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CO-REGULATION OF CROSS-BORDER FACTORS: DEMYSTIFYING THE CHIMERA OF FREE MOVEMENT OF CAPITAL WITHIN THE EAST AFRICAN COMMUNITY COMMON MARKET

By

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To

DR FEMI OLUYEJU

September 2019

DECLARATION

I, AKINYI J. EURALLYAH, do hereby declare that the Co-regulation of Cross-Border Factors: Demystifying the Chimera of Free Movement of Capital within the East African Community Common Market is my original work and has not been submitted for any degree or examination in any other university or institution of higher learning. While I have relied on numerous sources and materials to develop the main argument presented in this dissertation, all the materials and sources used have been duly and properly acknowledged.

Supervisee: Akinyi J. Eurallyah

Signed...

Date...

Supervisor: Dr Femi Oluyeju

Signed...

Date..

DEDICATION

I dedicate this work to Benjamin Anthony & Rozita Pnini, without whom this thesis would have been complete two weeks earlier. The stay in Israel was worth the sacrifice though.

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LIST OF ABBREVIATIONS

EAC -	East African Community
EU -	European Union
FCI -	Factors Chain International
GATT -	General Agreement on Tariffs and Trade
SMEs -	Small and Medium-sized Enterprises
SRO -	Self-Regulatory Organization
TFEU -	Treaty on the Functioning of the European Union
UNCITRAL -	United Nations Commission on International Trade Law
UNIDROIT -	International Institute for the Unification of Private Law
WTO -	World Trade Organization

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European Union

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CHAPTER ONE

INTRODUCTION

1.1. Background

The Privy Council in *Chow Yoong Hong v Choong Fah Rubber Manufacturer* quipped, evocatively so, that 'there are many ways of raising cash besides borrowing . . . one is by selling book debts.'[1] Factoring is a form of trade finance that involves the sale of trade receivables to a factor in exchange for working capital.[2] It has gained momentum as one of the most used forms of trade finance, especially to the Small and Medium Enterprises (SMEs), in less than a century.[3] Factoring can be done either with recourse or without recourse. Recourse factoring entails the creditor bearing all the risks such as non-payment by the debtor.[4] On the other hand, non-recourse factoring places the risks on the factor. It can be done both at the local and international spheres.[5] Its cross-border practices enhances movement of working capital to multinational companies and SMEs, thus ensuring that they have a continuous cycle of capital.

According to the Trade Finance Global 2018 survey on the factoring industry, in 2018, the global factoring industry recorded an increase in volume amounting to 2,767 billion euros, a 6% increase from the 2017 figure.[6] Regionally, despite Israel's negative figure of -19%, the Middle East still recorded an increase of 10% thanks to the United Arabs Emirates volume that saw its factoring industry grow by 38%. In the South Americas factoring volume increased by 4%, recording a volume of over 100 billion euros. However, Brazil's figure dropped by 6%. The Asia Pacific region showed an upward trajectory of 6%, recording a combined volume of over 600 billion euros, with China leading with an over 411 billion euros record.

Europe remains to be the largest factoring market, accounting for almost 65% of the world factoring transactions. In 2018, it recorded an increase of 7% from its 2017 figure in its

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[1] The Privy Council in *Chow Yoong Hong v Choong Fah Rubber Manufacturer* (1962) AC 209

[2] Factors Chain International Annual Review 2018 available at https://fci.nl/downloads/Annual%20Review%202018.pdf p 13

[3] Ibid

[4] Yvonne Tan, 'International Factoring, Factoring: The Devise' (1984) 5 SING L REV 192 available at https://heinonlineorg.uplib.idm.oclc.org/HOL/Page?public=true&handle=hein.journals/singlrev5&div=18&start_page=192&collection=journals&set_as_cursor=4&men_tab=srchresults accessed on 31 July 2019

[5] Ibid

[6] James Sinclair Global factoring and receivables finance industry increased by 6% in 2018, *Trade Finance Global* available at https://www.tradefinanceglobal.com/posts/new-global-factoring-and-receivables-finance-industry-increased-by-6-in-2018/ accessed on 19 July 2019

factoring industry. Table 1 below shows the EU's factoring industry from the year 2010 to 2017.

Table 1: Factoring Statistics in the EU between 2010 and 2017

	2010	2011	2012	2013	2014	2015	2016	2017	Change y/y
Total Turnover (M €)	992.746	1.142.718	1.209.587	1.259.343	1.373.774	1.470.821	1.503.170	1.605.697	
of which:									
Domestic	847.022	902.283	1.034.361	1.063.752	1.121.238	1.188.768	1.174.747	1.259.652	7%
International	145.724	240.435	175.226	195.591	252.536	282.053	328.424	346.044	5%
Recourse	710.056	767.592	666.318	757.301	808.048	797.997	777.135	830.013	7%
Non Recourse	282.690	375.126	543.269	502.042	565.725	672.824	726.035	775.683	7%
Owned by banks and banking groups			1.131.994	1.156.876	1.269.056	1.337.292	1.439.932	1.528.357	6%
Owned by non banking companies			77.593	102.467	104.718	133.529	63.238	77.340	22%
Total Advances (M €)	71.856	72.053	169.358	162.415	172.963	168.154	201.596	217.725	8%
Total Security Values (M €)	116.966	105.828	222.376	224.433	237.151	251.070	261.480	277.027	6%
Number of Active Client Relationships	126.269	119.739	160.066	166.502	164.069	171.426	179.675	201.520	12%
Average yearly turnover per client (M €)	7,9	9,5	7,6	7,6	8,4	8,6	8,4	8,0	-5%
Average yearly advances per client (M €)	0,6	0,6	1,1	1,0	1,1	1,0	1,1	1,1	-4%
Average outstanding per client (M €)	0,9	0,9	1,4	1,3	1,4	1,5	1,5	1,4	-6%
Advances/ total receivables	61%	68%	76%	72%	73%	67%	77%	79%	2%
Average no of days outstanding	43	34	67	65	63	62	63	63	-1%

Figures in this table are estimated on the basis of the data provided by the EUF Members and the significance of the sample on total turnover

Source: EU Federation for Factoring and Commercial Finance[7]

Closer home, the Trade Finance Global 2018 survey revealed that Africa's wider regional factoring industry, despite the low volumes, recorded an increase of 2%, with South Africa accounting for 9%, Egypt 24%, and Mauritius industry accounting for 9%. Morocco's industry dropped by 25%. Domestic factoring in the West African region accounted for approximately 50 million euros in 2017, with Nigeria's record being the highest. In the Northern region, domestic factoring in Tunisia accounted for 95% of the transactions, financing the telecom, white goods, and agriculture industries.[8] In the East African region, Kenya, being the region's economic powerhouse, had very dismal results in its international factoring industry, with its domestic factory accounting for 97%. This is despite an existing common market in the region that should enhance cross-border movement of capital.

[7] Available at https://euf.eu.com/facts-and-figures/facts-and-figures/euf-estimates-on-eu-market.html accessed on 19 July 2019

[8] Supra n 2 p 19

According to Enga Kameni, factoring in Africa records low volumes because of, *inter alia*, the poor legal framework governing the industry.[9]

The East African Community is a regional economic integration that was notified to the WTO under the auspices of the Enabling Clause. It draws its mandate from Article 2(1) of the Treaty for the Establishment of the East African Community (the Treaty). It comprises Uganda, Kenya, Tanzania, Rwanda, Burundi, and South Sudan. Its fundamental principles include, *inter alia*, 'equitable distribution of resources, and co-operation for mutual benefit.'[10] As parts of its integral pillars, the Community has in place a Customs Union that establishes the Community's common external tariff;[11] a Common Market that facilitates the free movement of factors of production;[12] a Monetary Union[13] and an ultimate objective of forming a Political Federation.[14] The political federation objective is an integration too deep that is yet to be seen in any other African regional economic agreements.[15]

The EAC Partner States signed the Protocol on the Establishment of the East African Community Common Market (the Protocol) in 2009, which later came into force in 2010. The Protocol gives effect to Article 76 of the Treaty. The Protocol serves to accelerate the economic development of the Partner States by facilitating, *inter alia*, free movement of capital, labour, goods, and services.[16] The Partner States unanimously agreed to eliminate all forms of technical barriers to trade and any restrictions to that would impede the movement of capital within the Common Market, an act that would see the Community have an integrated financial system.[17] This they would do through 'harmonizing their standards and implementing a common trade policy for the Community.'[18] In fact they are not to introduce

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[9] Enga K. *'An insight into recent legal and regulatory reforms of factoring in Africa'* available at https://elibrary.acbfpact.org/acbf/collect/acbf/index/assoc/HASHc005/0f80ba73/9c03529e/33.dir/Contemporary-Issues-in-African-Trade-and-Trade-Finance-VOL.1-No-1.pdf accessed on 19 July 2019 p 30

[10] The Treaty for the Establishment of the EAC art 6(e) & (f)

[11] The Protocol for Establishment of the EAC Customs Union was signed on 2 March 2004, paving way for the customs union to become fully operational on 1 January 2005, See https://www.eac.int (accessed on 8 May 2019); See also Treaty (n 10) art 75

[12] The Protocol for the Establishment of the Common Market was signed on 20 November 2009, entered into force on 1 July 2010, See https://www.eac.int (accessed 8 May 2019); See also Treaty (n 10) art 76

[13] The Protocol for the Establishment of the EAC Monetary Union was signed on 30 November 2013 and is yet to come into force

[14] EAC Treaty (n 10) art 5(2)

[15] W Masinde and OO Christopher, 'The Road to East African integration', in Emmanuel Ugirashebuja et al (eds) *East African Community Law: Institutional, Substantive and Comparative EU Aspects* Brill (2017) p 17-18 available at < https://brill.com/view/book/edcoll > (accessed 10 May 2019)

[16] Treaty (n 10) Preamble para 5; art 2

[17] EAC Treaty (n 10) art 5(2)(f)

[18] EAC Treaty (n 10) art 5(2)(a)

new restrictive or apply more restrictive measures to impede free movement of capital,[19] unless such restriction relates to financial sanctions.[20] The EAC Secretariat and the other Partner States should, however, be informed of such restriction, and evidence furnished as to why such restriction is justifiable.[21]

Interestingly, there exist a plethora of laws regulating the financial sector in each of the Partner States domestic realms that undermine the very existence of the Community and its free movement of capital objective.[22] In fact, an objective scrutiny of Annex VI of the Common Market Protocol exposes the exasperating nonchalance by the Partner States (to the extent of imposing more restrictive measures and regulations)[23] to liberalize their capital markets, thus impeding the free movement of capital as envisaged. The areas where such restrictions should be abolished include, *inter alia,* money markets,[24] collective investment schemes,[25] direct investments[26] and repatriation of profits.[27] Such liberalization is aimed at achieving a regional financial integration, making the freedom of movement of capital a reality.[28] Neither the Treaty nor the Protocol defines what 'movement of capital is'. The Protocol instead enumerates a non-exhaustive list that could be construed as capital. These include, *inter alia,* direct investment; equity and portfolio investments; bank and credit transactions.[29]

Direct investment refers to cross-border "investments of all kinds, by natural or legal persons, that serve to establish or maintain lasting and direct links between the person providing the capital and the entrepreneur or undertaking to which the capital is made available in order to

[19] EAC Treaty (n 10) art 24(1)
[20] EAC Treaty (n 10) art 25(1)
[21] EAC Treaty (n 10) art 25(2)
[22] World Bank report on the *East Africa Common Market Scorecard* 2016; A more detailed report on the restrictive measures and regulations that impede the freedom of movement of capital will be discussed in Chapter 3
[23] See for example Rwanda's Capital Market Licensing Securities Requirement of 2012 on approval of foreign securities exchange; See also Uganda's Income Tax Act on withholding tax rate on dividends of listed securities for non-residents which is 15% compared to the one for residents which is 10%
[24] The EAC Common Market Schedule on the Removal of Restrictions on the Free Movement of Capital Annex VI operation 3
[25] Schedule (n 24) operation 4
[26] Schedule (n 24) operations 17 - 19
[27] Schedule (n 24) operation 20
[28] EAC Treaty (n 24) art 5(2)(f)
[29] EAC Treaty (n 24) art 28

carry on an economic activity."[30] It can be inward, outward or through repatriation of profits.[31]

Cross-border factoring is a form of direct investment.[32] Factoring is a contract between a creditor and a factor whereby the creditor transfers his commercial receivables whereas the factor performs at least two of the following: (a) provision of finance to the creditor, (b) maintenance of accounts relating to the trade receivables, (c) collection of the trade receivables, and (d) protection against payment risks by the debtor.[33] It is an activity whose main customers are the SMEs that seek alternatives to debt financing.[34] In a Community where its biggest percentage of investors are SMEs, it is imperative that these SMEs get more access to more alternative sources of funding like factoring. However, a common trend among the EAC Partner States has been to regulate non-bank factors under the same umbrella as banks[35] or the tendency to restrict the right of establishment of companies from other EAC partner states, without recognizing that they should be treated differently from other non-EAC nationals.

For example Uganda's Financial Institution Act of 2014 defines factoring to be a financial activity conducted by banks thus to be regulated by the Central Bank of Uganda. This means that the factors, which are not necessarily banks, are subjected to the same requirements as their banking counterparts e.g. capital adequacy. Further, its *Investment Code Act* defines a foreign investor as an individual who is not a Ugandan, or a company whose majority of shares (more than 50%) are held by non-citizens.[36] Similarly, in Tanzania, a foreign investor is defined in the *Capital Markets and Securities (Foreign Investors) Regulations* as an individual or a corporate body that is a non-Tanzanian.[37]

In addition, all the EAC countries restrict inward direct investments, with only Kenya, Rwanda and Uganda liberalizing their outward direct investments.[38] With the potential

[30] J Nakagawa 'Multilateralism and regionalism in global economic governance: trade, investment and finance' *Routledge Studies in the Modern World Economy* (2012) 127
[31] Schedule (n 24) operation 18
[32] J Dalhuisen 'Dalhuisen on international commercial, financial and trade law' *Hart Publishing* (2nd ed) (2004) 897
[33] UNIDROIT Convention on International Factoring 1988 art 1
[34] Dalhuisen (n 32) 951
[35] Uganda's Financial Institution Act of 2014 section 2
[36] Investment Code Act section 9
[37] *Capital Markets and Securities (Foreign Investors) Regulations* regulation 2
[38] World Bank Report (n 17)

proliferation of factoring entities in Africa,[39] these regulations have made it almost impossible for factors to establish their businesses within the Community, consequently making it difficult for the EAC entrepreneurs to access alternative sources of finance, especially the SMEs that have inadequate (or lack) collateral assets. Consequently, intra-EAC trade will continue to diminish.

Intra-EAC trade has recently significantly depreciated, thanks to the frustrating complacency of the EAC countries to liberalize their financial sectors in order to achieve the Community's financial integration agendum. Intra-EAC trade has recorded low volumes because of, among other reasons, lack of (or inadequate) working capital.[40] According to the International Monetary Fund Report of 2016, intra-EAC trade transactions was as low as 18.1% in 2015, depreciating from the 2012 figure of 19.7%. Similarly, according to the 2017 EAC trade report[41], Uganda's intra-EAC trade imports amounted to $565.5 million, recording a 6.2% increase from the previous year. In the same year, Tanzania's intra-EAC imports were valued at $243.2 million, a figure 18.6% lesser than 2016.

The Report exposes Burundi's 2017 value which depreciated by 3.1% amounting to $151.0 million. Rwanda has had consistent import figures of slightly above $400 million since 2013, with its 2017 volume amounting to $476.6 million, an unimpressive increase of 2.2% from its 2016 import values. As for South Sudan, despite joining the Community late in 2015, recorded very high volumes of imports amounting to $563.2 million in 2015, which, unfortunately, consistently regressed to $462.5 million in 2017, a figure 17.8% lower than its 2015 counterpart but 15% higher than its 2016. Kenya, the region's economic powerhouse, has also had its fair share of both progress and regress in the intra-EAC trade imports, accounting for $589.5 million, a progress of 81.7% from the 2016 value.

On the flipside, the Report[42] states that intra-EAC trade exports amounted to an aggregate of $2898.2 million in 2017, with Uganda accounting for $1126.3 million, recording an increase of 18.4% from its 2016 intra-EAC export values. Tanzania accounted for $464.5 million, a 33.7% increase from its 2016 value. Burundi recorded an extremely low figure of $11.5

[39] Dr E Kameni, '*An Insight into Recent Legal and Regulatory Reforms of Factoring in Africa*' available at https://afreximbank.com (accessed 13 May 2019)
[40] CNBC Africa '*How factoring can improve access to finance in Africa'* available at https://www.cnbcafrica.com/videos/2019/04/26/how-factoring-can-improve-access-to-finance-in-africa/ accessed on 31 July 2019
[41] Draft EAC trade report 2017 available at http://eabc-online.com/resources/business-guides/105-the-east-african-community-eac-trade-and-investment-report-2017/file accessed on 31 July 2019
[42] Ibid

million, a 6% decrease from its 2016 value of $12.3 million. Rwanda had a 6.4% increase from 2016 to 2017, with its 2017 intra-EAC export value amounting to $167.4 million from the 2016 value of $157.4 million. Just like Burundi, South Sudan's intra-EAC export value have been consistently low since its joining the Community, recording a $13.0 million in 2015, $23.6 million in 2016, and $17.9 million in 2017. Finally, Kenya has been recording fairly high intra-EAC export volumes, albeit its consistent regression. It recorded a value of $1,110.5 million in 2017, a figure that is 7.4% lesser than the 2016 value and 23.5% lesser than the 2013 figure.

The table below summarises the above findings.

