

**PUBLIC PRIVATE PARTNERSHIPS BY LOCAL
AUTHORITIES IN KENYA: LEGAL AND POLICY LESSONS
FOR COUNTY GOVERNMENTS**

**A THESIS SUBMITTED IN PARTIAL FULFILLMENT OF THE
REQUIREMENTS OF THE MASTER OF LAWS (LL.M)
DEGREE IN PUBLIC FINANCE AND FINANCIAL SERVICES
LAW**

BY

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G62/77809/2009

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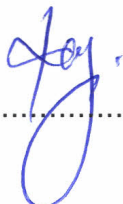


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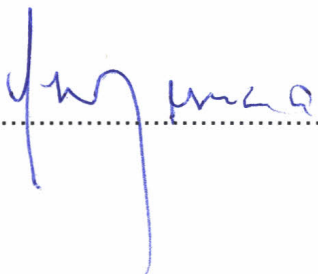
Dated at Nairobi this 15th day of November 2011

Signed.....



Supervised by Professor Albert Mumma

Signed.....



DEDICATION

I dedicate this thesis to:

*God Almighty: my everlasting Father for giving me the
opportunity to undertake this course;*

To Jesus Christ my Saviour for the never failing grace;

and

The Holy Spirit, my ever present Help.

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ABBREVIATIONS AND ACRONYMS

1. CBD.....Central Business District
2. BOI.....Board of Investments
3. IDA.....International Development Association
4. LA.....Local Authority
5. LASDAP.....Local Authority Service Delivery Action Plan
6. LATF.....Local Authority Transfer Fund
7. MBK.....Maji Bora Kibera
8. MDG.....Millenium Development Goals
9. MIGA.....Multilateral Investment Guarantee Agency
10. UK.....United Kingdom
11. UN.....United Kingdom
12. UNCITRAL..... United Nations Commission on International Trade Law
13. UNGAUnited Nations General Assembly
14. UNECE.....United Nations Economic Commission for Europe
15. USA.....United States of America
16. NGO.....Non-Governmental Organization
17. NRW.....Non-Revenue Water
18. NWSC.....Nairobi City Water and Sewerage Company
19. PPDA.....Public Procurement and Disposals Act
20. PPP.....Public Private Partnership
21. PPIAFPublic Private Infrastructure Advisory Facility
22. RVR.....Rift Valley Railways
23. TFDG.....Task Force on Devolved Governments
24. TISA.....The Institute for Social Accountability
25. PRG.....Partial Risk Guarantees (s)

PUBLIC PRIVATE PARTNERSHIPS BY LOCAL AUTHORITIES IN KENYA: LEGAL AND POLICY LESSONS FOR COUNTY GOVERNMENTS

CHAPTER ONE: PROJECT PROPOSAL

1. BACKGROUND AND INTRODUCTION TO THE STUDY

Public Private Partnerships (herein after referred to as PPPs) are widely becoming modes of service delivery both in Kenya and around the world. Governments are increasingly turning to the private sector for the delivery of infrastructure services. The United Nations Economic Council for Europe (UNECE) has acknowledged that PPPs in the delivery of public service have become a phenomenon which is spreading in the globe and generating great interest.¹

In general terms, a PPP means an institutional relationship between the state and the private for-profit and/or the private not for-profit sector, where the different public and private sector actors jointly participate in defining the objectives, the methods and the implementation of co-operation in development.² PPPs are thus arrangements between the government or government agencies and private sector entities for the purposes of providing public infrastructure, community facilities and related services.

Local Authorities in Kenya (LAs) and especially the City Council of Nairobi and the Mombasa Municipality have in the recent past embraced PPPs and have partnered with private entities in provision of services.

Research has however shown that implementation of PPPs by LAs in Kenya has been done without proper appreciation of the nature of PPPs resulting into challenges to the PPPs with adverse effects to the private actors and the public as well, being the consumers of the services and works. Francis Fukuyama has observed that "while privatization involves a reduction in the scope of state functions, it requires functioning markets and high degree of state capacity and commitment to implement"³

LAs in Kenya have also been subjected to in-appropriate legal and regulatory framework and inability to efficiently provide services and poor governance and this contributed to their inability to successfully implement PPPs. It is said that most

¹ United Nations Economic Council for Europe: ' Guide Book on Promoting Good Governance in PPPs' (2008) http://www.undp.ro/download/UNECE_ppp.pdf accessed 15th May 2011.

