ORARO & COMPANY ADVOCATES

Oraro & Co. NEWS
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From the Senior Partner,

I take this opportunity to welcome you, our esteemed clients, to the launch of our Newsletter. This is the first edition of what will be a quarterly publication.

Our enduring ambition and commitment as a Firm is to endeavour to render to you efficient services at competitive rates and with utmost integrity. We tried to achieve this through a merger but quickly realised that this was not possible.

We have therefore retraced our steps back to our humble beginnings, and embarked on a path of organic growth with a view to occupying our space as an efficient, dynamic, effective and independent Firm with active affiliations both in the region and internationally.

To achieve this end, it is critical that we have a dynamic delivery team and we are happy to announce that we have been active in the market looking for and recruiting fellow professionals who share our vision. Our latest entrants are Geoffrey Muchiri and Noella Lubano who come with a wealth of experience in dispute resolution to join our Litigation Team at partnership level, while Nelly Gitau joins our Commercial/ Conveyancing Team in the same capacity. We have also recruited a Tax Consultant, Lena Onyango Onchwari, who is both a lawyer and a qualified accountant - CPA (K).

The purpose of our Newsletter is to engage you and to create effective communication by providing you with an overview of legal developments particularly in the area of legislation and decisions by our Courts at this time when we experience a plethora of statutory enactments and amendments to the law and when there has been an exponential increase in the number of judicial officers resulting in multiplicity of decisions and a rapid development of law.

We hope that you will find our Newsletter useful in at least providing you with some information on those areas of the law which may affect your business or you personally.

Have a happy and enjoyable reading.

George Oraro, SC

New Entrants

Geoffrey Muchiri
Partner, Litigation

Noella Lubano
Partner, Litigation

Nelly Gitau
Partner, Commercial/ Conveyancing

Lena Onchwari
Tax Consultant

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Walking a Tight Rope: Thin Line between Tax Planning and Tax Abuse

Globalization has had its bright side. Liberalization of domestic markets as well as the feeble returns in most Western markets has resulted in dramatic growth in foreign direct investment by multinational companies especially across the globe with developing countries receiving a substantial share. This has been of great benefit to developing countries spurring economic growth. Their tax authorities should also be smiling as growth results in more tax revenue. However this is not guaranteed as tax efficient multi-nationals are astute at avoiding taxes. Consequently, developing countries have seen the need to drastically amend and enact tax laws that will give them a wider tax base, curb tax evasion and mitigate against tax avoidance.

It is noteworthy that despite the statutory obligation to pay taxes, a taxpayer is allowed under law to so arrange its affairs to mitigate its tax liability. This is encapsulated in the statement of *Lord Clyde*, in the case of *Ayrshire Pullman Motor Services & Ritchie v Inland Revenue Commissioners where* he stated that; "….No man…. is under the smallest obligation, moral or other, so to arrange his legal relations to his business or to his property as to enable the Revenue [authority] to put the largest possible shovel in to his stores. The Revenue [authority] is not slow – and quite rightly – to take every advantage which is open to it under the taxing statutes for depleting the taxpayer's pocket. And the taxpayer is, in like manner, entitled to be astute to prevent, so far as he honestly can, the depletion of his means by the Revenue [authority]…." This passage recognizes the inevitable game of cat and mouse where the tax authorities seek to legally maximize tax collection while the tax payer seeks to legally reduce his/her tax obligations, with the Courts determining the legality of the transaction or structure when confronted with such matters.

The increased sophistication of financial arrangements to minimize tax obligations and the advancement of tax law to address this has occasioned numerous court decisions on tax planning. The Courts have become more sagacious and have moved away from solely looking at the legality of the transactions on the face of it as they have deemed that approach insufficient, the Courts now also examine the underlying commercial rationale of a scheme to determine whether it amounts to an abuse of law.

In the landmark case of *Halifax plc v C & E Commrs (and related appeals)*, the Court stated that '…the application of Community legislation cannot be extended to cover abusive practices by economic operators, that is to say transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by Community law. That principle of prohibiting abusive practices also applies to the sphere of VAT….' The judgment of the court in this case could not be more discerning. The Court opined that despite the legality of a tax planning scheme, the tax payer cannot employ the same without an accompanying commercial purpose as that would be tantamount to an abusive practice. It is therefore pertinent for the tax payer when formulating a tax planning structure, to take cognizance of the developments in both statutory and juridical law to ensure that the structure will not be deemed to be an abuse of law.

That said, tax planning can be approached from three different angles namely legal, financial and operational.

Legal Structure

A company's legal structure relates to its ownership or share holding. This is especially important when it comes to withholding taxes on dividends and most importantly in the eventuality of an exit from a country. In the Chinese *Chongqing case (State Tax Bureau, 27 November 2008)* a Singapore parent company sold to a Chinese buyer its Singapore subsidiary, which was a SPV (special purpose vehicle) that held a subsidiary in China. The Chongqing tax bureau disregarded the Singapore subsidiary and treated the transaction as a sale by the Singapore parent of the Chinese subsidiary. Consequently, the Singapore parent company had to pay income tax in China at a 10% rate on the capital gain from the sale, as if it had sold the Chinese subsidiary directly. The tax bureau was of the view that the Singapore subsidiary had a very small amount of capital and also did not carry on any business activity other than owning the shares of the China subsidiary. Hence, the Singapore subsidiary lacked economic substance.

Financing Structure

Companies finance their operations in two major ways, intercompany loans or loans from third party financial institutions. However the deductibility of the relevant interest expense is governed by certain specific and general anti-avoidance rules.