Table 2: Total intra-EAC Trade for the year 2013-2017 (US$ million and percentage change)

		2013	2014	2015	2016	2017	Percentage Change			
							2014	**2015**	**2016**	**2017**
Imports	Uganda	616.9	686.1	631.0	532.6	565.5	11.2	-8.0	-15.6	6.2
	Tanzania	397.0	709.9	278.6	298.8	243.2	78.8	-60.8	7.3	-18.6
	Kenya	334.5	416.9	407.8	324.4	589.5	24.6	-2.2	-20.5	81.7
	Burundi	171.4	168.1	151.1	157.2	151.0	-1.9	-10.1	4.0	-3.9
	Rwanda	485.0	554.2	492.7	466.2	476.6	14.3	-11.1	-5.4	2.2
	South Sudan	_	_	563.2	402.0	462.5	_	_	-28.6	15.0
	Total	**2,004.8**	**2,535.3**	**2,524.4**	**2,181.1**	**2,488.3**	**26.5**	**- 0.4**	**-13.6**	**14.1**
Exports	Uganda	802.8	922.5	1,036.7	950.9	1,126.3	14.9	12.4	- 8.3	18.4
	Tanzania	1,118.0	779.5	337.4	338.3	464.5	-30.3	-56.7	0.3	37.3
	Kenya	1,451.0	1,430.8	1,285.9	1,199.0	1,110.5	-1.4	-10.1	- 6.8	-7.4
	Burundi	20.1	15.7	14.8	12.3	11.5	-21.9	-5.3	-17.1	-6.0
	Rwanda	125.8	141.6	135.2	157.4	167.4	12.6	-4.5	16.4	6.4

	South Sudan	13.0		13.0	23.6	17.9			81.4	-24.2
	Total	**3,517.6**	**3,290.1**	**2,823.0**	**2,681.4**	**2,898.2**	**-6.5**	**-14.2**	**-5.0**	**8.1**
Total Intra-EAC Trade value	Uganda	1,244.0	1,608.6	1,667.7	1,483.5	1,691.8	29.3	3.7	-11.0	14.0
	Tanzania	1,515.0	1,489.4	616.0	637.1	707.7	-1.7	-58.6	3.4	11.1
	Kenya	1,785.5	1,847.7	1,693.7	1,523.4	1,700.1	3.5	-8.3	-10.1	11.6
	Burundi	191.4	183.8	165.9	169.5	162.6	-4.0	-9.7	2.2	-4.1
	Rwanda	610.8	695.8	628.0	623.5	644.1	13.9	-9.7	-0.7	3.3
	South Sudan	-	**-**	576.2	425.6	480.4	**-**	**-**	-26.1	12.9
	Total	**5,346.7**	**5,825.3**	**5,347.4**	**4,862.6**	**5,386.6**	**9.0**	**-8.2**	**-9.1**	**10.8**

Source: Annex VII Draft EAC trade report 2017[43]

These figures prove that indeed intra-EAC trade occurs. However, the trade decline is due to, *inter alia,* declining competitive advantage among the region's manufacturers due to inadequate working capital, and the restrictive (protectionist) regulatory framework surrounding free movement of factors of production like capital exposing a dearth of political will among the countries.[44] The liquidity challenge has seen most multinational companies and SMEs go under due to unreliable flow of working capital, thus braking the chain of production and supply. A liberalised regional factoring industry, if achieved, will increase intra-EAC trade, thus being one of the ways to ensure that intra-EAC free movement of capital is enhanced.

1.2. Research Problem

Factoring, in most of the EAC countries, has been subjected to, *inter alia*, highly restrictive and unclear regulatory infrastructure with inaccurate terminology,[45] capital adequacy, licence

[43] Available at http://eabc-online.com/resources/business-guides/105-the-east-african-community-eac-trade-and-investment-report-2017/file p 26 accessed on 31 July 2019
[44] Ivan Mugisha 'Why intra-EAC trade is dwindling' *The East African* dated 23 March 2019 available at https://www.theeastafrican.co.ke/business/Why-intra-EAC-trade-is-dwindling/2560-5038534-uobi5r/index.html accessed on 31 July 2019
[45] Kameni (n 37) p 27

and partly-local ownership requirements, making it difficult for factors to offer their services in the other Partner States. This, therefore, impedes the freedom of movement of capital within the Community, rendering Article 76 of the EAC Treaty and Article 24 of the Common Market Protocol nugatory.

Movement of capital within the EAC Common Market has for far too long been considered the duckling that hardly grows due to restrictive Partner States regulations.[46] Despite the EAC Treaty prohibiting such restrictions, the Partner States have exuded some exasperating nonchalance towards liberalizing their internal financial markets to allow the free movement of capital.[47] One of the sectors that the EAC Treaty demands liberalization but has attracted very dismal performance by the Partner States is in direct investments.[48] One of the ways through which movement of capital within the Community can be enhanced is through cross-border investments, and one of the lucrative areas for investment within the Common Market is in factoring.[49] Factoring has been regarded as a significant vehicle that can drive the global economy to development.[50] Regionally, factoring volumes are expected to ameliorate to US$ 200 billion.[51]

Despite such impressive current and prospects for future growth, cross-border factoring regulations remain largely restrictive, thus impeding free movement of capital within the EAC common market.

1.3. Aims and Objectives of Research

This thesis seeks to:

a) Analyse the theories underpinning regulation of factoring and international movement of capital;
b) Illustrate the competing approaches towards regulation of factors;
c) Evaluate the legal framework governing cross-border factoring within the EAC Partner States;
d) Compare the EAC legal framework governing factors to that of the EU;
e) Propose reforms necessary for regulation of factors within the EAC in order to enhance its movement of capital.

[46] World Bank Report (n 17)
[47] World Bank Report (n 17)
[48] World Bank Report (n 17)
[49] Kameni, (n 37) 27
[50] Kameni (n 37) p 27
[51] Kameni (n 37) p 27

1.4. Research Questions

This research paper seeks to answer, definitively so, the following questions:

1. What are the underpinning theories surrounding regulation of factoring and international movement of capital?
2. What are the competing approaches towards regulation of factoring?
3. What are the tenets of regulation of factoring that can enhance free movement of capital within the EAC financial market?
4. What lessons can the EAC draw from the regulation of factors in the EU?
5. What reforms are necessary for regulation of factors in the EAC in order to enhance the free movement of capital?

1.5. Significance of Study

This thesis will go a long way in aiding the EAC partner states legislators in formulating sound, reliable and pragmatic solutions to the existing chimera of free movement of capital within the EAC Common Market in a bid to minimise the inconsistencies between their domestic regulations and the EAC Treaty obligations. This benefits both the Community in terms of achieving its financial integration agendum and the SME investors in terms of, *inter alia,* financial inclusivity and availability of continuous working capital. The ultimate beneficiary of this is the consumer in the Community who gets continuous supply of goods and services at better costs.

Besides, this paper will create more awareness to the citizens of EAC partner states as far as the benefits of belonging to a common market is concerned. Such benefits include free movement of factors of production e.g. capital that stems from factoring.

Finally, this study is important because it will inform scholars and other academics who would want to conduct further research on the EAC Common Market on how best to enhance *inter alia,* free movement of capital.

1.6. Literature Review

Regulation of the financial sector has been fodder for both academics and financial institutions regulators. In the recent past, there has arisen a heated discourse on whether the financial market needs to be regulated or not. Some scholars advance that through regulation, the adverse impacts of the financial operations will be curbed. On the other hand, some counter the aforesaid statement by positing that through deregulation of the financial markets, investors have easier and faster access to capital, leading to lower costs of production, thus better prices for products. These scholars and legal practitioners have penned down their views in order to inform *inter alia*, governments and investors on the right trajectory to be pursued in furtherance of this discourse. A review of their writings, hereunder, sheds some light into the existing lacuna that this thesis seeks to fill.

The World Bank Report of 2014,[52] in determining the extent to which the EAC has complied with the requirements of Annex VI of the Common Market Schedule,[53] reports that the stronger the financial market the more the mobility of domestic markets, resulting in an increase of the quality and quantity of investments in terms of diminished information asymmetry, outstripped competition and corporate governance in the financial markets. The Report goes further to encourage the EAC Partner States to liberalize their financial markets, for in so doing, the EAC will be a better attraction site for both foreign and domestic investment, resulting in a long-term solution for the poor financial infrastructure. Further, the Report proposes that the Partner States should consider, among other solutions, prioritizing a rollback of financial regulations. However, it warns that despite the benefits of financial integration that still outweigh the costs, such integration may lead to the risk of financial contagion and diminished domestic regulators' oversight. Despite such a detailed pro-financial integration report, the Report fails, in detail, to provide for *how* EAC can achieve such financial inclusivity. This thesis seeks to fill this gap by proposing that a balance ought to be struck between a Partner States regulation versus self-regulatory mechanisms.

The 2018 survey[54] by the European Bank for Reconstruction and Development defines factoring as a financial service involving sale of receivables, with or without recourse, through easier and an 'off balance sheet access to working capital,' especially for the SMEs. The Survey further states that regulations have a sieve-like tendency of filtering the potential providers of the factoring services. The survey brings out quite evocatively that an overly regulated financial sector tends to result in factoring services being concentrated in the banking institutions as a bank's side-activity, impeding competition and specialization, and barring new smaller entrants into the market. On the flipside, zero regulation may lead to arbitrage, adverse selection, and confusion in distinguishing factoring, last resort financing,

[52] World Bank Report (2014) on *East African common market scorecard 2014: tracking EAC compliance in the movement of capital, services and goods* (Vol. 2) available at http://documents.worldbank.org/curated/en/799871468194049251/Main-report as accessed on 13 May 2019
[53] Schedule (n 24)
[54] European Bank for Reconstruction and Development Report (2018) *Factoring Survey on EBRD Countries of Operation* (3rd ed) which analyses the legal and regulatory framework for factoring in EBRD countries of operation available at https://www.ebrd.com/what-we-do/legal-reform/access-to-finance/factoring.html as accessed on 13 May 2019

and bad debt collection. The Survey advises countries considering updating their factoring legal regimes to take into account an appropriate pitch of oversight since it benefits the factoring industry by creating a positive impact on the public perception of the factoring industry, thus its enhanced usage.

Dr. Enga Kameni in his paper titled – *An Insight into Recent Legal and Regulatory Reforms of Factoring in Africa*[55]- exposes how factoring, as a source of trade finance, is gaining momentum in Africa, having an average growth of approximately 14.2% per annum. In monetary terms, he estimates that factoring volumes will increase to about US$ 200 billion by 2020. However, he is sceptical of the positive results of factoring given that African countries hardly have any comprehensive facilitative legal and regulatory infrastructure governing factoring. In fact, at least according to the author, African countries hardly know what factoring is. Other challenges the author mentions are *inter alia*, that factoring is given inaccurate terminology, lacks judicial precedents, and inadequate and inappropriate enforcement regimes. Despite such acknowledgement of the benefits of factoring, the author hardly gives any solution that is inherently African given the unique factors like historical context, resources, and more pressing need for financial integration. Besides, the author hardly approves of factoring being a banking activity. This thesis will fill this gap by advancing that if a factor adheres to the strict definition of the UNIDROIT Convention on International Factoring, then he/she is a factor, regardless of whether it is a bank or not.

K.K. Mwenda in defence of a unified system of financial regulation in his article titled - *Legal Aspects of Unified Financial Services Supervision in Germany* [56]- reviews the various institutional and structural developments in relation to unified financial services in Germany. He theorizes that 'where segments of the financial sector are quite inter-connected, a good case of moving towards unified supervision exists.' He adds that due to the complexity and multi-functional operations of the banking and financial sectors, it is important that countries adopt the unified system in regulating their domestic financial set-ups. However, the author fails to give a clear formula on how such unification is to be achieved, since with such unification, factors (who are not necessarily banks) are subjected to the same regulatory requirements as banks, thus impeding new entrants into the market that cannot keep up. This

[55] Kameni (n 37)

[56]KK Mwenda 'Legal Aspects of unified financial services supervision in Germany' available at <https://www.siteresources.worldbank.org > (accessed 12 May 2019)

stifles competition, and the end beneficiary of such low competition is the consumer who gets highly-priced commodities.

Similarly, according to Professor David T. Llewellyn in his paper titled - *The Creation of a Single Financial Regulatory Agency in Estonia: the Global Context*, [57]- some countries e.g. Sweden, Canada, Denmark, Korea, and Iceland, have reduced their level of regulation of their financial markets. On the other hand, some countries e.g. the United Kingdom, Iceland, Korea, and Finland, have created a single agency, whereas others have settled on multiple agencies to regulate their financial markets. Such decisions on the approach to settle on, according to the author, have been influenced by *inter alia*, historical evolution, political structures and culture, system of the financial system, a country's size and its financial market. The author points out that the incentives that have led countries into having a unified regulatory system include the blossoming financial innovations and dynamism in the financial market; ballooning financial conglomerates; and proliferating internationalization of financial operations. The author advises countries, when setting up institutional and legal framework of their financial markets, to take into account, *inter alia*, the cost of regulation and the role of self-regulatory mechanisms.

Finally, Eugene L. Versluysen in making a case for deregulation of financial markets in the paper titled - *Financial Deregulation and the Globalization of Capital Markets*[58]- advances that the need for such deregulation was necessitated by the international expansion of the commercial banks, transpiration of offshore banking centres, and positive growth of technology in terms of data processing and communication. The author quips that other factors that compelled central banks in Europe to become more flexible on their stance on strict regulation of the financial markets were rapid growth of financial innovation in the Euromarkets and internationalization of banks that bestrode both locally and abroad. This led to enhanced mobility of capital. The author, however, does not give any solution to the impediments of free movement of capital, especially with the proliferating regional economic arrangements that aim at achieving financial integration. This thesis will fill this gap by proposing pragmatic solutions to achieve such integration, especially in a Common Market.

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[57] D.T Llewellyn, *'The creation of a single financial regulatory agency in Estonia: the Global Context,'* conference paper (2001) p 4

[58] EL Versluysen "*Financial Deregulation and the Globalization of Capital Markets"* Background Paper for the World Development Report (1988)

The foregoing pieces of literature, and the many that will be referenced, will provide an informative stepping stone through which a well thought out solution for the EAC to achieve its free movement of capital objective through factoring will be proffered.

1.7. Research Methodology

This research adopts both the doctrinal and comparative methods. The doctrinal approach entails research and systematic analysis of existing primary and secondary sources including legislative instruments both within the EAC Partner States municipal borders and the Common Market and previously written pieces of literature with the aim of finding flaws hampering free movement of capital within the Community and consequently drawing logically sound conclusions and offering pragmatic solutions where necessary.

In addition to the doctrinal approach, the comparative method, as adopted by this study, entails analysing the legal instruments of another jurisdiction (in this case the European Union) with the aim of comparing its factoring industry to that of the EAC. The import of this is to distil some of the best practices as practiced in the EU that will inform the formulation of a regionally-sound regulatory mechanism on the factoring industry, with an aim of enhancing free movement of capital within the EAC. Since the factoring industry is still in its rudimentary stages in the EAC and blighted with a paucity of literature, this thesis will adopt an exploratory analysis in coming up with new ideas that could be of help to the Community.

The method adopted by this research is largely by way of desktop research. This is so due to time constraints that did not give the author the opportunity to come up with questionnaires and travel to the relevant offices to seek the opinions of experts in the factoring industry.

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CHAPTER TWO

THEORETICAL UNDERPINNING AND COMPETING APPROACHES TO REGULATION OF CROSS-BORDER FACTORING

2.0. Introduction

Several theories have been advanced to explain the rationale behind government regulation and international movement of capital. Besides, there exists various approaches that have been used by governments in their attempts to regulate factors. These theories and the lacuna in the extant approaches to regulation of factors inform the foundation upon which this study is built in order to put up a better structure that informs the formulation of policies and regulations that will govern the factoring industry within the EAC Common Market. Before analysing the theories and the competing approaches towards regulation of factors, an understanding of the relationship between cross-border factoring and international movement of capital is imperative.

2.0.1. Relationship between Cross-border Factoring and Movement of Capital

Modern SMEs face challenges like significant amplification of capital mobility, especially at the international spheres. Given the recent economic crises that resulted in growing credits and their subsequent default and liquidity risks thereof, there has been need to come up with pathways that ensure companies increase their competitiveness in the field of growth finance. This can be done through access to finance that ensures that companies remain competitive due to continuous cycle of liquid capital. Faster access to finance also encourages such companies to expand their businesses beyond their country's borders by ensuring they undertake productive investments. The sources of such capital can be credit or equity. A company that opts for credit can access such finance by way of *inter alia,* bank loans. On the other hand, a company that opts for equity can gain such access through *inter alia*, issuance of shares, initial coin offering, factoring, and forfaiting.[59]

Understanding the technicalities of credit, e.g. bureaucracy and need for *sufficient* collateral which most SMEs may not have, is helpful in appreciating the need for more accommodative alternative sources of finance. As mentioned earlier, these alternative sources of finances include factoring and forfaiting. Factoring is a far reaching alternative source of finance used in most industries that conduct business-to-business or business-to-government types of

[59] Surbhi S. Difference between factoring and forfaiting dated 24 May 2017 available at <https://keydifferences.com> accessed 9 July 2019

sales.[60] Through globalization that is as a result of increased need for a wider market base, companies have become more desirous of expanding their business beyond their national borders. However, during such expansion, such companies are faced with the various impediments that make it almost impossible to establish their companies in another country. This means that companies, like those of factors, can hardly conduct cross-border transactions.

Due to this, countries have come together to form common markets and free trade areas under the ambit of the General Agreement to Trade and Tariffs article XXIV. The EAC common market is an example of a common market that allows free movement of factors of production. Given that factoring is a form of trade finance that provides capital to companies, it is therefore one of the vehicles that drives movement of capital within the Community.

The following section analyses the various conceptual, legal and institutional frameworks on factoring.

2.1. Exegesis on Factoring

This section defines what factoring is, distinguishing between its contractual and proprietary aspects. It then proceeds to establish the relevance of factoring to SMEs, thus the need for the inexistence of such regulatory impediments.

2.1.1. Factoring Defined

Several attempts have been made to define what factoring is. For example, the Factors Chain International Secretary-General, Peter Mulroy in the FCI Annual Review 2016 described the concept of factoring in these terms:

> Factoring is an alternative and flexible means of finance which is widely used especially amongst SMEs. This is achieved by the supplier assigning and selling its accounts receivables to a bank or non-bank financial institution. The factor will provide a range of services to its clients, including providing capital against the assignment of their receivables, accepting the risk of bad debts and collecting on past due accounts. Factoring has been considered a stable financing alternative by many companies, particularly since the start of the financial crisis [in 2008]. As many SMEs were unable to obtain traditional bank funding during the crisis, due to the fact that SMEs are perceived to have a higher probability of default compared to larger firms,

[60] Tamara M., Ksenija D., '*Factoring in the changing environment: legal and financial aspects*' Procedia - Social and Behavioral Sciences (2012) 428 – 435 p 44 available at < https://www.sciencedirect.com > accessed 9 July 2019

> factoring filled the void. Central banks around the world have come to appreciate the product as a safe and secure method of financing trade.[61]

Similarly, according to Hoti:

> Factoring may be defined as the relationship, created by an agreement, between the seller of goods/services and a financial institution called the factor, whereby the latter purchases the receivables of the former and also controls and administers the receivables of the former. Factoring may also be defined as a continuous relationship between a financial institution (the factor) and a business concern selling goods and/or providing service (the client) to a trade customer on an open account basis, whereby the factor purchases the client's book debts (account receivables) with or without recourse to the client, thereby controlling the credit extended to the customer and also undertaking to administer the sales ledgers relevant to the transaction.[62]

In the same breadth, legislative instruments have attempted to come up with what factoring entails. The UNIDROIT Convention defines factoring as a contract between a creditor and a factor whereby the creditor transfers his commercial receivables and performs at least two of the following: (a) provision of finance to the creditor, (b) maintenance of accounts relating to the trade receivables, (c) collection of the trade receivables, and (d) protection against payment risks by the debtor.[63] Factoring is a form of trade finance and an alternative to secured lending. It could involve prepayment between the factor and the creditor amounting to a funding arrangement, normally between 70 and 90% of the total face value of the outstanding receivables.[64] The remainder may be settled upon collection or partly serve as factor's reward.[65] Such funding and collection involves risk. The type of factoring settled upon by the parties depends on who bears the risk of non-payment by the debtor. If the risk of non-payment and expense of collection is transferred to the factor, there is usually a discount is deducted to cater for such risk. This is referred to as *non-recourse* factoring. However, if the creditor retains such risk, the factor can still claim from the creditor the non-collected or non-paid receivables. This is known as *recourse* factoring.