² D. O Ongolo 'Public Private Partnerships in Kenya' prepared for The Institute of Economic Affairs, Kenya (7th July 2006) at 9. www.ieakenya.or.ke/documents/Public%20Private%20Partnerships.pdf accessed on 20th June 2010.

³ Francis Fukuyama: *State-Building, Governance and World Order in the Twenty First Century* (London: Profile Books, 2004) 24-25.

cities and urban centers that operate under the auspices of LAs can hardly provide services as mandated by the Local Government Act, Chapter 265 of the Laws of Kenya.⁴

There was no legal framework governing PPPs as well as privatization and public procurement generally in Kenya prior to 2005. There are now two pieces of legislation governing PPPs in Kenya; the Privatization Act, 2005, the Public Procurement and Disposals Act, 2005 (PPDA) and the Regulations made thereunder.

Notwithstanding the presence of the legal framework governing PPPs, a study of the some of the PPPs in LAs as indicated above reveals several issues arising out of use of PPPs by LAs which this thesis will seek to identify analyze and recommend solutions for benefit of county governments.

The dominant feature identified is that councils within LAs are not willing to be bound by PPPs entered by their predecessors after change of administration following civic elections and have taken steps to annul them or have declined to be bound and have sometimes allegedly committed breaches of the provisions of the contracts governing the PPPs. This is one of the indicators of political risks arising from PPPs which will form the backbone of this study.

The trend to challenge PPPs after succession in office has not been identified in central government, line ministries or parastatals that have partnered with private actors under the PPP mechanism. We have not seen reluctance by these bodies to implement PPPs when there is a succession of office either through general elections, by-elections or a change of the board members for state corporations or line ministries. We will in chapter 3 of this study briefly analyze the privatization of Kenya Airways Limited (KQ) and the RVR Concession with the governments of Kenya and Uganda relating to the Kenya- Uganda Railway to demonstrate the above position. In this regard, we will show that the respective national governments have taken deliberate steps to shield the private actors from the effects of political risks arising out of PPPs.

The issues thus arising for investigation in this study are:

1. The LA's Council's adherence to the principle of corporate personality and perpetual succession of LAs.
2. The general sanctity and succession of contracts and its import on PPPs by LAs in Kenya.

⁴ Task Force on Devolved Governments(Kenya), *Interim Report nterim Report on Devolved Governments*, (April 20 2011).
[http://www.communication.go.ke/documents/INTERIM%20REPORT ON DEVOLVED GOVERNME
NT.pdf](http://www.communication.go.ke/documents/INTERIM%20REPORT%20ON%20DEVOLVED%20GOVERNMENTS.pdf) accessed 16th May 2011 at 49

3. The appropriateness of current PPPs legislation in dealing with political risks arising from PPPs by LAs in Kenya.

The Task Force on Devolved Government (TFDG) established under the Ministry of Local Government in October 2010 has recognized the role of PPPs as one of the mechanisms to be adopted by County Governments in performing their functions. The TFDG has stated that PPPs are amongst other approaches for development and financing of County Governments.⁵ Devolution of government must be accompanied by sufficient resources and mechanisms for purposes of service delivery.⁶ The setting up of county government infrastructure is expected to cost the exchequer immensely. The county governments will certainly not be able to finance the county government infrastructure and that is how PPPs will come into play. Most of the functions and powers bestowed upon county governments vide the 4th schedule to the Constitution currently being undertaken by Local Authorities (LAs).

The provision of some of these functions are enormously capital intensive. There is typically a one –off capital outlay followed by ongoing maintenance costs of the assets.^{7 8} For instance the provision of water to a new urban housing development would represent a salient example of LAs and for that matter, county government's capital expenditure. It would usually include the costs of laying the pipe, lying down of pumping facilities and such like activities.

