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Project Finance 2020

A practical cross-border insight into project finance

Ninth Edition

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1 Overview

1.1 What are the main trends/significant developments in the project finance market in your jurisdiction?

2019 was a year of mixed fortunes as, on one hand, economic growth had been projected to be between 5.7% and 6.3%; however, there were also concerns that the economic environment was not investor-friendly, as quite a number of companies laid off staff either by folding operations or through restructuring.

The project finance market has not been any different. There were some new mega projects launched by the government, while others were shelved due to overpricing, corruption and viability concerns.

1.2 What are the most significant project financings that have taken place in your jurisdiction in recent years?

The Japan International Cooperation Agency (JICA) entered into a loan agreement with the Government of Kenya (GOK) for the construction of Dongo Kundu Phase 2 ByPass measuring 8.96 kilometres at a cost of KES 25,000,000,000. The project is aimed at decongesting the roads in the coastal city of Mombasa. It will include, among others, the construction of an interchange along the Likoni–Lunga Lunga highway and two bridges at different points over the Indian Ocean spanning 660 metres and 1440 metres respectively. It was launched in October 2019 and will take two years to complete.

The construction of a 180-kilometre Nairobi–Mau Summit highway, projected to cost KES 180,000,000,000, will be undertaken under a Public Private Partnership (PPP) deal between GOK and a consortium of four South African companies under the name Rift Valley Connect. The consortium will construct and manage the highway. It will also recover its investment through tolling.

A 26.7-kilometre expressway linking the Jomo Kenyatta International Airport and Westlands, is set to be constructed so as to decongest traffic in Nairobi. GOK has entered into a PPP deal with the China Road and Bridge Corporation (CRBC) that is expected to last for 30 years. CRBC will construct the road and will recoup the investment through toll stations along the road. The project is expected to cost KES 62,200,000,000.

2 Security

2.1 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

In Kenya, a general financing agreement would be used, either in the form of a loan agreement or facility agreement. Security documentation would differ depending on the type of security a financier has opted to obtain. For example, where the assets of a company include movable assets such as machinery and motor vehicles, then the financier would have a charge by way of debenture registrable in the Companies Registry. On the other hand, where the security was to be over immovable property, for example land and/or buildings, then Kenyan law requires that a charge be created over these particular immovable assets and be registered in the Lands Registry. Third-party securities in the form of guarantees would entail the preparation of a separate security document.

For movable property, there is also an additional requirement of registering the security online, by filing an Initial Notice under the Movable Property Security Rights Act of 2017.

2.2 Can security be taken over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground)? Briefly, what is the procedure?

Yes. In the case of a company, requisite board resolutions would need to be obtained from the company borrower authorising the creation of the security. A charge document would be prepared, securing the financial obligations of the borrower to the financier. This charge would then be executed by all the parties in the presence of an advocate. Thereafter, the stamp duty, based on the amount secured, would be paid to the Commissioner of Domestic Taxes. In cases where the charge involves agricultural land, the consent of the relevant land control board would have to be sought and obtained. Further, where the charge involves leasehold property, the consent of the lessor would need to be obtained. Where the charge is over a property belonging to a married individual, then the consent of the spouse would be obtained. The charge would thereafter be submitted for registration at the relevant Lands Registry, accompanied by a rates clearance certificate from the relevant county government

(confirming that all land rates applicable have been paid in full) and, in the case that the property is leasehold, a rents clearance certificate (confirming that the applicable land rent has been paid in full). Where the charge is created by a company, the charge would also have to be registered in the Companies Registry. In the event that the proposed security is already charged to a financier, the consent of the financier is required. An Inter-lenders Agreement or a Security Sharing Agreement will be required in such circumstances, to govern the relationship between the various lenders.

2.3 Can security be taken over receivables where the chargor is free to collect the receivables in the absence of a default and the debtors are not notified of the security? Briefly, what is the procedure?

Security can be taken over receivables. It is the practice in Kenya to either have a charge over the receivables or have a deed of assignment created over such receivables. Financiers are usually advised to place an obligation on the borrower to notify the debtors of such security. The financier will also be required to file an Initial Notice online at the Moveable Properties Securities Registry (MPSR). The requirement for filing under the MPSR is a new development which took place in 2017.

2.4 Can security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

When a customer places a deposit with a bank, the deposit represents a loan made to the bank. The bank is the debtor and the customer is the creditor. It had generally been recognised by legal practitioners that there was no difficulty in a bank taking a charge over a cash deposit it held. It has generally been accepted that with regard to a fixed deposit, the secured party must take control over the charged accounts and prevent the chargor from withdrawing monies from, or otherwise dealing with, the charged accounts without consent from the chargee.

The bank is also required to file an Initial Notice under the MPSR, as noted under question 2.3 above.

Where the borrower is a company, the charge instrument should also be registered in the company's records at the Companies Registry.

However, the legality of a charge over a cash deposit was not accepted in the English case of *Re Charge Card Services*. This judgment caused a major controversy in legal and banking circles in England. The judge in this case argued that as the deposit represented a debt owed by the bank and grants the right for the depositor to sue the bank for its recovery, the debt cannot be assigned or taken as security, as a debtor – the bank – cannot sue for a debt it owes. The judge stated that it was "conceptually impossible" for a debtor to take a charge over his own debt.

2.5 Can security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Briefly, what is the procedure?

Yes. Shareholders (especially those in private companies) are usually granted share certificates in respect of the shares they own. If a company holds shares in another company and it wishes to offer these shares to a financier as security, then a charge may be prepared over these shares and registered in the Companies Registry. It should, however, be noted that a company cannot create security over its own shares. In the case of shares owned by a natural person, it has been the practice in Kenya by most financial institutions to require the borrower to surrender the relevant share certificate to the financial institution. In addition, the borrower is required to execute a blank share transfer form and give the financial institution authorisation to transfer the shares to any person in case of default.