Factoring has two facets: the contractual and proprietary facets. The two facets are briefly discussed hereunder:

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[61] P Mulroy 'Introduction by the Secretary-General' FCI Annual Review 2016 available at < https://www.fci.nl > accessed on 10 July 2019

[62] U Hoti 'Factoring: A Financial Instrument' (2014) Interdisciplinary Journal of Research and Development Vol (I), No. 2 available at < www.uamd.edu.al/new/wp-content/uploads/2015/07/2.-Ulpian-Hoti.pdf > accessed on 10 July 2019

[63] UNIDROIT Convention on International Factoring 1988 art 1

[64] Dalhuisen (n 27) p 886

[65] Dalhuisen (n 27) p 886

2.1.1.1. Contractual aspects

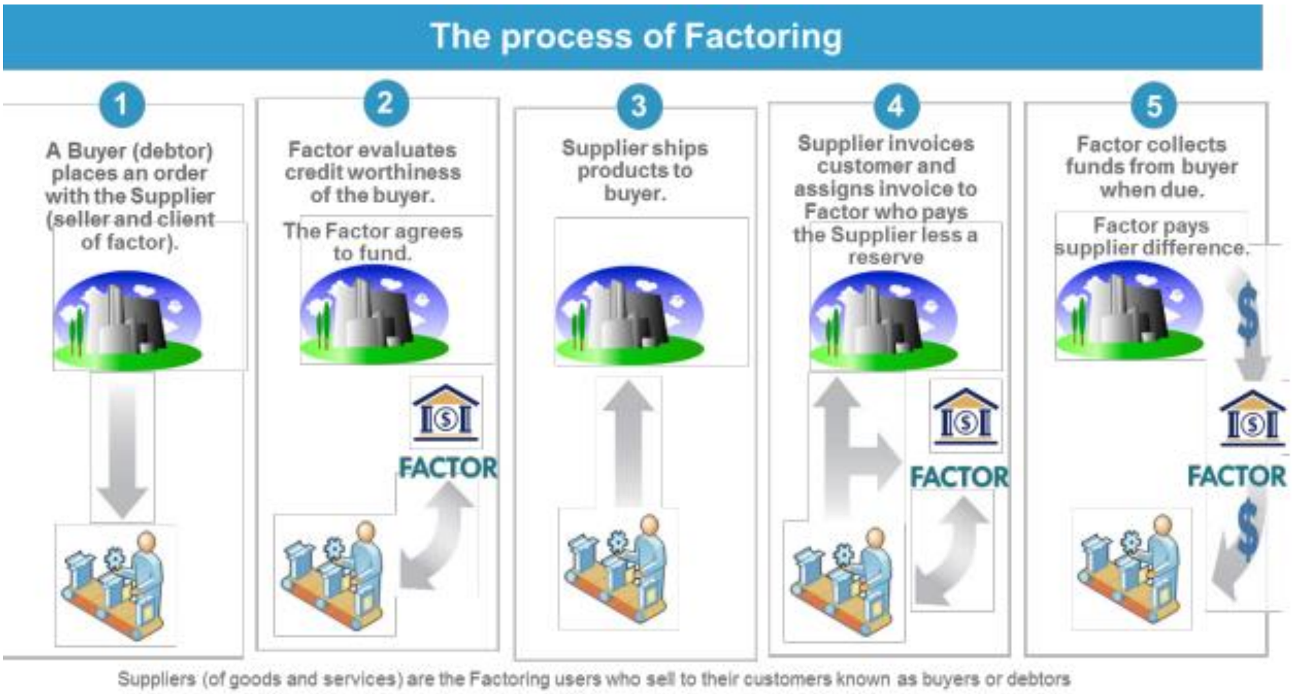
There may exist different forms of factoring agreements, however, there are some constant denominators that lead to their general identification. Firstly, there may be a mere *collection agreement* which involves administration and collection.[66] Secondly, the agreement could be in the nature of a *credit risk transfer* involving the grant of a guarantee of payment by the factor who bears the risk of non-payment.[67] Thirdly, the agreement could be of a *funding type*, whereby the factor advances some percentage of the capital.[68] A concoction of the three is also permissible.

2.1.1.2. Proprietary aspects

The proprietary aspects of factoring involve the actual transfer, normally an assignment of *bulk* or *future* claims.[69] This bulk assignment or future claims is not possible in legal systems that e.g. debtor notification of such assignment is a pre-condition of the validity of the assignment.[70] Further, in collection agreements, there is usually an outright assignment where future receivables are transferred to the factor, often done to facilitate his collection, and in return the factor transfers his collection to the assignor whenever collection or payment is received.[71] However, in guaranteed collection agreements, such transfer of receivables is often conditional. It may be deemed completed only upon *approval* of each receivable, or when not *exceeding* in total a certain amount per debtor.[72]

[66] Dalhuisen (n 27) p 889
[67] Dalhuisen (n 27) p 889
[68] Dalhuisen (n 27) p 889
[69] Dalhuisen (n 27) p 890
[70] Dalhuisen (n 27) p 890
[71] Dalhuisen (n 27) p 890
[72] Dalhuisen (n 27) p 890

A summary of the above exegesis is seen below:



2.1.2. Benefits of Factoring to SMEs

The benefits of factoring as a form of trade finance include:

a) Creates a continuous cycle of liquid capital to SMEs;
b) Creates and supports employment opportunities;
c) Promotes productivity since the creditor is relieved of the duties of debt collection and can instead use that time for production;[73]
d) Steers economic growth;
e) Guarantees against payment default by foreign buyers.[74]

2.2. Theoretical Framework

This section aims at analysing the various theories advanced towards regulation, international movement of capital and regional integration. The rationale behind this is to understand why the government regulates, and the various conflicting interests between domestic regulation and regional integration that provides an environment for international movement of capital.

[73] Hamanyati M. '*Factoring as an international trade finance product: making a case for the enactment of a factoring act in Zambia'* (dissertation)
[74] G Shams 'Egypt' World Factoring Yearbook 2017 Edition (2017) 161 available at <www.ebglaw.com/content/uploads/2017/06/Tatge-World-Factoring-Yearbook-2017-eBook.pdf > accessed on 10 July 2019

2.2.1. Theories on Economic Regulation

Theories on economic regulation rationalise any sort of government intervention in any facet of the economy through regulation subsidies, taxes, or any other form of control with regards to new entrants etc.[75] There are two major theories that have been advanced to explain the reasons why the government intervenes in a market economy.

2.2.1.1. Public interest

This theory is founded on two assumptions: that an economy is very vulnerable and susceptible to inefficient operations (e.g. monopolies) if left to operate on its own, and secondly, that government intervention into the market economy is cost-free and capable of correcting the inefficient operations.[76] According to Andrei,[77] governments regulate prices to prevent natural monopolies from overpricing, set import quotas to protect the domestic producers from going under, impose safety standards to protect workers, set health standards on products to protect its consumers, etc. This theory has been used to justify public ownerships and other forms of government encroachment into the market economy.[78]

The public interest theory has received its fair share of criticisms. First, market economies are capable of taking care of its operation inefficiencies whether the government intervenes or not.[79] This is so because the theory exaggerates the levels of market failures, failing to recognize the importance of internal market competition.[80] For instance, competition for labour, the critique goes, creates a better working environment to attract labourers. Similarly, competition in the production industry creates better quality goods and services since failure to do so will direct consumers to other producers of better quality products, leading to the automatic 'death' of the producer of low quality products. In addition, the criticism maintains that *sometimes* cartels fall off due to parties that betray the trusts of their fellow cartels. Finally, that what the government regards as monopoly may be subject to competition.[81] The foundation of this criticism is that any market anomaly not caused by impersonal competition forces is limited, and so is the desire for regulation in that instance.

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[75] Richard Posner, *Theories of economic regulation*, working paper no 41 May 1974 available at https://www.nber.org/papers/w0041.pdf accessed on 7 August 2019 p 2
[76] Andrei Shleifer *Understanding regulation* European Financial Management, Vol. 11, No. 4, 2005, 439–451 available at https://scholar.harvard.edu/files/shleifer/files/02_eufm00121.pdf accessed on 7 August 2019 p 440
[77] Ibid
[78] Botero, F., Djankov, S., La Porta, R., Lopez-de-Silanes, F. and Shleifer, A., 'The regulation of labor', Quarterly Journal of Economics, Vol. 119, no. 4, 2004
[79] George J. Steigler, *'The theory of economic regulation'* Bell Journal of Economics and Management Science, Vol. 2, No. 1 (Spring, 1971), available at https://www.jstor.org/stable/3003160 p. 3-21
[80] Richard Posner p 3
[81] Andrei Shleifer p 441

The second criticism towards public interest theory suggests that in the event of a market operation inefficiency then private litigation may be the most appropriate route to seek remedy.[82] According to Coase, the private litigation route offers the complainant an opportunity to seek redress through e.g. having a contract enforced and adhering to the common law rules on tort. For instance, an employer can have a clause in the contract stipulating the options an employee has in the event of an accident at the workplace. Similarly, issuers of security can voluntarily disclose information about the securities to potential investors in order to minimise information asymmetry.[83] A caveat on the criticism proposes that this is only efficient in a system that respects the rule of law and is ready to enforce these contracts. And when this happens, the desire for government intervention through regulation is limited.

The third criticism to the public interest theory follows up on the above mentioned two criticisms, advancing that even if the courts and the market are incapable of solving the market operations inefficiencies, still the scope for the desire for government regulation is limited because government regulators are 'incompetent, corrupt, and captured' thus regulation worsening the situation.[84] This is the crux of Stigler's theory, where he questions the benevolence of the government.[85] First, the government is forcefully captured by the industry.[86] So instead of the government intervention eliminating monopoly it sustains it. Secondly, in most markets that enjoy the privilege of having organised consumer groups, government regulators that promote social welfare are normally incompetent thus leading to the consequent failure of the social welfares.[87] And even if they were competent, an effective government intervention is like 'a firm whose production costs are very high and increase with alternate an increase in output.'[88] All these factors make government regulation of the market economy undesirable.

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[82] Coase, R., 'The problem of social cost', Journal of Law and Economics, Vol. 3, 1960, pp. 1–44.
[83] Ibid
[84] Andrei Shleifer p 440
[85] Arrow, Kenneth J. (1970), '*The Organization of Economic Activity: Issues Pertinent to the Choice of Market Versus Nonmarket Allocation',* in Haveman, Robert H. and Margolis, Julius (eds.), Public Expenditure and Policy Analysis, Chicago, Rand MacNally College Publishing Company, 67-81 cited in Johan den Hertog, *Review of economic theories of regulation* Discussion paper series 10-18
[86] Stigler, G. J., *The theory of economic regulation*, Bell Journal of Economics, Vol. 2, 1971, pp. 3–21
[87] Richard Posner p 11
[88] Isaac Ehrlich & Richard A. Posner, '*An Economic Analysis of Legal Rulemaking',* 3 J. Leg. Studies 257 (1974)

2.2.1.2. Marxist Theory

In contradicting the public interest theory, the Marxist theory propounds that the driving force behind economic regulation is not public interest benefits, but rather how various (regulated) interests groups can promote their private interests.[89] It conforms to the syllogism that capitalists wield so much power in the market economy that they often control important institutions, e.g. regulation, thus it is justifiable that capitalists control regulation. Despite the fact that the theory sounds appealing to the ear, the syllogism is wrong. This is so because regulation does not only serve the interests of the capitalists (big businesses) but rather intervenes to protect the interests of small enterprises like barber shops, kiosks, pharmacists, and most importantly unions.[90]

Stemming from the Marxist theory of regulation is the "capture" narrative which suggests that the regulated capitalists with time dominate the regulatory agencies, and this explains why some interests are well taken care of by the regulators while other are not, and also why some of these interests succeed or not.[91]

This theory has also received its fair share of criticism. First, its ideologies are not any different from the public interest theory since the underlying score between both of them is the protection of interests of a particular group of people in the market economy.[92] Secondly, Richard Posner criticizes it for not meeting the basic threshold of a theory, thus describing it as a hypothesis whose assumptions have failed terribly.[93] This is so because the theory fails to convincingly explain why the conquest metaphor characterizes the interplay between the regulator and the regulated.[94] Besides, the theory falls short for not explaining the rationale behind the capitalists being the only interest group that can influence the regulator, yet other players like consumers also contribute largely to the economy performance.[95]

In addition, no exegesis has been advanced to explain the rationale behind the capitalists' ability to capture the extant regulator, instead of establishing a new one that will categorically take care of its interests. Besides, if these capitalists wield so much power over the regulator, then they should be in a position of preventing the existing regulator from being created in

[89] Richard Posner p 11
[90] Ibid
[91] David B. Truman, '*The Government Process: Political Interests and Public Opinion*' (1951) as cited in Richard Posner, *Theories of economic regulation*, working paper no 41 May 1974 available at https://www.nber.org/papers/w0041.pdf p 11
[92] Richard Posner p 11
[93] Ibid
[94] Ibid
[95] Ibid

the first place.[96] Finally, the criticism maintains that the theory, despite the glaring plethora of evidence founded on the structural and procedural characteristics of regulation, fails to acknowledge the import of consumers in the market economy.[97] Most regulators protect the interests of consumers instead of the producers.

As a solution, George Steigler quips, evocatively so, that given the positive outcomes of government intervention in the economy, the allocation of such intervention (regulation) is dependent on the laws of supply and demand.[98] And in order to spot such demand and supply, the potential regulators should eye the position of cartels. If treated to the rules of demand and supply, then the product e.g. regulation, will be channelled to the most appropriate clientele.

2.2.2. Theories of International Movement of Capital

Any change in an economic activity significantly affects capital movement.[99] Two contender theories explain such syllogism: the 'classical' theory and the 'modern' theory.[100]

2.2.2.1. Classical Theory

Mill's theory, to quote verbatim, states:

> Commerce being supposed to be in a state of equilibrium when the obligatory remittances begin, the first remittance is necessarily made in money. This lowers prices in the remitting country, and raises them in the receiving. The natural effect is that more commodities are exported than before, and fewer imported, and that, on the score of commerce alone, a balance of money will be constantly due from the receiving to the paying country. When the debt thus annually due to the tributary country becomes equal to the annual tribute or other regular payment due from it, no further transmission of money takes place, the equilibrium of exports and imports will no longer exist, but that of payments will, the exchange will be at par, the two debts will be set off against one - another, and the tribute or remittance will be virtually paid in goods. The result . . . will be . . .: the paying country will give a higher price for all that it buys from the receiving country, while the latter, besides receiving the tribute, obtains the exportable produce of the tributary country at a lower price.[101]

On the face of it, no objection has been raised as to the theory's applicability to foreign lending or tribute.[102] However, an analysis of the theory exposes that the theory ignores some

[96] Ibid
[97] Ibid
[98] George J. Steigler p 9
[99] John Knapp, '*The theory of international capital movement and its verification'* The Review of Economic Studies, Vol. 10, No. 2 (Summer, 1943), pp. 115-121, Oxford University Press available at https://www.jstor.org/stable/2967428 accessed on 8 August 2019 p 115
[100] Ibid
[101] Mill JS, *Principles of Political Economy*, Book III Chapter II
[102] John Knapp p 115

fundamental elements, making it almost impossible to appreciate the existence of the theory's assertion.[103] For example, according to Mill, payments raise and lower the interest rates in the paying and receiving countries respectively. This, normally, causes a reduction of income in the former and an increase in the latter. This syllogism cannot be ruled out *ab intio,* but there is no sufficient evidence for asserting its occurrence.[104] This is so because if the change in interest rate is insignificant as compared to the change in exports, whether a shift in interest rates will, *in sui,* cause a global increase or decrease instead of the opposite shift of incomes of paying and receiving countries is left to chance.[105] Mill takes this chance for granted.

2.2.2.2. Modern Theory

Whereas Mill's classical theory emphasises the role interest rates play in the commercial field, the modern theory (others refer to it as 'income' theory) does not acknowledge it at all. According to Iversen,

> In the absence of capital movements the total amount of buying power in each of the two regions will correspond to the value of its total social product. The effect of the loan is to increase the aggregate of buying power in A and reduce it in B; it enables A to buy a larger share of the combined social products of the two regions . . . whereas B must be content with a smaller share. . . .An international capital transfer is likely to affect the direction of demand . . . and also the localisation of demand. Other goods will be demanded . . . at different places. . .[106]

The modern theory dwells on the assumption that foreign securities purchasers should simultaneously contract their current expenditure.[107] Meaning home investment is sacrificed at the expense of foreign securities, consequently diminishing the propensity to consume.[108] Similarly, the theory is founded on an ideologically convoluted narrative that purchasers of foreign securities do so to raise the prices of those securities. However, based on recent trends, the theory has fallen short of its glory since instead of raising the prices of the securities, security borrowers spend the money.[109] Therefore, demand, as well as interest rate, is left unaltered.[110]

[103] Ibid
[104] Ibid
[105] John Knapp p 115
[106] Iversen, *International Capital Movements*, p. 452
[107] John Knapp p 116
[108] Ibid
[109] Ibid
[110] Ibid p 117

As a critique, Knapp proffers that 'movement of capital is said to have occurred *if* it is proven that trade movements were as a result of consequent movement of interest rates caused by increased foreign lending, and *nothing less.*'[111]

Given that the premises upon which both the classical and modern (income) theories are founded are not true, several other models have emerged to further demystify the theories behind international movement of capital. They are, in piecemeal:

2.2.2.3. Adam Smith's theory

According to Smith, capital accumulation is dependent upon the rate of saving and investment.[112] The ability to save is limited to one's income, as such, as long as profits exceed investment risks then capital accumulation is guaranteed.[113] This is summarised by the equation below:

$$dk/dt = k(r-r^*,y) \qquad \text{where } dk/dt > 0$$

r = rate of profit at a time t

r* = minimum profit needed to cover investment risk

2.2.2.4. Ricardo's Theory

Just like Smith, Ricardo propounds that capital accumulation is dependent upon income increase and consumption reduction, and the rate of such capital accumulation is dependent on the willingness and ability to save.[114]

2.2.2.5. Marxian Theory

The theory suggests that capital accumulation is dependent upon accumulation of profits as a result of surplus production caused by labour.[115] The theory maintains that this is the reason why capitalists exploit labour in the name of profit accumulation, being the main driving force behind the rise and fall of capitalism.