This study will seek to analyze the PPPs experience by LAs in Kenya with the intention of identifying existing challenges and corresponding lessons and proposing recommendations to be adopted by County Governments established under the current Constitution promulgated in 2010.

2 PROBLEM STATEMENT:

The use of PPPs by the Government of Kenya through agencies such as LAs is an emerging frontier that had prior to 2005, been unregulated under the law in Kenya. Notwithstanding the legal framework now in place, there exist legal and policy issues arising out of PPPs entered by LAs.

PPPs are an important vehicle that can be used by LAs to foster development of infrastructure and service delivery. These duties will in most part be performed by county governments established under the current Constitution. PPPs will thus form

⁵ *Supra* note 4 at 285 and 288

⁶ UN- Habitat, 'Local Democracy and Decentralization in East and Southern Africa: Experiences from Uganda, Kenya, Botswana, Tanzania and Ethiopia' www.unhabitat.org accessed on 3 August 2011.

⁷ Brian Dollery, 'Public Private Partnerships and Local Government Infrastructure' http://www.lgsa-plus.net.au/resources/documents/dollery-ppps-and-local-government-infrastructure_2005.pdf accessed 2nd August 2011.

a vital avenue for the county governments to perform their duties as set out in the Constitution.

An analysis of some of the notable PPPs entered by the major LAs reveals that the councils have not been willing to be bound by PPPs entered by their predecessors, after change of administration in general or by-elections.

The key legal and policy issue that will be the subject of this research will thus be whether the current PPPs legislation is sufficient to deal with the political risk arising from challenges by LAs of PPPs entered by their predecessors and whether there is sufficient protection under the law to secure the long-term nature of PPPs.

3 JUSTIFICATION FOR THE STUDY

There are two main justifications for this study. Firstly, PPPs are important vehicles that have increasingly been used by LAs in Kenya order to achieve efficient service delivery and infrastructural development. The Government of Kenya has recognized the benefits arising from PPPs and as such there is a proposal to use PPPs as one of the vehicles for the implementation of Vision 2030.⁹ The Local Government structure is to be revamped with the coming into effect of the Constitution in 2010 and most of the functions being carried out by LAs will be taken over by County Governments. The TFDG has identified the use of PPPs as one of the ways county governments will perform their infrastructural duties. There is therefore need to study this emerging frontier and identify the issues arising as well as propose the way forward in order for LAs and county governments to effectively and efficiently use PPPs without adverse effects to the private sector.

Secondly, prior to 2005, PPPs in Kenya were generally unregulated under the law. Notwithstanding the legal framework now in place, there are legal and policy issues arising out of PPPs entered by LAs. This therefore raises the question of whether current the legal framework is appropriate to govern PPPs by LAs. The main underlying legal issue will be the challenge by council's of PPPs entered by their predecessors after a change of office in elections. This study will thus justified on there being a need to address the adequacy and appropriateness of the current regulatory and legal framework to deal with political risks in PPPs by LAs and recommend ways of dealing with this issues so as to avoid county governments being faced by the same problem.

⁹ See www.vision2030.go.ke accessed 22nd August 2011

4. THEORETICAL AND CONCEPTUAL FRAMEWORK

a. Theoretical framework of the study: The legal personalities in law and their inter play with binding nature and sanctity of contracts

In view of the unique problems identified from LAs in Kenya to the effect that councils have been shown to be un-willing to be bound by PPPs entered into by their predecessors, the theoretical framework underlying this study will be based on the legal personality and perpetuity of corporate bodies and their nature as separate legal entities from their members and the interplay with the binding nature and sanctity of contracts.

i. Legal personalities in law

There are three types of legal entities: natural persons (that is individuals), corporations and bodies politic.¹⁰¹¹ The last two categories are further grouped into the class of "artificial persons" and one of their common features is that they are created and dissolved by legislative and administrative fiat.¹²

A natural person is someone who is born, lives and dies according to natural processes. The context of this discourse necessitates the focus on the attributes of bodies corporate and bodies politic and not natural persons *per se*.

Bodies politic according to Seddon include the various level of government (except LAs which are incorporated under local government legislation) and foreign governments¹³. The national government and the county governments in Kenya would thus fall within the definition of bodies politic.

