



Institute of  
Economic Affairs

# Law and Economics of Privatization in Kenya

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# Outline

- Background
- Context Issues: State of fiscal finances, Growth
- State Corporations and Legal Ambiguities
- Privatization Process in Privatization Act, 2023
- State of Play: Fiscal Risks
- Conclusion

# Part of CLE's Series on Privatization....



## Privatization Reforms in Kenya: History, Objectives and Lessons

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**Constitution, Law and Economy Programme**

Nov 25, 2021

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**IEA Kenya Webinar 38of2021 Privatization and Economic Reforms in Kenya:**  
<https://www.youtube.com/watch?v=G76hnctk0yQ&t=2122s>

# Background; CLE's focus on Privatization

- Analysing the constitutional framework for privatization in Kenya, including adherence to constitutional thresholds.
- Evaluating the legal aspects of privatization, such as regulatory frameworks and legal implications.
- Assessing the economic impacts of privatization on various sectors and the overall economy.
- Monitoring the performance of institutions involved in privatization, ensuring transparency and accountability.
- Studying the policy choices related to privatization, considering legal, economic, and constitutional implications.

# The Basis for Privatization Reforms

## 1. Limited Government

1. John Locke- (2d Treatise on Govt: Of Civil Govt) Chapter IX, Section 131: The government should only do good for the people
2. Thomas Jefferson (A summary view of the rights of British America, 1774)- Individual & firms susceptible to the Spirit of Tyranny
3. Adam Smith (An inquiry into the nature and causes of wealth of Nations, 1776)- Limited Govt should allow invisible hand (Dd & SS) to drive the economy.

2. Efficiency in Resource Allocation (Market Fn)

3. Creation of Fiscal Space- (Kenya's Debt Crisis)

4. Constancy & Predictability of Economic Policy- Constitutional Guarantee

5. Privation Allows Govt to Focus on Role of Government

1. Provision of Public Goods: Stormwater Management Systems, Public Safety, Disease control (Mass Vaccination)
2. Constitutional Obligations (Article 43): Private Goods such as Education, Healthcare with positive externalities

# Legal Issues with Designation of State Corporations

- **Definition:** A State Corporation in Kenya is established by order under the State Corporations Act, an Act of Parliament, a licensed Bank or financial institution, or a company where the Government holds all or a controlling share.
- **Exclusions:** State Corporations do not include local authorities, co-operative societies, building societies, or companies where the Government does not wholly own or control.
- **Scope:** The Kenyan definition includes commercial and non-commercial entities, regulatory bodies, services, universities, training institutions, and research institutions.
- **Semi-Autonomous Government Agencies (SAGAs):** SAGAs are largely State Corporations established under the State Corporations Act and are not treated separately under any other law, unless exempt (e.g., the Central Bank of Kenya and the Capital Markets Authority).
- **Public Funds:** National public funds are established as State Corporations under their own laws or by the State Corporations Act. Other public funds, established predominantly under the PFM Act, are not considered State Corporations and are controlled by the line Ministry (e.g., Civil Servants Accident Claim Fund).

# Two Types of State Corporations

## Commercial State Corporations

Operate on commercial principles, aim to be profitable, self-financing, and accountable to stakeholders and the public.

## Non-commercial State Corporations

Operationally autonomous from Government, expected to operate on a cost recovery basis, funded mainly through appropriations from Parliament, levies, and fees. Deliver services on behalf of line Ministries.

# Privatization Process in The Privatisation Act, 2023



# Functions of Privatization Authority

1. Advise the government on all aspects of privatisation of public entities.
2. Facilitate the implementation of government policies on privatisation.
3. Implement the privatisation programme.
4. Implement specific privatisation proposals in accordance with the privatisation programme.
5. Collaborate with other organisations, within or outside Kenya, as it may consider appropriate in furtherance of Privatization
6. Prepare long-term divestiture sequence plan.
7. Monitor and evaluate the implementation of privatisation programs in Kenya.
8. Take such measures as are necessary to ensure that the provisions of this Act are complied with.
9. Perform any other functions under this Act or any other legislation as may be conferred, from time to time, on the Authority.