2.2.2.6. Gurley and Shaw's Theory

According to the two theorists, with economic development comes self-financed capital investment which necessitates bank-intermediated debt financing and consequently equity

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[111] John Knapp p 119

[112] Shodhganga, *International capital movement: a theoretical overview* available at https://shodhganga.inflibnet.ac.in/bitstream/10603/13010/9/09_chapter%202.pdf accessed on 9 August 2019 p 1

[113] Ibid

[114] Ibid

[115] Ibid

markets as additional sources.[116] To back up the theory, Adam Smith quips that liquid equity markets make investments less risky and more attractive since they permit savers to purchase assets and thereafter dispose of them when need arises, consequently leading to more saving and investment.[117]

2.3. Competing Approaches to Regulation of Factoring

Should factors be regulated or not? This is a question that has been fodder for academics. This chapter will answer this question by outlining the three *usual* and *basic* ways of regulating factors. The degree and mode of regulation of factors in a country largely depends on the nature of the regulation of all the country's financial institutions. To some extent, others also depend on whether the country is part of the wider international financial community like a regional economic community. This chapter does not necessarily limit itself to regulation of the factoring industry by countries in a common market, but rather, as a whole, how countries (their membership to a regional economic community regardless) *generally* regulate (or not) their factoring industries. This is in a bid to establish the basic ways in which the industry can be regulated.

The following section will analyse the three basic approaches to regulation of the factoring industry as laid out by Hulki Kara in the 2017 World Factoring Yearbook.[118]

2.3.1. Laissez Faire

In this approach, Kara quips that there is no specific regulatory authority governing the industry. Instead, factoring is governed within the extant fiscal framework. Most factors and other non-bank financial institutions operate based on their corporate governance principles and other contractual obligations. An example of this form of *laissez faire* form of regulation is seen in Cyprus.

2.3.1.1. Cyprus

According to the EBRD Survey,[119] the country's factoring industry is largely unregulated thus the inexistence of any requirements regarding licencing, reporting and capital adequacy. Besides, there is no supervisory body supervising the industry. It is also noteworthy that the

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[116] Shodhganga p 4
[117] Shodhganga p 5
[118] Hulki K. *To regulate or not to regulate factoring?* World Factoring Yearbook 2017 available at p 4
[119] Factoring survey in EBRD countries of operation conducted by the European Bank for Reconstruction and Development on September 2018 available a t< https://www.ebrd.com/documents/ogc/factoring-survey.pdf > accessed on 29 July 2019

country is not a party to both the UNIDROIT Convention on International Factoring and UNCITRAL Convention on the Assignment of Receivables in International Trade. The factoring industry in the country largely depends on its corporate governance principles and contractual obligations.

As a country's principle, any payment made on accounts receivables by obligors to buyers or sellers are not subjected to any form of withholding tax. Similarly, any payment made by an obligor out of the country to a buyer or seller who is a non-resident of Cyprus will attract no VAT. However, if both the obligor and sellers or buyers are tax residents in Cyprus, any interest on payments will be susceptible to the withholding tax.

2.3.2. Public Regulatory Authority

According to Kara, the government, through the Central Bank, takes a central role in regulating its factoring industry and other non-bank financial institutions. In most countries, the Central Bank uses regulations that are quite distinct from the other commercial banks to regulate the non-banking financial institutions.

This approach to regulation can take place in three different models:

2.3.2.1. Silo Model

As seen in both Kenya and Tanzania, this model regulates and supervises financial institutions in accordance with their functions e.g. banking, insurance and the securities sectors. Every sector is supervised by a different regulatory authority. Therefore, if factoring services are offered by insurance companies then the relevant regulatory body in charge of insurance companies will regulate those factoring services. The same applies to banks.

However, this model has been criticized for not taking into account the existence of conglomerates where deposit-taking commercial banks also offer insurance services and can also provide factoring services. Such a financial institution will have to be regulated by the three different regulatory bodies. The shortcoming of this is that it may lead to regulatory arbitrage.

2.3.2.1.1. Kenya

Kenya is an example of a financial system that uses this model. The Central Bank of Kenya, which was established in 1966 under the auspices of the Central Bank of Kenya Act, is responsible for the formulation and implementation of the country's monetary policy in a bid to attaining price and financial stability.[120] All banks that offer factoring services fall under the umbrella of the Central Bank. On the other hand, the Insurance Regulatory Authority, established within the ambits of the Insurance Act (Amendment) Act of 2006, is largely responsible for ensuring compliance with legal requirements by (re)insurance companies and intermediaries. Therefore, all insurance companies that offer factoring services are regulated and supervised by the Insurance Regulatory Authority.

The other regulatory bodies governing the financial system include;

a) The Capital Markets Authority that is largely responsible for providing funds for the country's long term development of the capital market by removing impediments to the attainment of such development;
b) Kenya Revenue Authority that in charge of regulation and supervision of the tax system on behalf of the government;
c) The Ministry of Finance that is responsible for formulating, implementing and monitoring macro-economic policies related to expenditure and revenue.

2.3.2.2. Unified Model

As in Malawi, this approach entails a single universal public regulatory authority, normally the Central (Reserve) Bank, regulating and supervising all the financial institutions in a country.[121] The single universal regulator ensures both safety and proper conduct of business requirements are adhered to. With the rapid proliferation of conglomerate institutions like Equity Bank of Kenya, this type of regulation is beneficial in that it creates certainty in the law since it regulates and supervises these conglomerates without creating unnecessary confusion, thus no conflict over jurisdictional lines.[122]

Besides, unlike in 'twin peak' that could lead to duplicity of roles, unification minimizes duplicity and reregulation since a single body regulates and supervises all the institutions.[123]

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[120] *Central Bank of Kenya Act* of 1966 sec 4
[121] Llewellyn DT *Institutional Structure of Financial Regulation and Supervision: The Basic Issues* (2006); Countries like Malawi have embraced this type of regulation, where the Reserve Bank of Malawi takes charge of the Malawian financial institutions
[122] G30 report 2008 p 14
[123] Quinn J 'Rainmaker: *Twin Peaks regulation gets a poor review'* The Telegraph 31 March 2012 accessed 20 at http://www.telegraph.co.uk/finance/comment/james-quinn/9178018/Rainmaker-Twinpeaks-regulation-gets-a-poor-review.html as accessed on 24 July 2019

In addition, it prevents regulatory arbitrage by the investors and a race to the bottom by the regulator since there will be no regulatory lax and competition for a better regulated sector.[124]

However, its shortcoming is that it may create the risk of unchecked powers of the regulator.[125] Besides, unlike in a 'twin peak' and silo system that has flexible regulators and supervisors, the unified model lacks an attractive regulatory framework since it fails to appreciate the dynamic nature of the financial sector.[126] In addition, a unified system fails to steer competition and innovation among the institutions, a fact that can be cured by a silo model since a silo focuses on a particular sector only, thus promoting specialization.[127]

2.3.2.2.1. Malawi

Malawi adopted a fully unified model of financial regulation. The Reserve Bank's Governor, by virtue of the Financial Services Act,[128] is both the regulator and supervisor of all the financial institutions in the country.[129] The Reserve Bank of Malawi not only ensures compliance with the financial stability rules, but also monitors the conducts surveillance in order to tighten its financial sector. In a bid to cushion itself from external contagion and enhance its resilience, the government of Malawi teamed up with the Reserve Bank to adopt several policy drives.[130]

One of them is the Pensions[131] and insurance department that is in charge of the insurance and pension industry, the bank supervision department that supervises the banking activities to ensure compatibility, and the capital markets department that is responsible for funding the country's long term development. All these, although conducting different functions and dealing with different institutions, are housed under the Reserve Bank of Malawi, thus the

[124] Financial Services Authority Occasional Paper 2 The Rationale for Single National Financial Services Regulator (May 1999) 11
[125] International Monetary Fund Working Paper, *Issues in the Unification of Financial Sector Supervision* (December 2000); International Monetary Fund Working Paper, *Regulatory and Supervisory Independence and Financial Stability* (March 2002) 10; See also Madise S *Developing an Independent Regulatory Framework for the Financial Sector in Malawi* (unpublished LLM thesis, University of the Western Cape 2010-2011)
[126] Di Giorgio G & Di Noia C *'Financial Market Regulation and Supervision: How Many Peaks for the Euro Area?'* (2003) Brooklyn Journal of International Law 4
[127] PEW Economic Policy Department Financial Reform Project The International Experience with Regulatory Consolidation Briefing Paper p 6 (2009)
[128] Malawian Financial Services Act available at https://www.rbm.mw/documents/basu/FINANCIAL%20SERVICES%202010.pdf accessed on 29 July 2019
[129] *Financial Services Act* Preamble; See also Mitchaisi Chintengo presentation on regulation of financial cooperatives: the case of Malawi being the Chief Examiner (Microfinance Institutions and SACCOS) at the Reserve Bank of Malawi accessed 12 December 2014
[130] Ibid
[131] *Pensions Act* 2011

unified approach. Therefore, in Malawi, factors, the service provider regardless, are all under the direct supervision of the Reserve Bank, although under different departments.

2.3.2.3. Twin Peak Model

As seen in the South African regulatory system, this model of regulation driven by objective, whereby prudential supervision is a function of one regulator whereas the conduct of business is a preserve of another regulator.[132] Expressed differently, the former regulator is concerned with the protection of the customers' assets whereas the latter concerns itself with consumer protection.[133] The benefits of this model is that each regulator has clearly defined objectives with proper checks and balances.[134] Besides, it has been lauded for having a balanced regulatory and supervisory framework thus preventing regulatory arbitrage.[135] Just like the unified approach, this model is also in a better position to regulate conglomerates.[136]

The demerits of this model is that the financial institutions are susceptible to overregulation.[137] Also, if the objectives are not clearly defined, it may lead to an overlap of regulatory obligations.[138]

2.3.2.3.1. South Africa

South Africa prides itself in having a well-established financial regulatory system. It shifted from having a combination of self-regulatory organizations and multiple government agencies to having a twin peak model of regulation in 2007. The South African Reserve Bank has the overall duty of overseeing banking activities. Similarly, the Financial Sector Regulation Act of 2017 establishes a Prudential Authority that supervises banks, insurance companies, and other financial institutions that offer factoring services to ensure they comply with the requirements of the Bank Act[139] and Insurance Act (2018) respectively. The

[132] Strickett C '*What do the changes in regulation mean for the SA insurance industry?*' Cape Times Business Report 30 April 2015
[133]Ibid
[134] lewellyn DT *Institutional Structure of Financial Regulation and Supervision: The Basic Issues* (2006) 28
[135] Group of Thirty The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace (2008) 40 available at
http://www.group30.org/images/PDF/The%20Structure%20of%20Financial%20Supervision.pdf accessed on 25 July 2019
[136] Taylor M *'The Road from "Twin Peaks" and the Way Back'* (2009) 16(1) Connecticut Insurance Law Journal
61 80.
[137] Quinn J 'Rainmaker: *Twin Peaks regulation gets a poor review'* The Telegraph 31 March 2012 accessed 20 February 2015 at https://www.telegraph.co.uk/finance/comment/james-quinn/9178018/Rainmaker-Twinpeaks-regulation-gets-a-poor-review.html accessed on 25 July 2019
[138] Financial Services Authority Occasional Paper 2 *'The Rationale for Single National Financial Services Regulator'* (May 1999) 25
[139] Financial Sector Regulation Act 2017 sec 4

Financial Service Conduct Authority is in charge of overseeing the conduct of financial institutions (like those of factors) including how they treat their consumers.[140] Another regulator is the Financial Intelligence Centre ensures that financial institutions are accountable and comply with the requirements of Know-Your-Client in the Financial Intelligence Centre Act of 2001.

2.3.3. Autonomous Self-Regulatory Organization (SRO)

Most people view government regulations as the bane of commercial financing.[141] This has largely contributed to the recent shift of SMEs from the highly regulated industries to the less regulated ones in order to get financing.[142] One of the areas with less government regulation is the self-regulated industries. A self-regulatory organization is a non-governmental organization with the mandate of creating and enforcing regulations and standards.[143] The SRO often guards the industry against professional misconducts and other malpractices.[144] In most cases, its ability to act as a watchdog does not flow from governmental power donation. Instead, its ability to do so stems from its internal mechanisms or external agreements among participants of the industry.[145] This is in a bid to exclude government intervention.

The regulations set by the SRO are often binding, such that a participant's failure to adhere to them attracts some sanctions.[146] These regulations set the standards and conditions to be met before becoming a member. The SRO can also undertake to educate its members on the most appropriate business practices. Besides, the SRO can also have the power to resolve disputes among its participants.[147]

The merits of a self-regulation include minimising information asymmetry, boosting consumer confidence, being flexible enough to accommodate new entrants, internalizing ethical behaviours since the rules are based on a peer approach and not the top-down government model.[148] Its limitations can be either economic or legal. The economic implications include the free rider challenge where non-participants that conduct the same business but are not members of the SRO can still enjoy the benefits of the SRO. Besides,

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[140] Centre for International Finance and Regulation Research Working Paper Series *'The Financial Sector Regulation Bill in South Africa: Lessons from Australia* (January 2015)
[141] *Business factors and finance* available at https://businessfactors.com accessed on 25 July 2015
[142] Ibid
[143] Mitchel G. & Adam H. *'Self-regulatory organization – SRO definition'* dated 19 July 2019 available at https://www.investopedia.com accessed on 25 July 2019
[144] Ibid
[145] Ibid
[146] Ibid
[147] Ibid
[148] Ibid

SROs may hardly regulate the intricacies of the industry, especially where government regulation comes in to protect issues to do with fundamental rights.

2.3.3.1. United States of America

The factoring industry in the USA is not regulated by any formal government body.[149] This prompted most factors to team up to form various organizations where they share their best practices and regulate their activities. Some examples of Self-Regulatory Organizations in the USA are the International Factoring Association, Independent Factoring Standards Association, the Secured Finance Network, etc.

The Secured Finance Network is one of the SROs that brings together all data, tools, and providers of capital like factors, finance companies and secured lenders.[150] The SRO fosters interests that generate opportunities for its members. Besides, it imparts best practices by training its members through in-person and online training.[151] It also represents its members in advocating for critical issues that impact on the factoring industry.

The Independent Factoring Standards Association is another SRO that advocates for a more self-regulated factoring industry in the USA.[152] The SRO enhances consumer education by advocating for enhanced transparency among factors.[153] The SRO boasts of having the world's largest and publicly available factoring companies' database. The SRO's objectives include creation of awareness of the existence of the factoring industry, train its members on the use of best practices, achieve uniformity, and to set minimum standards upon which members are to comply with.[154]

2.4. Regulation of Factors in a Common Market: The Hybrid Approach

The previous sections of this Chapter established the various approaches towards regulation of financial institutions like factors. However, this was a broad analysis aimed at laying the foundation of how factors can be regulated. It is also noteworthy that the analysis did not establish how factors can be regulated in an international financial community, given that countries, like those in the EAC common market, are mandated to ensure that free movement

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149 Business Factors and Finance *How are invoice factoring services regulated* available at https://businessfactors.com/invoice-factoring-services-regulated/ accessed on 30 July 2019

150 Secured Finance Network available at https://www.sfnet.com/utility-navigation/about-sfnet accessed on 30 July 2019

151 Ibid

152 Independent Factoring Standards Association available at https://www.factoringcompanyguide.com/factoring-organizations/independent-factoring-association-ifsa/ accessed on 30 July 2019

153 Ibid

154 Ibid

of capital within the common market is achieved. The approach used by an EAC Partner State to regulate its factoring industry will determine whether or not free movement of capital within the common market is achieved. This section demystifies the chimera of free movement of capital and consequently suggests a hybrid approach that will ensure that the factor of production freely moves within the common market. This is so because *global games require global rules*.

2.4.1. Hybrid Approach

As exposed by the 2007 financial crisis, the absence of government rules does not mean business entities engage in bad behaviour, neither does their presence imply they are engaging in good behaviour.[155] As earlier on stated, state government regulation can be more restrictive or permissive.[156] It could be a source of conflict in the economy since whereas others may want the intervention to be more restrictive in a particular industry, others favour a more permissive approach.[157] A permissive government regulation favours the autonomy of the participants in the market economy thus self-regulation, whereas a restrictive one circumscribes their autonomy.[158]

Government regulation of business entities uses the ‘coercive power’ of the state to regulate *inter alia,* prices, new entrants, investment, foreign invasion, growth of start-ups.[159] The benefits of government regulation include: ease of comprehension; certainty of sanctions; minimises information asymmetry; and predictability.[160] On the flipside, the limitations include: the cost of implementation; prevention of the operation of price mechanism; and may lead to government failure if such regulation leas to misallocation of resources.[161] It is therefore safe to conclude that government regulation cannot be plainly understood as a blanket efficient remedy for market failure.[162] Contextually, how government regulates

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[155] Daniel Castro, Benefits and limitations of industry self-regulation for online behavioral advertising, *The information technology and innovation foundation* dated December 2011

[156] Porket JL., *The pros and cons of government regulation*, Institute of Economic Affairs, 3rd IEA discussion paper dated 23 January 2003 available at https://www.iea.org.uk accessed on 25 August 2019

[157] Ibid

[158] Ibid

[159] Nancy Rose, *Regulation, political economy of,* International Encyclopedia of the Social & Behavioral Sciences (2nd ed) 2015 available at https://doi.org/10.1016/B978-0-08-097086-8.71033-6 p 178-180

[160] Smith T., *Government regulation*, dated 5 January 2013 available at https://getrevising.co.uk accessed on 28 August 2019

[161] Ibid

[162] Ibid

financial institutions like factors affects the industry in diverse ways.[163] On the other hand, government regulations enhances accountability, increases internal controls, increases consumer confidence due to cemented and clearly structured consumer protection guidelines.[164] The major demerits are that it increases the workload for people ensuring that such regulations are implemented, increase in costs, and also stifles innovation.[165]

It is for these reasons, among others, that there have been numerous calls for deregulation by the government in the financial markets and instead have a self-regulatory organization (SRO).[166] Self-regulation may be defined as a 'regulatory process whereby an industry-level organization (such as trade association), as opposed to governmental- or firm-level organization sets and enforces rules and standards relating to the conduct of firms in the industry.'[167] Business have often opted for self-regulation to enhance consumer confidence and combat the adverse effects of government regulation. In most instances, self-regulation comes in as a response to excessive government intrusion or in cases where the government has not regulated.[168]

Most financial SROs involve many stakeholders, including those that represent consumers and the public at large. Such stakeholders engage in crafting rules and monitoring for compliance, thus addressing concerns beyond the narrow purview of government regulation e.g. protection of other stakeholders. The benefits of a self-regulatory organization include: faster rulemaking, monitoring, enforcement and remediation process as compared to government regulation, thus enabling sooner protection of consumers.[169] Besides, self-regulation encourages entities to internalize ethical behaviour and principles since they are based on social norms and conduct of peers rather than top-down approach taken by government regulation.[170] In addition, self-regulation minimises information asymmetry in the market.[171] For example, most SROs have in place independent third party organizations

[163] Investopedia, *How government regulation affects the financial services sector*, dated 14 July 2019 available at https://www.investopedia.com-how-government-regulation-affects-the-financial-services-sector.asp accessed on 28 August 2019
[164] Ibid
[165] Ibid
[166] Ibid
[167] Anil G. & Lawrence J., 'Industry self-regulation: an economic, organizational and political analysis,' *The Academy of Management Review* 8, no 3 (1983) p 417
[168] Boddewyn JJ, 'Advertising self-regulation: private government and agent of public policy' *Journal of Public Policy and Marketing* 4 (1985) p 131
[169] Daniel Castro, Benefits and limitations of industry self-regulation for online behavioral advertising *The information technology and innovation foundation* dated December 2011 p 5
[170] Ibid
[171] Ibid

that are responsible for monitoring compliance.[172] Further, where government regulation protects established interests, self-regulation is more flexible enough to accommodate new entrants and other market participants.[173] Such flexible regulations provides firms with a conducive environment to operate efficiently, besides minimising compliance costs. The end result of such efficient operation is more innovation.[174]

SROs in the financial sector have received their fair share of criticisms. For example, if not properly supervised, they may encourage money laundering and protect the interests of a few individuals.[175] Besides, SROs are not effective in instances where solutions are known and the circumstances unlikely to change, neither in high-risk situations.[176] Finally, without express or implied endorsement by the government the SRO may suffer from adverse impacts of regulatory uncertainties and lack of public confidence.[177]

Given that most jurisdictions have opted for either active government regulation of the domestic financial markets as others opt for self-regulation, settling on one approach to regulation of factors is catastrophic. This is so because the demerits of government regulation, in most instances, far outweigh the advantages thereof. On the flipside, if SROs are left to operate on their own there may be instances of money laundering, protecting their own interests etc. amounting to putting a fox in charge of the hen house.

