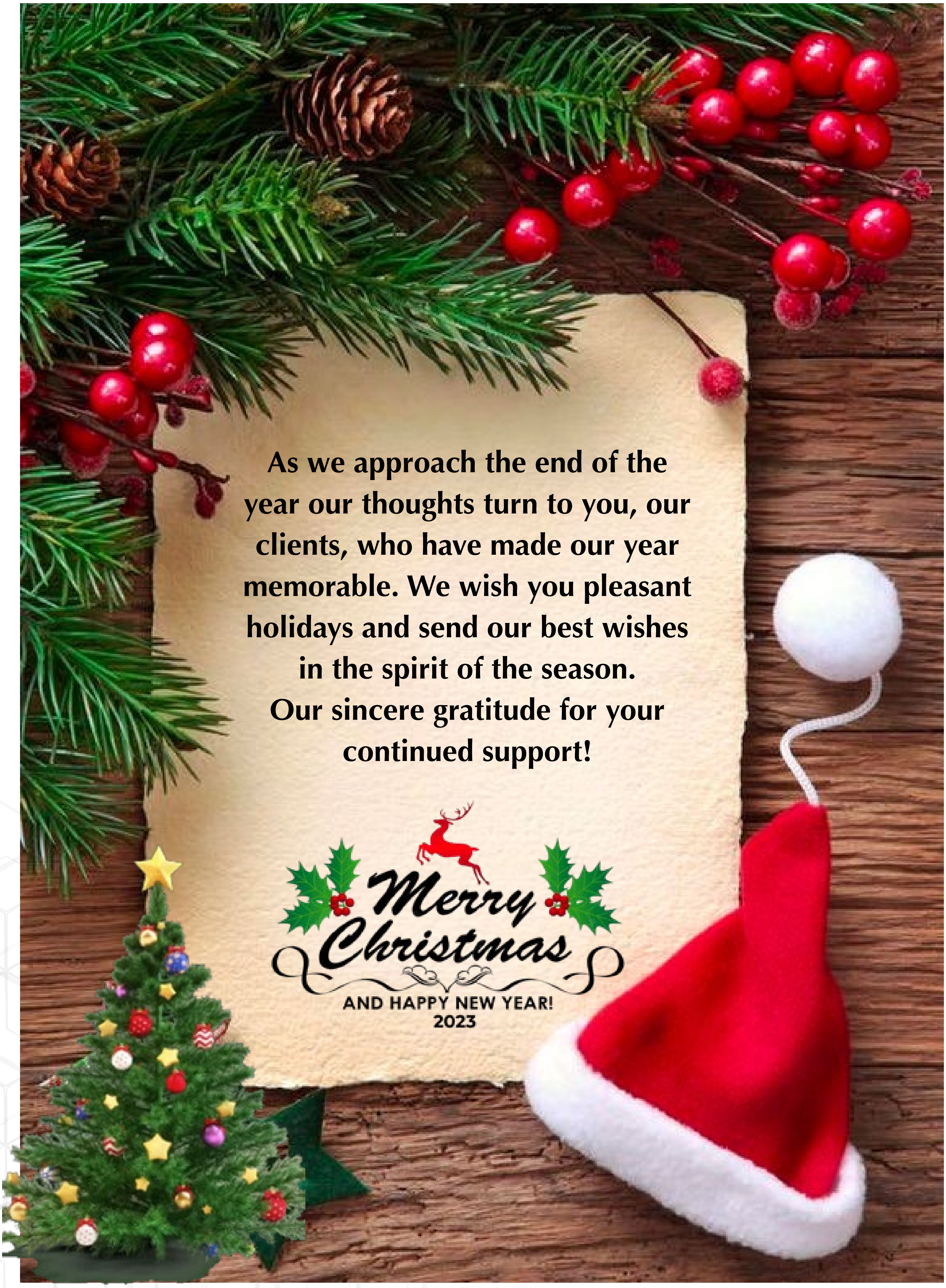
As we approach the end of the year our thoughts turn to you, our clients, who have made our year memorable. We wish you pleasant holidays and send our best wishes in the spirit of the season.
Our sincere gratitude for your continued support!
Merry Christmas
AND HAPPY NEW YEAR!
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CONTRIBUTORS' PLATFORM

A Closer Look At Non-Fungible Tokens (NFT's) And Their Regulation In Kenya

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Digital assets are electronic files of data that can be owned and transferred by individuals and used as a currency to make transactions. The functioning of a digital asset is made distinguishable and identifiable through a type of decentralized database of electronic ledger called a blockchain.