The lender is required to file an Initial Notice under the MPSR concerning the security.

2.6 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets (in particular, shares, real estate, receivables and chattels)?

The following are the charges payable in respect of a charge:

- Security documents are required to be prepared by an advocate and legal fees at the rate set out in the Advocates Remuneration Order are applicable. Attestation fees would also be payable to any advocate witnessing the execution of the security documents.
- The stamp duty payable is based on the amount secured by the charge or debenture at the rate of 0.1%, which is a fixed rate regardless of the type or sequence of security. For example, the stamp duty payable on a charge, further charge or debenture is the same rate of 0.1% of the principal amount. In the case of a guarantee, the stamp duty payable is the nominal amount of KES 200.
- Bank charges – KES 120.
- Lessor's consent (if the relevant property is leasehold) – this varies from lessor to lessor.
- Land Control Board Consent (if the property is agricultural) – KES 1,000. In addition, the Land Control Act provides that: an allowance of KES 500 inclusive of lunch shall be paid to each unofficial member of a land control board for every meeting which he attends; an allowance of KES 1,300 inclusive of lunch shall be paid to each unofficial member of a provincial land control appeals board for every meeting which he attends; and a mileage allowance at prevailing government rates shall be paid to unofficial members of a land control board.
- Registration fees at the Lands Registry (if security is over immovable property) – KES 500.
- Filing fees at the Companies Registry (if the chargor is a company) – KES 14,000.

2.7 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Provided that the security documents have been duly executed and consented to (where applicable) and the requisite stamp duty paid and rates and rents clearance certificates obtained, registration of securities at a Lands Registry may take a day, or even much longer. There have, however, been instances where a file relating to a particular property cannot be located, and this usually causes significant delays in the registration process. It should be noted that time varies from registry to registry depending on how busy that particular registry usually is. There have also been instances where different registries are closed by Executive Orders to pave the way for urgent developments in various registries, such as digitalisation of records or reorganisation of the registries. It has been our experience that registration at the Companies Registry would take approximately one week.

2.8 Are any regulatory or similar consents required with respect to the creation of security over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground), etc.?

The Land Control Act requires that the consent of the relevant Land Control Board be obtained in cases where the land is agricultural.

The Matrimonial Property Act prohibits the alienation in any form of matrimonial property during the subsistence of a marriage without the consent of both spouses either by way of sale, gift, lease, mortgage or otherwise.

Where the title is a lease from the Kenya Railways Corporation (KRC), for example in some coastal areas of the country, the consent of KRC is required to charge the property.

Where securities are to be shared between financiers, the existing financier has to give consent for its collateral to be shared with another financier of the same borrower.

3 Security Trustee

3.1 Regardless of whether your jurisdiction recognises the concept of a "trust", will it recognise the role of a security trustee or agent and allow the security trustee or agent (rather than each lender acting separately) to enforce the security and to apply the proceeds from the security to the claims of all the lenders?

If the parties involved have an instrument recognising this role, then the provisions in the particular instrument will be binding to the parties, because this would be a contractual matter.

3.2 If a security trust is not recognised in your jurisdiction, is an alternative mechanism available (such as a parallel debt or joint and several creditor status) to achieve the effect referred to above which would allow one party (either the security trustee or the facility agent) to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

See question 3.1 above.

4 Enforcement of Security

4.1 Are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction or the availability of court blocking procedures to other creditors/the company (or its trustee in bankruptcy/liquidator), or (b) (in respect of regulated assets) regulatory consents?

Charges rank according to the order in which they are registered unless so provided in the charge instrument.

The Land Act sets out the remedies available to a charge in the event of default. If a chargor fails to pay interest or any other periodic payment due under any charge, and continues to be in default for one month, the chargee may serve on the chargor a notice, in writing, to pay the money owing. If the chargor does not comply within two months after the date of service of the notice, the chargee may:

(a) sue the chargor for any money due and owing under the charge;
(b) appoint a receiver of the income of the charged land;
(c) lease the charged land, or if the charge is of a lease, sublease the land;
(d) enter into possession of the charged land; or
(e) sell the charged land.

In the event that a chargee opts to appoint a receiver, the chargee shall serve a notice in the prescribed form on the chargor and shall not proceed with the appointment until a period of 30 days, from the date of the service of that notice, has elapsed.

In the event that a chargee opts to exercise the power to sell the charged land, the chargee shall serve on the chargor a notice to sell in the prescribed form and shall not proceed to complete any contract for the sale of the charged land until at least 40 days have elapsed, from the date of the service of that notice to sell. The notice is required to be served on several people, including:

(a) the National Land Commission, if the charged land is public land;
(b) the holder of the land over which the lease has been granted, if the charged land is a lease;
(c) a spouse of the chargor who had given the consent;
(d) any lessee and sub-lessee of the charged land or of any buildings on the charged land;
(e) any person who is a co-owner with the chargor;
(f) any other chargee of money secured by a charge on the charged land of whom the chargee proposing to exercise the power of sale has actual notice;
(g) any guarantor of the money advanced under the charge;
(h) any other person known to have a right to enter on and use the land or the natural resources in, on, or under the charged land by affixing a notice at the property; and
(i) any other persons as may be prescribed by regulations, and shall be posted in a prominent place at, or as near as possible to, the charged land.

A chargee shall, before exercising the right of sale, ensure that a forced sale valuation is undertaken by a valuer. The price at which the charged land is sold should not be 25% or below the market value at which comparable interests in land of the same character and quality are being sold in the open market.