This research study, therefore, proposes that at the regional level, it is impertinent that EAC Partner States come up with a regional self-regulatory organization empowered with legislative powers to set standards for factors, dispute resolution and enforcement powers, regularly updates its members of factoring statistics in the region, periodically offers training services to factors providing them with updated information on how best to improve their services, etc. The regional SRO will be comprised of national associations of factors with similar powers in their respective national jurisdictions. Similarly, the level of government involvement in those national associations of factors is limited to supervision.

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172 Ibid

173 Daniel Castro, Benefits and limitations of industry self-regulation for online behavioral advertising *The information technology and innovation foundation* dated December 2011 p 6

174 Lisa S., Stephen T., & Kelly D., 'The food industry and self-regulation: standards to promote success and to avoid public health failures' *American Journal of Public Health* 100, no 2 (2010) p 242

175 Daniel Castro, Benefits and limitations of industry self-regulation for online behavioral advertising *The information technology and innovation foundation* dated December 2011 p 6

176 Neil G. & Joseph R., 'Industry self-regulation: an institutional perspective,' *Law & Policy* Vol. 19 No. 4 (1997)

177 Christopher Marsden, *Internet co-regulation: European law, regulatory governance and legitimacy in cyberspace* Cambridge University Press (2011)

In order to counter the adverse impacts of self-regulation like money laundering, this paper proposes that the regional SRO will periodically report to the Partner States the progress of the regional factoring industry. This, therefore, means that there will be co-regulation of the factoring industry, comprised of the regional SRO that is in charge of the prudential actions of the factors, whereas the EAC Partner States will be in charge of supervision to ensure compliance and consistency with their domestic and international financial obligations. The end result is a 'best of breed' combination that conflates narrowly-tailored government regulations and supervisory guidelines and a Self-Regulatory Organization (SRO) empowered with legislative, dispute resolution and enforcement powers over the activities of factors.

2.5. Conclusion

This Chapter aimed at evaluating the various theoretical frameworks underpinning regulation of cross-border investment of factors, economic regulation and international movement of capital, and the competing approaches towards regulation of factors. In order to do so, it first laid the foundational ideologies on what factoring is, its benefits and its relationship with movement of capital in an internal market. It then analysed the various theories that have been advanced to explain the need for government intervention through regulation of the economic environment. The major theories that the study analysed are the public interest and the Marxist theories. In addition, the study looked into the theories underpinning international movement of capital. The major rival theories were the classical and modern (income) theories. Also analysed were Adam Smith's, Ricardo, Marxian, Gurley and Shaw's theories. Finally, the study looked into the competing approaches towards regulation of factors in order to establish, generally so, how factors are regulated in other jurisdictions. Importantly, the Chapter came up with a hybrid approach to regulation of factors in a Common Market that will aid in formulating sound regionally-approved regulations and policies that will enhance free movement of capital through cross-border factoring.

CHAPTER THREE

LEGAL FRAMEWORK GOVERNING FACTORING WITHIN THE EAC COMMON MARKET

3.0. Introduction

There is no legislative instrument exclusively governing factoring within the EAC. What exist instead are fragmented sections of the various civil laws, both regionally and domestically. These laws include the various agreements signed by the EAC Partner States, their respective constitutional provisions and common law underpinnings. According to Sylvia Ostry[178] 'the WTO is too large an organization with too few analytical and technical resources to foster dialogue, training, knowledge diffusion and networking that is essential for forging mutually accepted policy outcomes.' She states that the creation of a wider market can be catalysed at the regional level by the regional institutions. With this epiphany, the EAC Partner States took this position to ratify some agreements among them.

This section describes and analyses the law relating to factoring within the Community. This chapter is important because there exists a lacunae in this area, with regards to enhancing free movement of capital within the area. How best to resolve this lacunae is to fill the gaps in this area through deregulation of the current policy and legal framework governing factoring as a form of trade finance. A piecemeal elaboration of the relationship between cross-border factoring and movement of capital is also imperative.

3.1. International Legal Instruments

EAC Partner States e.g. Kenya in its Constitution,[179] have provided a cemented status to international laws and have gone ahead to ratify some. Due to the challenges of different legal systems governing factoring, institutions like the International Factors Group (now integrated into Factors Chain International), the UNIDROIT and the UNCITRAL deemed it fit to come up with guidelines that would govern international factoring, with an aim of harmonizing the rules for greater certainty and predictability.

These legal instruments are briefly discussed hereunder:

[178] Ostry S. *Reinforcing the WTO*, Occasional Paper 56, Group of Thirty (1998)

[179] Constitution of Kenya 2010 art 2(5) provides that the general rules of international law shall form part of the law of Kenya. Article 2(6) goes ahead to state that any treaty or convention ratified by Kenya shall form part of the law under the Constitution.

3.1.1. UNIDROIT Convention on International Factoring (1988)

The Convention is effective[180] having attained its minimum ratification threshold.[181] However, none of the EAC Partner States has ratified this Convention, save for Tanzania that signed it on 28 May 1988, but has since joined its EAC sisters in not ratifying the Convention. Its plurilateral nature gives it a non-binding aspect upon the countries that have not ratified it. However, for the sake of this paper, its analysis is imperative since in it are concepts that will be helpful in establishing reasons for such better regulation of factoring laws.

The Convention defines factoring as a a contract between a creditor and a factor whereby the creditor transfers his commercial receivables and performs at least two of the following: (a) provision of finance to the creditor, (b) maintenance of accounts relating to the trade receivables, (c) collection of the trade receivables, and (d) protection against payment risks by the debtor.[182] The Convention, however, gives no clear distinction between the contractual and proprietary facets of factoring, thereby, as a consequence, fails to address the challenges that come with such cross-border transfer of trade receivables.

The applicability of the Convention to a particular factoring contract is dependent on whether the receivables assigned arise from the sales or service agreements between the creditor and a debtor whose places of business are in different states, provided (a) those States, including the factor's, are Contracting States; or (b) both the contract of the sale of goods out of which the receivable arose and the factoring contract are governed by the Contracting State.[183]

3.1.2. UNCITRAL Convention on the Assignment of Receivables in International Trade (2001)

Unlike the UNIDROIT Convention, the UNCITRAL Convention is yet to gain entry into force with only Luxembourg, Madagascar, and USA signing but yet to deposit their instruments of ratification, and Liberia that deposited its instrument of accession in 2005.[184] Five more actions are needed for its entry into force.[185] The EAC Partner States, in the spirit of enhancing cross-border factoring, can (re)consider acceding to this Convention.

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[180] The Convention entered into force on 1 May 1995
[181] The signatories include France, Italy, Nigeria, Germany, Belgium, Hungary, Latvia, Russian Federation, and Ukraine. Available at https://www/unidroit.org accessed on 22 June 2019
[182] UNIDROIT Convention on International Factoring 1988 art 1
[183] UNIDROIT Convention art 2
[184] Information available at https://www.uncitral.org accessed on 22 June
[185] Ibid

This Convention provides a more comprehensive effort in dealing with cross-border factoring issues in comparison to the UNIDROIT Convention.[186] It applies to all assignments involving international receivables if, at the time of the conclusion of the contract of assignment, the assignor is located in a Contracting State.[187] The Convention does not affect the rights and obligations of the debtor unless, at the time of conclusion of the contract, the debtor was located in a Contracting State, or the law governing the contract is the law of a contracting state.[188] It also provides for the rights and obligations of both the assignor and the assignee,[189] and obligates either the assignor or the assignee to notify the debtor of such assignment.[190]

3.1.3. International Factors Group Model Factoring Law (2014)

The Model Law is designed for adoption in whole by countries without changing the substance.[191] This is in a bid to achieve unification of municipal private laws on factoring. Questions concerning matters governed by the model law that are not expressly settled in it are to be settled in conformity with the general principles on which it is based.[192] Further, it encourages legislators to reconsider and modernize their domestic laws on factoring to ensure they are compatible with the model law for the benefit of promoting finance and trade.

The Model Law applies to both domestic and international assignment of domestic or international trade receivables made under a factoring contract.[193] It defines a factor as one who performs *any* of the following functions: (a) 'finance for the supplier, including advance payments that are directly related to the value and risk assessment of the receivables (b) maintenance of accounts (ledgering) relating to the receivables; (c) collection of receivables; collection made by the client for the benefit of the factor is deemed to be made by the factor; and (d) protection against default in payment by debtors.[194]

With regards to international factoring i.e. export and import factoring, such international factoring shall be governed by the rules of an association of which the factors are members, in whose absence, the law mutually consented to by the factors.[195]

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186 Dalhuisen (n 27) p 904
187 The UNCITRAL Convention on the Assignment of Receivables in International Trade (2001) article 1(1)
188 The UNCITRAL Convention article 1(3)
189 The UNCITRAL Convention article 11
190 The UNCITRAL Convention article 13
191 Factors Chain International Model Law on Factoring p 3
192 Ibid
193 Ibid article 1.1
194 Ibid article 1.2.4
195 Ibid article 25.1

3.2. Regional Legal Instruments

At the regional level, efforts have been put forward to establish a regional framework that will guide states to remodel their domestic laws to enhance easier cross-border factoring. Some of them are discussed hereunder:

3.2.1. Afreximbank Model Law on Factoring (2016)

This Model Law borrows heavily from the UNCITRAL Convention (2001). It primarily covers assignment of receivables. Just like the IFG Model Factoring Law, the Afreximbank Model also aims at promoting uniformity of factoring transactions, as such encourages states to adopt it in whole without changing its substance.[196] Its interpretation should be in a manner that promotes uniformity and observance of good faith in the factoring spheres.[197] Noteworthy, it does not provide for the procedures for assignment, neither does it define the various factoring products. Besides, it fails to provide for how factoring companies should be regulated, who can be a factor, tax treatment of the factor's fees.[198]

According to the Law, a factor is one who performs any of the following: (a) 'providing or procuring finance for the client, including loans and advance payments that are directly related to the value of each trade receivable and its perceived credit risk at the time the receivable; (b) maintenance of accounts (ledgering) relatingto the assigned receivables; or (c) collection of assigned receivables'.[199] Also, just like the IFG Model Law, the Afreximbank Model Law equally applies to both domestic and international assignment of domestic or international trade receivables made under a factoring contract.[200] It validates an international factoring contract concluded between persons located in different states provided it satisfies the requirements of either the law which governs the contract or the law of one of those states.[201]

Further, regarding international factoring i.e. export and import factoring, such international factoring shall be governed by the rules of an association of which the factors are members, in whose absence, the law mutually consented to by the factors.[202] Unless otherwise agreed by the factors involved or regulated by the rules of an association of which the factors are both members, the Model Law applies accordingly. To the extent that any shall not apply to

[196] Afreximbank Model Law on Factoring p 4
[197] Ibid p 5
[198] Ibid p 6
[199] Ibid article 1.1
[200] Ibid article 3.1
[201] Ibid article 23.1
[202] Ibid article 24.1

any aspect of their relationship then the applicable law shall be that of the country in which the factor giving the assignment is located.[203]

3.3. Sub-regional Legal Instruments

The EAC has in place, as one of its integral pillars, a common market that is to ensure that free movement of people, goods, services and capital is achieved. The legislative instruments guiding the Partner States towards achieving such free movement include:

3.3.1. Treaty Establishing East African Community (2000)

Article 76 of the Treaty establishes a common market, whose establishment shall be progressive and in accordance with the provided schedules.[204] In evinces that there should be free movement of labour, goods, services, capital, and the right of establishment.[205] The treaty empowered the Partner States to conclude a Protocol to give effect to the establishment of the Common Market.[206]

3.3.2. Protocol for the Establishment of the EAC Common Market (2010)

This protocol came into force on 1st July 2010, following its ratification by all the five EAC Partner States, save for South Sudan that acceded to it upon its joining the Community in 2016. It evinces that Partner States should remove restrictions on the movement of capital belonging to persons resident in the Community.[207] In addition, they are not to exercise discriminatory practices based on nationality, place of residence, or place where capital is invested.[208] They are also to remove restrictions related to current payments connected with the movement of goods, persons, services or capital between Partner States.[209]

However, such restrictions, if need be, must be justified based on prudential supervision, public policy considerations, money laundering, and financial sanctions *agreed* upon by Partner States.[210] A Partner State that adopts any restriction must inform the EAC Secretariat and consequently notify the other Partner States furnishing reasons that such adoption was necessary, reasonable and justifiable.[211] Further, a Partner State can take safeguard measures where such movement of capital causes disturbances in the functioning of its domestic

[203] Ibid
[204] The EAC Treaty article 76(2)
[205] The EAC Treaty article 76(1)
[206] The EAC Treaty article 76(4)
[207] The Protocol article 24(1)(a)
[208] The Protocol article 24(1)(b)
[209] The Protocol article 24(1)(d)
[210] The Protocol article 25(1)
[211] The Protocol article 25(2)

financial market.[212] However, such safeguard measures are not to be discriminatory in favour of third parties, or 'exceed the safeguard measures necessary to deal with the circumstances.'[213] The EAC Council is tasked with the obligation of 'establishing procedures for periodic consultations including, where desirable, prior consultations with the objective of making recommendations to the concerned Partner State for the removal of the safeguard measures.'[214] This instrument, therefore, forms part of the basis on which free movement of capital, at large, and factoring, in specificity, may be regulated among the Partner States.

3.4. Domestic Legal Instruments in EAC Partner States

The Partner States, in compliance with their international obligations, have exuded some exasperating nonchalance toward harmonizing their domestic financial markets in order to ensure the Community achieves its financial integration objective. What is evident, however, is the continued restriction in the domestic legal underpinnings that impede such free movement of capital. This section looks into the various domestic instruments that are not in tandem with the sub-regional, regional, and international provisos alluded to herein before.

The importance of this section is that in so doing, some of the impediments will be exposed, thus encouraging the Partner States to rollback their restrictions. This section adopts the definition that a factor can be a bank, an insurance company, or any other investor who engages in factoring activities. As such, an analysis of legislations relating to general investment, banking and other financial institutions will be made herein. Data on South Sudan has been deliberately neglected due to inadequate relevant online material.

A discussion of the impediments are briefly discussed below.

3.4.1. Constitutional Underpinning

Kenya, being a dualist state, radiates the importance of fulfilling its international obligations.[215] Moreover, it has cemented the status of its national values which include equality, non-discrimination, transparency, and sustainable development.[216] As such, it is obliged to ensure that its domestic legislations are at per with its international requirements. Additionally, the Constitution of Burundi article 59 guarantees foreigners (non-Burundians) in Burundi's territory and their property equal protection it accords its nationals.

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[212] The Protocol article 26(1)
[213] The Protocol article 27(1)
[214] The Protocol article 27(5)
[215] The Constitution of Kenya, 2010 article 2(6)
[216] Ibid article 10(2)

3.4.2. Statutory Underpinning

In Tanzania, a foreign investor is defined in the *Capital Markets and Securities (Foreign Investors) Regulations* as an individual or a corporate body that is a non-Tanzanian.[217] The regulations also restrict both inward and outward investment, which includes factoring. A similar distinction between foreign and domestic investors is seen in its *Investment Act of 1997*. For instance, the Act defines a foreign investor as a person who is not a citizen of Tanzania (or incorporated in Tanzania in the case of a company), a citizen of any EAC Partner State regardless.[218] Similarly, as a business, like a factor, in order to enjoy the benefits and protection that accrue from the Act, a foreign investor or a joint venture must have a capital investment of at least $300,000, a figure way exorbitant compared to their domestic counterparts whose capital investment should be at least $100,000. Further, a foreign investor in Tanzania, e.g. a factor, can obtain credit from Tanzanian financial institutions only to the extent that such credit is used for its intended purpose, whose use can be monitored by the bank issuing the loan, and up to the limit established by the Bank of Tanzania in consultation with the Tanzania Investment Centre.

Uganda's *Investment Code Act* defines a foreign investor as an individual who is not a Ugandan, or a company whose majority of shares (more than 50%) are held by non-citizens.[219] In order to engage in trade in Uganda, a foreign investor, like factors, must first deposit $100,000 at the Bank of Uganda to be used for their purchase of imports or other goods to be traded within the Ugandan jurisdiction. Also, just like Tanzania, a foreign investor in Uganda must make a capital investment of $500,000 in order to be eligible for the incentives under the Act. Their domestic counterparts should make a paltry $50,000 capital investment. However, there have been recent positive developments to amend the Act to accommodate the provisions of the EAC Treaty. For instance, the *Investment Code Act* of 2019 amends the previous Act to define a foreign investor as a natural or artificial person who is not a citizen of an (or incorporated, in the case of companies, in) East African Community Partner State.[220] Its definition of a domestic investor acknowledges the locality of other nationals of other EAC Partner States.[221] Despite such positive strides, the Act defines foreign capital as any convertible currency, other than good will, that enter Uganda

[217] Capital Markets and Securities (Foreign Investors) Regulations, 2014 regulation 2
[218] The Tanzanian Investment Act 1997 section 3
[219] Investment Code Act section 9
[220] Uganda Investment Code Act 2019 section 1
[221] Ibid

(from other EAC partner states regardless) with initial disbursement of Uganda's foreign capital intended for the production of goods and services related to a business enterprise.

