ORARO & COMPANY ADVOCATES

LEGAL & KENYAN

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IN THIS ISSUE

Editorial Note

John Mbaluto
Partner | john@oraro.co.ke

A mixed bag of insights

Greetings!

It is said that one of the key attributes of any successful relationship, the Advocate-Client relationship being no exception, is good communication. Indeed, an indispensable quality of a good lawyer is regular communication with the client with respect to the client's matter. At Oraro & Company Advocates, we pride ourselves at going a step further by striving to keep clients updated not just with their matters, but also with the latest developments in the Kenyan legal scene. Our quarterly newsletter, aptly named Legal & Kenyan, is one of the ways through which we achieve this - by bringing you pithy, interesting and well-researched articles touching on diverse areas. In what is the 3rd edition of our newsletter, our team of authors delivers an exciting blend of topics, yet again for your reading pleasure:-

Juliet C. Mazera and Cindy Oraro explore Kenya's investor-friendly renewable energy sector and make out a case (no pun intended!) that the country's renewable energy sector remains largely untapped. Noella Lubano discusses the growth of international arbitration as a means of dispute resolution while Nelly Gitau and Cindy Oraro look at the role of joint ventures in large scale real estate projects. Pamella Ager and Jeal Aduke review the new guidelines issued under the Capital Markets Act, Cap. 485A aimed at preventing financial crimes and conclude that if well implemented, the new guidelines could go far in curbing money laundering and terrorism finance. Walter Amoko and Jackson Awele analyse the "twin" principles of confidentiality and disclosure in public-private partnerships procurement as elucidated by the High Court in the APM Terminals case, highlighting that the key is to strike a balance between this two principles. Noella Lubano and Patricia Ouma examine the state of deposit insurance in Kenya as compared with other jurisdictions such as the UK and the US, while Juliet C. Mazera addresses the question of jurisdiction in Islamic finance including what the current Banking law portends for institutions offering Islamic banking products such as the *murabaha* and the diminishing *musharakah*. Nelly Gitau and Daniel Okoth give a detailed overview of the regulatory framework within which investment managers and financial analysts work, while Geoffrey Muchiri and Lena Onchwari discuss the new Tax Procedures Act, 2015 as the herald of a new era in taxation in Kenya, expressing that the new law is a positive way forward for tax administrative procedures.

As always, we look forward to receiving your feedback and our authors are happy to answer any queries you might have with respect to any of the articles.

Enjoy the read!

Sincerely,

John Mbaluto,
Editor

The Editorial Team
Angela Ogang - Legal Assistant
Beryl Rachier - Associate
Carol Njiru - Legal Assistant
Daniel Okoth - Associate
Eddy Owiti - Associate
Edwin Odundo - Associate
Geoffrey Muchiri - Partner
Georgina Ogalo-Omondi - Senior Associate
Jill Barasa - Associate
John Mbaluto - Partner
Kevin Kwaria - Business Development Assistant
Loise Machira - Legal Assistant
Olivia Kiratu - Head of Business Development
Pamella Ager - Partner
Walter Amoko - Partner

Contributors
Angela Ogang - Legal Assistant
Carol Njiru - Legal Assistant
Cindy Oraro - Senior Associate
Daniel Okoth - Associate
Geoffery Muchiri - Partner
Grace Mwangome - Legal Assistant
Jackson Awele - Senior Associate
Jeal Aduke - Associate
Juliet C. Mazera - Consultant
Lena Onchwari - Senior Associate
Nelly Gitau - Partner
Noella Lubano - Partner
Pamella Ager - Partner
Patricia Ouma - Associate
Walter Amoko - Partner

CONTENTS

KEY FIRM STATISTICS

28
Number of lawyers.

2006
The year our Senior Partner (George Oraro SC) and Managing Partner (Chacha Odera) were first ranked as leading lawyers in Chambers Global.

1977
Year of establishment.

Pamella Ager
Partner | pamella@oraro.co.ke

Jeal Aduke
Associate | jaduke@oraro.co.ke

TIGHTENING THE REINS:

FIGHTING FINANCIAL CRIMES IN THE KENYAN CAPITAL MARKETS

A financial system can be accessed through several avenues such as capital markets, banking and insurance industries. Such access has over time opened doors for engagement in money laundering and terrorism financing, which are white collar crimes with adverse effects on the modern day economy.

Capital markets are part of a financial system concerned with raising capital by dealing in shares, bonds and other long-term securities. Money laundering on the other hand, has been defined in a number of ways. The Financial Action Task Force (**FATF**) which is an inter-governmental body established in 1989, with the aim of setting standards and promoting effective implementation of measures for fighting money laundering and terrorist financing, has defined money laundering as "the processing of criminal proceeds to disguise their illegal origin."

The Proceeds of Crime and Anti-Money Laundering Act, 2009 (**the Act**) defines money laundering as "an offence under any of the provisions of Sections 3, 4 and 7." Section 3 of the Act provides that a person who knows that property forms part of the proceeds of crime and enters into an agreement or performs any other act in connection with such property whose effect is to conceal the source or assist any person who has committed an offence to avoid prosecution, or remove any property acquired as a result of the commission of an offence, commits an offence. Section 4 provides that a person who acquires, uses or has possession of property and who, at the time of acquisition, use or possession of such property, knows that it forms part of proceeds of a crime committed by him or by another person, commits an offence. Lastly, Section 7 of the Act provides that a person who, knowingly transmits or receives or makes the attempt to transmit or receive a monetary instrument or anything of value to another person with intent to commit an offence, commits an offence.

Terrorism financing has been defined in the Prevention of Terrorism (Implementation of the United Nations Security Council Resolutions on Suppression of Terrorism) Regulations, 2013 to include the offence specified under Section 5 of the Prevention of Terrorism Act, 2012 (**PTA**). Section 5 of the PTA provides that a person who collects, provides or makes available any property, funds or a service knowing that such property, funds or service shall be used for the commission of a terrorist act or by a terrorist group or by a natural person in the commission of a terrorist act commits an offence.

In the past, money launderers targeted banks to launder their unlawful funds. However, the global nature, anonymity, speed at which transactions are executed, ability to pool funds through means such as collective investment schemes and the highly liquid nature of capital markets, have provided fertile breeding ground for money laundering and terrorism financing. Furthermore, the capital markets sector is distinctive among other financial sectors in that it can both be used to launder illicit funds obtained outside of the financial markets and also to generate illicit funds within the market itself, through fraudulent activities such as insider trading.

In an endeavour to curb the aforesaid, the Capital Markets Authority (**CMA**) pursuant to powers vested in it under Section 12A(1) of the Capital Markets Act, Cap. 485A enacted the Guidelines on the Prevention of Money Laundering and Terrorism Financing (**the Guidelines**) in the Capital Markets vide Gazette Notice Number 1421 on 4th March, 2016.

The Guidelines, which are aligned to the Kenyan Anti-Money Laundering and Counter Terrorism Financing laws mentioned above as well as the recommendations of FATF, are meant to form part of efforts to improve corporate governance and encourage capital inflows to Kenya. The Guidelines provide an explanation of certain features of the capital markets that have made it prone to money laundering and also give an account of the three stages involved in the money laundering process. The first is the 'placement' stage which involves the introduction of proceeds of crime into the financial system.

The capital markets sector is distinctive among other financial sectors in that it can both be used to launder illicit funds obtained outside of the financial markets and also to generate illicit funds within the market itself, through fraudulent activities such as insider trading.

The second is the 'layering' stage where the proceeds are moved through a series of transactions in order to distance them from their source. The third stage is 'integration' which places the laundered proceeds back into the legal economy.

The Board of Directors of a person licensed to transact business by the CMA (market intermediary) have under Guideline 3 been vested with the responsibility of establishing Anti-Money Laundering and Counter Terrorism Financing policies, procedures and internal controls, as well as ensuring compliance with existing legislation. The said policies, procedures and controls are to be reviewed once in every two (2) years to guarantee their effectiveness.

To effectively mitigate money laundering risks in capital markets, Guideline 4(2) provides that a market intermediary must adopt a risk-based approach and methodologies to determine a holistic view of the level of risk posed and avoid a silo approach, when assessing the relationship between risks. A market intermediary may assess the money laundering risks of individual customers by assigning money laundering risk rating to their customers and in doing so, the market intermediary shall consider factors outlined in the Guidelines which include in relation to country risk, customers in connection with high-risk jurisdictions, for instance, those that have been identified by the FATF as jurisdictions with high strategic Anti-Money Laundering deficiencies or are believed to have strong links to terrorist activities.

Factors which indicate that a customer presents a high risk of money laundering as enumerated under Guideline 4(4)(d), include where the origin of wealth cannot be easily verified as well as a politically exposed person. Examples of customers that might be considered to carry lower money laundering risks are those with a regular source of income from a known legitimate source, those with a positive reputation and public entities. A market intermediary is to keep records of the risk assessment for a minimum of seven (7) years from their official date of creation. Guideline 4(6) makes it mandatory for a securities exchange to have surveillance systems and mechanisms intended to detect activities that might be a consequence of market manipulation or insider trading, which are offences often associated with money laundering.

A market intermediary shall under Guideline 5 obtain satisfactory evidence of the identity and legal existence of persons applying to do business with it. It should reject transactions with clients who fail to provide proof of their identity. Due diligence and scrutiny of customers' identity and their investment objectives should be done throughout the course of a business relationship.

Where there is a perception of increased risk with regard to face-to-face transactions, a market intermediary may request for submission of additional documentation such as a reference letter from a current employer, bank statements, a lease for a rental house or business premises and a passport or a national identity card. These additional documents would enable the market intermediary obtain further independent verification.

With regard to prospective non-resident customers who wish to open an account with a market intermediary in Kenya, the Guidelines provide for adoption of effective identification procedures akin to those applied to Kenyan resident customers. Guideline 7 indicates that such customers will be required to provide identity documents, such as a copy of their passport, national identity card or documentary evidence of address which shall be certified by the embassy of the country of issue, a commissioner of oaths or notary public or a senior officer of the market intermediary. A market intermediary may further verify identity through a reputable institution authorised to carry out the role in the applicant's country of residence.