A government, which is a body politic, is in many ways like a corporation and each government is governed by a constitution which directly or indirectly provides for perpetual succession of such bodies.¹⁴ Since the continuity of a body politic as well as corporations is indefinite, they are said to be capable of perpetual succession and thus have attributes of a corporate entity. As such, governments must necessarily act through natural persons, either individuals as the president, ministers or through arms of governments that is the executive, the judiciary the parliament, but they take independent status separate from the natural persons.¹⁵ Natural persons supply the thoughts and actions necessary for the continued operations of bodies corporate and

¹⁰ Nicholas Seddon, *Government Contracts: Federal, State and Local* (Federation Press 2004) at 135

¹¹ This categorization is only true for domestic purposes as there are other entities such as the UN bodies in the international arena.

¹² Seddon *supra* note 10

¹³ Seddon *supra* note 10 at 135

¹⁴ Seddon *supra* note 10 at 139

¹⁵ *ibid*

politics. As such, in the context of bodies politic, perpetual succession implies an arrangement to elect or appoint natural persons to provide the continuity despite losses of persons occasioned by retirement, death or change of office. The bodies corporate must as of necessity act through natural persons comprising of the organs of the company that is the members, the individual directors and the board of directors but the companies are separate and distinct legal persons from the natural persons.

When it comes to corporations, it is trite law that a body corporate is separate from its officials and members and thus has perpetual succession notwithstanding a change of officials or shareholders unless wound up in accordance with the provisions of the law. It is as Lord Macnaghten observed¹⁶ “a different person altogether from the subscribers to the memorandum of association” and as Lord Selborne said “a mere abstraction of law”.¹⁷ As such, the fundamental attribute of an incorporated company is that it is a legal entity distinct from its members and is capable of enjoying rights and of being subject to duties which are not the same as those enjoyed or borne by its members.¹⁸ It is in effect a metaphysical entity or a fiction in law with legal but no physical existence.¹⁹

Once properly incorporated, a company is regarded as an autonomous legal person in its own right, capable of owning property, bearing rights and obligations and existing independently from its original incorporators and the controlling minds who operate its business at any particular time.

This principle of the separate legal nature of bodies corporate and especially companies has been recognized since the celebrated case of *Salomon v Salomon & Company Limited*²⁰ and has been applied in myriad of cases in England, commonwealth jurisdictions including Kenya and other jurisdictions.

As per Lord Macnaghten in *Salomon v Salomon & Company Limited* “The company is at law a different person altogether from the subscribers ... and though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive profits, the company is not in law the agent if the subscribers or trustee for them. Nor are the subscribers as members liable, in any shape or form, except to the extent and in the manner provided by the Act.”²¹

¹⁶ *Salomon v Salomon* [1897] AC 22 at 51

¹⁷ *G. E Ry v Turner* (1872) LR 8 Ch 149 at 152

¹⁸ Clive M Schmittotoff and James H. Thompson: *Palmer's Company Law* (21st edn, Stevens and Sons Limited 1968) at 124

¹⁹ *ibid*

²⁰ [1897]AC 22

²¹ At p 51.

The corporate veil of incorporation can only be lifted in limited situations but the same are not within the scope of this study.²²

The concept of separate legal personality in company law has been recognized and codified in a number of other statutes relating to governments, government agencies, societies, as well as non-governmental organizations.

Section 2 of the Local Government Act²³ establishing the City Council of Nairobi provides that any reference to any written law to a municipality or a municipal council shall be construed as including a reference to the City Council of Nairobi. Section 12 of the said Act provides that every municipal council shall be a body corporate with perpetual succession and a common seal and shall be capable in law of suing and being sued. Similar provisions relating to county councils and urban councils are found in sections 28 and 21 of the Act.

In the same manner as a company acts through natural persons comprising of shareholders and members, directors and the Board of Directors to provide continuity, LAs perform their functions through natural persons comprising of councilors, the Mayor, Chairman Town Clerk as well as Committees who are separate and distinct from the LAs.