If a chargee or a receiver becomes entitled to exercise the power of sale, that sale may be by private contract at market value or public auction with reserve price. If a sale is to proceed by public auction, it shall be the duty of the chargee to ensure that the sale is publicly advertised in such a manner and form as to bring it to the attention of persons likely to be interested in bidding for the charged land and that the provisions relating to auctions and tenders for land are, as near as may be, followed in respect of that sale.

A chargee exercising the power of sale may, with leave of the court, purchase the property. A court shall not grant leave unless the chargee satisfies the court that a sale of the charged land to the chargee is the most advantageous way of selling the land.

The purchase money received by a chargee who has exercised the power of sale shall be applied in the following order of priority:

(a) first, in payment of any rates, rents, taxes, charges or other sums owing and required to be paid on the charged land. The Rating Act provides that any land rates due in respect of land shall be a charge against the land on which the rate was levied; and the charge shall take priority;
(b) second, in discharge of any prior charge or other encumbrance subject to which the sale was made;
(c) third, in payment of all costs and reasonable expenses properly incurred and incidental to the sale or any attempted sale;
(d) fourth, in discharge of the sum advanced under the charge or so much of it as remains outstanding, interests, costs and all other money due under the charge, including any money advanced to a receiver in respect of the charged land; and

(e) fifth, in payment of any subsequent charges in order of their priority, and the residue, if any, of the money so received shall be paid to the person who, immediately before the sale, was entitled to discharge the charge.

4.2 Do restrictions apply to foreign investors or creditors in the event of foreclosure on the project and related companies?

See question 4.1 above.

5 Bankruptcy and Restructuring Proceedings

5.1 How does a bankruptcy proceeding in respect of the project company affect the ability of a project lender to enforce its rights as a secured party over the security?

The recently enacted Insolvency Act provides that if the property of a bankrupt is subject to a charge, the creditor who holds the charge may choose either of the following options:

(a) to realise the property by having it sold (but only if the creditor is entitled to do so under the terms of the charge);
(b) to have the property valued and prove in the bankruptcy as an unsecured creditor for the balance due (if any) after deducting the amount of the valuation; or
(c) to surrender the charge to the bankruptcy trustee for the general benefit of the creditors and prove in the bankruptcy as an unsecured creditor for the whole debt.

The bankruptcy trustee may at any time, by notice, require a creditor who holds a charge over a bankrupt's property:

(i) within 30 days after receipt of the notice, to choose one of the options above; and
(ii) if the creditor chooses option (b) or (c), to exercise the chosen option within that period.

A creditor who fails to comply with the notice is taken to have surrendered the charge to the bankruptcy trustee under option (c) for the general benefit of the creditors, in which case the creditor may prove as an unsecured creditor for the whole debt.

Further, the Insolvency Act provides that if property of a bankrupt is subject to a security, the bankruptcy trustee may make an application to the court for an order enabling the bankruptcy trustee to dispose of the property as if it were not subject to the security, but only if it is satisfied that the disposal of the property would be likely to provide a better overall outcome for the creditors of the bankrupt.

5.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g. tax debts, employees' claims) with respect to the security?

The Insolvency Act provides that debts of a person who is adjudged bankrupt or of a company that is in liquidation are payable in the following order of priority:

(a) The expenses of the bankruptcy or liquidation will have first priority.
(b) The following debts will have second priority:
- all wages or salaries payable to employees in respect of services provided to the bankrupt or company during the four months before the commencement of the bankruptcy or liquidation;
- any holiday pay payable to employees on the termination of their employment before, or because of, the commencement of the bankruptcy or liquidation;
- any compensation for redundancy owed to employees that accrues before, or because of, the commencement of the bankruptcy or liquidation;
- amounts deducted by the bankrupt or company from the wages or salaries of employees in order to satisfy their obligations to other persons (including amounts payable to the Kenya Revenue Authority in accordance with the Income Tax Act);
- any reimbursement or payment provided for, or ordered by the Industrial Court under the Labour Institutions Act, 2007 to the extent that the reimbursement or payment does not relate to any matter specified in the Labour Relations Act, 2007 in respect of wages or other money or remuneration lost during the four months before the commencement of the bankruptcy or liquidation;
- amounts that are preferential claims under sections 175(2) and (3); and
- all amounts that are, by any other written law, required to be paid, in accordance with the priority established by this subparagraph, by a buyer to a seller on account of the purchase price of goods.

(c) The following debts will have third priority:
- tax deductions made by the bankrupt or company under the "pay as you earn" rules of the Income Tax Act;
- non-resident withholding tax deducted by the company under the Income Tax Act; and
- resident withholding tax deducted by the company under the Income Tax Act.

5.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

No entities are excluded from bankruptcy proceedings.

5.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of the project company in an enforcement?

The Land Act, 2012 provides similar remedies to a chargee in the event that a chargor defaults. The statute gives a clear procedure to be followed in such circumstances. If a chargor fails to pay interest or any other periodic payment due under any charge and continues to be in default for one month, the chargee may serve on the chargor a notice, in writing, to pay the money owing. If the chargor does not comply within two months after the date of service of the notice, the chargee may:

(a) appoint a receiver of the income of the charged land;
(b) lease the charged land, or if the charge is of a lease, sublease the land;
(c) enter into possession of the charged land; or
(d) sell the charged land.

5.5 Are there any processes other than formal insolvency proceedings that are available to a project company to achieve a restructuring of its debts and/or cramdown of dissenting creditors?

No, there are no other processes of this nature available. To this extent, companies can only enter into private contractual negotiations which may then introduce new payment plans. Under the Insolvency Act of 2015, the law provides for eligibility

thresholds for companies that may or may not enter into moratoria under voluntary arrangements for payment of debt. For eligible companies who wish to enter into such arrangements, a procedure is followed.