Stringent measures that ought to be taken with regard to establishing the true identity of corporate and legal entities have been outlined in the Guidelines. For a body corporate, there should be evidence of registration, a corporate resolution authorising a person to act on behalf of the body corporate, as well as a copy of the latest annual returns. In the case of partnerships and unit trusts, the identity of all partners and signatories to the account must be verified and the relevant deeds and documentation should be obtained. The Guidelines emphasise the need for particular care to be exercised when trust, nominee and fiduciary accounts are set up in locations with strict bank secrecy or confidential rules, as the said accounts are a popular vehicle for money laundering.

Stringent measures that ought to be taken with regard to establishing the true identity of corporate and legal entities have been outlined in the Guidelines.

The Guidelines also provide that all records of customers, business relationships and transactions shall remain up-to-date, relevant and accessible and that a market intermediary shall maintain and keep the said records for a minimum period of seven (7) years, from the date the relevant transaction was completed or following the termination of a business relationship.

Robust measures and procedures are to be undertaken while using new technologies and non-face-to-face business transactions. These measures include confirmation of the customer's address through the exchange of correspondence or other appropriate methods, certification of identification documents, confirmation of the customer's salary and any other reliable verification checks.

A market intermediary incorporated in Kenya, as stated under Guideline 9, shall develop a group policy on anti-money laundering and countering financing of terrorism which shall apply to all its branches and subsidiaries, where applicable outside Kenya.

A market intermediary is required to report suspicious transactions to the Financial Reporting Centre established under Section 21 of the Proceeds of Crime and Anti-Money Laundering Act, 2009 within seven (7) days of the date of the transaction. In addition, a market intermediary is required to report to the Financial Reporting Centre, all cash transactions carried out by it equivalent or exceeding USD 10,000 (approximately KES 1 million) or its equivalent in any other currency whether or not the transaction appears to be suspicious.

The issuance of a licence or an approval to a market intermediary by the CMA shall be determined by the market intermediary's compliance with the Guidelines and similar legislation. A market intermediary is required under the Guidelines to monitor on an ongoing basis, its business relationships with its customers, as well as conduct training programmes to ensure that the requirements under the Proceeds of Crime and Anti-Money Laundering Act are well understood and implemented. It is an offence for anyone who knows that a disclosure has been made in connection with an investigation into money laundering or terrorist financing, to inform the person who is the subject of a suspicion of the disclosure.

Finally, in relation to combating the financing of terrorism, the Guidelines provide that market intermediaries shall, upon receipt from the CMA, keep updated the various resolutions passed by the United Nations Security Council (**UNSC**) on counter-terrorism measures, maintain a database of names and particulars of listed persons and ensure the database is easily accessible to its employees. Market intermediaries are required to conduct regular checks on names of both the new, existing and potential customers against the names in the database. Moreover, where there is any name match and there has been confirmation of the identity, the measures to be taken include freezing the customer's funds and informing the relevant bodies.

If properly implemented, there is no doubt that these Guidelines will to a large extent curb money laundering and terrorism financing in the capital markets. The Guidelines mark a bold and laudable move by the CMA to rein in financial crimes.

Nelly Gitau
Partner | nelly@oraro.co.ke

Cindy Oraro
Senior Associate | cindy@oraro.co.ke

BUILDING ON SHARING

THE PLACE OF JOINT VENTURES IN LARGE SCALE REAL ESTATE DEVELOPMENTS

Overview of the Kenyan real estate market

The real estate sector in Kenya is ranked as the fourth biggest contributor to the country's economy according to the Kenya National Bureau of Statistics (**KNBS**). Nairobi has also received recognition as one of the fastest growing real estate markets in the world. Factors such as Kenya's strategic geographic location, rural migration and rapid urbanisation, ongoing economic growth, improved government policies and increased foreign direct investment have driven the development and expansion of existing real estate. The country's booming real estate market is also said to be influenced by an expanding middle class, defined by KNBS as capturing anyone with a monthly income between USD 278 (KES 28,184) and USD 2,310 (KES 234,192).

The sector, particularly commercial real estate, is expected to continue to grow amid recent discoveries in oil and gas, growth in manufacturing, technology and telecoms, outsourcing and retailing. However, developers are not able to satisfy the demand due in part to non-availability of loan capital, sky-rocketing interest rates, rapidly rising real estate prices and general low levels of income. In fact, land and finance have been identified as the two major factors affecting real estate development in Kenya. Property prices in major cities and especially Nairobi have increased exponentially in the last couple of years and the cost of borrowing remains high and unpredictable, making it increasingly difficult for both landowners and property developers to implement real estate projects. Simply put, a developer who buys land may not have enough money left to develop the land, while landowners lack capital and financial resources to engage in property development. It is against this backdrop that property developers and landowners are increasingly turning to joint ventures as a means of financing acquisitions and developments.

What are real estate development joint ventures?

A joint venture is a commercial collaboration in which two or more unrelated parties pool, exchange or integrate some of their resources with a view to achieving mutual gain. The joint venture may be for a fixed or indefinite duration. In real estate development joint ventures, the landowner typically enters into an agreement with the property developer to contribute land while the latter finances the development. The profits derived from the joint venture are then apportioned according to the value of what each party has brought to the table. Joint venture partners could also be consultants such as architects, contractors, quantity surveyors, project managers, structural engineers, physical planners, accountants or lawyers who may agree to offer their professional skills and services as their contribution to the joint venture.

Reasons to enter into real estate development joint ventures

The reasons for choosing to go by way of a joint venture are diverse but most joint ventures are formed as a way of raising additional capital or to bring in people with the required development skills and expertise.

Joint ventures are advantageous to landowners because they reduce the risk associated with bank loan repayments such as unexpected increase in interest rates and enable access to services from consultants without having to pay the initial consultancy fees. Joint ventures also cushion developers, and home buyers by extension, from exorbitant land prices due to the elimination of the costs related to land acquisition.

As a rule of thumb, there needs to be a good reason to enter into a real estate development venture. Below are a few other scenarios where joint ventures would be advantageous for a real estate developer:

- Where the landowner is unwilling to agree to an outright sale of the land and the only available option is to enter into a joint venture
- Where an awarding authority requires a local business partner and this requirement cannot be satisfied without entering into a joint venture
- Where a potential partner has strong ties with the regulators and permit-granting authorities or influential individuals who control the process
- Where a potential partner can source or facilitate funding
- Where a potential partner is willing to provide a substantial portion of the required equity or guarantees
- Where the prevailing laws require a partnership with local entities or individuals
- Where there is a need for a local partner with a better understanding of the local environment (e.g. politics, lenders, market expectations, project consultants etc.) when entering into a new geographic market
- To exploit an opportunity that has execution time constraints or a narrow window of opportunity that can only be enjoyed by enlisting a joint venture partner

Choosing the right legal vehicle

The choice of structure is usually driven by issues such as tax and regulations as well as ease of transacting. Depending on a variety of factors, the joint venture partners may opt to either use a contractual agreement to govern their relationship while retaining their independent status or use a joint venture vehicle.

Contractual development agreements

If the landowner prefers to pay the developer a fee for its development expertise, a contractual agreement would suffice so long as it clearly sets out the obligations of the developer in procuring the development in return for its fees. Contractual development agreements are quick to set up and easy to dissolve due to the fact that there is no separate legal entity. Joint venture parties retain ownership of their own assets and they are not usually liable for the debts of the other joint venture party but they may share liability on specific third party contracts. Each party will be taxed directly on its share of the profits and losses of the venture.

However, it may be difficult to raise external financing because there is no legal entity. There is also the risk of the joint venture being considered a partnership, which will trigger unlimited joint and several liability, making all parties liable for the losses of the venture.

Joint venture vehicles

Due to the disadvantages and risks of contractual agreements, the joint venture partners may opt to use any of the many joint venture vehicles which typically take the form of limited companies, partnerships or limited liability partnerships (**LLPs**). Also, if there are a number of parties who come together to purchase a series of developments, it may be best to use an incorporated joint venture to simplify matters such as acquisitions of property and dealings with third parties, including financiers and contractors.

Most real estate development joint ventures will be formed as limited liability companies (**LLCs**). LLCs offer the benefits of limited liability to all partners, simplicity in formation and a straight-forward management scheme. In Kenya, LLCs are governed by the Companies Act, 2015. An LLC can hold its own assets and arrange its own financing. Share structures can be flexible with preference shares allowing for priority returns to members. On the contrary, the accounting obligations of LLCs may impose onerous obligations on members and directors. Moreover, LLCs are taxed on profits before distribution to shareholders who also pay tax, so there is a risk that profits may be double taxed.

General and limited partnerships offer flexibility because they are governed by an agreement between the members and are not restrained by a rigid legislative regime. Moreover, they offer fiscal transparency in that the individual joint venture partners are taxed directly and the partnership is not taxed on its profits. However, general partnerships are not suitable for commercial joint ventures because each joint venture party has unlimited liability. In a limited partnership, the general manager manages the joint venture and has unlimited liability while the limited partners have limited liability but they are not allowed to take part in the day to day management of the partnership. Furthermore, these structures make it difficult to raise external financing because the entity lacks a separate legal identity and does not own any assets. Moreover, any change in identity of the joint venture parties would give rise to a new partnership arrangement and additional costs.

LLPs are regulated by the Limited Liability Partnerships Act, 2011 and have a number of advantages including tax transparency, limited liability and flexibility. Each joint venture party is taxed directly on its share of the profits and losses of the venture and the LLP is not taxed on its profits. LLPs also create a separate legal entity and offer members limited liability.

The joint venture agreement

A thoroughly considered and well-drafted joint venture agreement is a definite step towards all parties achieving their mutual and independent aspirations. Joint venture agreements are usually intensively negotiated to address the needs of the particular development project. Below are some of the salient features of a joint venture agreement.

Initial contributions and future capital needs

If one party is contributing in kind, such as providing land or professional skills, a value will need to be attributed to these contributions in order to determine the parties' respective contributions. It is also not unusual for real estate developments to require more capital than initially budgeted and failure to contribute may trigger defaults for non-payments under major project contracts. The joint venture agreement should therefore state which members are entitled to require a capital call and the consequences of a member failing to provide the additional capital.

LLCs offer the benefits of limited liability to all partners, simplicity in formation and a straight-forward management scheme.