An LA has both a political and an administrative arm. The political arm is made up of elected and nominated councillors. The political arm of a local authority (which is called "the council") conducts its business through a committee system. At the apex of a local authority's governing structure is the 'full council'. This is the governing body. The full council is made up of all the councillors in a local authority. The full council is headed by a chairman (in the case of a county or town council) or a mayor (in the case of a city and municipal council). The chairman or mayor and their deputies are elected biannually by all the councillors from among themselves.²⁴

The same principle of separate corporate entity also finds recognition in the Trustees (Perpetual Succession) Act²⁵ under which trustees who have been appointed by anybody or association of persons established for any religious, educational, literary, scientific, social, athletic or charitable purpose, or who have constituted themselves for any such purpose, or the trustees of a pension fund may apply to the Minister in

²² See for example *Gilford Motor Company v Horne* [1933] Ch 93 (CA) at 95 where Lord Keith of Kinkel (with whom Lord Wilberforce, Lord Fraser and Lord Russell agreed) stated "*it is appropriate to pierce the corporate veil only where special circumstances exist indicating that it (the company) is a mere facade concealing the true facts*"

²³ Chapter 265 of the Laws of Kenya

²⁴ See sections 14, 15 29 and 30 of the Local Government Act.

²⁵ Chapter 164 of the Laws of Kenya

the manner provided the Act for a certificate of incorporation of the trustees as a corporate body. Upon incorporation as a body corporate, the trustees shall become a body corporate and shall have perpetual succession and a common seal, and power to sue and be sued in their corporate name.²⁶

The Government Contracts Act²⁷ has no express provision on perpetual succession of government and/or the separate legal entity but the same is implied by section 6 of the Act which provides that no public officer shall be liable to be to be sued personally upon any contract which he makes in that capacity unless he expressly pledges personal security. This section thus clearly sets out that the government is a separate legal entity from its officials.

This project will thus analyse the legal personalities of LAs and find out whether, by challenging the PPPs entered by their predecessors, the councils appreciate the separate and distinct legal personality and perpetual succession of the LAs as enshrined in the Act.

ii. Binding nature and sanctity of contracts

Section 2 of the Law of Contracts Act,²⁸ provides that “ save as may be provided by any written law for the time being in force, the common law of England relating to contract, as modified by the doctrines of equity, by the Acts of Parliament of the United Kingdom applicable by virtue of subsection (2) of this section and by the Acts of Parliament of the United Kingdom specified in the Schedule to this Act, to the extent and subject to the modifications mentioned in the said Schedule, shall extend and apply to Kenya.”

This section thus provides for the application of the English Common Law to contracts in Kenya.

There are a number of norms of English law of contract of a generality pervasiveness and importance to have attracted the designation of principle.²⁹ A number of legal norms could be advanced as included within the category of principle, including the principle of privity of contracts, the principle of objectivity in agreement and the principles of contractual interpretation.³⁰ However two linked principles remain of central importance, viz , the principles of freedom of contract and the binding force of contract (sanctity of contracts).³¹ Few rules for the ordering of society have such a deep legal, moral and even religious influence as the principle

²⁶ Section 3(3) of the Trustees (Perpetual Succession) Act.

²⁷ Chapter 25 of the Laws of Kenya

²⁸ Chapter 23 of the Laws of Kenya

²⁹ Joseph Chitty , H.G Beale *Chitty on Contracts*, 21st Edition Common Law Library , Sweet & Maxwell [2004] at 10

³⁰ *ibid*

³¹ *Ibid*

of the sanctity of contracts: *Pacta sunt servanda* translated to mean "Promises must be kept".³²

The rule posits that parties to a contract must hold fast to their promises, since no security and no commerce would otherwise be possible between parties. A valid and binding contract creates, for nations and individuals alike, the complete right to demand from the other party the performance of the contract, so long as the contracting party, on his side, has performed satisfactorily his obligations. It is thus right to hold that the source of contracts is the common will of the contracting parties and thus the rule of sanctity of contracts which entitles a party to compensation.