The directors shall:

(a) prepare:
  (i) a document setting out the terms of the proposal; and
  (ii) a statement of the company's financial position containing such particulars of its creditors and of its debts and other liabilities and of its assets as may be prescribed by the insolvency regulations for the purposes of this section, and such other information as may be so prescribed; and
(b) unless a provisional supervisor has already been appointed in respect of the proposal, appoint as its provisional supervisor an authorised insolvency practitioner who has consented to supervise it.

After preparing the proposal and statement and, if appropriate, making the appointment, the directors shall submit the proposal and statement to the provisional supervisor for consideration and comment.

The directors shall then vote on the proposal.

5.6 Please briefly describe the liabilities of directors (if any) for continuing to trade whilst a company is in financial difficulties in your jurisdiction.

Such directors are liable to imprisonment if convicted. Courts also have the power to disqualify directors. Under section 218 of the Companies Act, a court shall make a disqualification order against a person if satisfied, on an application made to it, that the person is or has been a director or secretary of a company that has at any time become insolvent, whether while the person was a director or secretary or subsequently and in the circumstances where the conduct of the person as a director or secretary of that company, either taken alone or taken together with the person's conduct as a director or secretary of any other company or companies, makes the person unfit to take part in the management of a company.

6 Foreign Investment and Ownership Restrictions

6.1 Are there any restrictions, controls, fees and/or taxes on foreign ownership of a project company?

No. The government provides the right for foreign and domestic private entities to establish and own business enterprises and engage in all forms of remunerative activity. However, a company whose shareholders are not Kenyan cannot own agricultural land, freehold land or leasehold property whose term exceeds 99 years. There are also restrictions as to foreign shareholding in the banking, insurance and telecommunications industries. In an effort to encourage foreign investment, the government repealed some regulations that imposed little foreign ownership limitation for firms listed on the Nairobi Securities Exchange, allowing such firms now to be 100% foreign-owned, as reported by the *UNCTAD World Investment Report 2016*. In 2015, the government established regulations requiring that Kenyans own at least 15% of the share capital of derivatives exchanges, through which derivatives such as options and futures can be traded.

When the Companies Act of 2015 came into force, foreign companies seeking registration in Kenya were required, under section 975(2)(b) of the Act, to ensure that by the time they are making the application for registration, at least 30% of their shareholding is held by a Kenyan citizen. However, this requirement has since been repealed.

6.2 Are there any bilateral investment treaties (or other international treaties) that would provide protection from such restrictions?

No, there are no such treaties with such protection provisions ratified by Kenya. In the recent past, Kenya has received an improvement in Foreign Direct Investment. Foreign investors seeking to establish a presence in Kenya generally receive the same treatment as local investors, and multinational companies make up a large percentage of Kenya's industrial sector. Through its official bilateral trade promotion agency, Ken Invest, Kenya has been viewed favourably by the international trade community. According to the United Nations Conference on Trade and Development (UNCTAD)'s Global Enterprise Registration Network, the Ken Invest site makes Kenya one of only 25 countries to have earned a perfect rating on its information portal. Further, before any laws touching on foreign investment are passed, there are substantive reviews and deliberations by stakeholders before any such laws are passed. As there is no bilateral treaty protecting investors from harsh trade restrictions, investors are made to feel secure by Kenya's local arrangements and foreign investment policies. However, Kenya has signed 14 bilateral investment conventions. This shows the commitment that Kenya has in advancing foreign investment.

6.3 What laws exist regarding the nationalisation or expropriation of project companies and assets? Are any forms of investment specially protected?

There are no laws regarding the nationalisation and expropriation of project companies or assets. The Constitution protects the right to private property, save in the case where such property needs to be compulsorily acquired for public benefit. Article 5 of the Foreign Investments Protection Act states that investments by investors of a Contracting Party in the territory of another Contracting Party shall not be expropriated, nationalised or subjected to any other measures, direct or indirect, having an effect equivalent to expropriation or nationalisation, except for a purpose which is in the public interest, on a non-discriminatory basis, in accordance with due process of law, and against prompt and full compensation. Any compensation that may need to be made under the Act shall be done at current commercial rates and shall be settled at freely convertible currencies.

7 Government Approvals/Restrictions

7.1 What are the relevant government agencies or departments with authority over projects in the typical project sectors?

The relevant agency is the Kenya Investment Authority (KIA), whose role is to assist and facilitate investments in Kenya. Its main functions are to promote investments in Kenya by local and foreign business enterprises, to liaise with the relevant Ministries responsible for approving all new private sector projects and expansion of existing projects, to assist business enterprises in implementing the projects approved by the relevant Ministries and, generally, to assist all business enterprises in overcoming managerial, institutional and bureaucratic problems.

7.2 Must any of the financing or project documents be registered or filed with any government authority or otherwise comply with legal formalities to be valid or enforceable?

Financing and project documents would need to be stamped in respect of the applicable stamp duty payable. Most mega projects that need project financing usually involve development projects that impact heavily on the community. As such, government agencies are usually involved in oversight roles. Since project financing consists of a long string of contractual deals, lawyers ensure all paperwork regarding payment of duties is completed to the end.

7.3 Does ownership of land, natural resources or a pipeline, or undertaking the business of ownership or operation of such assets, require a licence (and if so, can such a licence be held by a foreign entity)?

In the case of land and/or immovable property, an owner is usually provided with a document of title, and this could either be a Grant, a Certificate of Title, a Title Deed or a Lease. There is a restriction on foreign ownership of freehold land, leases exceeding 99 years and agricultural land. These leases can, however, be renewed with the expiry of the 99-year period.