Joint venture agreements will typically include a mandatory notification process to give the non-contributing party an opportunity to contribute. Possible consequences after the defaulting party is notified could be as follows:

- The other joint venture parties may contribute additional cash instead of the defaulter in return for more equity, resulting in the dilution of the defaulter's interest
- The other joint venture parties may make a loan to the joint venture on preferential terms, often combined with a suspension of the defaulter's voting rights
- The other joint venture parties may exercise their right to buy-out the defaulter at a preferential price

Distribution of profits

The provisions governing distributions are the most critical part of any joint venture agreement. The timing and priority of cash distributions need to be clearly understood by the partners and clearly expressed, preferably with examples to avoid the possibility of future misunderstandings. It is also useful to agree on a formula as regards distributions, subject always to change by the partners.

Real estate joint ventures usually establish a series of thresholds or waterfalls that provide a set percentage return to each member based on their capital contributions. However, if the developer makes an actual cash contribution, the developer's return should match the investor partner's return on a pro rata basis.

Once those returns have been obtained, there is often a "promote" return to the developer, which is very often subordinated to the investor partner's return. Promoters are often back-loaded by the investor partner to create a financial incentive for the developer to create and manage an asset in a manner that will maximise long term value. The split between the investor partner and the developer might initially be 80%/20%. However, if a minimum return is achieved by the investor partner, for instance 15%, the developer's share may be increased to 30% if the actual return is in fact between 15% and 20%. But if the actual return exceeds 20%, then the split might be further increased (promoted) in favour of the developer.

In joint ventures where the investor partner has multiple deals with the developer, the investor partner may want to reduce its risk by "pooling" deals and having individual deals subject to a "claw-back" whereby the profits on one deal in the pool can be redirected to offset the investor partner's losses on another deal in the pool.

Management responsibility

Decision-making powers should be based on the levels of shareholding or the agreement may grant the investor partner more powers. Out of fairness, however, it is recommended that no party has more voting powers than their respective shareholding. Day to day management issues can be delegated to the project manager or architect and major decisions can be taken by the stakeholders during monthly or quarterly review meetings.

The joint venture agreement should include a set of major decisions for which the investor partner's consent is required, including admission of new members, reinvestment of proceeds, refinancing and approval of budgets. In practice, many management issues can be avoided by simply requiring the investor partner's approval of construction and annual operating budgets while prohibiting the developer's incurrence of fees in excess of approved budgets. The agreement should also prohibit payment of fees to members or their affiliates that are not approved by the other members.

In most joint ventures, the developer is also the managing partner. However, once the project is completed and the construction loan guarantees are released, it is the investor partner that carries the most risk of loss. The agreement should therefore define the circumstances in which the investor partner may remove the developer as manager and take over management responsibilities without the developer's consent, including the power to sell, refinance and approve budgets.

Exit mechanism

The joint venture agreement should make provision for the termination of the joint venture and/or the exit of one partner from the joint venture. The agreement should specify the types of events that will trigger a dissolution or a buy-out of the defaulting party's interest by the non-defaulting partner.

When one of the joint venture partners wishes to exit the joint venture, the joint venture agreement will often provide for a buy/sell option where a member can set a price at which it will either sell its interest or buy the other member's interest. A neutral appraiser can be used to evaluate the leaving member's fair share of the business if the parties are unable to agree. From the outset, the parties should have an input on the identity of the valuer appointed for this purpose and applicable assumptions will also need to be considered and should be set out in the schedule to the joint venture agreement. Another option is to allow either member to offer the property for sale to third parties. If one party approves an offer that the other member does not, the non-approving member must either acquire the approving member' interest or sell its interest to the approving member using the valuation method established through the third party bid process.

Dispute resolution

The joint venture agreement should provide for either arbitration or mediation, establish the jurisdiction, applicable law and the venue or forum for resolving disputes. The agreement should also provide for a practical means of resolving minor disputes to avoid breakdowns in trust, which can ultimately lead to the dissolution of the joint venture.

Conclusion

It is interesting how limited access to financing has presented real estate developers and investors with opportunities to work together and share risk and rewards through joint ventures. Joint ventures have proven to be an excellent way to combine the complementary strengths of a developer and an investor in real estate developments as well as a means for the partners to achieve their mutual and independent aspirations. As discussed above, the joint venture's success will depend not only on the adequacy of capital contributions, but also on careful structuring of the joint venture and preparation of the agreement that will govern the relationship of the parties in an often risky enterprise. However, this cannot fully substitute for careful due diligence regarding the project and the prospective joint venture partner. It is highly advisable that the partners undertake a feasibility study before embarking on a real estate development project. The study will reveal critical benchmarks for the project's success, including return on investment, target market and land value ratio to the total project cost. Additionally, the feasibility study will reveal available infrastructure such as sewer lines and any zoning laws that will determine the type of concept to adopt.

Juliet C. Mazera
Consultant | juliet@oraro.co.ke

Cindy Oraro
Senior Associate | cindy@oraro.co.ke

"MORE POWER" TO INVESTORS

KENYA'S PROMISING RENEWABLE ENERGY MARKET

No doubt, Kenya offers one of the fastest growing and dynamic markets for renewable energy in Africa. In 2015, the Climatescope Index ranked Kenya 6th out of 55 countries that invest in the generation of renewable energy. The country's renewable energy flagship projects include the Lake Turkana Wind Power Project which aims to provide 310 MW of reliable, low cost windpower to the Kenyan grid. This is equivalent to approximately 20% of the current installed electricity generating capacity. As the single largest private investment in Kenya, the Project will replace the need for Kenya to spend approximately KES13.7 billion (USD 135 million) per year on importing fuel for electricity generation. Construction of the power plant commenced on 25th October, 2014. 50 MW to 90 MW of capacity will be ready for commissioning in September 2016. It is notable that when fully operational in April 2017, the windfarm will be the single largest one of its kind in Africa.

Smaller windpower projects such as a 90 MW windpower project in Mpeketoni, Lamu County have been proposed. Regulatory approvals have been granted for this KES 20 billion (approximately USD 200 million) project sponsored by Electrawinds, a Belgian company, in partnership with International Finance Corporation and a Kenyan company, Kenwind Company Holdings.

In Kajiado County, the Kipeto windpower project is set to generate 100 MW of electricity. The project results from one of the most substantial United States

The country's renewable energy flagship projects include the Lake Turkana Wind Power Project which aims to provide 310 MW of reliable, low cost windpower to the Kenyan grid.

foreign direct investments in Kenya. A Chinese firm was recently contracted to construct the plant at the cost of KES 22.6 billion (approximately USD 223 million). The construction phase has been estimated to be two (2) years.

In addition, SkyPower, the developer and owner of various utility-scale solar photovoltaic energy projects, signed an agreement in July 2015 with the Ministry of Energy and Petroleum for the development of 1 GW of world-class solar projects to be built in four phases in Kenya over the next five (5) years.

Centum Investments, a Kenyan investment company, together with three other foreign firms have also sponsored the construction of the 140 MW Akiira geothermal power plant at a projected cost of KES 30 billion (approximately USD 296 million). The project will be developed in two phases; it is estimated that 70 MW will be connected to the national grid.

The legal and policy framework

The above projects have been facilitated by Kenya's extensive regulatory framework which supports the growth of Kenya's renewable energy sector.

The Energy Act, 2006 defines renewable energy to mean "all non-fossil sources including but not limited to biomass, geothermal, small hydropower, solar, wind, sewage treatment and plant gas".

The Sessional Paper No. 4 of 2004 on Energy, which is the foundational document for energy liberalisation in Kenya, provides for the government to undertake pre-feasibility and feasibility studies on the potential for renewable energy sources and for the packaging and dissemination of information on renewable energy sources to create investor and consumer awareness on the economic potential offered by renewable sources of energy.

The Energy Act, establishes the Energy Regulatory Commission (**ERC**). The ERC's key functions include the regulation of production, distribution, supply and use of renewable and other forms of energy. The ambit of its functions covers the protection of interests of consumers, investors and other stakeholder interests. To compound this, the Energy Act obligates the Cabinet Secretary to promote the development and use of renewable energy technologies.

Government policy on feed-in-tariffs

In a bid to attract private investment into the renewable energy sector, the Government issued a policy on renewable energy feed-in-tariffs in 2008. The feed-in-tariffs were originally introduced for electricity generated from wind, biomass and small hydropower sources but after revision in 2010, they also provide support to geothermal and biogas sources as well as solar electricity generation. A feed-in-tariff as described in the policy is an instrument that allows power producers to sell renewable energy-generated electricity to an off-taker (the buyer of electrical energy for the purpose of selling the electricity to customers connected to the national or mini-grid systems) at a pre-determined tariff for a given period of time.

The objectives of the feed-in-tariffs system as outlined in the policy are: to facilitate resource mobilisation by providing investment security and market stability for investors in electricity generation from renewable energy sources; reduce transaction costs, administrative costs and delays associated with the conventional procurement processes. Another objective is to finally encourage private investors to operate their power plants prudently and efficiently so as to maximise returns.

The policy provides that small renewable energy projects with a capacity of up to 10 MW shall have a standardised power purchase agreement which shall incorporate certain features such as no bidding for renewable sites and resources. Feed-in-tariff values for small renewable projects are provided in the policy which further outlines principles that underline the calculation of the said values which include as stated in Section 25, a calculation on a technology-specific basis using the principle of cost plus reasonable investor return.

The policy further provides that renewable energy projects which are larger than 10 MW of installed capacity shall meet load flow or dispatch and system stability requirements. The policy gives the feed-in-tariffs for each of the renewable energy sources it covers and one of the common features is that the feed-in-tariff is to apply for twenty (20) years from the date of the first commissioning of the respective power plants.

The developer is to bear the costs of interconnection including the costs of construction, upgrading of transmission lines, substations and associated equipment. The off-taker is to recover from electricity consumers 70% of the portion of the feed-in tariff, except for solar plants connected to off-grid systems, where the off-taker recovers 85%. Finally, the policy provides that renewable energy generators feeding into the grid will require a power purchase agreement and further that the project sponsor for such renewable generation projects must be an entity legally registered in Kenya.

The promulgation of the Constitution of Kenya, 2010 changed the governance structure of the country by creating a decentralised system of government with functions that were formerly exercised by the National Government being devolved to Counties. The roles of the National and County Governments in relation to energy have been clarified and hence this necessitated the review of the energy sector framework which led to the Draft National Energy and Petroleum Policy, 2015 as well as the Energy Bill, 2015 (**the Energy Bill**).