Quite commendably, the Kenya *Insurance Act* of 2015 mandates insurance companies (including those that provide factoring services) registered in Kenya to ensure that they are body corporates registered under the Companies Act 2015 and at least a third of their controlling interests in the body are held by citizens, a corporate body whose shares are wholly owned by citizens of an EAC Partner State; a partnership whose partners are all citizens of a Partner State of the EAC; or by a body corporate whose shares are wholly owned by citizens of a Partner State of the EAC or the government, or a combination of both.[222] The same ownership rule applies to at least 60% of the paid-up capital of insurance brokerages. As far as minimum capital requirements is concerned, out of the amount of the paid-out capital, not less than one-third shall be owned by citizens of the EAC Partner States, by a partnership whose partners are all citizens of such states, wholly owned by citizens of such states or by the Government.[223] However, such a body corporate incorporated in Kenya with or without a share capital shall not be registered and if registered shall have such registration cancelled if at least one-third of the members of its board of directors or managing board are *not citizens of Kenya.*[224]

Just like Kenya, in Rwanda, according to its *Law on Investment and Export Promotion and Facilitation* of 2015, a foreign investor is a natural person who is not a citizen of Rwanda or of a member state of the EAC or COMESA; a business company or partnership not registered in Rwanda, a member state of the EAC or COMESA; or a business company or a partnership registered in Rwanda whose foreign capital from countries other than EAC or COMESA member states is at least fifty-one percent (51%) of the invested capital.[225] According to the Act, an investor may invest and purchase shares in an investment enterprise in Rwanda and shall be given equal treatment with Rwandan investors with regard to incentives and investment facilitation.[226] However, a more minimum capital is required from investors from Tanzania as compared to other investors from the other EAC Partner States.

In Burundi, article 15 of the *Land Act* of 2014 implicitly defines a foreign investor as legal entities not instituted in accordance with the laws of Burundi. Foreign investors can

[222] Kenya Insurance Act section 22
[223] Ibid section 23(4)
[224] Kenya Insurance Act section 27A
[225] Rwanda *Law on Investment and Export Promotion and Facilitation* of 2015 Chapter I Article 24
[226] Ibid Chapter II Article 5

experience procedural and substantive barriers as they enter, operate in and exit and economy. Besides, these barriers, which are intentional, require foreign investors and traders (including those from other EAC partner states) to designate at least $50,000 to their business.[227] This poses a cumbersome approval requirement to invest in Burundi, which consequently hampers foreign investment. Besides, *Law 1/23 of 24 September 2009* article 3 in determining tax advantages provides that eligible investments are those which contribute to the achievement of the use of locally produced raw materials, in particular by stimulating the production of goods services intended for the internal market. In addition, a percentage of ownership should be reserved for Burundians upon privatization of state enterprises.

3.5. Conclusion

This Chapter evaluated the various legal instruments governing cross-border investment of factoring in each of the EAC Partner States in a bid to understand why free movement of capital as envisaged in the EAC Treaty is still a chimera. The analysis exposed that all the Partner States practice protectionism tendencies in their financial industries thus failing to recognize that any national of any other partner state should be treated the same way as they do their own nationals since that is what the EAC Treaty aims at achieving. This, therefore, necessitates the study of how factors, as cross-border investors, have been regulated generally in other jurisdictions, especially in the EU, with an aim of finding the loopholes of such regulations, consequently formulating a pragmatic approach that will help the EAC partner states to enhance the requirements of the Treaty as far as free movement of capital is concerned. This is what the next chapter is about.

[227] Burundi Ministerial Order 550/29 of December 1980

CHAPTER FOUR

REGULATION OF FACTORING IN THE EUROPEAN UNION: A COMPARATIVE ANALYSIS

4.0. Introduction

The European Union (EU) is one of the most advanced models of regional integration in the world.[228] The EU success can be attributed to visionary politicians like France's Robert Schuman; the Franco-German leadership axis; consensus approach coupled with tolerance; and the strong political will to ensure the region's agenda are achieved.[229] These, among other fundamental tenets, have been the driving force behind the region's steady rise after stumbling during the 2008 global financial crisis. To ensure a multi-speed Europe with several tiers of integration, the EU recently adopted a flexible approaches like voluntary membership to the Eurozone, Schengen passport-free zone etc. Nonetheless, just like the EAC, the fundamental objective of the EU is to ensure they share strong common institutions for the benefit of their denizens. It is for this reason that the EU was the best option to analyse in order for EAC to draw lessons that will help its partner states achieve its objective in its common market.

4.1. Free Movement of Capital within the European Union

The European Union draws its mandate from two treaties: the Treaty on the European Union and the Treaty on the Function of the European Union (TFEU).[230] The TFEU provides for both exclusive and shared competences of the Member States and the Union.[231] The exclusive competence of the EU include the customs union, establishing competition rules necessary for the function of the internal market, and common commercial policy.[232] Shared competence between the Member States and the Union include consumer protection, internal market, and economic, social and territorial cohesion.[233] The TFEU categorically prohibits any form of discrimination based on nationality.[234] In fact, any national of a Member State

[228] Fraser Cameron *The European Union as a model for regional integration* Council on foreign relations, International Institutions and global governance and program, available at https://cfrd8-files.cfr.org/sites/default/files/pdf/2010/09/IIGG_Eurozone_WorkingPaper_Cameron.pdf accessed 02 August 2019 p 1
[229] Ibid p 1
[230] *Treaty on the Function of the European Union* article 1(2)
[231] TFEU article 2(1)&(2)
[232] TFEU article 3
[233] TFEU article 4(2)
[234] TFEU article 18

automatically and additionally becomes a citizen of the Union.[235] Such a citizen of the Union has the right to, *inter alia,* move freely within the Union.[236] Other benefits that flow from being a citizen of the Union is that one enjoys the free movement of the other factors of production like goods, services, and capital within the Union's internal market.[237] In fact the TFEU obligates the EU Member States to remove any restrictions regarding a citizen of the Union's right of establishment within their respective internal borders, including setting up agencies, branches or subsidiaries.[238] The same restrictions as regards free movement of capital within the Union and third parties are abolished.[239]

Companies established within the Union enjoy the same treatment as natural persons.[240] As such, they enjoy the privileges of, *inter alia,* national treatment, especially with regards to requirements of the company capital.[241] The European Parliament and Council adopt measures that ensure the achievement of free movement of capital involving 'direct investment establishment, provision of financial services, and admission of securities to capital markets.'[242] In the event movement of capital threatens to cause significant challenges for the operation of the internal market, the Council, in consultation with the European Central Bank, shall take safeguard measures, *only if necessary*, for a period not more than six months.[243]

Additionally, in order to strengthen trade among the Contracting Parties, the EU created a European Economic Free Trade Area governed by equal competition rules, and whose aim is to facilitate such movement of factors of production.[244] The Agreement prohibits the Contracting Parties from having in place any measures that restrict such movement,[245] including discrimination based on nationality.[246] Besides, where domestic regulations governing the financial market are liberalised, their application is to be in a non-discriminatory manner.[247] Just like the TFEU, the AEECA also permits the Contracting

[235] TFEU article 20(1)
[236] Ibid article 20(2)
[237] Ibid article 26
[238] Ibid article 49
[239] Ibid article 63
[240] Ibid article 54
[241] Ibid article 55
[242] Ibid article 64(2)
[243] Ibid article 66
[244] Agreement on the European Economic Area (AEECA) article 1
[245] AEECA article 3
[246] AEECA article 4
[247] AEECA article 42(1)

Parties to adopt safeguard measures in the event such liberalisation of their financial markets may lead to disruption of their internal markets.[248]

It is noteworthy that the TFEU permits the Member States to come up with the requisite measures to prevent infringement of their domestic laws as regards prudential supervision of their financial institutions, or to implement their internal procedures for declaration of capital movements for statistical, administrative, or public policy and security reasons.[249] However, such measures, as long as they are compatible with the provisions of the EU Treaties,[250] shall not be deemed to be arbitrary discrimination or restrictive on movement of capital.[251]

Just like the EAC Treaty and its Protocol Establishing the Common Market, none of the EU Treaties defines what capital is. Instead, Annex I of the repealed Directive 88/361/EEC provides a list what could be referred to as capital. They include, *inter alia*, direct investments, transfers in performance of insurance contracts, physical import and export of financial assets, etc.[252] Given the EU internal market provides a platform for economic growth due to free movement of capital, in the past two decades, intra-EU trade has since continued to grow as seen from table 3 below, save for the 2008 depression due to the global crisis.

[248] AEECA article 43(2)
[249] TFEU article 65(1)
[250] TFEU article 65(2)
[251] Ibid article 65(3)
[252] Republic of Turkey, Ministry of Foreign Affairs, Directorate for EU Affairs, *Chapter 4: Free movement of capital* dated 04 June 2018 available at https://www.ab.gov.tr/chapter-4-free-movement-of-capital_69_en.html accessed on 2 July 2019

Table 3[253]

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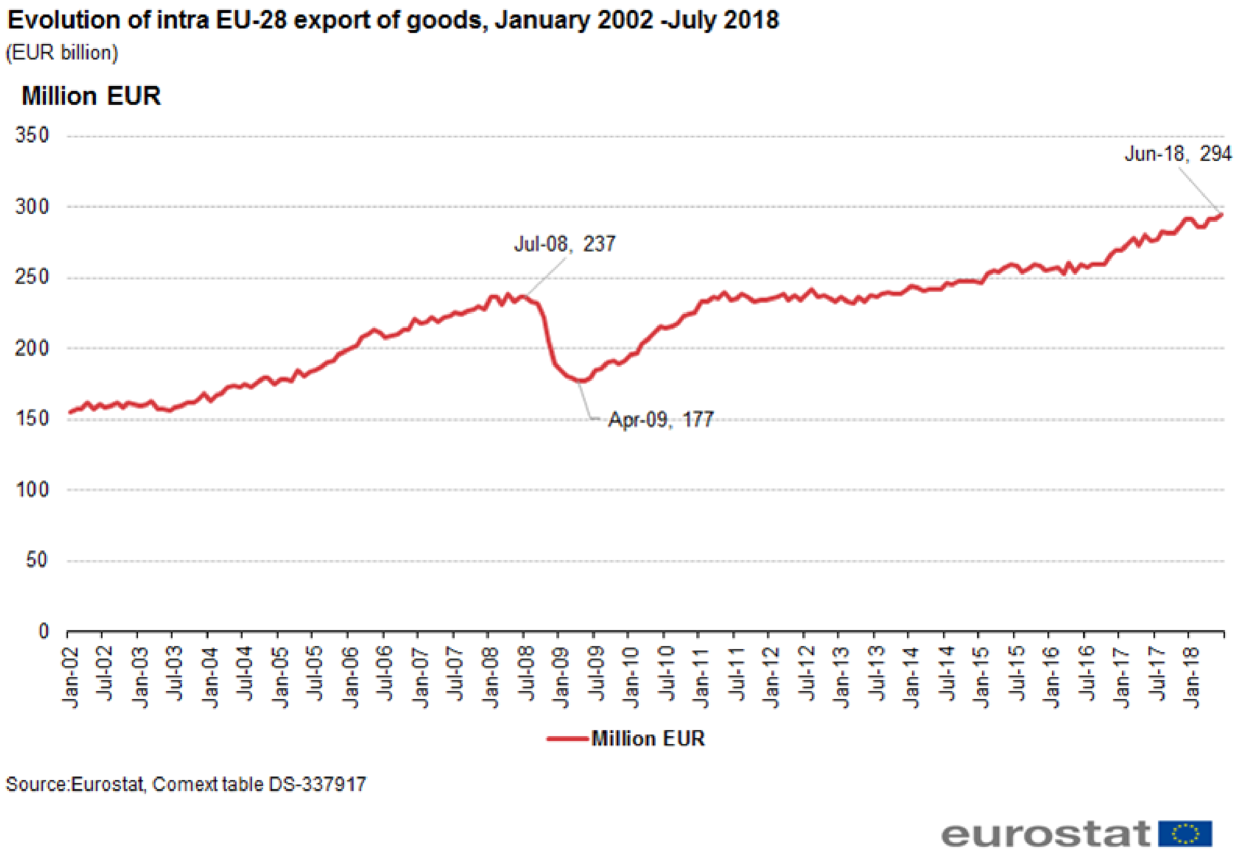

As regards intra-EU exports, the 2017 values ranged between EUR 750 billion (Germany) and slightly above EUR 1 billion (Cyprus).[254] As seen from the table below, Germany's figure accounted for 22.4% of the total intra-EU export while Cyprus' figure accounted for approximately 0.3% of the same. Table 4 below shows the value of the total intra-EU exports in 2017.

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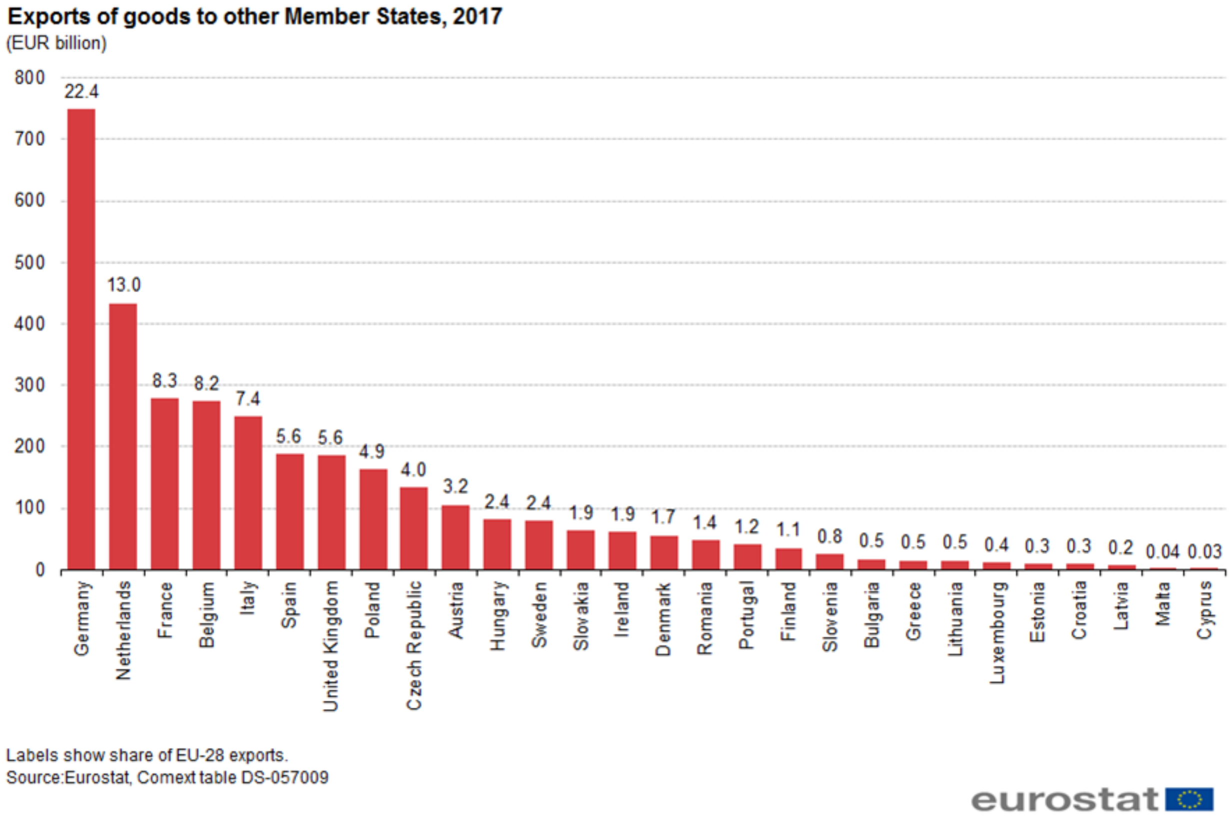
[253] Available at https://ec.europa.eu/eurostat/statistics-explained/index.php/Intra-EU_trade_in_goods_-_recent_trends#Intra-EU_trade_in_goods_balance accessed on 02 August 2019
[254] Ibid

Table 4



4.2. The Nature and Trends of the Factoring Industry in the European Union

The higher volume of trade transactions, as compared to the EAC lower figures, has been attributed to the existence of working capital that freely moves within the Union,[255] with asset-based finance taking the lead as a form of trade and commercial finance to the Union's enterprises.[256] Factoring in Europe, as a form of asset-based finance, has been hailed as one of the forms of trade finance that provide easy and faster access to capital compared to the secured lending form, no wonder the EU factoring industry accounted for close to 15% of the total EU Gross Domestic Product (GDP) in 2017,[257] a percentage that rose by 0.5% in 2018 to record a value of over EUR 1.7 trillion.[258]

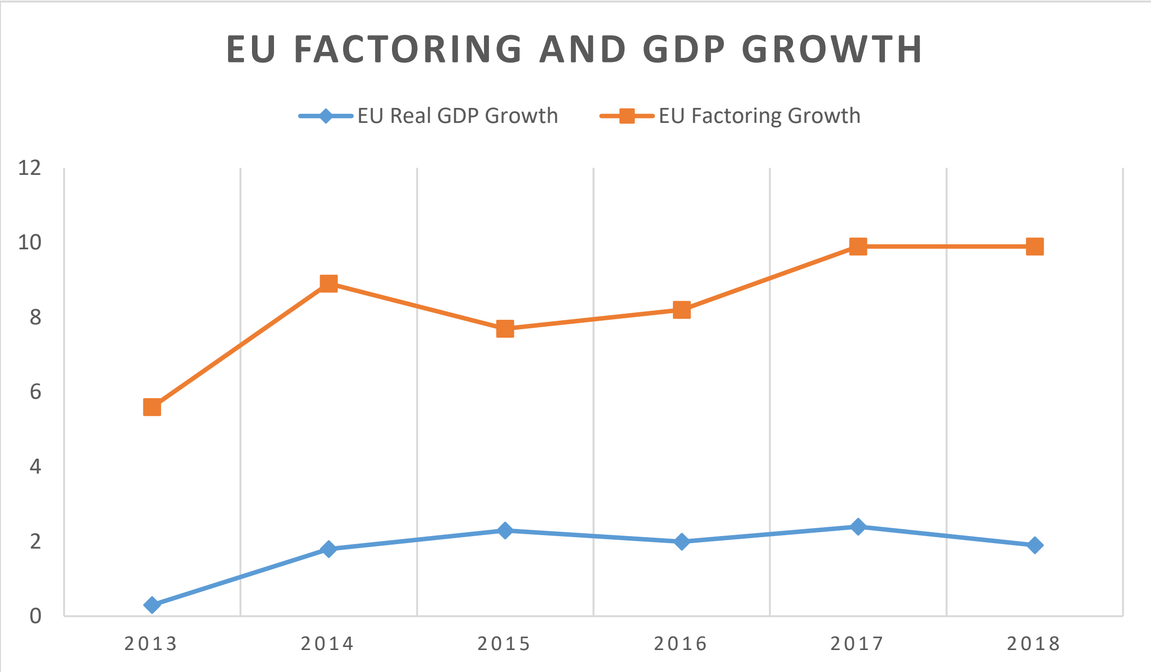
[255]European Commission Single Market Scoreboard available at https://ec.europa.eu/internal_market/scoreboard/integration_market_openness/fdi/index_en.htm accessed on 2 August 2019