# Privatization Process: (Part III & IV, The Privatisation Act, 2023)

Steps	Sub steps
Initiation	<ul style="list-style-type: none"><li>• Identification of entities for privatisation.</li><li>• Formulation of the privatisation programme by the Cabinet Secretary.</li></ul>
Consultation	<ul style="list-style-type: none"><li>• Consultation with affected parties, experts, and the public.</li></ul>
Approval	<ul style="list-style-type: none"><li>• Approval of the privatisation programme by the Cabinet.</li><li>• Submission of the programme to the National Assembly for ratification.</li></ul>
Ratification	<ul style="list-style-type: none"><li>• National Assembly ratification of the programme within sixty days.</li></ul>
Publication	<ul style="list-style-type: none"><li>• Publication of the ratified privatisation programme in the Kenya Gazette.</li></ul>
Implementation	<ul style="list-style-type: none"><li>• Implementation of the programme by the Authority.</li><li>• Preparation of a privatisation proposal for each entity.</li><li>• Approval of privatisation proposal by the Cabinet.</li><li>• Implementation of the finalised privatisation according to the approved method.</li></ul>

# Execution of Privatization Agreement

## (Part V, The Privatisation Act, 2023)

- ❖ The execution of a privatisation agreement is not binding unless it is executed by the registered owner of the shares and countersigned by the Cabinet Secretary.
- ❖ The agreement to give effect to a privatisation cannot be signed until the period for filing an objection has lapsed.
- ❖ If an objection or appeal has been lodged, the agreement cannot be executed until a determination has been made, and the time for filing a notice of appeal has expired.
- ❖ If a proposed privatisation may result in an unregulated monopoly, the Authority must ensure that the agreement provides for the regulation of the monopoly and seek approval from the Cabinet Secretary.
- ❖ After an agreement becomes binding, the Authority must promptly publish a notice of the privatisation in the Kenya Gazette, specifying the entity being privatised, a summary of the transaction, and the names and addresses of the persons to whom the shareholding is being transferred (except for privatisations through initial public offer of shares), among other relevant information.

# Proceeds of Privatization

## (Part VI, The Privatisation Act, 2023)

- Proceeds from the sale of a direct National Government shareholding must be paid into the Consolidated Fund.
- Proceeds from the sale of a public entity's shareholding must be deposited in a special interest-bearing account established for that entity's privatisation.
- The purpose of the special account is to protect the erosion of the balance sheet of the public entity.
- The proceeds from the special account must be credited into the Consolidated Fund Account within ninety days.

# Methods of Privatization (Second Schedule; The Privatisation Act, 2023)

## 1. Initial Public Offering (IPO) of Shares

- Offering of shares in accordance with the Capital Markets Act, Cap 485A.

## 2. Sale of Shares by Public Tendering

- **Invitation of Expression of Interest (EOI's)** through a notice specifying entity details, eligibility, submission details, timelines, and other relevant information., Advertising the EOI notice in the Government tenders' portal, or on the Authority's website, and in at least two newspapers of nationwide circulation,
- **Evaluation of EOIs by a technical committee based on set procedures and criteria**, Shortlisting of qualified persons and issuance of Request for Proposal (RFP), Submission of proposals by shortlisted persons within a specified timeframe, Evaluation of proposals by a technical committee based on set procedures and criteria.
- **Selection of the successful proposal based on the highest ranked bidder, subject to the reserve price.**
- Submission of a detailed report to the Board for approval.
- Notification to the successful and unsuccessful tenderers.

## 3. Sale Resulting from the Exercise of Pre-emptive Rights

- Sale undertaken according to the procedure specified in the entity's constituting instruments.
- Application of relevant laws if the constituting instruments do not provide a procedure for exercising and selling pre-emptive rights.

# State of Play

# State of Play: 2023 Privatization Plan

No.	Entity	Brief Description
1	Kenya Literature Bureau (KLB)	State Corporation established by the Kenya Literature Bureau Act of Parliament Cap 209 of 1980.
2	National Oil Corporation of Kenya (NOCK)	Government-owned enterprise with dual mandate of oil & gas upstream and downstream operations.
3	Kenya Seed Company Limited (KSC)	State corporation majority owned by Agricultural Development Corporation.
4	Kenyatta International Convention Centre (KICC)	Government-owned enterprise under the Tourism Act 2011. Good financial performance but receives Exchequer support.
5	Mwea Rice Mills Ltd (MRM)	Subsidiary of the National Irrigation Authority. Operates as the main rice mill at Mwea Irrigation Scheme.
6	Western Kenya Rice Mills Ltd (WKRM)	Jointly owned by NIA and Western Kenya schemes Rice Farmers. Processes and markets milled white rice mainly from Western Kenya Schemes.
7	Kenya Pipeline Company Limited (KPC)	Wholly owned by GoK. Established under the Companies Act in 1973. Monopoly in gas and refined white oil product pipeline transportation.
8	New Kenya Cooperative Creameries Limited (NKCC)	Wholly owned by GoK. Established under the Companies Act in 2004. Plays strategic roles in milk off-take, price stabilization, and strategic milk reserves.
9	Numerical Machining Complex Limited (NMC)	State corporation jointly owned by Kenya Railways Corporations and Kenya Shipyards Limited.
10	Vehicle Manufacturers Limited (KVM)	Incorporated as Leyland Kenya Limited in 1974, changed name to Kenya Vehicle Manufacturers in 1989. Originally designed for commercial vehicle body buildings, diversified to buses and trucks.
11	Rivatex East Africa Limited (REAL)	Wholly owned by GoK through Moi University. Textile manufacturing, training, research, and extension.