The Energy Bill

The preamble of the Energy Bill provides that it aims to achieve among other things the promotion of renewable energy. The Energy Bill describes obligations of the National Government and the Cabinet Secretary is mandated to develop a conducive environment for the promotion of investments in energy infrastructure development. The Energy Bill further provides that the National and County Governments shall, in their effort to promote energy investments, facilitate the acquisition of land for energy infrastructure development in accordance with the law.

The Energy Bill establishes the Energy Regulatory Authority whose functions shall be to regulate the production, distribution, supply and use of renewable and other forms of energy as well as to protect the interests of consumer, investor and other stakeholder interests.

The Energy Bill additionally establishes the Rural Electrification and Renewable Energy Corporation, whose functions shall include undertaking feasibility studies and maintaining data with a view to availing it to developers of renewable energy resources. Also to develop and promote the use of renewable energy and technologies.

The Energy Bill also establishes an inter-Ministerial Committee known as the Renewable Energy Resource Advisory Committee. This Committee is charged with the task of advising the Cabinet Secretary on amongst other things, the criteria for allocation of renewable energy resources, licensing of renewable energy resource areas, management of water towers, water catchments and management (and development) of renewable resources e.g. multi-purpose dams and reservoirs.

Lastly, the Energy Bill establishes a renewable energy feed-in-tariff system with the objective of catalysing the generation of electricity through renewable energy sources and encouraging locally distributed generation, thereby reducing demand on the network and technical losses associated with transmission and distribution of electricity over long distances, among other objectives.

Conclusion

Although Kenya has attracted notable large scale energy projects and has sought to streamline the regulation of its renewable energy sector, the country's renewable energy potential remains largely untapped. This could be attributed to amongst others, a focus on large scale energy projects. Efficient licensing procedures and the ease of access to information on the same would therefore bolster the growth of smaller scale renewable energy projects in Kenya.

Noella Lubano
Partner | noella@oraro.co.ke

Patricia Ouma
Associate | patricia@oraro.co.ke

TESTING THE SAFETY NET IN BANKING

IS DEPOSIT INSURANCE ADEQUATE?

Recent events in the banking industry in Kenya have caused the Central Bank of Kenya (**CBK**) and other financial regulatory bodies to pause and rethink the current approach towards the regulation of the banking sector. Presently, the main issues facing Kenya's banking industry are excessive insider lending, non-performing loans, inadequate or non-existent credit documentation and securities, liquidity problems and the poor management of banks (and other financial institutions). These issues have in some cases proved to be sure recipes for highly-publicized scandals or the downright collapse of the financial institutions involved.

Of utmost concern obviously is the impact that the collapse of several financial institutions has had on their depositors, bondholders, creditors and customers. Serious questions have been raised regarding the adequacy of the measures put in place for the protection of their deposits in the form of deposit insurance or otherwise. Indeed, anyone affected by the failure or collapse of a bank or financial institution should take a keen interest in the role that deposit insurance plays in such a situation.

Deposit insurance is a mechanism that has evolved over time to provide protection to depositors of commercial banks or deposit-taking entities, in the event of failure of the institution. It is also intended to play a critical role in contributing to the stability of the financial system of a country and in fostering economic development while encouraging savings.

The Deposit Insurance Fund

Kenya has in place the Deposit Insurance Fund (**the Fund**) which provides insurance protection to depositors against potential loss of their deposits in the event of failure of a member financial institution. The Fund is managed by the Kenya Deposit Insurance Corporation (**KDIC**), which was established under the Kenya Deposit Insurance Act, 2012 (**the Act**). Membership is compulsory for all institutions licensed to carry on deposit taking business such as commercial banks, financial institutions, mortgage finance companies, building societies and micro finance institutions.

The Banking Act (Cap. 488) also empowers CBK to intervene in the management of a bank or other financial institution by among other things, appointing KDIC to administer or liquidate any institution if it is established that its assets are less than its liabilities to its creditors.

KDIC is both publicly and privately funded. It is autonomous in its operations and not subject to the control, direction or supervision of any other entity in the exercise of its rights, powers, and privileges. However, any party aggrieved by the exercise of those powers may apply to the High Court for appropriate orders.

Degree of Protection

As stated above, one of the functions of KDIC is to provide and manage a deposit insurance scheme for depositors. However, the degree of protection provided to depositors and customers of collapsed financial institutions in

Kenya is fairly low in comparison to that provided by other countries. KDIC offers limited coverage for deposits placed with an institution up to KES 100,000 (approximately USD 1,000) or such higher amount, as it may from time to time determine.

Furthermore, the Act provides that where a depositor owns more than one deposit account with an institution, the aggregate of those deposits is insured up to only KES 100,000 – hardly an incentive to keep a large deposit or have more than one deposit account in the same institution. Nonetheless, in recent months CBK has allowed depositors to withdraw up to KES 1 million (approximately USD 10,000) in situations where a bank or financial institution is placed under receivership. This has been a great relief to small depositors but it is disadvantageous to large ones whose deposits far exceed the maximum amount that can be claimed.

The deposit insurance scheme in other countries such as the United Kingdom and the United States of America is relatively advanced in terms of funding and coverage. For instance, in the US the Federal Deposit Insurance Corporation covers up to USD 250,000 (KES 25 million) depending on the type of account one holds with an institution. This amount is quite generous and lends credibility to the ultimate objective of deposit insurance. In the UK, quite apart from insuring deposits, the Financial Services Compensation Scheme extends the protection offered to insurance policies and insurance brokers. Furthermore, deposits are covered up to a maximum of GBP 75,000 (approximately USD 100,000)(KES 10 million). Naturally, this kind of protection comes at a price as it is commensurate to the high premiums levied on member institutions.

Interestingly, it has been argued that the deposit insurance system in the UK is unduly expensive and that it unfairly subsidizes poorly managed banks. It has also been argued that deposit insurance undermines market discipline. The rationale being that as a result of having such an insurance scheme in place, financial institutions tend to take undue risks while customers take little or no interest in the way these institutions are being run.

In Kenya, despite the relatively low level of protection offered, unscrupulous financial institutions do not seem to shy away from taking very high (and in certain cases illegal) risks with depositors' funds. Such unrestrained risk-taking, coupled with depositors' disinterest, ignorance or blind trust in financial institutions ultimately leads to their imminent failure or collapse.

The Banking Act (Cap. 488) also empowers the CBK to intervene in the management of a bank or other financial institution.

Ideally, deposit insurance should reduce the risk of a bank run based on the premise that depositors who are assured that the insurer will reimburse their deposits in the event of a bank failure, are less inclined to withdraw their deposits in the event of an institution's insolvency.

Need for Reforms

While the country is experiencing a number of long-awaited reforms in the banking sector, more focus should be directed towards the reform of the existing deposit insurance legislation. The current approach to banking in Kenya is reactionary as opposed to pre-emptive, with protective measures being adopted after the event of a collapse, failure or liquidation of a financial institution, often being a case of too little, too late. In the absence of a significant increase in deposit insurance coverage which is aligned with the current inflation rate, it is doubtful whether the objectives of the scheme will ever be achieved.

The Act provides that premiums are limited to a maximum of 0.4 per cent of the average of a members total deposit liabilities in a twelve (12) month period prior to assessment. This percentage needs to be adjusted upwards for the deposit insurance to be of any relevance and coverage of deposits should also be increased, so as to be in tune with changing economic times.

Such reforms will serve the country better in terms of enabling KDIC to fulfill its deposit insurance mandate, as well as enhancing confidence and, in turn, stability in the financial system. Indeed, President Franklin D. Roosevelt aptly remarked while exhorting citizens to remain calm and avoid making the panicked withdrawals, which had crippled America's banking system in 1933:

"After all, there is an element in the readjustment of our financial system more important than currency, more important than gold, and that is the confidence of the people."

Noella Lubano
Partner | noella@oraro.co.ke

AT A GLOBAL LEVEL

THE CASE FOR INTERNATIONAL ARBITRATION

The rise in cross-border transactions in recent years has brought with it a need for the parties involved, (many of whom are nationals of different states), to have an established method of resolving any disputes that may arise, in a manner that is quick, efficient and constructive. This trend, coupled with the parties' common preference to settle matters privately and somewhat amicably in the hopes of maintaining a working business relationship has spurred the move towards international arbitration.

In a nutshell, international arbitration is an alternative form of dispute resolution usually involving parties from different states. The parties must have in place an agreement, either by way of an arbitration clause in the contract, or as a separate arbitration agreement, to have their disputes determined by an impartial arbitral tribunal. The decision of the tribunal will be binding on both parties and the award is enforceable in any of the one hundred and fifty six (156) countries that are signatories to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the New York Convention. The New York Convention, requires courts of contracting states to give effect to private agreements to arbitrate and to recognise and enforce arbitration awards made in other contracting states.

Neutrality

There are several benefits to parties choosing international arbitration over litigation. Firstly, international arbitration provides a neutral forum for dispute resolution and safeguards one party from having to submit to the jurisdiction of the other party's national courts. This is aimed at reducing or eliminating any occasions of bias. In addition, if the parties agree to have the arbitral tribunal composed of three arbitrators, as a general rule no more than one of the arbitrators may be of the same nationality as each of the parties. However, in the unlikely case where two of the arbitrators are of the same nationality as the parties to the dispute, the third arbitrator will be from a neutral nationality.

Expertise

Another benefit that international arbitration has over litigation, is that the parties can select the arbitrators for their experience and familiarity with the area of law which forms the subject matter of the dispute. This is unlike litigation, where the parties may find themselves before a judge with little or no knowledge of the relevant commercial practices, trade usages and international legal structures underpinning the parties' agreement. Whereas the Kenyan Court system has specialised tribunals and courts such as the Employment & Labour Relations Court and the Environment & Land Court which are manned by judges with specialist knowledge of the relevant law, parties may still find that the judges have no prior experience handling disputes involving complex comparative law issues. International arbitration therefore offers an added assurance that can only be obtained by personally selecting arbitrators based on their expertise and ability to deal with issues requiring the application of different national laws. Furthermore, the selected arbitrator need not be a lawyer and may hold any other specialised or professional qualifications such as accounting, engineering, architecture among others.