As already stated above, the Courts expect financing arrangements between companies to be driven by an economic goal. This was reflected in the recent judgment of the *Supreme Court of Netherlands dated 5th June 2015* in a case that involved a listed parent company of a South African media group. The parent company issued shares of which approximately 60% of the proceeds were directly wired to its Dutch third-tier subsidiary. From a legal perspective, the proceeds were contributed as capital to a second-tier Mauritian company, which in turn granted an interest free loan to its 100% owned Mauritian subsidiary, the group's internal financing (low-substance) company. This company lent the proceeds to the Dutch holding company through an interest bearing loan. The Dutch holding company used the proceeds to acquire other companies and claimed interest deduction on the Mauritian Debt. The

Walking a Tight Rope: Thin Line between Tax Planning and Tax Abuse (continued)

Supreme Court denied the claim for interest deduction and consequently referred the matter back to a lower Court to determine whether commercial reasons had duly motivated the funding provided by the holding company.

Operational Structure

It is common practice for companies in a group to offer other sister companies services at a cost. These services include management and professional services, marketing services, intellectual property leasing among others. Payments for such services will be allowable deductions in one company and may be subject to taxation in another. It is however prudent to note that the transfer pricing guidelines will apply in such transactions.

The spaghetti plate of divergent views on tax planning is not only of a legal nature, but also of a moral, economic and political nature. As already discussed above, tax planning or avoidance is not illegal but it may be deemed by the Courts and the revenue authorities to be an abuse of law, in which case the tax payer may be denied the tax advantage they sought to enjoy.

There are proponents, especially the civil society, who consider tax planning to be outright immoral. Such a stance may adversely affect a company's reputation, especially in cases where there is public outcry. However, such reputational risks can be allayed by putting in place certain measures which among others include intense lobbying and engagement with the government and tax authorities.

Flowing from the above, it is noteworthy that the Courts look at a number of factors in order to determine whether a company's tax planning activities amount to an abuse of law. It was the trend that Courts mainly considered whether the structure was highly motivated by a commercial or economic benefit to the company. However a recent judgment of the UK Supreme Court in the case of *HMRC V Pedragon plc & 5 others (2015) UKSC* added a new twist to this. In the case the court held that it is not sufficient that a transaction has a commercial benefit, this will be open to challenge if the accrual of a tax advantage is established to be the principal aim of the transaction.
In essence, while determining whether a tax planning structure amounts to an abuse of law or not, the Court will now consider two key factors; whether a company wished to obtain a tax advantage and whether the tax planning structure was driven by a commercial benefit. This decision of the Court is mirrored in the recent development of tax legislation in developing countries. For instance the Tax Procedures Bill in Kenya intends to look beyond the legality of the structure or transaction; it seeks to determine the commercial purpose of the same. It essentially lays the burden upon the tax payer to demonstrate the commercial purpose of certain transactions, failure of which the tax payer may be subjected to paying double the tax avoided as a penalty.

Therefore a tax payer should ensure that they structure their affairs in such a way that on one hand they are able to achieve their commercial or economic goals and on the other hand they get to optimally benefit from tax advantages brought about by the structure, without abusing the law.

Lena Onchwari
Walter Amoko

Tax statutes update

THE INCOME TAX ACT:

Legal Notice No.91 of 2015
Subject to this Legal Notice, interest paid on loan financing from foreign sources for purposes of investing in the energy and water sectors, or in the development of roads, ports, railways or aerodromes shall be exempt from tax.

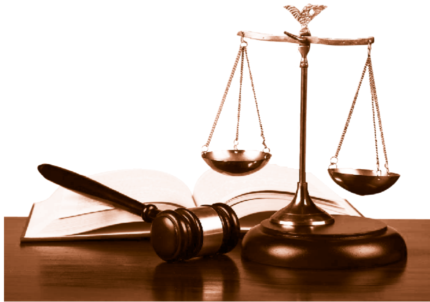
Legal Notice No.59 of 2015
The Double Taxation Relief (Qatar) Notice, 2015
The Double taxation Agreement entered into between the Republic of Kenya and the Government of the State of Qatar which was signed on the 23rd of April. 2014, with a view of affording relief from double taxation in relation to income tax and any rates of similar character imposed by the laws of Kenya is now effective.

THE STAMP DUTY ACT:

Legal Notice No. 106 of 2015
Subject to this Notice, instruments executed in respect to transactions relating to loans from foreign sources received by investors in the energy and water sector, infrastructure (roads, ports, water sector, railways and aerodromes) development sector, shall be exempted from Stamp Duty.

Legal Notice No. 105 of 2015
The Stamp Duty Act will not apply to documents executed in connection with asset backed securities approved by the Capital Markets Authority in respect of securitization transactions or any document executed to give effect to or for an on-going transaction.

Arbitration: A time to rethink?



"See you in Court" is a common refrain of TV court dramas, which obscures an open secret. This formal method of dispute resolution, which is of ancient vintage and is adversarial in common law countries, does not enjoy universal acclaim. The process is often too complex, formal, expensive and fraught with antagonism and sometimes, negative publicity. More often than not, due to its winner-takes-all approach, parties who 'see you in court' come out of it so bruised, that to expect them to be friendly thereafter is a product of fertile imagination, without any compensating social benefit.

The disadvantages of the Court processes have exacerbated over time and led to the clamour for a less formal, friendlier and conciliatory alternative process, whose outcome is still binding on disputants. Arbitration was seen as a God-sent alternative which accommodates these needs. Arbitration in Kenya is largely contractual and is governed by, among others, the Arbitration Act of 1995 (which is based on the UNICITRAL Model Law on Arbitration). This act was enacted in part, to reduce and limit Court interference with the arbitral process and enable it play a more supportive role.

Parties entering into any written contract have the liberty to include an arbitration clause in their contracts. Such a clause is helpful, as parties are then able to submit any dispute contemplated under the said clause for arbitration, instead of going through the court process.

There are a few pre-requisites that a party must consider before referring a dispute to arbitration. Key among these considerations are: the composition of the arbitral tribunal, the powers of the arbitrator(s), the seat of the arbitration, as well as the applicable law. All these considerations are best handled by a well-drafted and comprehensive arbitration clause. However, no matter how well drafted such a clause may be, a recalcitrant counter party may stymie the process, hence the continued role of the Court.