The Constitution, the Mining Act and the Petroleum (Exploration and Production) Act all provide that natural resources in the form of minerals and petroleum belong to the Government of Kenya. An interested party may obtain a prospecting right or licence from the Government in respect of such natural resources. There are currently no restrictions on foreign ownership of companies intending to undertake such businesses.

To undertake a business in Kenya, the business entity would need to apply for a single business permit in addition to the licences that may be required in the particular economic sector. The KIA will process and grant approvals of new investment, once proposals are submitted on a prescribed application form. Proof of company registration must be attached to the application.

7.4 Are there any royalties, restrictions, fees and/or taxes payable on the extraction or export of natural resources?

Yes. There are applicable fees which one must pay to obtain a mining licence or a petroleum exploration licence. One must obtain a licence from the relevant authorities in order to be allowed to export extracted minerals or petroleum out of Kenya. There are also royalties that are payable in respect of extracted natural resources. For example, the Mining Regulations provide that "there shall be payable on all diamonds originating in Kenya an *ad valorem* royalty of fifteen per centum of the gross value thereof as assessed by an approved valuer appointed under the Diamond Industry Protection Regulations".

There is the National Resource Benefit Sharing Bill of 2014 which if passed will establish formulae in which proceeds from exploitation of natural resources shall be shared by the mining companies, national government, county governments and local communities. This role shall be under the scope of the Benefit Sharing Authority.

7.5 Are there any restrictions, controls, fees and/or taxes on foreign currency exchange?

Kenya does not operate a fixed exchange rate against any foreign currency. Therefore, the exchange rate between the Kenyan Shilling and any other currency is determined by market forces, subject of course to interventions from time to time by the Central Bank of Kenya (the CBK). The CBK and the commercial banks usually publish the exchange rates applicable on a day-to-day basis.

7.6 Are there any restrictions, controls, fees and/or taxes on the remittance and repatriation of investment returns or loan payments to parties in other jurisdictions?

Kenya does not have exchange control laws in force since the repeal of the Exchange Control Act in December 1995. However, the CBK Act establishes the CBK. Under the CBK Act, the CBK is empowered to formulate and implement the monetary policy in Kenya.

According to Central Bank Circular No. 12 of 1996 – "Revised Foreign Currency Transaction Guidelines to Authorised Banks", commercial banks were assigned a monitoring role by the CBK and each commercial bank is required to submit returns to the CBK on a regular basis. Foreign currency is freely repatriable from Kenya, provided there is written evidence of an underlying business transaction and the respective bank handling the repatriation is satisfied as to the genuineness of the transaction. However, for any amount equivalent to USD 500,000 or more, the CBK has requested that a commercial bank first consult with them as to the amount and purpose of the remittance. This is stated to be for statistical purposes. For any amount below the equivalent of USD 10,000, commercial banks are not required to obtain any documentary evidence to back the transaction, although in certain cases banks will nonetheless seek an explanation.

The Foreign Investments Protection Act provides that a foreign national who proposes to invest foreign assets in Kenya may apply to the Cabinet Secretary in charge of finance, for a certificate that the enterprise in which the assets are proposed to be invested is an approved enterprise. The Cabinet Secretary shall consider every application made and, in any case in which he is satisfied that the enterprise would further the economic development of or would be of benefit to Kenya, he may in his discretion issue a certificate to the applicant. The holder of a certificate may, in respect of the approved enterprise to which such certificate relates, transfer out of Kenya in the approved foreign currency and at the prevailing rate of exchange:

(a) the profits, including retained profits which have not been capitalised, after taxation, arising from or out of his investment in foreign assets, provided that any increase in the capital value of the investment arising out of the sale of the whole or any part of the capital assets of the enterprise or revaluation of capital assets shall not be deemed to be profit arising from or out of the investment for the purposes of the Foreign Investments Protection Act;

(b) the capital specified in the certificate as representing and being deemed the fixed amount of the equity of the holder of the certificate in the enterprise for the purpose of this Act, provided that:

- where any amendment or variation is made in the amount of the said capital, the amended or varied amount shall be substituted for the original amount; and

- no additional amount or sum shall be added to the capital specified in the certificate (as amended or varied) to represent any increase in the capital value of the investment since the issue of the certificate or since the last amendment or variation of the certificate; and

(c) the principal and interest of any loan specified in the certificate.

7.7 Can project companies establish and maintain onshore foreign currency accounts and/or offshore accounts in other jurisdictions?

Yes, they can.

7.8 Is there any restriction (under corporate law, exchange control, other law or binding governmental practice or binding contract) on the payment of dividends from a project company to its parent company where the parent is incorporated in your jurisdiction or abroad?

No, there is no such restriction.

7.9 Are there any material environmental, health and safety laws or regulations that would impact upon a project financing and which governmental authorities administer those laws or regulations?

Yes. The Environmental Management and Co-ordination Act (the EMCA) requires a project proponent to carry out an environmental impact assessment (EIA) study and submit a project report "before financing, commencing, proceeding with, carrying out...or causing to be financed, commenced, proceeded with, carried out..." any undertaking of certain projects, including mining, activities out of character with their surroundings, and major changes in land use.

The EMCA requires the owner of premises or the operator of a project to take all reasonable measures to mitigate any undesirable effects not contemplated in the EIA study report, and shall prepare and submit an environmental audit report on those measures to the National Environment Management Authority (NEMA) annually or as NEMA may in writing require. NEMA is established under section 7 of the EMCA with the mandate, *inter alia*, to coordinate and supervise environmental matters and serve as the principal government institution for the implementation of environmental policies.