Control

International arbitration is a more flexible approach to dispute resolution than litigation. Unlike in litigation where the parties have very little say or sway over the procedure, the parties to arbitration can shape the dispute resolution process by selecting among other things the governing law for the arbitration, the place of arbitration, the arbitrators who shall form the arbitral tribunal and various other aspects of the arbitral procedure. However, the amount of flexibility the parties have in the process is affected by their decision to select institutional arbitration, or opt for the ad hoc approach. In the case of institutional arbitration, the parties choose to rely on the arbitration rules administered by a particular institution. Alternatively, the ad hoc approach enables the parties to draft a custom-made arbitration procedure for the contract.

Confidentiality

Whereas court proceedings are usually made public, it is often assumed that international arbitration provides a confidential alternative form of dispute resolution, as both the procedure and outcome tend to be private with the details known only by the arbitrators and the parties. However, this is not something that should be taken for granted. This implied confidentiality is not universally applied; therefore, if the parties wish for the arbitration proceedings to be confidential, there must be an explicit confidentiality clause contained in the arbitration agreement.

Finality

One of the main reasons why international arbitration is considered to be more attractive than litigation is because an arbitral award is final and binding. While the court system provides the unsuccessful party with a right of appeal or the right to have the decision reviewed, depending on the jurisdiction which the arbitration is subject to, there is normally a very limited right of appeal where

arbitral awards are concerned. This finality prevents further delay in resolving the dispute, thus saving the parties' time, in addition to the costs of an appeal procedure.

Enforceability

An arbitral award can be enforced in foreign courts more easily and consistently than court judgments owing to the New York Convention. Under the Convention, the court of a signatory country is obligated to enforce an arbitral award, save for limited circumstances. The international enforceability of an arbitral award therefore provides significant comfort to parties, as they are assured that the award can be enforced in any foreign country which is a signatory to the Convention. To this end, it would be prudent for a party seeking to rely on the international enforceability of an arbitral award, to check that the party with which it is entering into an arbitration agreement is a national of and holds assets in a country which is a signatory to the Convention.

Conclusion

In closing, in order for a dispute to become the subject of international arbitration, the party wishing to refer the matter to the arbitral tribunal must first show that there exists a binding international arbitration agreement between the parties to the dispute. For an international arbitration agreement to be binding it must be in writing, whether as an arbitration clause in the main body of the contract, or as a separate arbitration agreement. The agreement must also be signed by the parties, as it is only parties who have signed the agreement that may be bound by it. Further, the signatory to the agreement must be a person who is authorised to bind the company in an international arbitration agreement and the company itself must also have capacity to enter into such an agreement.

In addition to the above considerations there are several key things that must go into the international arbitration clause. First and foremost, the parties must agree which disputes arising between them will be subject to arbitration. In this regard, it is important that the arbitration clause is drafted as widely as possible so as to increase the scope of issues that may be referred to arbitration. It is also useful to draft a carefully worded escalation clause in the agreement, so as to clearly outline at what point a dispute may be subjected to arbitration. The parties must also select the number of arbitrators that will make up the arbitral tribunal. The parties generally have free reign on the number, provided that it is an odd number so as to provide a tiebreaker for the tribunal's decision. Three (3) is usually the recommended number.

Other details which must go into the arbitration agreement include the language of the arbitration, the place or seat of the arbitration, the governing law of the arbitration agreement (which may be different to the governing law of the contract between the parties), the parties' choice of institutional or ad hoc arbitration and a confidentiality clause.

Whereas court proceedings are usually made public, it is often assumed that international arbitration provides a confidential alternative form of dispute resolution.


Walter Amoko
Partner | wamoko@oraro.co.ke


Jackson Awele
Senior Associate | awele@oraro.co.ke

A MATTER OF "COMPETING" PRINCIPLES

CONFIDENTIALITY AND DISCLOSURE IN PPP PROCUREMENT

Even though public-private partnership (**PPP**) projects are increasingly widespread across the world, it is only now that they are beginning to gain traction in Kenya. However, the efficacy of PPPs as a new investment phenomena in Kenya (like most developing countries) is virtually untested.

More importantly, despite the passage of relevant legislation to facilitate PPPs for public investment, the principles and practices that underpin the attitudes of PPPs' implementation remain largely undeveloped. There is still a lot of ambiguity and weaknesses in the interpretation and implementation of key provisions of the law that are critical to the realisation of the true objectives of PPPs for achievement of the maximum public benefit from such projects.

This is particularly true in Kenya where the Public Private Partnerships Act, (**PPP Act**) was only enacted in 2013. Though prior to the enactment of the said Act, a number of national projects were developed using the PPP approach, such projects were under-regulated and provisions were largely tucked into the Public Procurement and Disposal Act (Cap.412C(as amended)). As such, some projects were successful while some failed for varied reasons, including the lack of proper controls and poor regulation of for instance, the tendering processes. Successes include the Mtwapa and Nyali Bridges Concessions, the 74 MW Tsavo/Kipevu IPP, 2000, Orpower-Olkaria III 2000/2008 (48 MW Geothermal Plant), Mumias (34 MW power plant) and the Port of Mombasa Grain Terminal – BOO, 1998. One notable failure is the Nairobi Urban Toll Road, 2009.

Kenya now has a substantive Act of Parliament that governs the entire PPP process from project conception to hand over and establishes the relevant institutions such as the PPP Committee, the PPP Unit and the PPP Petition Committee (**the Petition Committee**) to oversee PPP projects from conception to execution and finally completion. So far, a number of independent power production projects are ongoing under the new legislation and a number of projects have been identified and approved by the Cabinet to be implemented under the new PPP framework. The current list of pipeline projects includes fifty nine (59) projects from different sectors of the economy.

Nonetheless and perhaps owing to the nascent state of the PPP Act, the underlying principles and values that ought to govern the critical tendering processes of PPPs and to ensure competitive, fair and transparent private investment under the framework remain largely undeveloped. Key among them being the proper balance between the need for transparency and accountability vis-à-vis the protection of commercially sensitive information

relating to the tendering process, all of which are aimed at protecting the integrity of the entire process.

Confidentiality is Essential

One of the fundamentals of any PPP process is confidentiality of information exchanged between the contracting authority and bidders. The underlying theory on the need for confidentiality is for the protection of commercially sensitive information which, if disclosed to the public, may harm the financial position of the Government or of a competitive bidder. Confidentiality is also required to ensure that none of the bidders abuse the system by knowing the contents of the bids submitted by the others and thus compromising the competitive process.

But so is Transparency

However, of equally fundamental importance to ensure integrity and competitiveness of the process is transparency, fairness and accountability through the entire process. The PPP Act and regulations plainly espouse these fundamentals both during and after tender evaluation and award. Notably, Regulation 40(5) of the Public Private Partnerships Regulations, 2014 requires that, "the proposal evaluation team shall preserve the confidentiality of a tender evaluation process and shall not be influenced or directed by any person regarding the evaluation of a proposal except in accordance with the Act and these Regulations." Section 29 on the other hand, requires that, "unless otherwise provided under the Act, all projects shall be procured through a competitive bidding process and that in procuring and awarding a contract to a private party under the Act, a contracting authority shall be guided by the principles of transparency, free and fair competition and equal opportunity in accordance with the guidelines made under this Act."

A Balancing Act

These two fundamentals require careful balance as it is almost impossible to achieve transparency and accountability without information. Still, unless the flow of information is checked, particularly at the stage of pre-award and execution of the tender agreement, commercially sensitive information may

The efficacy of PPPs as a new investment phenomena in Kenya (like most developing countries) is virtually untested.

be jeopardised both for the bidders and the Government. This may thereby put to question the competitiveness of the entire process with serious ramifications on value for public funds. In this regard, the Petition Committee, which was established to adjudicate challenges relating to a PPP process, plays a major role. Unfortunately, in the initial challenges brought before the Petition Committee in which the issue of disclosure arose, it adopted a very narrow understanding of its powers, rejecting applications by aggrieved parties to compel disclosure of relevant information relating to the evaluation process by contracting authorities. The Petition Committee held that it had no jurisdiction to do so, a holding that wholly undermined its ability to review impugned decisions of contracting authorities. This seemingly, elevated confidentiality over transparency and accountability with the resulting twin effects of considerably limiting the rights of parties challenging evaluation outcomes to fair hearing and compromising the competitiveness of PPP tender awards.

The APM Terminals Case

The above position has now been put right by the High Court in Republic vs. Public Private Partnerships Petition Committee & 3 Others ex Parte APM Terminals (2015) eKLR (**the APM Terminals Case**). As appreciated by the High Court (Korir J.) in that case, the Petition Committee's jurisdiction was focused and specialised for the development of jurisprudence on PPP matters. It goes without saying therefore that its decisions, especially at the nascent stage of the PPP Act, are bound to play a crucial role in developing the PPP procurement regime in the country, in the same fashion as other monitoring mechanisms provided for in law. It is therefore crucial that it grasps these principles and develops the same to the highest standards possible.

Confidentiality of commercial information if over protected would obviously threaten the integrity of PPPs and foster a lack of trust, unfair competition and unaccountability. The need to strike a balance between the two is therefore critical and more so in circumstances where, as per the court in the APM Terminal case, 'shenanigans' in public procurement have been known to cost taxpayers value for money in public projects'. Therefore, confidentiality and/or technical rules for the same should not be used by parties or condoned by the Petition Committee as a shield, when questions are raised on hideous decisions and/or actions of the contracting authority and/or any other person involved in the process. Transparency and accountability is nothing without information.

A matter of merits

Yet disclosure cannot and should not be a remedy in all instances. Each situation must be considered on its own merits and disclosure ordered only in deserving circumstances and within regulated parameters, so as to assure protection of commercially sensitive data. Establishing a threshold for the same is therefore critical. The Court in the APM Terminals case has set the ball rolling in that regard and has established sound principles that can be built on, going forward. The said principles re-affirm the fundamentals of fairness, transparency and accountability in PPPs and shall hopefully assist the Petition Committee, private investors and the contracting authority in making decisions on disclosure rights and obligations while ensuring confidentiality and integrity of commercially sensitive information.