Once a dispute has been referred to arbitration and the preliminary issues sorted out, the process of resolving the dispute commences and is finally concluded when the tribunal delivers its award. Such award is binding and enforceable, just like any other decree of the Court.

It is often the case that a party for one reason or another, may be dissatisfied with an award and seek to challenge it. Consistent with the philosophy of party autonomy and encouragement of arbitration, the grounds for such challenge are limited. These grounds include: incapacitation of a party at the time of entering into an arbitration agreement; invalidity of an arbitration agreement; where an award goes beyond the scope of the arbitral reference; improper composition of the tribunal; where an award is tainted by fraud, bribery or undue influence; where an award is in conflict with public policy; among other grounds.

It has always been the case that where a party is aggrieved with the finding of the High Court, especially where such finding sets aside or varies the award delivered in its favour through arbitration, it has a limited avenue through which to appeal to the Court of Appeal. Though there have been conflicting decisions as to whether or not such decisions are appealable.

In a recent decision, a specially constituted five-judge panel of the Court of Appeal resolved this conflict by snuffing out that avenue. In Nyutu Agrovet Limited vs Airtel Networks Limited, Civil Appeal No. 61 of 2012, the Court of Appeal emphatically stated that no appeal lies to it from the High Court, where a party is appealing from a decision setting aside an arbitral award, or a decision affirming the award. As a decision of an intermediate appellate court, this decision has far reaching ramifications on the conduct of arbitration in Kenya. For one, it emphasises the finality with which arbitral awards are viewed. The decision effectively bars a party from appealing against a High Court decision setting aside or confirming an arbitral award.

The obvious danger of the foregoing is that a party has limited recourse against decisions of arbitral tribunals to the High Court and no recourse at all from the decision of the High Court, even in instances where these institutions have clearly misdirected themselves in law, or fact, or both. Once the High Court makes a determination, the matter is presumed to have been concluded.

The resultant effect of this is that parties now need to make a careful judgment and be guided by two fundamental questions, namely: 'should we include an arbitration clause in our contracts or refer disputes to arbitration in the first place?' and secondly, 'are we ready to bear the brunt of the finality principle even where a tribunal and/or the High Court misdirects itself?'.

The above questions are difficult to answer, bearing in mind the policy considerations behind arbitration. However, parties certainly need to be more careful in drafting arbitration clauses. One factor that parties need to seriously consider is the composition and size of the arbitral tribunal. Having a tribunal comprising more than one arbitrator, though costly, is a good suggestion, though the reality is that there is little assurance for a risk-averse party.

In the meantime, the effect of all this is that though arbitration now has a Constitutional anchor and Courts are empowered to compel arbitration (as well as mediation). Additionally, as arbitral awards are now increasingly impervious to challenge and in the absence of a credible process for error-correction, the Court process, warts-and-all, has seemingly become more attractive. The big question therefore is: has the time come to rethink whether we really need arbitration in Kenya? The jury is still out.

Eddy Ochieng Owiti
Walter Amoko

An overview of Regional Systems for IP Protection

Introduction

Intellectual property refers to inventions of the mind that are intangible in nature and are protected as such as trademarks, Patents, Copyrights and related rights and industrial designs.

They are a core component of most businesses in the 21st Century and valuable assets for which management efficiencies are as important as for any other asset. The dynamics of globalization and the effects that it has on strategies for every business, whether national or multinational, require that businesses pay closer attention to opportunities that help maximize benefits to the company and reduce costs to free up resources for other strategic interests of the business.

Given its territorial nature, protection of IP has often been undertaken by local, regional and multinational entities at national level. That means that subsidiaries or branches at national level are left to determine and follow up on protection and enforcement of IP rights in their respective jurisdictions. This in turn impacts on the cost of protection and enforcement, quality control, and ultimately the overall business strategies of the group.

A number of regional and international frameworks for IP protection however exist that can help reduce dispersed protection measures and facilitate central management and uniform strategy formulation for the group without impacting on local peculiarities of the business. Though enforcement ultimately remains territorial, these regional and multinational processes greatly contribute to better and central control of enforcement strategies and facilitate exchange of best practices.

The ARIPO System

In this edition, we provide commentary on the ARIPO System which is the key Africa region framework of significance to multinationals with Kenyan operations/interests.

ARIPO was the result of an idea mooted at a regional seminar on patents and copyright held in Nairobi in the early 1970's and the first draft agreement on the creation of a regional intellectual property organization was adopted in 1976 by a diplomatic conference – The Lusaka Agreement [also known as the draft Agreement on the Creation of the Industrial Property Organization for English-speaking Africa (ESARIPO)]. The idea was that the organization would serve mainly Anglophone countries. In practice that remains the case with very few exceptions. A number of lusophone and francophone countries have since joined ARIPO (The latest being the Republic of Sao Tome and Principe). Membership remains open to any member of the African Union or the Economic Commission for Africa.

The principal idea behind the establishment of ARIPO, was the pooling of resources of member countries in industrial property matters in order to utilize to the maximum available resources in these countries to ensure effective protection of industrial property, capacity building and training of staff in their respective industrial property institutions, development and harmonization of laws and general efficiencies.

Legal Framework

The Lusaka Agreement on the Creation of the African Regional Intellectual Property Organization (ARIPO)

The Lusaka Agreement was adopted at a diplomatic conference at Lusaka (Zambia) on December 9, 1976 and establishes ARIPO at Article 1 thereof.

Pursuant to its functions and powers under the Agreement (Article VII) the Administrative Council of ARIPO has developed protocols and regulations that form the background of the legal and operational design of intellectual property protection in member states under the system. These include:

(a) The Harare Protocol on Patents and Industrial Designs within the Framework of the African Regional Industrial Property Organization
(b) The Banjul Protocol on Marks; and
(c) The Swakopmund Protocol on the Protection of Traditional Knowledge and Expressions of Folklore.