The EMCA provides that no owner or operator of any trade or industrial undertaking shall discharge any effluents or other pollutants into the environment without an effluent discharge licence issued by NEMA. The EMCA defines "effluent" to mean "gaseous waste, water or liquid or other fluid of domestic, agricultural, trade or industrial origin treated or untreated and discharged directly or indirectly into the aquatic environment".

In line with Sustainable Development Goals No. 13 on climate action, foreign investment companies that set up in Kenya are required to strictly adhere to environmentally friendly practices for realisation of sustainable development.

7.10 Is there any specific legal/statutory framework for procurement by project companies?

This is governed by the Public Procurement and Disposal Act (which establishes procedures for efficient public procurement and for the disposal of unserviceable, obsolete or surplus stores, assets and equipment by public entities) and the Public Private Partnership Act (which provides for: the participation of the private sector in the financing, construction, development, operation, or maintenance of infrastructure or development projects of the government through concession or other contractual arrangements; and the establishment of the institutions to regulate, monitor and supervise the implementation of project agreements on infrastructure or development projects).

8 Foreign Insurance

8.1 Are there any restrictions, controls, fees and/or taxes on insurance policies over project assets provided or guaranteed by foreign insurance companies?

There are no restrictions against insurance policies over project assets provided or guaranteed by foreign insurance companies. There may be VAT implications as the provision of insurance by a foreign company may be deemed to be an imported service.

8.2 Are insurance policies over project assets payable to foreign (secured) creditors?

Yes, they are.

9 Foreign Employee Restrictions

9.1 Are there any restrictions on foreign workers, technicians, engineers or executives being employed by a project company?

Such workers would need to apply for and obtain visas (where applicable) and any requisite work permits. Work permits and visas are issued under different classes by the Department of Immigration. The general guiding principle for issuance of work permits by the government is that these should be issued to foreign workers, technicians, engineers or executives only where the tasks cannot be undertaken by qualified Kenyans. Even where the work permits are issued to foreigners, there is a general expectation by the government that there should be knowledge transfer before the lapse of the work permit.

10 Equipment Import Restrictions

10.1 Are there any restrictions, controls, fees and/or taxes on importing project equipment or equipment used by construction contractors?

There are no restrictions on importing project equipment. Applicable customs duty would, however, be payable.

The Import Declaration Fee was recently lowered from 2.25% to 2% of Cost Insurance and Freight.

Goods and services for the construction of infrastructure works in industrial and recreational parks of 100 acres or more in Nairobi, Nakuru, Kisumu, Mombasa and Eldoret are VAT-exempt.

10.2 If so, what import duties are payable and are exceptions available?

The Customs and Excise Act contains an extensive list of the items attracting import duty. In terms of exceptions, the

Customs and Excise Act also contains quite an extensive list of the institutions and persons that enjoy exemptions in respect of various items as indicated in the Act.

11 *Force Majeure*

11.1 Are *force majeure* exclusions available and enforceable?

Yes. These would have to be set out in the applicable contracts. *Force majeure* exclusions do not apply to payment obligation.

12 Corrupt Practices

12.1 Are there any rules prohibiting corrupt business practices and bribery (particularly any rules targeting the projects sector)? What are the applicable civil or criminal penalties?

State officers and public officials are involved in major projects. Chapter 6 of the Constitution of the Republic of Kenya (which is the supreme law of the country) provides for Leadership & Integrity of state officers.

Chapter 6 clearly stipulates that such officers are required to take an oath of office before assuming office and conduct themselves ethically. The Chapter further provides for financial probity of state officers. Any officers found to have been engaged in unethical or corrupt business practices are, under the Constitution, prohibited from holding such offices in the future.

There is also the Leadership & Integrity Act No. 19 of 2012 (the LIA), which is a statute that gives effect to the provisions of Chapter 6 of the Constitution discussed above.

Under the LIA, where there have been investigations and a public officer is found to have committed an offence, a referral may be made for civil or criminal proceedings against the officer and, under section 43, the matter may be referred to the Ethics and Anti-Corruption Commission (established under the Ethics and Anti-Corruption Act No. 22 of 2011) or the Attorney-General, for civil matters, the Director of Public Prosecutions, for criminal matters or any other appropriate authority.

Under section 49 of the LIA, where it is proved that a state officer obtained any property in breach of the Act, the officer shall be subject to any appeal, which he/she may make, forfeit the property and the property shall be held by the Commission or an agent appointed by the Commission, in trust for the country, until it is lawfully disposed of. The Commission may also order the state officer to compensate such sum including interest, as may be determined by the Commission as just, with regard to the loss suffered by the government and such order shall be deemed to be a decree under the Civil Procedure Act.

The LIA further creates various offences and penalties. For example, under section 47, "any person who has convicted an offence under this Act, for which no penalty is expressly provided, shall be liable on conviction to a fine not exceeding five hundred thousand shillings (KES 500,000), or to imprisonment for a term not exceeding three years, or to both".

The Anti-Corruption and Economic Crimes Act provides for the prevention, investigation and punishment of corruption, economic crime and related offences. There are several offences under this Act and each offence attracts a penalty. Penalties range from fines of KES 300,000 to KES 2,000,000, to maximum prison sentences ranging from three years to 10 years.

Government officials are also subject to Public Officer Ethics Act, which regulates the conduct of public officers in the discharge of their duties. The purpose of the Act is to advance the ethics of public officers by providing for a code of conduct and ethics, and requiring financial declaration from certain public officers. Under this Act, where a person is found to have hindered or interfered with others exercising their duties under the Act, they shall be liable under the Act and may be convicted for a fine not exceeding KES 5,000,000 or to imprisonment for a term not exceeding five years.

13 Applicable Law

13.1 What law typically governs project agreements?

Project agreements are typically governed by contract, save in the case where one of the parties is the government, a state corporation or a county government, in which case provisions of statutes such as the Constitution, the Government Contract Act, the State Corporations Act, the County Governments Act, Public Private Partnerships Act and the Public Procurement and Disposal Act would need to be considered.