The Court crystallised the principles to be considered in balancing the twin confidentiality and disclosure obligations in PPP Procurement thus;

- Where a losing bidder desires disclosure, the application should be made without delay at the time of filing the petition or complaint. The request should be accompanied by the reasons for the application for the disclosure and the specific information required to be disclosed
- A request for disclosure before the Petition Committee is not of the nature under Article 35 of the Constitution. It is for the protection of the right to fair administrative process and fair hearing as provided by Articles 47 and 50(1) of the Constitution
- Statutory administrative procedures such as those before the Petition Committee can be augmented with common law rules whenever it appears necessary to promote fair hearings. Where it would be in the interests of justice to allow discovery, an administrative tribunal should do so even where its rules do not expressly provide for discovery. The main point to consider is whether denial of discovery would result in denial of justice to a party
- In order for contracting authorities to embrace fairness, transparency, competitiveness, equity and cost-effectiveness in public procurement, the Petition Committee must stress this message by giving decisions that encourage and support these principles. A decision that goes against these principles is a decision against public policy
- The requirement for confidentiality is only found in the Public Private Partnerships Regulations, 2013 which limits confidentiality to the proposal evaluation team. That provision does not apply to the Petition Committee or mainstream courts and both are therefore not bound by the same. They have the power to order disclosure of information relating to PPP evaluations on application
- As is the case in the European Union, contracting authorities are under an obligation to disclose substantial information concerning other tenderers' offers (notably, at least the winning tenderer) to all participating tenderers and/or disappointed bidders in order to allow them to effectively challenge award decisions. This obligation is sufficiently discharged only when the contracting authority provides very detailed information about the tender evaluation process and, in particular, gives information that enables the disappointed tenderer to perform a relative comparison of its offer vis-à-vis the tender of the winning bidder

The underlying theory on the need for confidentiality is for the protection of commercially sensitive information which if disclosed to the public, may harm the financial position of the parties.

- An unsuccessful tenderer who wishes to challenge the evaluation process is in a uniquely difficult position. He knows that he has lost, but the reasons for his failure are within the peculiar knowledge of the public authority. In general terms therefore and always subject to issues of proportionality and confidentiality, the challenger ought to be provided promptly with the essential information and documentation relating to the evaluation process actually carried out, so that an informed view can be taken of its fairness and legality
- Due to the short time limits imposed by the Regulations on those who wish to challenge the award of public contracts, the start of the relevant period is triggered by the knowledge which the claimant has (or should have) of the potential infringement
- However, the Court must always consider applications for specific disclosure in procurement cases on their individual merits. In particular, a clear distinction may often be made between those cases where a *prima facie* case has been made out by the claimant (but further information or documentation is required), and those cases where the unsuccessful tenderer is aggrieved at the result but appears to have little or no grounds for disputing it
- Any request for specific disclosure must be tightly drawn and properly focused. The information/documentation likely to be the subject of a successful application for early specific disclosure in procurement cases is that which demonstrates how the evaluation was actually performed, and therefore why the claiming party lost. Other material, even if caught by the test of standard disclosure, is unlikely to be so fundamental that it should form the subject of a separate and early disclosure exercise
- Ultimately, applications for disclosure must be decided by balancing, on the one hand, the claiming party's lack of knowledge of what actually happened (and thus the importance of the prompt provision of all relevant information and documentation relating to that process) with, on the other, the need to guard against such an application being used simply as a fishing exercise, designed to shore up a weak claim, which will put the defendant to needless and unnecessary cost
- It is only such disclosure which will assure those who participate in public tenders that the tender process is above board

As aptly stated by the Court in the APM Terminals Case, there should be nothing to hide and nothing to be ashamed of, where goods and services of good quality are being procured at the best prices in the market. Indeed, the only way to assure that is by jealously guarding the transparency of the procuring process.

Juliet C. Mazera
Consultant | juliet@oraro.co.ke

THE JURISDICTION QUESTION

A FOCUS ON ISLAMIC FINANCE

The growth of Islamic finance in Kenya inevitably means the beginning of Islamic finance disputes which will need to be adjudicated by the Kenyan judicial system. Seeing as Islamic finance contracts apply *Shari'ah* principles, there is a possibility that Kenyan courts would be reluctant to recognise the underlying nature of Islamic financial contracts. Even though Islamic finance contracts are yet to be challenged in Kenyan courts on the basis of jurisdiction and applicable law, incorporating Islamic finance within the Kenyan regulatory framework has already encountered some challenges based on Kenya's current legal environment. For example, the Banking Act, (Cap. 488) (**the Act**) prohibits banks from undertaking certain activities for which Islamic banks are primarily set up for, including trading and ownership of immovable property. This prohibition would affect an Islamic bank's products such as *murabaha* and diminishing *musharakah*, because in the case of a *murabaha*, an Islamic bank could be deemed to be trading in the goods being sold to the customer and in the case of a diminishing *musharakah*, an Islamic bank is required to own the property jointly with the customer.

All banks in Kenya are governed by the Act and are licensed by the Central Bank of Kenya whether they are conventional banks, fully fledged Islamic banks or banks offering Islamic banking products. The Cabinet Secretary in charge of Finance in Kenya has the power under the Act to exempt banking institutions from the provisions of certain sections of the Act, including those prohibiting banks from trading or owning immovable property. A bank intending to offer Islamic banking products like the *murabaha* and the diminishing *musharakah* may apply to the Cabinet Secretary in charge of Finance for exemption from the application of these provisions of the Act which could inhibit Islamic banking business.

Jurisdiction of the Kadhis' Court

Industry players foresee complications arising in the event that Kenyan civil courts are required to resolve disputes involving Islamic law, Muslim litigants and Islamic financial institutions. This is because Kenyan courts may have to overcome limitations on their ability to interpret religious laws imposed by the Constitution or other Kenyan laws in evaluating Islamic finance cases.

In addition, the Constitution provides that "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".

Further, the Kadhis' Courts Act, (Cap. 11) reiterates the provisions of the Constitution by providing that:

"A Kadhis' Court shall have and exercise the following jurisdiction; namely 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 effect of this section is twofold, in that the Kadhis' Court has jurisdiction only in the following instances:

(a) with regard to matters relating to personal status, marriage, divorce or inheritance; and
(b) where all the parties profess the Muslim religion and submit to jurisdiction of the Kadhis' Courts.

Therefore, based on the foregoing, the jurisdiction of the Kadhis' Court as provided for by the Constitution and the Kadhis' Courts Act does not extend to contractual relations.

Applicable law

The governing law clause specifies that the laws of a mutually agreed upon jurisdiction will govern the interpretation and enforcement of a contract. Islamic finance contracts usually make reference to *Shari'ah* with the intention of having Islamic legal principles applied in the interpretation of Islamic finance contracts. *Shari'ah* refers to all the laws of Islam's whole liturgical, ethical and jurisprudential systems. The Judicature Act (Cap. 8) states that the jurisdiction of the High Court, the Court of Appeal and of all subordinate courts shall be exercised in conformity with the Constitution, all other written laws, common law, the doctrines of equity, the statutes of general application in force in England on the 12th August, 1897 and African customary law. It is clear therefore, that the sources of Kenyan law do not recognise *Shari'ah* or Islamic finance law as forming part of the body of Kenyan law. It is therefore imperative that all documentation complies with applicable Kenyan statutes.

A conflict of law may arise especially where the choice of some form of Islamic law is incorporated into the terms of the contract whose outcome is inconsistent with that arising out of the application of the municipal laws of a country.

In the case of Islamic Investment Company of the Gulf (**IICG**) vs. Symphony Gems NV & Others, IICG entered into the *Murabaha* agreement with Symphony Gems which was subject to English law and the jurisdiction of English courts. The agreement further provided that the, "purchaser wishes to deal with the seller for the purposes of purchasing supplies under this agreement in accordance with Islamic *Shar'iah*". A dispute arose as to who took the risk of failing to deliver. Under Shari'ah, such a risk fell on IICG as it received a profit for accepting the risk. However, the contract provided for risk differently and the court held that the agreement was a contract governed by English law and that it simply had to be construed according to its terms as an English law contract.

> *A bank intending to offer Islamic banking products like the **murabaha** and the diminishing **musharakah** may apply to the Cabinet Secretary in charge of Finance for exemption from the application of these provisions of the Act which could inhibit Islamic banking business.*

In the case of Shamil Bank of Bahrain EC vs. Beximco Pharmaceuticals Ltd and others, the Court of Appeal in England was required to consider whether a particular *murabaha* contract was invalid under *Shari'ah*. The agreement in this case contained a choice of law clause which read, "subject to the principles of Glorious *Shari'ah*, this agreement shall be governed by and in accordance with the laws of England". The appellate court found this clause to be invalid on the basis that the 1980 Rome Convention on the Law Applicable to Contractual Obligations (**the Rome Convention**) allowed only one system of law to govern a contract. The Rome Convention further required that the chosen law had to be a law of a particular country, that is, a national law. Observers have argued that the appellate court in Shamil Bank made its own decision without reference to the commercial ends of a *murabaha* contract in Islamic finance and the intentions of the parties to the contract.

The Rome I Regulation governs the choice of law in the European Union and it replaced the Rome Convention. It, was adopted to harmonise the conflict of laws throughout Europe. The Rome I Regulation is different from the Rome Convention in that its thirteenth recital or preamble provides that "this Regulation does not preclude parties from incorporating by reference into their contract a non-State body of law or an international convention".