Non-Fungible Tokens are an increasingly innovative way to prove digital ownership and trade valuable collectible items. An NFT is a unique digital asset whose authenticity can be verified on a block chain ledger. Each NFT is distinct and traceable and can be used to label, identify digital assets and control their supply. 'Non-fungible' means an NFT is not interchangeable for other items because they all have unique properties and features. NFTs have enabled people to tokenize items such as art, tweets, real estate, photos, videos, and music. People then sell them on blockchain-backed marketplaces.

"An NFT is therefore a representation of data, such data being the result of the expression of artistic creativity by an individual or group, on a digital ledger system with unique identifiers embedded in its metadata. This metadata, which can be accessed and viewed on a Blockchain Explorer such as Etherscan, contains details about the original owner (crypto wallet) and any new owners since, transaction number, transaction value and fee, and a timestamp. Therefore, the metadata embedded in a NFT can be used to authenticate the ownership of the token..." *(Kenyan Wall Street, https://kenyanwallstreet.com/non-fungible-tokens-vs-kenyan-copyright-law/).*

ARE NFTS REGULATED IN KENYA?

As an emerging technology, NFTs and blockchain are not regulated in most jurisdictions. The industry itself is still in its infancy stage and is volatile in its own right. To this day, digital assets are neither regulated in Kenya nor backed by any governmental institution. This has been consistent for the past six years. Not withstanding the original public notice issued by the Central Bank of Kenya in 2015 cautioning the public on virtual currencies, there are also discussions on whether they might be treated as securities and not currencies. This could potentially make them regulated under the 'securities umbrella'. In February 2022, the Central Bank of Kenya published a discussion paper on the suitability of a Central Bank Digital Currency **('CBDC').** The CBDC (if accepted) will be a universally acceptable form of payment as sovereign legal tender in Kenya (electronic currency).

Additionally, it was recently reported that the Joint Financial Sector Regulators Forum agreed to consider the recommendation to form a working group that will advise the Cabinet Secretary for the National Treasury and Economic Planning on crypto assets and players in Kenya. This is a step in the right direction towards understanding financial technology innovations with a view to regulating the same

A member of parliament" has also proposed the Capital Markets (Amendments) Bill 2022, which seeks to impose taxation on digital asset exchanges, wallet providers and traders.

The Bill provides that where the digital currency is held for a period not exceeding twelve months, the laws relating to income tax shall apply and where it is held for a period exceeding twelve months, the laws relating to capital gains tax shall apply. If approved, the Bill will be the first legislation that caters to the digital asset sector in the country. Kenya has seen an explosion in digital asset adoption over the past few years, ranking atop the global peer-to-peer trading volume chart for 2020 and 2021. In this year's Chainalysis Global Crypto Adoption Index, the country ranked in the top 20 globally for adoption.

CORRELATION BETWEEN NFT'S AND KENYAN COPYRIGHT LAW

NFT's have a close relation to Intellectual Property Rights. What is important to understand is the distinction between the ownership of the NFT and the ownership of the underlying Intellectual Property Rights ("IPR's"). The rights granted by the seller of the NFT will depend on the terms of the-e purchase that will be reflected in the transferred metadata.

For example, with regards to copyright, in the context of digital art, a buyer may be granted certain rights in how they are able to use the work – for example, the right to display and sell the artwork but no right to reproduce. An individual may take a screen recording of a memorable world cup goal from a live airing of a game on one of the television channels (broadcaster), upload the same on a blockchain as his Non-Fungible Token and monetise the same from the resale of the NFT to new owners. Ownership of the NFT would be claimed courtesy of the metadata embedded.

The individual would however have infringed on the copyright ownership of the broadcaster.

There is thus need for legislation to regulate this fast-growing field.

A UNIFIED SEPARATION?

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Generally, the main goal of most businesses is to make profit and grow. This occurs when an organization is able to offer either goods or services on a large scale therefore increasing their output and generating more income. However, business entities may grow to a point where it becomes difficult for a single entity to handle the growth of the business solely. This may lead the business to diversify the internal structure of the organization by creating different internal departments to cope with the increased needs of the company.

Although beneficial from a production perspective, such a situation may come with pitfalls including: dual regulation, stifling innovation and monopolization of the market by the organization. This leads to calls from regulators and the market alike to declare the organization as dominant. Market dominance refers to a company or product's control over particular market or industry. This can be measured by a variety of metrics, such as market share, revenue or number of customers. A company with a high level of market dominance is considered a market leader and may have a significant competitive advantage over its rivals.

Dominance is not a problem in itself, the challenge occurs for organizations when it leads to increased scrutiny to ensure the company is not engaging in practices that amount to abuse of dominance.