Membership to the Lusaka Agreement does not necessarily imply membership to the protocols. Each protocol applies to different aspects of intellectual property and membership to each is voluntary.

The Harare Protocol

The Harare protocol applies to protection of patents and Industrial designs and currently has 19 contracting States, namely; **Botswana, The Gambia, Ghana, Kenya, Lesotho, Liberia, Malawi, Mozambique, Namibia, Rwanda, Sierra Leone, Sudan, Swaziland, Tanzania, Uganda, Zambia, Zimbabwe** and the **Democratic Republic of São Tomé and Príncipe** (the latest member as at August 19, 2014).

How the filing System works: brief overview

The Harare Protocol provides a framework for filing and protection of patents and industrial designs within member

states. The Protocol is supplemented in its provisions by administrative regulations that make further and detailed provisions for the manner in which an application is treated from the date of filing to grant of patent or refusal as the case may be.

There are principally two regulations under the Harare protocol in this regard;

(a) The regulations for implementing the protocol on patents and industrial designs within the framework of the African regional intellectual property organization ('the regulations'); and
(b) The administrative instructions under the regulations for implementing the protocol on patents, industrial designs and utility models within the framework of the African regional intellectual property organization (the Administrative instructions)

The regulations are made by the Administrative council pursuant to section 5 of the Harare Protocol and mainly deal with substantive matters relating to the content of applications filed with the ARIPO office including on the requirements for patentability, the right of priority, Appeal procedures against decisions of patent examiners and treatment of PCT applications under the ARIPO system.

Administrative instructions on the other hand are made by the office of the Director General of ARIPO pursuant to rule 2(5) (a) of the regulations and mainly deal with the day to day administrative requirements of ARIPO including the formality details in respect of applications under the protocol, filing timings, fees payable for each service, detailed steps in the filing and examination of applications up to grant, notification and communication procedures, the forms to be used for various filings etc.

Patents

In summary the ARIPO system is registration based and subject to notifications of refusal by national offices whereas the PCT system is a filing system.

An applicant for the grant of a patent for an invention or the registration of an industrial design can, by filing only one application, either with any one of the Contracting States or directly with the ARIPO Office, designate any one of the Contracting States in which that applicant wishes the invention or industrial design to be accorded protection.

The ARIPO Office, on receipt of the patent application, undertakes both formality and substantive examination to ensure that the invention which is the subject of the application is patentable (i.e. it is new, involves an inventive step and is capable of industrial application).
If the application complies with the substantive requirements, copies thereof are sent to each designated Contracting State which may, within six months, indicate to the ARIPO Office that, according to grounds specified in the protocol, should ARIPO grant the patent that grant will not have effect in its territory.

For industrial design applications, only a formality examination is performed. If the application fulfills the formal requirements, the ARIPO Office registers the industrial design which has effect in the designated States. However, the same right to communicate to the ARIPO Office within six months that the registration may not have effect in the designated States concerned is reserved.

The Administrative Council, at its Second Extra-ordinary session held in April 1994, adopted amendments to the Harare Protocol and its Implementing Regulations to create a link between the protocol and the WIPO-governed Patent Co-operation Treaty (PCT). This link commenced operation on July 1, 1994, and has the following effects:
(i) Any applicant filing a PCT application may designate ARIPO which in turn means a designation of all States party to both the Harare Protocol and the PCT;
(ii) The ARIPO Office acts as a receiving office under the PCT for such States; and
(iii)The ARIPO Office may be elected in any PCT application.

All current Harare Protocol Contracting States are also signatory to the PCT.

The Banjul Protocol

The Banjul Protocol on Marks, adopted by the Administrative Council in 1993, establishes a trademark application filing system along the lines of the Harare Protocol. Under the Banjul Protocol, an applicant may file a single application either at one of the Banjul Protocol Contracting States or directly with the ARIPO Office. The application should designate Banjul Protocol Contracting States as the States in which the applicant wishes the mark to be protected once the ARIPO Office has registered it.

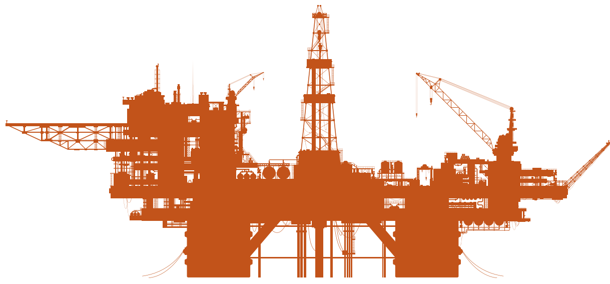
States currently party to the Banjul Protocol are: **Botswana, Lesotho, Liberia, Malawi, Namibia, Swaziland, Tanzania, Uganda** and **Zimbabwe**. (Total: 9 States.). Kenya is yet to accede to this treaty and so trademarks filing can only be done locally or through the Madrid system as we shall see in the next edition of the newsletter.
Since 1997, the protocol has been extensively revised in order to make it compatible with the TRIPs Agreement to make it more user-friendly.

Conclusion

The ARIPO system is highly advised for clients with regional interests. We represent a number of clients in patent applications using the system and recommend it for costs savings and efficient management of the application process (more so for bulk applications) in several member countries.

In the next edition of the newsletter, we shall provide commentary on international filing systems to give a broader perspective for multinationals operating in Africa and beyond.

Jackson Awele Onyango
Chacha Odera



Taxation in the upstream oil and gas sector

26th May 2012 is a date that will forever remain etched in the minds of Kenyans as it is the day when the announcement was made that vast quantities of oil had been discovered in Turkana County. Commercial viability of those discoveries had not been determined but from that date Kenya became a new petroleum province of great interest to all in the global oil and gas industry. It is in the context of this discovery that Kenya's numerous oil blocks are seeing a renewed interest from International Oil Companies (be they: small independents or the oil majors/seven sisters and their successors in title) or National Oil Companies from other countries.