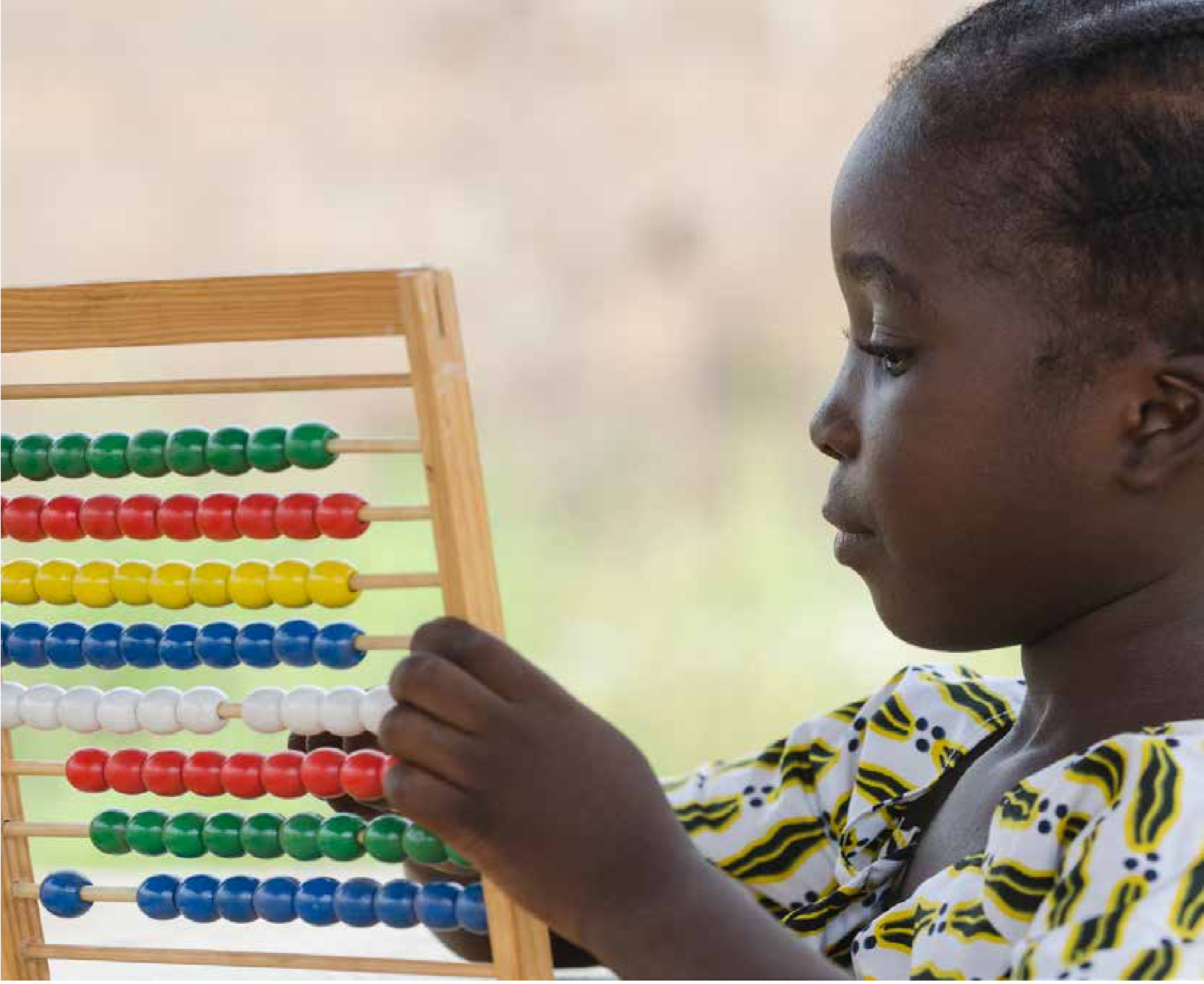
Consequently, it is left to speculation as to whether the appellate court in Shamil Bank would have reached a different conclusion, had the case been heard after the Rome I Regulation came into force.

Conclusion

In Kenya, the case still remains that a contract cannot be governed by two different systems of law. As such, parties would need to make provisions in the contract for a governing law clause making it clear what law is applicable. *Shari'ah* Advisory Boards require Islamic finance contracts to comply with the principles of *Shari'ah*. Where Islamic law is not the law of the land, then Islamic finance documents would need to be enforceable under conventional legal structures.

Unlike Malaysia which enacted the Islamic Financial Services Act, 2013, Kenya is yet to enact a separate or specific statute governing Islamic finance. Kenyan civil courts may therefore have to involve a *Shari'ah* or Islamic law expert to assist in adjudicating Islamic finance matters before the courts. There is an obvious need to have Islamic finance transactions comply with both *Shari'ah* and Kenyan law especially where a security needs to be registered in Kenya. A drafter of Islamic finance contracts would therefore need to strike the delicate balance between the national laws and Islamic finance law.

Finally, Kenya is a common law country and therefore the decision reached in Shamil Bank is likely to be adopted in a Kenyan Court. It however remains to be seen how the Kenyan Courts will rule when similar cases arise.




Nelly Gitau
Partner | nelly@oraro.co.ke


Daniel Okoth
Associate | daniel@oraro.co.ke

THE "RISE AND RISE" OF INVESTMENT MANAGEMENT FIRMS IN KENYA

A REGULATORY VIEW

The real estate sector has seen tremendous growth in the country thus attracting both corporate and individual investors. This growth has coincided with the increased demand for service industries incidental to real estate, among them the financial services offered by private equity firms. This has resulted in a rise in demand for investment managers (also referred to as fund managers) and financial analysts, both of whom have been pivotal in driving investment opportunities from the stock market/securities exchange into the real estate industry through private equity.

Investment Management Firms are a relatively new phenomenon in the Kenyan financial scene and have grown in popularity in recent years due to investors chasing for higher returns from sectors of the economy that tend to enjoy strong growth. In fact, at the end of 2015 it was reported that billions of shillings were raised in investing funds by a private equity firm just months after its inception, for the purpose of investment in the real estate sector. In October of the same year, another private equity firm launched Kenya's first Real Estate Investment Trust (**REIT**) which raised money to go towards the purchase of a mix of rental properties with the aim of earning high returns for the investors, a testament to the prevalence of the firms.

The Investment and Financial Analysts Act, 2015

The recent growth of Investment Management Firms has not surprisingly prompted the professionalisation and/or regulation of the sector. To this end, the Investment and Financial Analysts Act, 2015 (**the Act**) was passed into law on 11th August, 2015 with the commencement date set for 8th December, 2015. The purpose of the Act is to create a professional body that will set the standards of practice and regulate investment managers and financial analysts-the Institute of Certified Investment and Financial Analysts (**the Institute**).

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The Institute is established under Section 3 of the Act and designated with powers which include:

a) Promoting standards of professional competence and ethical practice amongst members of the Institute;
b) Advising the regulator for the time being responsible for capital markets, in respect of licensing of investment and financial analysts; and
c) Designing and administering an initial ethics and integrity test for the purpose of determining the professional suitability of all its members and subsequently designing and undertaking continuous development programmes for its members.

The effect of this is that there will now not only be a professional code of ethics, specifically for investment managers and financial analysts, but also a licensing procedure, in addition to continuous professional development programs. Prior to the Act, practice in this area was regulated by the Capital Markets Authority (**CMA**), albeit without a clear statutory framework. Thus, the creation of the professional body removes investment managers and financial analysts from the oversight of the CMA.

Council, Registration Committee and Disciplinary Committee

The Act further provides that the Institute shall be governed by the Council of the Institute, which is mandated to issue standards of professional practice including securities and investment standards, which shall form the basis of securities and investment practice for members of the Institute. With regards to the licensing procedure, the Act establishes a Registration Committee which is tasked with, among other things, considering and approving applications for registration of certified investment and financial analysts, granting practicing certificates and annual licences, monitoring compliance with quality assurance and where appropriate recommending to the Council that a member's conduct should be referred to the Disciplinary Committee for further inquiry.

Age Limit

Part III of the Act sets out the provisions on registration and practice as an investment manager and financial analyst. However, the part commences with a curious requirement for the Council to, by notice in the Gazette, fix the age which a person wishing to be so registered must have attained. The question that arises is whether the age requirement will infringe upon the right to equality and freedom from discrimination, as discrimination on any ground, including age, is expressly proscribed under Article 27(4) of the Constitution.

Chapter Six of the Constitution

Section 16 of the Act sets out the qualifications for registration, which include a certificate or document awarded by the Examination Board confirming that the applicant has passed the final certified investment and financial analysts' examination, and satisfaction of the requirements of Chapter Six of the Constitution on Leadership and Integrity. Section 16(3) further grants the Council discretion to require that a person seeking to be registered satisfies the Registration Committee that they have adequate knowledge of Kenyan law, including taxation law and the law governing financial markets. A person may be disqualified from registration under Section 17 of the Act if they have been convicted of an offence involving fraud or dishonesty, are an undischarged bankrupt, are of unsound mind, have failed to meet the requirements of Chapter Six of the Constitution, or have sat and failed the annual ethics and integrity test .

It is important to point out that this Act is largely intended to govern investment managers and financial analysts in private practice and thereby holders of private offices. However, Chapter Six of the Constitution applies only to State Officers. In the case of Luka Angaiya Lubwayo & Another vs. Gerald Otieno Kajwang & Another [2013] eKLR, the High Court of Kenya held that Chapter Six of the Constitution, which uses the words "State officer" more than ten times is targeting State officers as defined by Article 260 of the Constitution. Reference is also made to a State office as opposed to a private office. These words have a specific meaning, and though extrapolation to include all and sundry may be attractive to a casual mind, this was never the intention of those who painstakingly argued for and later crafted that Chapter. In view of the above decision, the provisions of Section 16 (1) (c) and 17 (d) of the Act may, in so far as it applies to private practitioners, fail to meet the constitutionality threshold pursuant to Article 2 (4) of the Constitution, which provides that any law that is inconsistent with the Constitution is void to the extent of the inconsistency.

Appeal Process

Section 19 of the Act establishes a clear appellate procedure from a determination of the Registration Committee, by first providing for an appeal to an arbitrator with a further provision for the right to a second appeal to the High Court. This is in consonance with both the right to a fair hearing and the non-derogable right to a fair trial. Section 21 of the Act then defines what constitutes the practice of an investment manager and financial analyst. Part III of the Act concludes by making it a mandatory requirement for a practitioner to have a practicing certificate and an annual license in order to practice. The annual licence can be procured either as a sole practitioner or as a partnership.

Disciplinary Provisions

Part IV of the Act deals with disciplinary provisions by detailing what constitutes professional misconduct. Section 27 in particular, establishes the Disciplinary Committee, which is mandated to inquire into matters of professional misconduct. As with determinations of the Registration Committee, decisions of the Disciplinary Committee may also be appealed through a clear appellate procedure, which is provided for in Section 30. The Act creates criminal offences by either persons or corporate bodies, which are punishable on conviction with a fine not exceeding KES 500,000. Finally, the Act contains four (4) Schedules sequentially detailing the procedural matters of the Institute, the Council, the Registration Committee and the Disciplinary Committee on Inquiry.