It has been said that one can scarcely disagree with the view that a contract in itself creates a right only through the union of wills (*duorum vel plurium in idem consensus*) and thus only for so long as this union exists.³³ In ancient times this principle was fortified by the justification under the "will theory" of contract under which parties were held to be the best judges of their own interests, and if they freely and voluntarily entered into a contract, the only function of the law was to enforce it.

³⁴

In those ancient times, this principle was developed in the East by the Chaldeans, the Egyptians and the Chinese in a noteworthy way. According to the view of these peoples, the national gods of each party took part in the formation of the contract.³⁵ The gods were, so to speak, the guarantors of the contract and they threatened to intervene against the party guilty of a breach of contract.³⁶ So it came to be that the making of a contract was bound up in solemn religious formulas and that a cult of contracts actually developed.³⁷ By these two principles, English law has expressed its attachment to a general vision of contract as a free expression of the choices of the parties which must be given effect by the law.

Christianity exercised a great influence on the sanctity of contracts. Its basic idea demanded that one's word be kept, as is clearly expressed in the Gospel according to St. Matthew, in particular, where it is said, at Chapter 5, Verses 33 to 37, at the end: "But let your communication be, Yea, yea; Nay, nay: for whatsoever is more than these cometh of evil." For the Islamic peoples, the principle, *Pacta sunt servanda*, has also a religious basis: "Muslims must abide by their stipulations." This

³² Wehberg Hans, ' *Pacta Sunt Servanda*', *American Journal of International Law* Vol 53, No. 4 (October 1959) 775- 786.

³³ *Ibid* at 781

³⁴ Chitty *supra* note 29

³⁵ Wehberg Hans *supra* note 32 at 781

³⁶ *ibid*

³⁷ *ibid*

is clearly expressed by the Koran in many places, for example, where it is said: "*Be you true to the obligations which you have undertaken. . . . Your obligations which you have taken in the sight of Allah. . . . For Allah is your Witness*"³⁸

As such, the principle of *Pacta sunt servanda* has its basic roots from natural law. Thomas Hobbes (1588-1679), the English philosopher of utilitarianism, in particular in his *Leviathan*, recognized as natural law the principle that agreements are to be kept and that the concept of wrong arises out of the non-performance of a contract, the promisor being therefore in contradiction with himself.³⁹⁴⁰

The principle of "*pacta sunt servanda*", in its most common sense refers to private contracts, stressing that clauses contained in them are law between the parties, and implying that non-fulfillment of respective obligations is a breach of the pact.⁴¹

Certainly, the phrase *Pacta sunt servanda*, in the first instance, had a religious origin as has been shown above. With time, however, it was integrated into international law, and it can now be described as a part of customary international law.

Pacta sunt servanda essentially is the basic norm of all international law and has been codified by Article 26 of the Vienna Convention on the Law of Treaties which provides that "every treaty in force is binding upon the parties to it and must be performed by them in good faith" The law of nations is built less upon customary law than upon contracts essentially.⁴²

If a contract, validly concluded, were not binding, then international law would be deprived of a decisive foundation and a society of states would not longer be possible.⁴³ International law, and with it also the sanctity of contracts, results by a natural necessity from the inevitability of social intercourse. The binding force of contracts is an obligation which exists, not only *vis-à-vis* the contracting parties, but also *vis-à-vis* the international community as a whole.⁴⁴ We shall concern ourselves no further with the general foundations of international law, as such a discussion would go beyond the framework of the present study. It is however important to set out the general basis of the sanctity of contracts.

³⁸ *ibid*

³⁹ As quoted by Wehberg *supra* note 32 at 779

⁴⁰ However, also according to Hobbes, agreements need not be kept if the security of the state so requires.

⁴¹ Asanga Gunawansa, 'The Legal Consequences of Breach of Government Undertakings to Investors' (Dauphine University Paris 2010) http://www.rics.org/site/download_feed.aspx?fileID=8043&fileExtension=PDF accessed 30th August 2011

⁴² Wehberg *Supra* note 32 at 783.