The exploration and production of oil and gas is a very expensive capital intensive undertaking as the preliminary shooting of seismic and the drilling of exploratory wells in an oil block in accordance with the work programme agreed with any Government in any country may cost between US$1 million to over US$ 15 million and Kenya is no exception (this is coupled with the attendant risk that there is always a great possibility that the oil(if any that is found) may not be in commercial quantities). The development and production phase may involve the construction of the infrastructure necessary to transport the oil from the wellhead to the port of Mombasa or Lamu and may cost hundreds of millions of dollars.

For that reason any IOC that seeks to sign a Production and Sharing Contract (PSC) with the Kenyan Government in respect of the available oil and gas blocks (be they onshore or offshore) would like to ascertain up front what taxes if any are applicable during the exploration phase as well as the production before the IOC can proceed to make any contractual commitment by signing and sealing the PSC. This accords with what Lord Mansfield stated in 1774, that in all mercantile transactions the great object should be certainty. This aphorism holds true to this day especially in the oil and gas sector.

The taxes applicable to the oil and gas company undertaking exploration and production of oil in Kenya are as follows:

1. Corporation tax on the profits during the production phase (with an allowance being given for amongst others: production costs (recovered from the cost oil within a period of between 4 and 5 years), intangible drilling costs, payments to the government under the PSC, executive and general administrative expenditure incurred in Kenya (as well as outside Kenya with special exception in the sense that those expenditures although incurred outside Kenya relate to Kenya), management fees, interest paid on loans(provided tax on the interest has been deducted and paid). The corporation tax rate is 37.5% for non-resident companies and 30% for resident companies.
   N/B: Since many IOCs which happen to be oil majors are vertically integrated there is a likelihood they may sell oil to their subsidiaries involved in marketing and for that reason there are rules that govern and ensure that such sales are done on an arms- length basis.

2. A tax on any transfers of any interest in the property and/or shares of an oil company was introduced in 2012.This attempts to cover: take-overs and farm-outs as well as outright sales of the whole interest. This tax was introduced as a result of a battle that the Kenyan Government lost when it tried to call for its share of taxes when an international take-over of a company had the effect of resulting in the acquisition of stakes in some oil blocks in Kenya.

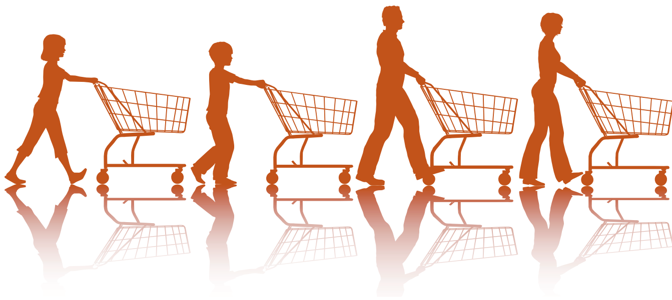
3. Government share of profit oil is also a tax from the IOC's perspective. The Government share of profit oil is calculated on a sliding scale with the government share increasing dependent on how many barrels of oil are produced from a particular oil block (akin to the sliding scale that applies to an individual person's income in Kenya whereby the government take/tax increases with each increasing level of income). The Government share of profit oil is a negotiable variable and this is a factor which ought to be taken into consideration as one engages the Government in negotiations leading up to the signing of a PSC.

4. Windfall profits tax may be included in some concluded Production Sharing Contracts. However, in light of the continued sharp price decline in the global oil prices. This might not be a very attractive tax model.

Ring-fencing is applicable to the upstream oil and gas sector in Kenya. This means that losses from one oil block cannot be used to reduce the taxable income in respect of another profitable oil block.

The Kenyan Government is currently at an advanced stage of concluding the preparation of new legislation that will govern the upstream oil and gas sector in Kenya

Geoffrey Muchiri



Consumer protection law in Kenya

Prior to the promulgation of the Constitution in the year 2010, there was no specific law dealing with consumer protection in Kenya. However, some aspects of consumer protection were covered in various pieces of legislation including the Trade Descriptions Act, Standards Act, Weights and Measures Act, Restrictive Trade Practices, Monopolies and Price Control Act (now known as the Competition Act), the Foods, Drugs and Chemical Substances Act, the Pharmacy and Poisons Act, the Public Health Act, the Fertilizers and Animal Foodstuffs Act, as well as private law measures in the law of contract and the law of tort.

These and other statutes touching on consumers are criminally oriented as they seek to ban one malpractice or the other and to prosecute offenders for breach of their provisions, but do not empower a consumer to sue the offender to get redress, including compensation, where the said breach affects him or her adversely. Herein lay the major set-back in protection of consumers under these statutes.

It is in this regard that the Article 46 of the Constitution of Kenya 2010 and its enabling statute, the Consumer Protection Act, 2010 are lauded as landmark achievements in the area of consumer protection. These new laws spell out consumers' rights and obligations vis-a-vis product and service liability; they make provisions for the promotion and enforcement of consumer rights as well as empower consumers to seek redress for infringement of their rights as consumers; and also provide for compensation.

Part II of the Act gives consumers a wide range of rights including the right to commence legal action on behalf of a class of persons in relation to any contract for the supply of goods or services to the consumer. This right cannot be ousted by any agreement between the parties. Other consumer rights provided for in the Act include the right to full pre-contractual information for the consumer to make an informed choice, the right to complain with regard to quality, delays in provision of rectification, quantity and price of such goods or services as are offered, the right to a reasonable notification of termination of service - particularly in relation to the provision of basic telecommunications services and/or internet access, among other rights.

The Act prohibits 'unfair practices' and proceeds to provide for radical sanctions against a supplier who engages in 'unfair practices'. Such practices include representing that goods or services have a sponsorship, approval, performance or characteristics that they do not have; or representing that goods or services are of a particular standard, quality, grade, style or model, if they are not, and so on.