# State of Play: National Treasury's Budget Policy Statement

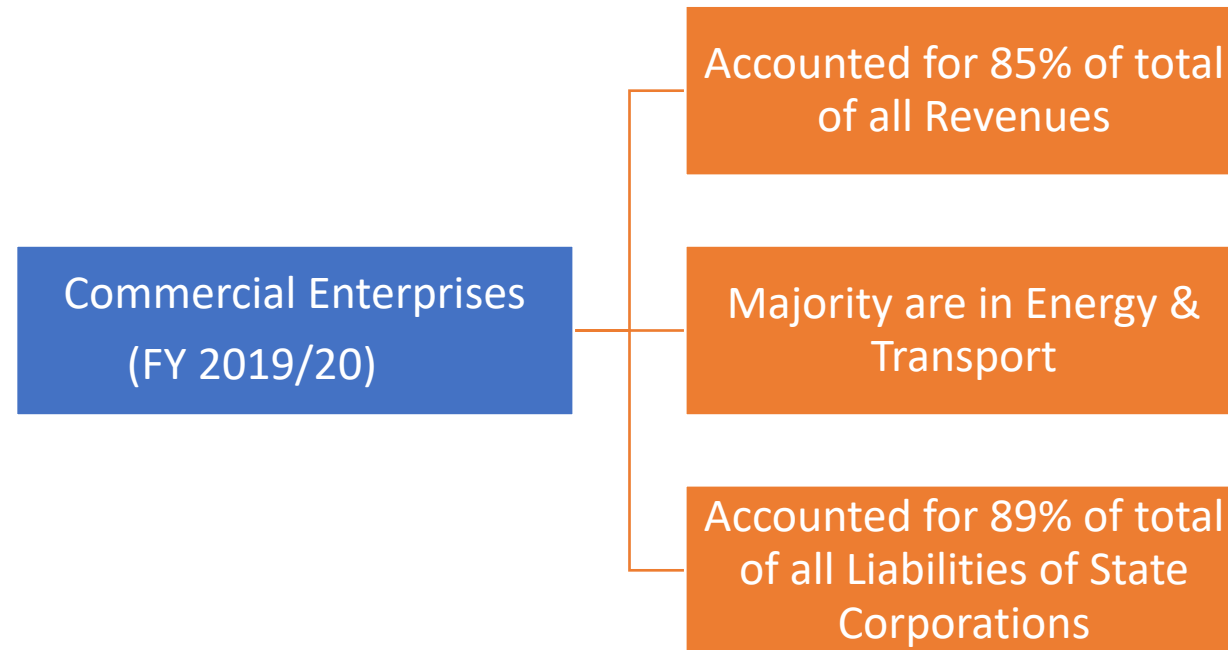
## Fiscal Risk Analysis of Government Owned Entities (GOEs)/State Corporations

1. In FY 2021/2022, a sample of eighteen major GOEs was analysed for fiscal risk exposure. The analysis revealed liquidity challenges due to unfavourable revenue and economic performance. Fourteen GOEs were found to have accumulated significant arrears/pending bills, posing high implicit risk to the Government.
2. For the 2023/2024 FY, the National Treasury is evaluating fifty GOEs using their 2022/2023 audited financial statements. The assessment aims to report fiscal risks to the Fiscal Risks Committee by June 2024, using a customized IMF Health Check tool in the Government Investments Management Information System (GIMIS).
3. Debt-stricken GOEs pose potential fiscal risks.
4. As of June 30, 2023, the National Treasury had guaranteed loans for three entities totalling approximately Ksh 170.229 billion, including loans for Kenya Airways resulting from novation of the Company's loans taken over by the Government.
5. Total undischarged GoK loans to GOEs were Ksh 961.683 billion by the end of FY 2022/23, compared to Ksh 916.762 billion in FY 2021/22. Commercial loans borrowed by GOEs amounted to Ksh 105.523 billion in FY 2022/23.
6. Pending bills among state corporations were high, with records showing Ksh 443.596 billion as at June 30, 2023. Major components of pending bills include unpaid contractors' fees for capital projects, undischarged tax obligations, and unremitted employer pension contributions.



# NT Assessment of Fiscal Risks Arising from the State Corporations

- State Corporations= 248
  - Commercial Enterprises: 46
  - Non Commercial Enterprises: 201



- Fiscal Risk concentration: Few State Corporations

# Conclusion

- Financial Risks due to Government Owned Entities (especially Commercial Enterprises are crystallizing
- Privatization without more focus on Commercial enterprises will not provide any meaningful fiscal relief
- Pending Bills out SC's are significant and play a bigger role in growth of NPLs