⁴³ *ibid*

⁴⁴ *ibid*

The principle of sanctity of contract and the related principle freedom of contract applied in the international arena as the doctrine of *Pacta sunt servanda* form the corner stone of modern contract law. The principle of the binding force of contract is a concomitant of the doctrine of freedom of contract, a force which a classical Roman Jurist compared it to the binding force of law itself.⁴⁵

It is well-accepted that individuals are free to determine their own affairs, decide who to contract with and on what terms. Lord Diplock thus observed that “the basic principle of the common law of contract is that parties are to determine for themselves what primary obligations they will accept.”⁴⁶

Once a contract has been lawfully formed, it is binding upon the parties. They are under a duty to perform their obligations under the contract, but also have the right to demand performance from the other party. The parties are bound by the terms of the contract and may not unilaterally modify them or cancel the contract. A party that fails to perform its obligations under the contract will be held liable, unless the non-performance is excused.

This position remains particularly strong and important in commercial contexts such as in PPPs. In this regard it has been said that “legal policy favours the furtherance of trade...commercial men must be given the utmost liberty of contracting”⁴⁷.

The doctrine is not however absolute and is thus subjected to exceptions such as illegality.

Concerning succession of contracts, the general rule is that contracts entered by a natural person abates upon the death or loss the person’s capacity to contract. A cause of action founded on contract can only be sustained if the cause of action survives the death of a person.⁴⁸

Contracts by companies remain binding at all times provided they are not *ultra vires* the objects of the company.⁴⁹

It was thus observed by Lindley L. J in the case of *Farrar v Farrar Ltd*⁵⁰ that:

⁴⁵ D. 16..3.1.6; D 50.17.23 as cited by Chitty *supra* note 29 at 14

⁴⁶ *Photo Production Ltd v Securicor Transport Company Ltd* [1980] AC. 827 at 848.

⁴⁷ *Homburg Houtimport B. V v Agrosin Private Company Limited (The Starsin)* UKHL: [2003] 3 W.L.R 711 at [57]

⁴⁸ See for instance Order 24 rule 1 of the Civil Procedure Rules 2010.

⁴⁹ Clive M Schmittohoff and James H. Thompson *supra* note 18 at 128

⁵⁰ (1888) 40 Ch. D 395

“A sale of property of the company to one of its members is not, either in form or substance, a sale by a person to himself. To hold that it is, would be to ignore the principle which lies at the root of the legal idea of a corporate body, and that idea is that the corporate body is distinct from the person composing it. A sale by a member of a corporation is in every sense a sale valid in equity as well as at law”

With respect to body politics, it has been stated that a contract entered into by one administration cannot be repudiated by succeeding administration just simply on the basis that it was made by the previous administration.⁵¹ The repudiation of subsisting agreements by a new administration can seldom be ventured with great success.⁵²

In view of the perpetual existence and distinct legal nature corporate entities and bodies politics, contracts entered by companies or government bodies such as LAs bind the bodies notwithstanding change of administration. The contracts entered by the companies of bodies politic are separate from the natural persons through which the bodies operate.

5. OBJECTIVES OF THE STUDY

1. To investigate why LAs' councils been challenging PPPs entered by their predecessors after a change of administration following civic elections.
2. To investigate the appropriateness of the current PPPs legislation in Kenya in safeguarding private actors against political risks arising from PPPs entered by LAs.
3. To propose appropriate legal and policy reforms that should inform the use of PPPs by the county governments in Kenya in order to deal with the problem of political risks.

6. HYPOTHESIS

1. The law regulating PPPs has not been appropriate to deal with challenges to PPPs by successive councils in LAs
2. There is need for legal and regulatory reform to deal with political risk arising from PPPs by LAs.

⁵¹ Seddon *supra* note 10

⁵² *New South Wales v Burdoph* (1934) 53 CLR 455 at 463 (Evatt J) as cited by Seddon *ibid* at 139.

7. RESEARCH ISSUES

1. Why have LAs' councils been challenging PPPs entered by their predecessors after a change of office elections?
2. Are the PPPs legislation in Kenya appropriate to safeguard private actors against political risks arising from PPPs entered by LAs?
3. What can be learnt from the use of PPPs by LAs to aid use of PPPs by county governments?