[256] Kevin Day, *'European ABF Factoring: why Germany and France are the markets to watch'* dated 20 May 2019 available at https://www.finextra.com/blogposting/17262/european-abf-and-factoring-why-france-and-germany-are-the-markets-to-watch accessed on 4 August 2019

[257] Ibid

[258] European Union Federation of Factoring and Commercial Finance May 2019 Newsletter available at file:///C:/Users/User/Downloads/EUF%20Newsletter_2019_spring.pdf accessed on 4 August 2019

Table 5: EU Factoring Industry versus GDP Growth from 2013-2018

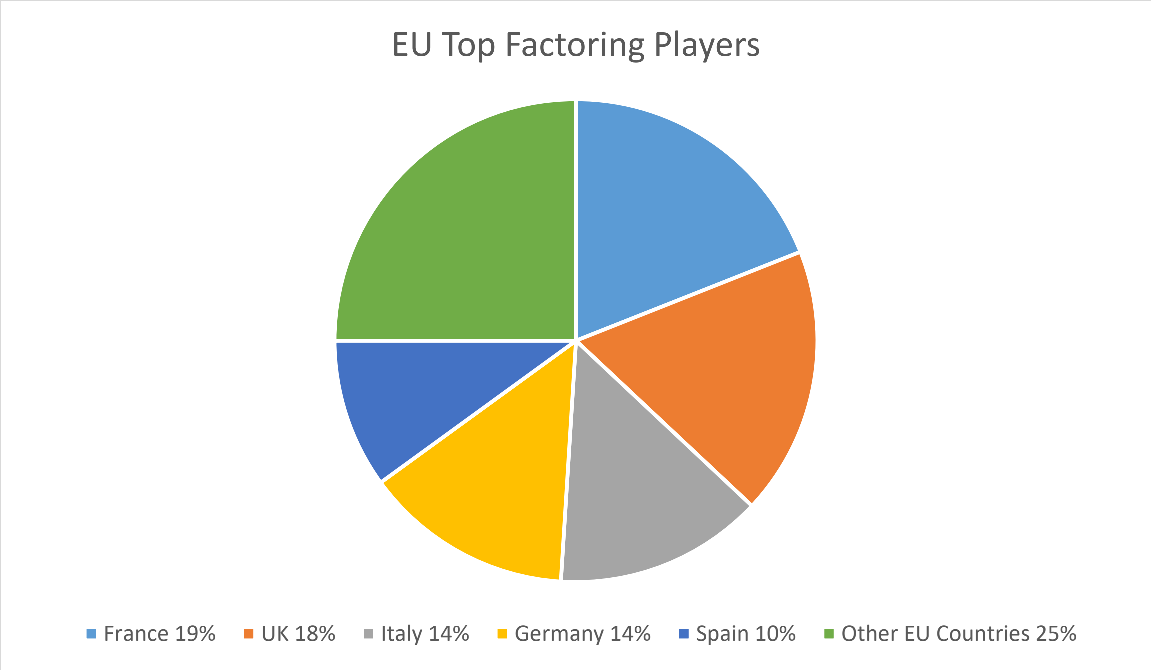


Source: EUF Factoring and Commercial Finance Newsletter 2019

As seen from the table 5 above, the growth of the EU factoring industry has been fairly consistent, its consistency proving it to be one of the significant financial resource options for the Union's companies. To be country-specific, the chart below shows the top five dominant players in the EU factoring industry. They are France (19%), United Kingdom (18%), Germany (14%), Italy (14%), and Spain (10%), with the other EU countries accounting for the remaining 25%.[259]

[259] Ibid p 5

Table 6: EU Top Factoring Players in 2018



Source: EUF Factoring and Commercial Finance Newsletter 2019

With regards to the Union's cross-border (intra-EU) versus domestic factoring, the Union records a sterling performance in its domestic factoring industry,[260] with its domestic factoring accounting for more than 75% of the total factoring transactions as seen in the graph below.

Notably, the Union's key players, in terms of ownership of the factoring companies and servicing of the same, is largely dominated by banks or companies owned by banks.[261] These banks and companies owned by banks serviced factoring transactions amounting to 96% in 2018 and 94% in 2017. The remainder, a lesser but significant figure, was serviced by other companies like insurance and other investment companies.[262]

4.3. Domestic and International Factoring in France

Internationally, France is a signatory to the UNIDROIT Convention on International Factoring. As was stated in chapter 2, the Convention aims at providing uniform laws applicable to international factors, including the rights and duties of the parties to a factoring contract.[263]

[260] European Union Federation of Factoring and Commercial Finance May 2019 Newsletter p 8
[261] Ibid
[262] Ibid
[263] UNIDROIT Convention on International Factoring (Ottawa 1988)

Regionally, Regulation (EU) 2015/760 aims at setting uniform standards within the Union's internal market regarding its long-term investment.[264] It regulates financial institutions that provide long-term investment funds to, *inter alia*, unlisted companies, listed small and medium enterprises that issue equity.[265] This is in a bid to contribute to the Union's real economy and aid in the implementation of its policies.[266] Its counterpart, Regulation (EU) 2017/1131, ensures that uniform standards are set to govern money market funds that provide short-term finance to governments and other financial institutions that cannot solely rely on their bank deposits.[267] This is in a bid to enhance the resilience of these financial institutions, like factors, and limit their contagion.[268]

Further, Directive 2009/138/EC provides a uniform legal framework for insurance and reinsurance undertakings to offer their services, like offering factoring services of protection against non-payment by debtors to creditors, within the internal market.[269] This is in a bid to make it easier for such insurance institutions to offer their services e.g. factoring. It regulates the conduct of insurance and reinsurance companies and how they are to be supervised within the Union.[270] It applies to all insurance and reinsurance institutions established within the territories of the Member States of the Union.[271] Regulation (EC) No 1606/2002 demands the Member States to ensure that such insurance and reinsurance companies, in addition to the other financial institutions, apply the globally recognized international financial accounting standards in their consolidated financial statements for the effective functioning of the internal market.[272]

According to Regulation (EC) No 924/2009 on cross-border payments within the Union, financial institutions, like factors, are expected to make similar charges for cross-border transactions, just as they would in their internal transactions.[273] The Regulation defines cross-border payment to be one that is electronically made by a payer's payment service provider

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[264] Regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 preamble para 6
[265] Ibid para 1
[266] Ibid
[267] Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on Money Market Funds preamble para 1
[268] Ibid para 6
[269] Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) para 2
[270] Directive 2009/138/EC (above) article 1
[271] Ibid article 2(1)
[272] Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards preamble para 2
[273] Regulation (EC) No 924/2009 of the European Parliament and of the Council of 16 September 2009 article 1

where the payer and the payee are located in different EU Member States.[274] Similarly, Directive 2002/87/EC permits the Member States to establish national competent authorities that monitor the activities of financial institutions like factors, in order to ensure compliance with the EU agendum on better prudential supervision of financial institutions.[275] Member States that have more than one competent authority supervising their financial institutions should ensure that such authorities coordinate for coherence purposes.[276] Directive (EU) 2016/97, in tandem with article 53(1) and 62 of TFEU, mandates Member States to harmonise their national laws on insurance with an aim of protecting their consumers.[277]

In order to ensure the above regional provisions are implemented, various French legal instruments governing financial institutions like factors have been implemented in a bid to ensure consistency between the national and regional regulatory frameworks. For example, to give effect to Directive (EU) 2016/97 above, the French Ordinance 2018-361 came into force to regulate *inter alia*, insurance pre-contractual information requisites, and continuous training of service providers. In addition, all French banking institutions, including those that provide factoring services, are subjected to both the French domestic laws e.g. French Monetary and Financial Code and any other positions issued by the French Prudential Control and Resolution Authority and the European Union's regulations and directives that govern several issues like prudential regulation and supervision e.g. Basel III reforms, Directive (EU) 2015/2366 on payment services, and Regulation (EU) 1024/2013 of the European Parliament and the Council of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies on the prudential supervision of credit institutions etc.[278] The same applies to insurance and other investment companies that are governed by both the EU Directives and domestic regulations like the French Insurance Code for the insurance institutions and supervised by the Financial Markets Authority.[279]

[274] Ibid article 2
[275] Directive 2002/87/EC of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC article 4
[276] Ibid article 5
[277] Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution preamble para 2
[278] Jérémie Duhamel, '*Establishing a financial institution in France*' Practical Law Country Q&A w-013-7972 dated 1 May 2019 available at https://uk.practicallaw.thomsonreuters.com/w-0137972?transitionType=Default&contextData=(sc.Default)&firstPage=true accessed on 6 August 2019
[279] Ibid

Unlike Kenya and Uganda that adopted the silo model of regulation, France adopted the twin-peak model. The principal regulatory and supervisory bodies for the French financial institutions are:

a) Financial Markets Authority (AMF)

The Financial Markets Authority is an independent organization that regulates, investigates, monitors, and where necessary, sanctions players in the French financial markets.[280] The Authority's key tasks are to protect investments in financial products, provide material information to investors, and ensure the financial market maintains order.[281] Besides, the Authority also ensures that these financial market players have access to dispute resolution mechanisms when need arises.[282] The financial institutions under the umbrella of the Authority include listed companies, financial intermediaries e.g. credit institutions that provide investment services, and other investment firms.[283]

According to the AMF General Regulation Book I, the ethical rules apply equally to financial institutions incorporated in France or in any other Member State of the Union. The same rule is established in Book III regarding service providers and Book IV on collective investment products.[284]

Given that factoring services are provided by banks and other investment firms, such factors fall within the ambit of the AMF regulation. These factors are, therefore, governed by the French Banking Act of 1984.[285]

b) Prudential Supervisory and Resolution Authority

This is an independent public body in charge of overseeing the French banking and the insurance sectors.[286] This is in a bid to ensure stability of the financial sector and enhance consumer protection.[287] It has several departments including a banking control department

[280] Autorite de Marches Financiers available at https://www.amf-france.org/en_US/L-AMF/Missions-et-competences/Presentation accessed on 6 August 2019
[281] Ibid
[282] Ibid available at https://www.amf-france.org/en_US/Le-mediateur-de-l-AMF/Presentation accessed on 6 August 2019
[283] Ibid
[284] Ibid available at https://www.amf-france.org/en_US/L-AMF/Missions-et-competences/Reglementation? accessed on 6 August 2019
[285] Factoring in France, 10 questions/10 answers available at http://www.asf-france.com/wp-content/uploads/Metiers/Livrets/Factoring-in-france.pdf accessed on 6 August 2019 p 14
[286] Prudential Supervisory and Resolution Control available at https://acpr.banque-france.fr/ accessed on 6 August 2019
[287] Ibid

that controls all types of establishments in the banking industry, including the banking institutions that offer factoring services.[288] The department of specialized and transversal control oversees the internal models of insurance companies.[289] The international affairs department handles cross-cutting issues with the EU and the extra-EU market in the two sectors relating to their prudential standards.[290] The Commercial Practices Control Branch ensures the safety of consumers in the banking and insurance industries that provide financial products like factoring.[291]

4.3.1. Association of Financial Companies (ASF)

With a view of promoting specialization in the financial market by credit institutions, investment firms, and other financial services, the French Banking Act of 1984 established the French Association of Financial Companies (ASF) whose members are permitted to offer financial services like factoring.[292] The activities of these financial institutions are regulated and supervised by the Financial Markets Authority and the Prudential Supervisory and Resolution Authority.[293] The ASF provides information relating to regulation and economic concerns to its members.[294] Besides, it closely monitors their statistics and consults with them to identify common practices of the French and the EU public bodies.[295]

As shown in the table below, the Association provides statistics relating to the French factoring industry. The most recent statistics show that the country's factoring industry grew in the first quarter of 2019 by 1.3% from the figure recorded in the last quarter of 2018.[296]

[288] Ibid available at https://acpr.banque-france.fr/lacpr/organisation/directions-du-controle-des-banques accessed on 6 August 2019

[289] Ibid available at https://acpr.banque-france.fr/lacpr/organisation/direction-des-controles-specialises-et-transversaux accessed on 6 August 2019; See also https://acpr.banque-france.fr/lacpr/organisation/directions-du-controle-des-assurances accessed on 6 August 2019

[290] Ibid available at https://acpr.banque-france.fr/lacpr/organisation/direction-des-affaires-internationales accessed on 6 August 2019

[291] Ibid available at https://acpr.banque-france.fr/lacpr/organisation/direction-du-controle-des-pratiques-commerciales accessed on 6 August 2019

[292] French Association of Credit and Investment Institutions available at http://www.afecei.asso.fr/Web/Afecei/content.nsf/DocumentsByIDWeb/7S6RZ2?OpenDocument&loglvl=7SGDWG accessed on 6 August 2019

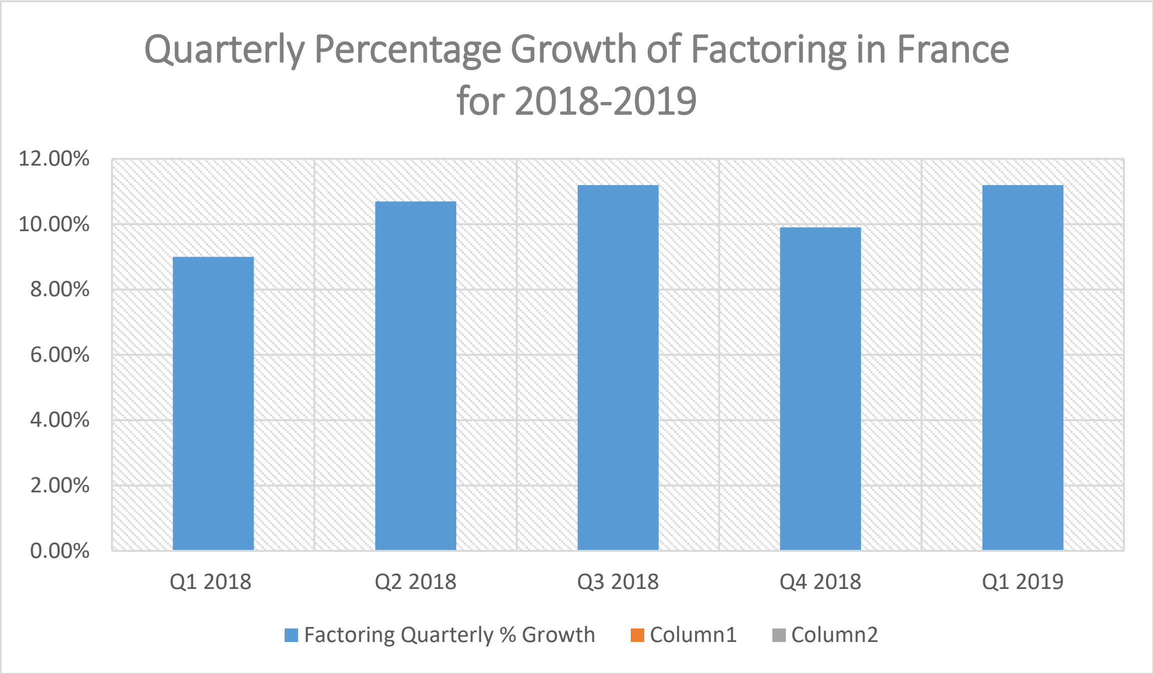
[293] French Association of Financial Companies available at https://www.asf-france.com/ accessed on 6 August 2019

[294] Ibid

[295] Ibid

[296] Available at https://www.asf-france.com/wp-content/uploads/Statistiques/Affacturage/201903-Activite-Affacturage.pdf accessed on 6 August 2019

Table 7: Factoring quarterly statistics in the French financial market in 2018-2019



Source: Association française des Sociétés Financières (ASF)

4.3.2. EU Federation for the factoring and commercial finance (EUF)

Regionally, the ASF chairs the European Union Federation for the factoring and commercial finance (EUF), the Union's representative body for the factoring and commercial industry.[297] Its membership comprises the EU Member States national factoring associations and international factoring bodies e.g. Factors Chain International active in the Union.[298] The aim of EUF is to engage the Member States governments on how their countries' enterprises can have enhanced access to finance through *inter alia*, factoring.[299] The EUF is the central platform that, besides offering expert advice and opinions regarding the Union's factoring industry, brings together the Union's legislators to discuss the cross-cutting issues in the factoring industry, and offers expert advice and opinions regarding the Union's factoring industry.[300] In addition, the function of the EUF is to ensure that Europe's factoring industry is well-structured with properly priced financial prices.[301]

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[297] EU Federation for the factoring and commercial finance industry available at https://euf.eu.com/what-is-euf/objectives/an-active-platform-in-the-eu.html accessed on 6 August 2019

[298] Ibid

[299] Ibid

[300] Ibid

[301] Ibid

Internationally, EUF has been a subdivision of Factors Chain International since its merger with International Factors Group in 2016.[302] Factors Chain International is the global association for open account trade finance. In 2017 the EUF conducted a legal study of the EU Member States legal framework governing the factoring industry in a bid to compile the relevant information regarding national factoring industries into a single document.[303] The legal study revealed some disparities in the practice of factoring in the Member States, where some countries e.g. France, do not have a specific legislation governing its factoring industry, but rather the services are governed by the extant French fiscal framework and the EU Directives and Regulations.

Commendably, the EUF collates data as frequently as possible in a bid to inform its members of up-to-date statistics on the industry.[304] As seen in the graph below, some of the information contains a comparative analysis of the Member States practice their domestic and intra-EU factoring tendencies in order to ensure that the internal market's agendum of financial integration and free movement of capital that will enhance access to capital is achieved.

The data compiled shows that the Union's cross-border (intra-EU) factoring still lags behind its domestic counterpart. The Union records a sterling performance in its domestic factoring industry,[305] with its domestic factoring accounting for more than 75% of the total factoring transactions as seen in the graph below.