Therefore where a consumer enters into an agreement, whether oral or written, after or while a person has engaged in an unfair practice, the Act provides that the consumer has the right to terminate the agreement and seek any remedy available to them in law, including a suit for damages.

Undoubtedly, the Consumer Protection Act is a far-reaching piece of legislation that will affect different sectors of our economy including real estate, e-commerce, manufacturing, agriculture, banking and finance, aviation, among many others. In this connection, the Act establishes the Kenya Consumers Protection Advisory (CPA) Committee that shall aid in the formulation of policy related to consumer protection, accredit consumer organisations, advise consumers on their rights and responsibilities, investigate complaints and establish conflict resolution mechanisms amongst other duties. A breach of any regulation made by the CPA, will make a person liable to a fine not exceeding five hundred thousand shillings or imprisonment for a term not exceeding two years or both such fine and imprisonment.

In conclusion, although consumer protection law within Kenya is very much in its infancy, there have been several significant developments in this area over the last three years, namely the promulgation of the new Constitution in 2010 and the subsequent enactment of the Consumer Protection Act, which came into effect in 2013 as well as enactment of the Competition Act, 2010. The Competition Act protects consumers from unfair and misleading market conduct.

Indeed the increased consumer protection has seen the formation of the Consumer Federation of Kenya (COFEK) which was registered on 26th March, 2010 and whose mandate is:

"to defend, promote, develop and pursue consumer rights as guided by Article 46 of the Constitution of Kenya 2010, the Consumer Protection Act, 2012 and the Competition Act, Cap 504 and make it possible for the consumers to get value for money."

COFEK has been at the forefront in acting as a watchdog in various consumer protection matters with the most recent being the institution of a suit against a leading retail supermarket for the alleged overcharging of items on its shopping tills brought about by the shelf and till price discrepancies at its outlets.

Cindy Oraro

Jill Barasa

Does your development require an environmental impact assessment licence?

Kenya has experienced a boom in development projects in the last couple of years with resulting transformation of whole neighbourhoods as the demand for land outstrips the prescribed zones. This rapid growth is due to growth in population leading to a soaring demand for housing in most parts of the country and a huge deficit in infrastructure such as rail, roads and ports. There are many considerations that prospective developers must deliberate on including the availability of raw materials, funding and compliance with laws such as the Physical Planning Act, Cap 286 Laws of Kenya and the Environment Management Coordination Act, Cap 387 Laws of Kenya (EMCA) as well as various provisions of the Constitution.

The impact of a proposed development on the environment is critical and the regulatory body charged with approving the environmental aspects of projects and issuing the relevant environmental licences is the National Environment Management Authority (NEMA). The requirements of EMCA with respect to development projects reflect a worldwide appreciation of the adverse effects of unbridled development that now find a Constitutional anchor in the right to a clean and healthy environment and public participation as well as the obligations of the Courts under Article 70 of the Constitution. These concerns are aptly captured by the phrases sustainable development and the pre-cautionary principle. With such enhanced rights and greater awareness, developers increasingly experience spirited resistance from residents and environmental activists.

At the heart of numerous cases filed in the National Environment Tribunal is the challenge by objectors of proposed developments with respect to developers' failure to conduct a proper Environmental Impact Assessment (EIA) as well as irregularities in the grant of EIA Licences.

When is an EIA report necessary?

An EIA is a systematic examination conducted to determine whether or not a programme, activity or project will have any adverse impact on the environment. The requirement of an EIA licence is prescribed in Section 58 of EMCA. It provides that any person, being a proponent of a project, shall before financing, commencing, proceeding with, carrying out, executing or conducting any undertaking specified in the Second Schedule of the Act, submit a project report to the Authority in the prescribed form. The proponent of the project is to undertake the EIA study at its own expense.

Section 1 of the Second Schedule sets out general projects that require EIA to include any activity out of character with its surrounding, any structure of a scale not in keeping with its surrounding and major changes in land use. Section 2 provides a more specific and comprehensive list of projects such as urban development, transportation, dams and rivers, mining, forestry and agriculture.

In the recent case of ***Registered Trustees of Jamie Masjid Ahl-Sunnait-Wal-Jamait Nairobi v Nairobi City County & 2 others [2015] eKLR*** the Plaintiff owner of a mosque sought to challenge the ongoing development of a public toilet facility by the 1st Defendant who owned the adjoining land. The Plaintiff contended that the intended project required a proper EIA and that the project being commercial in nature would result in a major change in land use. It was the 1st and 2nd Defendant's argument that the project did not fall under the projects prescribed in the Second Schedule of the Act.
The question faced by the Court was if a project does not fall within those listed in Section 2 of the Second Schedule, then who ought to determine if it falls within the general provisions of Section 1?

The Court stated that section 58 (1) of the EMCA suggests that the proponent of the project is the one to determine whether the project falls under the Second Schedule. The Court went on to state that the criteria for determination would be to first ascertain if the project falls and is specified under any of the sections of the Second Schedule. If it does not then a determination has to be made if it falls within section 1 of the Second Schedule. The Court recognized that this is not a simple task. The second criteria would be to appreciate and understand that an EIA is intended to help protect the environment. Third, would also be to appreciate and understand that the "EIA process is indeed to be an aid to an efficient and inclusive decision making in special cases, not an obstacle race".

The relevant matters that the developer ought to take into account in screening the project for the necessity of an EIA include but are not limited to:-

i) the characteristics of the intended development;
ii) the location of the intended development and characteristics of potential impact;
iii) the size of the development as well as cumulation with other neighboring developments;
iv) the probability of any environmental impact; and
v) the duration and reversibility of such impact.

The Court in the above case conclusively held that it was not enough to read through the second schedule to the EMCA and state that the intended project does not fall under the said schedule. The above listed matters must be exhaustively considered by the proponent and only upon thorough analysis of these matters shall a proponent rightfully conclude that an EIA report is not required. To this end, the Court granted the injunction prohibiting further works on the ground that there was no indication of the criteria used by the 1st and 2nd Defendants in determining whether or not an EIA was necessary.