13.2 What law typically governs financing agreements?

Financing agreements are typically governed by contract law, banking law and debt finance law.

13.3 What matters are typically governed by domestic law?

Contracting parties have the freedom to choose the governing law in respect of their contract. Parties would, however, still have to adhere to the laws of the land in respect of various aspects of their project, including but not limited to land. Land-related agreements, permits and consents, employment, etc. are normally governed by the law of the location of the project.

14 Jurisdiction and Waiver of Immunity

14.1 Is a party's submission to a foreign jurisdiction and waiver of immunity legally binding and enforceable?

Yes, it is. To this effect, bold pronouncements were made in the case of *Talaso Lepalat v The Embassy of the Federal Republic of Germany & 2 Others* [2014].

15 International Arbitration

15.1 Are contractual provisions requiring submission of disputes to international arbitration and arbitral awards recognised by local courts?

Yes, they are.

15.2 Is your jurisdiction a contracting state to the New York Convention or other prominent dispute resolution conventions?

Yes, it is. Kenya has also enacted the Investment Disputes Convention Act which gives legal sanction to the provisions of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States.

15.3 Are any types of disputes not arbitrable under local law?

Disputes involving matters that are criminal in nature are not generally arbitrable under local law.

15.4 Are any types of disputes subject to mandatory domestic arbitration proceedings?

No, they are not.

16 Change of Law / Political Risk

16.1 Has there been any call for political risk protections such as direct agreements with central government or political risk guarantees?

Kenya has had no recent call for political risk protections for companies investing in Kenya. Generally, letters of undertaking and guarantees are the two most common commitments that the government formally issues to guarantee payments. The Public Finance Management Act and the Public Private Partnerships Act, read together with the Constitution of Kenya, recognise guarantees by the government subject to specified conditions prescribed thereunder. The choice as to which one it issues will depend on the circumstances of each case. Although both can be binding in law, there is some doubt over the enforceability of letters of undertaking, especially considering that the Public Finance Management Act is silent on the same, though the Public Private Partnerships Act provides for their issuance, albeit vaguely. A guarantee may, in the context of the present legal framework, be preferable and recommended. Once issued, the Public Finance Management Act provides that no further parliamentary authorisation shall be necessary for payment under a guarantee, and that the same shall be a charge on the consolidated fund. Under the Public Finance Management Act, issuance of a guarantee is the prerogative of the Cabinet Secretary responsible for Finance. Once the guarantee is issued, parliament is required to approve it. As to changes in law, Kenya's Constitution provides that any newly enacted law shall not apply retroactively. To cushion any unfavourable changes in law, there is usually room for extensive deliberations by stakeholders before such a law is passed.

17 Tax

17.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Interest to be paid on loans from foreign lenders for the purposes of investing in the energy or water sectors, or in roads, ports, railways or aerodromes, are exempt from tax.

Further, instruments (including charges, debentures and guarantees) executed with respect to the transactions relating to loans from foreign sources received by investors in the infrastructure (energy, roads, ports, water, railways and aerodromes) development sector shall be exempted from the provisions of the Stamp Duty Act.

However, for companies not falling in the above bracket, Kenya imposes a withholding tax at the basic rate of 15% per annum. The Income Tax Act prescribes how to compute withholding tax on deemed interest.

17.2 What tax incentives or other incentives are provided preferentially to foreign investors or creditors? What taxes apply to foreign investments, loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

See question 17.1 above.

Both fiscal and non-fiscal incentives are available in Kenya. The Kenya Revenue Authority implements the issuance of the fiscal (tax) incentives in collaboration with other regulators and facilitators such as the Capital Market Authority and the Export Processing Zones Authority, among others, as provided under the Income Tax Act, Laws of Kenya.

18 Other Matters

18.1 Are there any other material considerations which should be taken into account by either equity investors or lenders when participating in project financings in your jurisdiction?

Equity investors and/or lenders should undertake due diligence investigations on a particular project and/or project company before advancing any funds. The due diligence exercise should cover the legal and financial status of the companies that the investors or lenders would be contracting with.

Further, due diligence should extend to the nature of projects invested in. Each project financing has its own unique structure. For example, many financiers shy away from funding road construction projects because of its high income return risks. Realistically, demand/traffic risk is often unavoidable. Financiers should, as need be, conduct their own traffic projections to be in a good position to assess this risk involved in financing these projects as opposed to relying on traffic projections done by project companies. This balancing of information is crucial in the steering of mega projects.

18.2 Are there any legal impositions to project companies issuing bonds or similar capital market instruments? Please briefly describe the local legal and regulatory requirements for the issuance of capital market instruments.

There are legal impositions on project companies issuing bonds or capital market instruments in Kenya. The local legal and regulatory requirements for the issuance of capital market instruments are set out in the Capital Markets Act. The Capital Markets Act prohibits any person from carrying on business as a stockbroker, derivatives broker, real estate investment trust (REIT) manager, trustee, dealer, investment adviser, fund manager, investment bank, central depository, authorised securities dealer, or authorised depository, or from holding himself out as carrying on such a business unless he holds a valid licence issued under the Capital Markets Act or under the authority of the Capital Markets Act. However, foreign companies can issue bonds even regionally according to part II section 7 of the Capital Markets Securities Public Offers Listing and Disclosures Regulations of 2002.

19 Islamic Finance

19.1 Explain how *Istina'a*, *Ijarah*, *Wakala* and *Murabaha* instruments might be used in the structuring of an Islamic project financing in your jurisdiction.