Dominance is abused when a company with a dominant market position uses that position to unfairly gain an advantage over its competitors. Also known as monopolistic abuse or monopolization, abuse of dominance can take the form of predatory pricing, exclusionary conduct, or refusal to deal with competitors. In general, abuse of market dominance is illegal under Competition Laws, as it is considered harmful to consumers and can stifle innovation and competition in a market. Companies found to be engaging in such behaviour can face significant fines and other penalties.

How then do you avoid dominance, its abuse, and dual regulation? Cling onto being a single entity? Make either of the departments a subsidiary of the other? Or have a non-operating holding company with operating subsidiaries?

Single Entity?

All businesses start out as a single entity and then grow into their full potential. Take Google for example that started out as an internet service provider and search engine. Their business grew to other fields such as human health, private equity, drug discovery, robotics, autonomous driving and drone-based technology. All under a single entity, Google Inc., the departments dealt with completely separate fields risking the entire company becoming a monopoly as well as exposure to dual regulation. This option, although promising in terms of retaining profit, may expose an organisation to threats of declaration of dominance and abuse stemming from it, dual regulation as well as limited innovation since either of the departments in the company have to factor in all the possible impacts innovations would have on the other. As if that is not enough, there could even arise public and regulatory pressure and calls for the separation.

So, which way then?

Vertical separation?

Vertical separation may work and is a quick fix. In this model, the parent company remains to run the core business while the other department, that could reduce the risk of being perceived a dominant player in the business, is vertically separated and made a subsidiary, fully owned by the parent company.

Vertical separation eliminates the possibility of dual regulation, delinks risks and creates a general outlook of separate business entities. On the other hand, since there won't be additional shareholders, the original shareholding is not diluted. However, there lurks a great risk which is the insolvency of the parent company.

This was witnessed recently when FTX, a global cryptocurrency trading company and its affiliate, Almeda Research and Coinbase ventures filed for insolvency. A simple meltdown on liquidity of the parent company resulted in shocks forcing the parent company to commence liquidation procedures, to meet its obligations to its debtors.

Were their subsidiaries spared? All their subsidiaries have been exposed to liquidation as well since they are fully owned by FTX. BitPesa Kenya is a good example of a victim of this model of separation as it was a fully owned subsidiary of FTX and now runs the risk of liquidation.

It is evident from the examples that whenever vertical separation is taken up, the business module, infrastructure established and even the brand presence of the subsidiary are at a far more risk of falling flat on their belly if the parent company goes insolvent.

Vertical-horizontal Separation?

This model of separation involves setting up a non-operating holding company (the "holding company") with each of the departments as an autonomous operational subsidiary of the holding company. The holding company is created to buy and own the shares of the operational subsidiaries (the "subsidiaries") fully. Once set-up, the holding company can do a share swap with the already existing company to have the shareholding as originally constituted undiluted and in full control of the holding company while the subsidiary becomes fully owned by the holding company.

Vertically, the holding company at the top centralizes cooperate control and maintains the fibres of business growth that resulted in the departments morphing into autonomous subsidiaries. Right below it, the subsidiaries are horizontally separated as autonomous companies.

Once achieved and fully implemented, the flood gates of independent innovation within the subsidiaries open resulting in them only having to deal with specific regulators. The possibility of dual regulations is also extinguished and the subsidiaries only have to deal with market specific regulators. This results in guaranteed uniformity in management, ready advisory and oversight, better financial and information accounting courtesy of the holding company.

The holding company can own the brand name, trademarks, and properties on behalf of the group ensuring utilization for the benefit of the group as a whole. It can also raise resources on behalf of the group to support the subsidiaries thus lowering the cost of operating capital. Most importantly is that the holding company can offer downstream guarantee by making pledges on loans on behalf of the subsidiaries. It also goes without saying that risks are significantly reduced.

If valuable assets of the group are owned by the holding company and are separate from the subsidiaries, the group will not lose them in case of poor performance or insolvency of the latter. Equally, the holding company cannot be pursued in case a subsidiary goes insolvent but may just decrease in worth. Holding companies are also helpful in succession planning since a centralized board of directors ensures continuity in business when key people from the operating companies exit.

On the downside, it may be difficult to find an accurate picture of the overall health of the holding company, losses may be hidden by moving debts among the subsidiaries, and subsidiaries may be forced to procure products and services at higher-than-market or below-market prices from each other.

In conclusion, any company that is pursuing separation should, subject to tax advisory, consider a non-operating holding company, with subsidiaries that operate as a group. The holding company can then do a share swap with the already existing company before it morphs into a subsidiary to have the original shareholding undiluted and in the hands of the holding company to continue growing without risks of dual regulation, calls for separation or a declaration of dominance.

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Merry Christmas

AND HAPPY NEW YEAR!

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