Therefore, it is important that proponents adhere to such guidelines in the interest of progressive, timely and sustainable development. The lesson of ***Registered Trustees of Jamie Masjid Ahl-Sunnait-Wal-Jamait Nairobi v Nairobi City County & 2 others [2015] eKLR*** is that in a sense developers should adopt for their developments the precautionary principle in favour of conducting an EIA and obtaining a licence.

Beryl Rachier
Chacha Odera

Section 23 of the Registration of Titles Act - Did it really protect the bona fide purchaser?

The Registration of Titles Act (Cap. 281) now stands repealed. Nonetheless, disputes in respect of land registered under the repealed Act, particularly those centered on the protection proffered by section 23 of the Act to bona fide purchasers for value without notice, will continue to rage on as we slowly transit into a new era of land laws.

The Registration of Titles Act was a product of the Torrens system of registration - a system which places emphasis on the accuracy of the land register and insists that the register must mirror all currently active registrable interests affecting a particular parcel of land.

The Government, as the keeper of the master record of all land and its respective owners, guarantees the indefeasibility of all rights and interests shown in the land register against the entire world; and in case of loss arising from an error in registration, the person affected is guaranteed Government compensation.

The statutory presumption of indefeasibility and conclusiveness of title under the Torrens system is rebuttable only by proof of fraud or misrepresentation, in which the buyer is involved. The object of the Torrens system was summarized in the Privy Council decision in ***Gibbs v Messer*** as follows:

> *"The main object of the Act and the legislative scheme for the attainment of that object are equally plain. The object is to save a person dealing with registered proprietors from the trouble and expense of going behind the register, in order to investigate the history of their author's title and to satisfy themselves of its validity. That end is accomplished by providing that everyone who purchases, in bona fide and for value, from a registered proprietor and enters his deed of transfer or mortgage on the register, shall thereby acquire an indefeasible right, notwithstanding the infirmity of his author's title."*

Back home in Kenya, the indefeasibility of title has received lip service from the Kenyan Courts including our own Court of Appeal. A case in point is the Appellate Court's decision in ***Dr. Joseph Arap Ngok v Justice Moijo ole Keiwua***, where the Court pronounced itself as follows:-

> *"Section 23 (1) of the Act gives an absolute and indefeasible title to the owner of the property. The title of such an owner can only be subject to challenge on grounds of fraud or misrepresentation to which the owner is proved to be a party; such is the sanctity of title bestowed upon the title holder under the Act. It is our law and law takes precedence over all other alleged equitable rights of title. In fact, the Act is meant to give sanctity of title, otherwise the whole process of registration of title and the entire system in relation to ownership of property in Kenya, would be placed in jeopardy."*

It would therefore appear that a plain reading of section 23 suggests that a bona fide purchaser is assured of protection, notwithstanding that previous dealings might be shown to have been mired in fraud. However, following a recent decision of the Court of Appeal in the case of ***Arthi Highway Developers Ltd v West End Butchery Ltd & Others***, it seems that the protection offered by section 23 is not quite as indubitable as first thought. In this decision, the Court struck down as invalid titles transferred to bona fide purchasers, after having found that there was fraud in the initial transfer from the first owner. In applying the nemo dat quod non habet (no one gives who possesses not) principle (which principle has no application to immovable properties), the Court found that the fraudsters did not obtain good title to pass on to the bona fide purchasers.

Yet the Court of Appeal's decision in the ***Arthi Highway Developers*** case is at glaring odds with an earlier decision by the same Court in ***Permanent Markets Society & Others v Salima Enterprises & Others***, where it was held that even where it is shown that previous registrations were obtained illegally, the title of the last bona fide purchaser for value was indefeasible under section 23.

In view of the conflicting decisions emanating from the Court of Appeal as to the extent of protection offered by section 23 of the Registration of Titles Act, all eyes now turn to the Supreme Court to pronounce itself on the matter and hopefully lay to rest the spectre of section 23.

This follows the Supreme Court's granting of leave to appeal to the said Court (the Court of Appeal having refused to grant leave to appeal on the basis that there was no controversy as to the application of section 23) in the case of ***Charles Karathe Kiarie & Others v The Administrators of the Estate of John Wallace Mathare (Deceased) & Others***. We shall keep our clients and readers updated on the Supreme Court's decision in the matter.

John Mbaluto
Carol Njiru

Redundancy process: Getting it right

Running a business is no easy task, running it profitably is even more difficult. Since the advent of liberalization in 2003, redundancy has become progressively more common in Kenya. Rapidly shifting markets driven mainly but not exclusively by technological innovation; uncertain economic times including cyclical downturns which in this age of globalization has world-wide effects, like the 2007-2008 economic melt-down; increased demand by shareholders for better performance etc, make existing business models superfluous pretty quickly. An inevitable consequence of adjusting the business model every so often is a reduction on head-count as positions or on occasion departments that were once crucial require elimination. However, this must be done within the framework of existing laws.

Redundancy is defined under Section 2 of the Employment Act, 2007 as the loss of employment, occupation, job or career by involuntary means through no fault of an employee. It involves termination of employment at the initiative of the employer, where the services of an employee are superfluous. Redundancy may arise under various circumstances including but not limited to the practices commonly known as abolition of office, job or occupation and loss of employment. Examples of these circumstances are:

a) the employer has ceased, or intends to cease continuing business;
b) the requirement for employees to perform work of a specific type or to conduct it at the location in which they are employed has ceased or diminished; or
c) re-organization of the workforce resulting in is less work and changes in conditions that result in the new job being quite different from the old one.