Istina'a – In Islamic finance, *Istina'a* is generally a long-term contract whereby a party undertakes to manufacture, build or construct assets, with an obligation from the manufacturer or producer to deliver them to the customer upon completion. This instrument may be used in the manufacturing industry and also in infrastructure projects.

Ijarah – This contract represents a transaction in which a known benefit (usufruct) associated with a specified asset is sold for a payment. In the course of this sale of usufruct, ownership of the asset is not transferred – the bank maintains ownership of the asset. An *Ijarah* may be used in a construction project where the financier would be involved in the construction of the development, then subsequently lease out the property to the end consumer, with the end consumer's last instalment being used as the amount required to purchase the property.

Wakala – Describes an agency or a delegated authority where a principal appoints the agent to carry out a specific job on behalf of the principal. *Wakala* agreements are agency agreements where the principal and the agent share in the profit and risk of loss of investment. Any guarantee on minimum return is not *Shari'ah*-compliant. This can be used where a company acts as the agent for a financier or lender by investing the funds from that financier or lender. The company may choose to invest the funds in different projects, and profits and losses would be shared equally by both parties.

Murabaha – It is often referred to as "cost-plus financing" and frequently appears as a form of trade finance based upon letters of credit. In its simplest form, this contract involves the sale of an item on a deferred basis. This could be used to finance the movable assets that may be used in a project; for example, motor vehicles.

19.2 In what circumstances may *Shari'ah* law become the governing law of a contract or a dispute? Have there been any recent notable cases on jurisdictional issues, the applicability of *Shari'ah* or the conflict of *Shari'ah* and local law relevant to the finance sector?

The Constitution is the supreme law of Kenya. Islamic finance products, on the other hand, are to be governed by *Shari'ah*.

Article 170(5) of the Constitution states that the jurisdiction of a *Kadhis'* court shall be limited to the determination of questions of Muslim law relating to personal status, marriage, divorce or inheritance in proceedings in which all the parties profess the Muslim religion and submit to the jurisdiction of the *Kadhis'* courts. As such, the jurisdiction of the *Kadhis'* court does not extend to contractual relations. The *Kadhis'* Courts Act further reiterates this point by providing that a *Kadhis'* court shall have and exercise jurisdiction over the determination of questions of Muslim law relating to personal status, marriage, divorce or inheritance in proceedings in which all the parties profess the Muslim religion.

The Judicature Act provides the sources of law in Kenya which include the Constitution, written laws, the substance of the common law, the doctrines of equity and the statutes of general application in force in England on 12 August 1897, and African customary law. It should be noted that *Shari'ah*, Islamic or Muslim law is not referred to in the Judicature Act. Therefore, although a contract may be prepared in accordance with *Shari'ah*, the governing law will be Kenyan, as Kenya does not recognise *Shari'ah* law as governing contracts in Kenya.

To our knowledge, there have not been any notable cases to date over jurisdictional matters pertaining to *Shari'ah* law.

19.3 Could the inclusion of an interest payment obligation in a loan agreement affect its validity and/or enforceability in your jurisdiction? If so, what steps could be taken to mitigate this risk?

Islamic finance prohibits the charging or payment of interest. Consequently, Kenya, in an attempt to regulate Islamic banking operations and products, made slight changes to its Banking Act. Initially, the Banking Act only made reference to "interest". The Banking Act was subsequently amended in 2008 by adding the phrase "or a return in the case of an institution carrying out business in accordance with Islamic law" when referring to interest chargeable on a savings account. It would be interesting to see what Kenyan courts would determine in cases where an interest payment obligation was included in a loan agreement that is meant to be *Shari'ah*-compliant. In the English case of *Dunlop Pneumatic Tyre Co Ltd v New Garages & Motor Co Ltd* [*1915*] *AC 79*, the court held that, generally, the inclusion of an interest payment obligation in a loan agreement would not affect its validity and/or enforceability unless that interest payment obligation is deemed a penalty offending the rules laid down in that particular case. With the common law doctrine of precedent, this position may have a bearing in future transactions in Kenya if *Shari'ah* law changes to allow charging or payment of interest.

Pamella Ager, as head of the Real Estate, Conveyancing and Securities teams, has been part of various ground-breaking Kenyan commercial transactions; for instance, the privatisation of several government entities – including Mumias Sugar Company and Kenya Electricity Generating Company. She also acted in a flotation exercise by KCB (Kenya's biggest bank, in network terms), two successful rights issues for KCB, the development of Kenya's Central Depository and Settlement Corporation, and the Private Placement of The Cooperative Insurance Company of Kenya (CIC). Pamella specialises in the following areas: banking & finance; capital markets; conveyancing; mergers & acquisitions; and regulatory work. Pamella is recognised for her breadth of expertise, and has served as a Lecturer at the University of Nairobi's renowned Faculty of Law. In addition, she holds an LL.M. degree, 1st Class Honours from Auckland University.

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Established 43 years ago, by George Oraro SC (one of Kenya's top litigators), Oraro & Company Advocates is a top-tier, full-service Kenyan law firm. The firm's areas of strength include Corporate & Commercial, Dispute Resolution, Intellectual Property, Real Estate, Conveyancing & Securities and Tax. Its partnership includes some of Kenya's best legal minds and its lawyers are recognised by several international leading legal directories. The firm is also well-recognised for its contribution to Kenyan jurisprudence (through its formidable dispute resolution team), work on some of Kenya's largest deals and its significant contributions to Kenya's legal profession. The firm's corporate and commercial team specialises in all aspects of transactional work such as banking and finance, capital markets, corporate finance, corporate regulatory work, energy law, mergers & acquisitions and project finance. It also has Islamic finance capabilities and has advised Islamic finance clients on a variety of matters, including *Shari'ah* compliance.

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