Conclusion

The Act has followed the path trodden by previously enacted legislation governing different professions, such as the Accountants Act, (Cap. 531) establishing the Institute of Certified Public Accountants of Kenya and the Certified Public Secretaries of Kenya Act (Cap. 534), establishing the Institute of Certified Public Secretaries of Kenya. In our view, the Act will go a long way in boosting investors' confidence in the fast-growing private equity sector, as it enhances professionalism and provides for the regulation of practitioners in the investment and financial analysis sector.

Geoffrey Muchiri
Partner | geoffrey@oraro.co.ke

Lena Onchwari
Senior Associate | lena@oraro.co.ke

THE HERALD OF A NEW TAXATION ERA IN KENYA

THE TAX PROCEDURES ACT , 2015

Sir Winston Churchill once quipped "*...for a nation to try to tax itself to prosperity is like a man standing in a bucket and trying to lift himself up by the handle...*" This quote could not be truer for a developing country like Kenya. The country's economy has seen steady growth over the years, characterised by the rise in infrastructure projects, growth in agricultural production, increase in foreign direct investments and improvement in the tourism sector. One would naturally expect that these developments would have a knock-on effect on the total tax revenue collected by the Kenya Revenue Authority (**KRA**). This however has not been the case with KRA falling short of its revenue collection targets every passing year.

In an effort to foster collection of revenue while encouraging investments in the country, Kenya has embarked on a tax reform journey which has seen the enactment of its new Value Added Tax Act, 2013 (**VATA**), Excise Duty Act, 2015 and the Tax Appeals Tribunal Act, 2013. A key milestone in this tax reform process is the recent enactment of the Tax Procedures Act, 2015 (**TPA**) which came into force on 19th January, 2016. The TPA resulted from the need to simplify and consolidate tax administration both from the Government and taxpayer perspectives, while mitigating the highly contentious issue of aggressive tax planning by corporate entities.

Changes brought about by the TPA

The TPA has not only proven to simplify tax administration for the government, it has also fostered easy tax compliance by the taxpayer. It has achieved this through making a number of changes in the following key areas:-

Record keeping

The TPA has limited a taxpayer's obligation to retain records to a period of 5 years. Previously, the Income Tax Act,(Cap. 470) had a retention period of seven (7) years while the VAT and the Customs and Excise Acts provided for five (5) years.

Tax assessments
KRA can only issue assessments for a maximum period of five (5) years. However, in a case where there is neglect, evasion or tax fraud by the taxpayer, an assessment may exceed the five (5) year limit.

Payment of taxes and filing of returns
A taxpayer can now request for an extension of the period to submit tax returns and payment of the tax associated with the returns, on condition that the Commissioner is satisfied with the reasons for delay.

Transfer of tax liability
Subject to the TPA, a taxpayer (transferor) can also transfer tax liability in the event that it transfers all or part of its business assets to a related party, in which case the person to whom the business assets are transferred will be liable for the taxes.

Information Technology (IT)
In an effort to enhance compliance, the TPA provides for the use of IT for purposes of submission of returns and payment or repayment of taxes on any day including weekends and public holidays which was not previously possible.

Public and Private Rulings
The Commissioner in accordance with provisions of the TPA, may make a public ruling which will be binding on him, unless he withdraws it by publishing a notice in at least two (2) newspapers with national circulation. This provision of guidance by the Commissioner is a most welcome development given the fact that tax disputes have often been as a result of conflict in the interpretation and/or applicability of tax statutes. In addition, taxpayers may also apply for private rulings which shall be published (with the taxpayer's identity concealed) in at least two (2) newspapers with national circulation. This will enable taxpayers to obtain clarity on the tax implications of certain transactions they intend to undertake. Not only will this achieve certainty of taxation, as already stated, it reduces the chances of future disputes on the tax treatment since the Commissioner will be bound by the ruling.

From a tax administration perspective, taxpayers can now be registered by the Commissioner for purposes of different tax obligations without their express application to be registered. It is noteworthy that before the enactment of the TPA, this was only provided for in the VATA.

Stringent penalties
The TPA also has punitive provisions. In particular, it has not only raised the stakes in terms of tax liability but has also introduced stringent penalties and offences in instances of non-compliance with certain tax law provisions as enumerated below:-

i) Late submission of PAYE returns previously attracted a penalty of KES 10,000 per return filed late. Subject to the TPA, the taxpayer will be subjected to a penalty equal to 25% of the PAYE due or KES 10, 000, whichever is higher.
ii) In the case of late filing of any other tax return; the penalty is now equal to 5% of the tax payable under the return to a minimum of KES 20, 000. The minimum amount has been reviewed from KES 10, 000 and KES 1, 000 in respect of corporate entities and individual taxpayers.
iii) In addition, the penalty for a tax shortfall attributable to a deliberate false or misleading statement was KES 1, 000,000 or imprisonment for a term of three years or both in the case of VAT and 200% of the tax amount involved in the case of Income tax. The TPA has now reviewed this to a penalty of 75% on the tax shortfall in case of fraudulent tax filing, and 20% where the shortfall is not as a result of fraudulent tax filing.

The TPA is a coat of many colours. It is not just punitive, it is practical.

iv) Subject to the TPA, the directors or senior officers of a company will now be liable if they enter into an arrangement with the intention of interfering with the company's current or future tax liability, if they fail to demonstrate that they did not benefit from the arrangement, opposed the transaction, were unaware of the arrangement or they failed to notify KRA of the same.

On a more positive note, the interest chargeable in the event of a late payment of tax, has been reduced to 1% from 2% per month and shall be charged as simple interest.

It is without a doubt that the TPA has and will continue to play a major role in administration and collection of taxes. This notwithstanding, the TPA has fuelled a major controversy on the fine line between tax evasion which is illegal and tax planning which is a legal application of the law with an aim of reducing tax liability. More specifically, it provides that in the event that the Commissioner deems a transaction to be entered into for purposes of tax planning, then the taxpayer will be liable to pay double the tax it would otherwise have paid as a penalty. This implies that a taxpayer will be penalised for taking advantage of loopholes in tax laws.

This attempt by the TPA to penalise efficient tax planning will undoubtedly be the subject of litigation in the not so distant future. This gives credence to what the UK's former Chancellor of Exchequer Denis Healey said when he stated that "*... the difference between tax avoidance and tax evasion is the thickness of the prison wall...*"

Conclusion
Clearly, the TPA is a coat of many colours. It is not just punitive, it is practical and most of all, a welcome way forward in regards to certain tax administrative procedures.

With its enactment, there is no doubt that a war has been "officially" waged against tax avoidance schemes. This is not only evident with the enactment of the TPA but also with Kenya recently, (on 8th February, 2016), becoming a signatory to the Convention on Mutual Administrative Assistance in Tax Matters. This convention is aimed at enhancing administrative co-operation between countries to counter international tax evasion, tax avoidance and other forms of non-compliance. It also aims at facilitating exchange of information, assistance in tax recovery, service of documents and joint tax audits by parties to the Convention.

Conjuring up the image of a man struggling to lift himself up by the handle of a bucket in which he is standing in, as described by Churchill, one may wonder whether the TPA is just a camel's nose of more stringent laws to come in Kenya that are aimed at tackling the greater 'evil' that is tax planning, culminating in an increase in tax revenue collection. It is therefore imperative to ensure that one is duly advised on the tax implications of a structure or business transaction before embarking on the same.

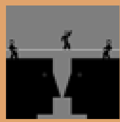
A FULL SERVICE FIRM

Our team of lawyers consists of some of Kenya's best legal minds; we have a breadth of expertise and remain at the forefront of Kenya's commercial and legal landscape. Some of our work highlights include:

Corporate & Commercial

National Government of Kenya and KenGen (Kenya's largest power producing company): advice on the sale of the former's stock in KenGen through an IPO

Contact: Pamella Ager
Email: pamella@oraro.co.ke

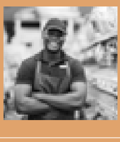


Dispute Resolution

Dufry International AG: representation in a dispute revolving around the award of a contract, to operate duty-free shops at Terminal 1A at the Jomo Kenyatta International Airport

Contact: George Oraro SC
Email: goraro@oraro.co.ke

Contact: Chacha Odera
Email: chacha@oraro.co.ke



Employment and Labour

Kenya National Union of Teachers: representation in a historic 2015 pay rise dispute against the teacher's employer, the Teachers Service Commission

Contact: John Mbaluto
Email: john@oraro.co.ke

Contact: Georgina Ogalo-Omondi
Email: georgina@oraro.co.ke

Energy, Projects and Infrastructure

International bidder: advice on the proposed construction of a 2000 km road Kenyan PPP project

Contact: Walter Amoko
Email: wamoko@oraro.co.ke

Intellectual Property

Software developer: representation at the High Court of Kenya in a copyright infringement claim

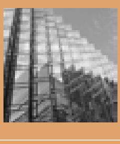
Contact: Jackson Awele
Email: awele@oraro.co.ke

Natural Resources

International Oil & Gas client: advised on an oil and gas contract revolving around the impact of the outbreak of the Libyan civil war

Contact: Geoffrey Muchiri
Email: geoffrey@oraro.co.ke

Contact: Noella Lubano
Email: noella@oraro.co.ke

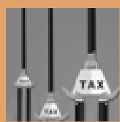


Real Estate, Conveyancing and Securities

Leading Kenyan bank with multinational coverage: preparation and perfection of security documentation (debenture, charges and corporate guarantees), the estimated matter value is USD 5.23 million

Contact: Pamella Ager
Email: pamella@oraro.co.ke

Contact: Nelly Gitau
Email: nelly@oraro.co.ke



Tax

Multinational bank: successful representation in a tax appeal before the High Court in which the taxman made a claim that group life premiums, paid by the bank for the benefit of its employees, were gains on profit chargeable to tax under the provisions of Section 5(2)(f) of the Income Tax Act

Contact: Lena Onchwari
Email: lena@oraro.co.ke

Contacts
ACK Garden Annex, 6th Floor, 1st Ngong Avenue
P.O. Box 51236-00200, Nairobi, Kenya
Dropping Zone No. 32 Revlon Professional Plaza
T: +254 20 271 3 636/20 271 1 480
M: +254 722 203 054/733 333 447
E: legal@oraro.co.ke