If the intended action of termination of employment arises from the above definition or examples of circumstances leading thereto, Section 40(1) of the Employment Act provides for the substantive and procedural legal requirements to be met by the employer to effect a termination of employment on account of redundancy as follows:-

"An employer shall not terminate a contract of service on account of redundancy unless the employer complies with the following conditions:-

(a) where the employee is a member of a trade union, the employer notifies the union to which the employee is a member and the labour officer in charge of the area where the employee is employed of the reasons for, and the extent of, the intended redundancy not less than a month prior to the date of the intended date of termination on account of redundancy;

(b) where an employee is not a member of a trade union, the employer notifies the employee personally in writing and the labour officer;

(c) the employer has, in the selection of employees to be declared redundant had due regard to seniority in time and to the skill, ability and reliability of each employee of the particular class of employees affected by the redundancy;

(d) where there is in existence a collective agreement between an employer and a trade union setting out terminal benefits payable upon redundancy; the employer has not placed the employee at a disadvantage for being or not being a member of the trade union;

(e) the employer has where leave is due to an employee who is declared redundant, paid off the leave in cash;

(f) the employer has paid an employee declared redundant not less than one month's notice or one month's wages in lieu of notice; and

(g) the employer has paid to an employee declared redundant severance pay at the rate of not less than fifteen days pay for each completed year of service."

In summary Section 40 (1) of the Employment Act prohibits an employer from terminating the services of an employee on account of redundancy unless the employee's union is notified or in the case where the employee is not a member of a union then the employee is notified personally in writing and the local labour officer is also informed in both cases. The employer is also expected to consider seniority, skill, ability and reliability of each employee; pay off pending leave in cash, pay one months' wages in lieu of notice and severance pay. For a termination on account of redundancy to be fair and lawful, an employer must adhere to the requirements set out in Section 40(1) of the Employment Act, 2007, unless the parties have entered into an agreement to the contrary with terms greater than the minimum statutory requirements which may be through a contract of employment or Collective Bargaining Agreement (CBA).

Over the past couple of years there has been an increase in claims filed in the Employment and Labour Relations Court against termination on account of redundancy. One of the most notable of these claims was ***Industrial Cause No. 1661 of 2013 Aviation Allied Workers Union Kenya & 3 others v Kenya Airways Limited***, wherein over 400 employees of

Redundancy process: Getting it right (continued)

the airline were rendered redundant following a restructuring exercise. The Union filed a claim seeking a declaration of unfair termination on account of redundancy claiming proper procedure was not followed in accordance with Section 40 of the Employment Act, an order for reinstatement of the affected employees and in the alternative payment for pecuniary loss and maximum compensation of twelve (12) months for loss of employment. The trial court found in favour of the Union on grounds that the Respondent did not have valid reasons for the terminations as all the airline was facing was a cyclical crisis which did not affect its bottom line. The trial Court also found that procedure employed by the airline was flawed as there was no meaningful consultation and the process for selection of the affected employees was flawed reeking of pre-selection and bad faith. It ordered immediate reinstatement of employees and payment of salaries for the period that the employees were out of employment.

The airline which was represented by the firm of Oraro & Company Advocates both before the Employment and Labour Relations Court and the Court of Appeal successfully appealed - ***Civil Appeal No. 46 of 2013 Kenya Airways v Aviation Allied Workers Union Kenya & 3 others.*** There were three separate judgments basically upholding the position of Kenya Airways in all matters except one in which two judges found the process fell short, that being the selection criteria. Thus while the judgment in the Industrial court was in most reversed, by a majority of two to one, the employees were awarded damages for a limited period rather than reinstatement. From this decision for any termination of employment under redundancy to be lawful, it must be both substantially justified and procedurally fair:

i) To establish substantive justification the appellate court looked at the definition of redundancy under Section 2 of the Employment Act. The employer must prove that the loss of employment in redundancy cases has to be by involuntary means and at the initiative of the employer, brought about by operational requirements of the employer e.g. reduction of head count so as to respond to adverse market condition or improve efficiency. While the Court should be eternally vigilant to ensure that the reasons given are not pre-textual, it is not for the Court to substitute its judgment for that of the employer. The Court found that Industrial Court had overstepped its limited role of review when it essentially trashed the reasons given by Kenya Airways and held that the Company facing a cyclical downturn which could address by being run more efficiently rather than laying off its staff.

ii) Procedural fairness is comprised two aspects:

(a) Firstly, the employer must strictly comply with the provisions of Section 40 (1) of the Employment Act for termination on account of redundancy to be lawful, which consist of issuance of notices in the prescribed manner and statutory period as detailed above, (unless the CBA or contract of employment stipulates a longer period). The purpose of the provision requiring notice to be given is to elicit consultation between the parties. Kenya is a state party to the International Labour Organization (ILO) and is bound by the ILO conventions. Article 13 of Recommendation No. 166 of the ILO Convention No.158- Termination of Employment Convention, 1982 which requires consultation between the employers on the one hand and the employees or their representatives on the other before termination of employment under redundancy. The requirement of consultation is implicit in the principle of fair play under Section 40 (1) of the Employment Act. The purpose of the notice under Section 40 (1) (a) and (b) of the Employment Act is to give the parties an opportunity to consider "measures to be taken to avert or to minimize the terminations and measures to mitigate the adverse effects of any terminations on the workers concerned such as finding alternative employment". Such consultations must be genuine rather than pre-textual- going through the motions merely to comply with the law

(b) Selection Criteria- The employer must develop and apply an objective process for identifying the employees who will be affected by the redundancy. This must, of necessity be related to the reasons of the redundancy. Selection must be not the basis of such invidious factors such as participation in protected union activities or race, gender etc

We are yet to see the effect of the decision of the Court of Appeal being adopted by the Employment and Labour Relations Court in similar matters. While this is based on casual empiricism, there seems to be some resistance to the lessons of the case. In the meantime, employers contemplating redundancy are well advised to ensure that every substantive and procedure 'Ts' and 'Is' are crossed and dotted.

Georgina Omondi

Walter Amoko

ORARO & COMPANY ADVOCATES

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