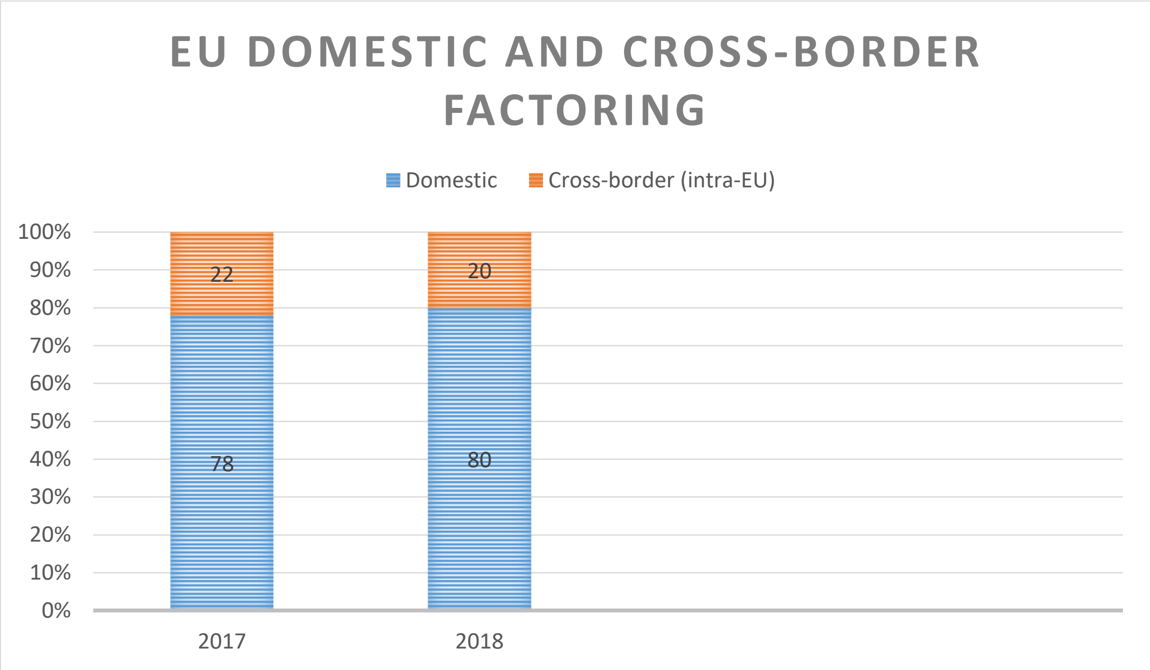
[302] Ibid

[303] EUF Legal Study available at https://euf.eu.com/what-is-euf/objectives/euf-legal-study.html accessed on 6 August 2019

[304] Ibid available at https://euf.eu.com/what-is-euf/objectives/what-is-factoring.html accessed on 6 August 2019

[305] European Union Federation of Factoring and Commercial Finance May 2019 Newsletter p 8

Table 8: EU Domestic versus Cross-border (intra-EU) factoring for the year 2017-2018



Source: EUF Factoring and Commercial Finance Newsletter 2019

In order to enhance its intra EU factoring, EUF conducts training on the best current practices in the industry, and also offers advice on how legislators can restructure their domestic legal instruments in order to ensure that a wider access to those domestic financial markets by other citizens of the Union is achieved.[306] This ensures that factors of production e.g. capital freely moves within the EU internal market.

4.4. Cross-border Factoring in the EU and EAC: a Comparative Analysis

The European Union draws its mandate from two treaties: the Treaty on the European Union and the Treaty on the Function of the European Union (TFEU).[307] The TFEU provides for both exclusive and shared competences of the Member States and the Union.[308] The exclusive competence of the EU include the customs union, establishing competition rules necessary for the function of the internal market, and common commercial policy.[309] Shared competence between the Member States and the Union include consumer protection, internal market, and economic, social and territorial cohesion.[310] On the other hand, the competence of the EAC is not expressly stated thus blurry. Instead, what can be interpreted as its

[306] Ibid
[307] *Treaty on the Function of the European Union* article 1(2)
[308] TFEU article 2(1)&(2)
[309] TFEU article 3
[310] TFEU article 4(2)

competence is inferred from its broad objectives as proffered in the EAC Treaty Article 5. In tandem with Article 8 of the Treaty, the EAC partner states have the obligation to collaborate with the EAC regional bodies in order to ensure that the Community's objectives are achieved.

Secondly, the TFEU categorically prohibits any form of discrimination based on nationality.[311] In fact, any national of a Member State automatically and ***additionally*** becomes a citizen of the Union.[312] Such a citizen of the Union has the right to, *inter alia,* move freely within the Union and enjoys the privilege of free movement of other factors of production.[313] On the flipside, its EAC counterpart also expressly prohibits discrimination based on nationality. However, the EAC, unlike the EU which is a supranational organization, is an intergovernmental organization that does not grant the EAC partner states additional citizenship. This means, therefore, that the benefits of extra citizenship as envisaged by the Community, is left at the mercy of the partner states.

In addition, the EU performs better than the EAC as far as free movement of capital is concerned because of the strong political will transcending the Members to their citizens. In fact the EU has an online Single Market Scoreboard that periodically informs the Members and their citizens of the performance of the Members towards implementation of their EU obligations.[314] This is in a bid to identify non-compliance and come up with better strategies to enhance compliance. For example, in the first quarter of 2019, the EU Commission sent formal notices to Spain, Latvia and Cyprus for their failure to comply with the EU requirements established in EU Directive 2016/97 on cross-border distribution of insurance services like factoring.[315] Depending on the Members compliance to EU law, they are awarded a yellow card for above average performance, green card for average, and a red card for below average performance.[316]

Further, the Scoreboard evaluates how useful the EU is in helping its citizens and their business entities by evaluating how open or closed the individual countries' markets are to

[311] TFEU article 18
[312] TFEU article 20(1)
[313] Ibid article 20(2)
[314] European Commission Press Release Database, Member states compliance with EU law: not yet good enough dated 6 July 2017 available at https://europa.eu/rapid/press-release_IP-17-1846_en.htm accessed on 23 September 2019
[315] European Commission Press Release Database, *March infringements package: key decisions,* dated 7 March 2019 available at https://europa.eu/rapid/press-release_MEMO-19-1472_en.htm accessed on 23 September 2019
[316] Ibid

intra-EU trade and investment.[317] Failure to comply with the EU law attracts sanctions in the form of financial penalties.[318] Such financial sanctions are calculated taking into account the period of non-compliance, ability of the non-compliant country to pay, and the impact of non-compliance to general and particular interests.[319]

On the flipside, EAC lacks strong political will from its partner states, to the extent that the same trickles down to their denizens' awareness and involvement in the Community's activities. This means that majority of the citizens in the EAC partner states do not fully enjoy the benefits stemming from a common market not because they do not want to, but rather because they have little or zero knowledge of the same. The same deduction cannot be deduced from the analysis of the data presented herein above concerning trade in the EU internal market because the citizens are actively involved, directly or otherwise, in the day-to-day activities of the EU institutions. In the same vein, there is little compliance with the EAC requirements as far as free movement of capital is concerned because the EAC, in its Common Market Protocol failed to provide for sanctions in the event of non-compliance.[320]

In order to expose instances of inconsistencies, this study opted for France domestic and international legal instruments governing cross-border factoring. This study's aim was not to paint France as the 'lamb without blemish' as far as its factoring industry is concerned, but rather to distil some of its best practices, because despite its flaws the country has still managed to compete fairly well in the factoring market. France still underperforms in international factoring, however, despite such underperformance, it still manages to be among the top five EU countries in international factoring volumes. This chapter settled for France as the most appropriate jurisdiction to analyses because, just like the EAC partner states, it has no specific legislation governing factors alone, but rather, the industry is governed by the extant fiscal regulations and supervised by public bodies. Similarly, France, just like the EAC countries, belongs to a regional economic community whose internal market obligates it to ensure that it liberalizes its financial markets to ensure that capital moves freely in the market.

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[317] Ibid

[318] European Commission Database, *Infringement procedure*, available at https://ec.europa.eu/info/law/law-making-process/applying-eu-law/infringement-procedure_en accessed on 23 September 2019

[319] Ibid

[320] The East African, *EAC Partner States delaying key regional protocol*, dated 9 May 2015 available at https://www.theeastafrican.co.ke/business/EAC-partner-states-delaying-key-regional-protocol-/2560-2710950-4sqt8t/index.html accessed on 23 September 2019

However, unlike the EAC countries, France regulation of its financial market has seen it record very high volumes in its factoring industry. It had the highest value in 2018, accounting for 19% of the total EU factoring volumes, followed by United Kingdom (18%), Germany (14%), Italy (14%), and Spain (10%), with the other EU countries accounting for the remaining 25%. The reason for such high performance is attributed to its model of financial regulation that gives effect to the requirements of the Union. Besides, unlike any of the EAC partner states, it has in place a functioning factoring national association (ASF) that closely monitors the industry and regularly provides relevant information and statistics on the trends of factoring within the country. In addition, the ASF chairs the EU federation of factoring and commercial finance, a regional representative body of factors and other financial institutions. The EUF, just like the ASF, constantly updates its Members of the trends and best practices in the regional industry. This creates more awareness of the factoring industry thus increasing access to finance to small and medium enterprises both within the Member States and out of the Union.

4.5. Conclusion

This chapter endeavoured to study the legal environment governing the factoring industry in the European Union as well as how its Member States have regulated the same within their national territories. The chapter also analysed the various EU Treaties, Directives, and Regulations in a bid to find out how the Union ensures that free movement of capital in its internal market is achieved. The analysis revealed that, for example, Directive 2009/138/EC provides a uniform legal framework for insurance and reinsurance undertakings to offer their services, like offering factoring services of protection against non-payment by debtors to creditors, within the internal market. The Directive applies to *all* insurance and reinsurance institutions *established within the territories of the Member States of the Union.*

In order to ensure the above regional provision, including others, are implemented, various French legal instruments governing financial institutions like factors have been implemented in a bid to ensure consistency between the national and regional regulatory frameworks. For example, all French banking institutions, including those that provide factoring services, are subjected to both the French domestic laws e.g. French Monetary and Financial Code and any other positions issued by the French Prudential Control and Resolution Authority and the European Union’s regulations and directives that govern several issues like prudential regulation and supervision e.g. Basel III reforms, Directive (EU) 2015/2366 on payment services, and Regulation (EU) 1024/2013.

Therefore, in order to enhance free movement of capital within the Community, this chapter concludes that the lessons that EAC Partner States can draw from the French regulatory approach to factoring include liberalising their financial markets to appreciate that investors, like factors, from the other EAC countries should be treated the same way as the nationals of a partner state. Similarly, a national factoring association should be formed that will ensure that it creates more awareness of factoring as a form of commercial finance, especially to the SMEs that account for the larger portion of intra-EAC trade because they are the majority. Besides, the EAC partner states ought to form a self-regulated and independent regional body made up of the national factoring associations. The regional body will maintain order in the factoring industry, by issuing sanctions to non-adherents. Also, the regional body will provide a platform for national legislators to come together to discuss cross-cutting issues affecting their financial industries. Finally, just like France, the EAC partner states ought to (re)consider acceding to the UNIDROIT Convention on International Factoring.

These, among other solutions, if implemented, will enable financial institutions including factors, to easily establish their businesses in the Community without any unnecessary impediments e.g. nationality. This will ensure that enterprises in the Community have a faster and easier access to working capital. This, consequently, will lead to enhanced impediment-free movement of capital and improved intra-EAC trade.

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

5.0. Introduction

Cross-border factoring, as has been contended throughout this study, is on a steady upward trajectory globally. This is due to its enormous contribution to domestic economic development and external regional economic integration. However, its growth in the EAC Common Market has been hampered because it has been viewed to be a fountain of a mammoth of challenges, including restrictive regulations within the domestic borders of the EAC partner states.

There have been propositions that cross-border factoring ought to be properly regulated in order to bring sanity to the seemingly 'defiant' Partner States who fail to adhere to the provisions of the Common Market Protocol with respect to liberalising their financial markets in order to achieve the Community's agendum of free movement of capital.

This study sought to evaluate the partner states regulations on cross-border factoring that hamper free movement of capital within the EAC Common market and their adherence to the Common Market Protocol. This Chapter is, therefore, a summary of the issues canvassed in this research paper, coupled with possible solutions to the question of how the EAC partner states can regulate their factoring industries in a bid to enhance free movement of capital within the Common Market.

5.1. Recap of the Research Questions

Each chapter of this thesis addressed the following research questions:

1. What are the underpinning theories surrounding regulation of factoring and international movement of capital?
2. What are the competing approaches towards regulation of factoring?
3. What are the tenets of regulation of factoring that can enhance free movement of capital within the EAC financial market?
4. What lessons can the EAC draw from the regulation of factors in the EU?
5. What reforms are necessary for regulation of factors in the EAC in order to enhance the free movement of capital?

5.2. Summary of Findings and Conclusions

Chapter One of this study laid bare the line of thinking that has been pursued, near exhaustively, throughout the penning down of the entire study. In its introduction, this paper pointed out the need for the EAC Partner States to adhere to the provisions of the Common Market Protocol as far as free movement of capital is concerned. An analysis of the region's intra-partner trade was conducted in a bid to find out whether there should, indeed, be need for international movement of capital since that would consequently enhance intra-regional trade. The introductory Chapter concluded that intra-EAC trade indeed takes place, albeit in low volumes, thus the need to ensure that it is enhanced through liberalisation of the factoring industry.

Chapter Two of the study analysed the theories underpinning economic regulation and international movement of capital. It also analysed, exhaustively so, the competing approaches towards general regulation of factoring industries. The study found out that despite the approaches, as laid down in Chapter Two, giving us a general overview of how the industry is governed, it is limited to regulation of factors in the domestic realms, forgetting that countries in a Common Market have extra obligations to ensure the objectives of the Common Market, including free movement of capital, are achieved. The Chapter concluded that it is of paramount importance that a different approach towards regulation of cross-border factoring be adopted since global games require global rules.

Chapter Three analysed the legal framework governing cross-border factoring in the EAC Common Market. This included an analysis on international legal instruments, regional regulations, Community-level treaty and protocols, and domestic legal underpinnings. The Chapter found out that despite the EAC Treaty and its relevant Protocol conclusively demanding liberalisation of the partner states financial markets, the partner states have exuded exasperating nonchalance towards such liberalisation, consequently hampering free movement of capital within the Community. Further, the Chapter also found out that the EAC partner states have not signed the international legal instruments like UNCITRAL Convention on the Assignment of Receivables in International Trade and UNIDROIT Convention on International Factoring. The Chapter concluded that in order to ensure that free movement of capital becomes an achieved objective, it is imperative that the EAC Partner States consider ways of better regulating their factoring industries.

Chapter Four compared the legal framework governing cross-border factoring in the European Union to that of the EAC. Thematic concerns such as the binding nature of the EAC versus EU treaties and the need to ensure harmony in the EAC Common Market versus EU internal market as far as regulation of cross-border factoring is concerned were addressed. The Chapter found out that the EU treaties are not too turgid to allow derogation. However, upon derogation, explicit or otherwise, the EU Members are to follow specific measures to ensure that such derogation do not impede the internal market's agenda. Besides, such derogation should not be arbitrary and unjustifiable. Comparatively, similar regulations were found to be present in EAC. The Chapter therefore had to delve into the substantive reasons why free movement of capital, as far as cross-border factoring is concerned, is still a chimera in EAC, yet, contrastingly, it records better performances in the EU. The Chapter concluded that whereas EU has both national and international factoring associations that are self-regulatory, EAC has nothing close to that. Besides, citizens of the Members of the EU automatically become citizens of the Union. In addition, the success of the EU initiative on free movement of capital is highly attributed to the strong political will among the EU Members to ensure that the objectives of the EU internal market are achieved, and the Union's leadership will *hardly* hesitate to issue sanctions, if need be, to any Member that fails to adhere to such requirements. Such moves are yet to be found in EAC.

Chapter Five posits solutions to the current negative growth trajectory towards adherence to the EAC Common Market Protocol as far as free movement of capital is concerned. This is it does by first drawing conclusions which clearly identify the legal issue in each Chapter. To address the legal issues identified in each Chapter, Chapter Five advances solutions by proffering recommendations to each issue raised in each Chapter that will ensure that free movement of capital is enhanced through better and smart regulation of the Community's factoring industry.

5.3. Recommendations

Going forward, the following, if undertaken, will facilitate the formulation of an informed and sound regulatory mechanism of enhancing free movement of capital in the Common Market.

5.3.1. Hybrid approach to regulation of factoring in the Common Market

As laid out before in Chapter Two, the extant competing approaches towards regulation of factors do not take into consideration the obligations of countries to ensure they achieve the objectives of a common (or internal) market. This created inconsistencies between the EAC and its partner states regulations on cross-border movement of capital like factoring. Nonetheless, global games require global rules. This, therefore, means that the EAC partner states need to come up a with a regional "best of breed" combination that conflates narrowly-tailored government regulations and a Self-Regulatory Organization (SRO) empowered with legislative, dispute resolution and enforcement powers over the activities of non-banks institutions like factors.

5.3.2. Accession of UNIDROIT Convention on International Factoring

Chapter Three concluded that EAC lacks a subtle regional legal pathway to ensure that free movement of capital like factoring is enhanced. As a solution, this study proposes that the partner states ought to (re)consider acceding to the UNIDROIT Convention. The Convention is effective having attained its minimum ratification threshold.[321] However, none of the EAC Partner States has ratified this Convention, save for Tanzania that signed it on 28 May 1988, but has since joined its EAC sisters in not ratifying the Convention. Its plurilateral nature gives it a non-binding aspect upon the countries that have not ratified it. Given that the aim of the Convention is to provide a uniform global framework governing international factoring, it is imperative that the EAC Partner States accede to the Convention. The benefit of this is that there will be no inconsistencies in how they regulate factoring both domestically and regionally.

5.3.3. Accession of UNCITRAL Convention on the Assignment of Receivables in International Trade

This Convention provides a more comprehensive effort in dealing with cross-border factoring issues in comparison to the UNIDROIT Convention. Unlike the UNIDROIT Convention, the UNCITRAL Convention is yet to gain entry into force with only Luxembourg, Madagascar, and USA signing but yet to deposit their instruments of ratification, and Liberia that deposited its instrument of accession in 2005.[322] Five more actions are needed for its entry into force.[323] The EAC Partner States, in the spirit of enhancing cross-border factoring, can (re)consider acceding to this Convention.

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[321] The signatories include France, Italy, Nigeria, Germany, Belgium, Hungary, Latvia, Russian Federation, and Ukraine. Available at https://www/unidroit.org accessed on 22 June 2019

[322] Information available at https://www.uncitral.org accessed on 22 June

[323] Ibid

5.3.4. Additional EAC citizenship

Chapter Four established that part of the reason why the EU flourishes is accredited to the additional citizenship it grants the citizens of its Members. This enables them to freely access and enjoy the benefits of an internal market. Just like the EU, EAC needs to grant additional citizenship to the partner states citizens. Efforts towards the same have been in place, including granting an EAC passport. However, such efforts are yet to bear fruits since despite the inception of the passport, more restrictive regulations are in place to hamper free movement of other factors of production.

Besides, more awareness about the activities of the EAC institutions ought to be created to educate the citizens about the benefits of belonging to the Common Market. Such benefits, which include free movement of factors of production like capital from factors, will enhance intra-EAC trade thus enhancing regional integration.

5.3.5. Sanctions for Non-compliance

Chapter Four also established that the EU has a solid foundation in terms of integration and successful implementation of its single market policies and regulations because it has a good back-up strategy in the event of non-compliance with its treaties. Such compliance or otherwise, are evaluated by the Commission, which makes periodic reports on individual countries performance and refers cases of non-compliance to the European Court of Justice which issues financial sanctions upon conviction. Such is yet to be seen in the EAC because the EAC lacks strong enforcement mechanisms to ensure compliance with its laws. As such, in order to demystify the chimera of free movement of capital within the Common Market, it is imperative that the EAC institutions come up with sanctions upon conviction on non-compliance. Perhaps this will encourage the Partner States to liberalise their factoring markets to allow cross-border investments of factors.

POST SCRIPTUM

I conclude that when done with this thesis, fate will not allow my family and society at large to continue wallowing in the doldrums of indigence.

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