8. METHODOLOGY

Research will be through:

- Primary sources such as books, relevant laws and applicable international instruments.
- Secondary sources including articles from journals and online resources.
- Field research including interviews and consultations with key informants such as officials from the Public Procurement Oversight Authority, Ministry of Local Government, Task Force on Devolved Government and specialists in the field of government investments as well as officials from the City Council of Nairobi and Municipal Council of Mombasa and proprietors/directors of entities that have partnered with LAs in PPPs.

9. LITERATURE REVIEW

This thesis's motivation is that while much has been written by economists and political scientist on the subject of privatization in Kenya, authors and particularly lawyers have not said much on PPPs by local LAs in Kenya and analyzed any arising legal problems.

The explanation for this dearth of legal analysis of PPPs by LAs may have several aspects. It is said that the main reason why LAs have been neglected in developing countries both factually and by literature is that strong central governments have not always been willing to share power and resources.⁵³ It is therefore not surprising that devolution was strongly advocated leading to its adoption in the current constitution in Kenya.

⁵³ UN- Habitat *supra* note 6 at 15.

The other explanation for the lack of legal analysis of privatization (which is a related concept to PPPs) has been due to the fact that the phenomenon and discourse of privatization has been and continues to be dominated by economists, whose concerns have been primarily revolved around the questions of economic efficiency and not the relation to the normative aspects of PPPs.⁵⁴

Of significance to this study is that there has been no exclusive study that has been carried out any normative issues arising from political risks in Kenya and its neighbouring countries and even generally in Africa. There is however literature written on the basis of experiences from other jurisdictions mainly from the western world touching on this issue.

For instance **Perotti, Enrico C & van Oijen, Pieter** who are authors from the Netherlands in an article, 'Privatization, political risk and stock market development in emerging economies'⁵⁵ investigate whether privatization in emerging economies has a significant indirect effect on local stock market development through the resolution of political risk. The authors argue that a sustained privatization program represents a major political test that gradually resolves uncertainty over political commitment to a market-oriented policy as well as to regulatory and private property rights. In this regard, they present evidence suggesting that progress in privatization is indeed correlated with improvements in perceived political risk. Their analysis further shows that changes in political risk in general tend to have a strong effect on local stock market development and excess returns in emerging economies. They conclude that the resolution of political risk resulting from successful privatization has been an important source for the rapid growth of stock markets and the economy in general in emerging economies

US based authors **Najja Bracey and Sonia Moldovan** in 'Public Private Partnerships: Risks to the Public and the Private Sector'⁵⁶ point out that political risk can arise from changes in government, changes in public policy, corruption and favouritism, lack of sanctity of contract, and arbitration difficulties.⁵⁷

Of particular significance to this study is the fact that the two authors have identified the fact that the political risk resulting from frequent changes in government can lead

⁵⁴ Migai Akech *Privatization and Democracy in East Africa: The Promise of Administrative Law* (East African Educational Publishers Limited, 2009) at 1

⁵⁵ Perotti, Enrico C & van Oijen, Pieter, 'Privatization, political risk and stock market development in emerging economies' (2001) *Journal of International Money and Finance*, Elsevier, vol 20 (1) pages 43-69 (February).

⁵⁶ Najja Bracey and Sonia Moldovan, 'Public Private Partnerships: Risks to the Public and the Private Sector' a paper presented under the auspices of the Louis Berger Group Incorporated, 6th Global Conference on Business and Economics (2006), www.louisberger.com at 4 accessed on 29th August 2011.

⁵⁷ *ibid*

to confusion, poor communication and poor exchange of information with a potential to creating the basis for withdrawal of support for PPPs entered by previous regimes.⁵⁸ An incoming government/administration may have a different opinion of the concessionaire than the outgoing government had, and thus, its perception or opinion of the project may change or they may prefer different actors for their own personal benefits.⁵⁹

Asanga Gunawansa another author who has written on political risks in PPPs identifies in 'The Legal Consequences of Breach of Government Undertakings to Investors'⁶⁰ points out that the relative stability of key investment conditions responsible for the economic and financial performance of an investment venture is at the heart of investor concerns when negotiating an investment contract with a public sector entity. It is particularly so for projects like PPPs where duration and risk exposure are long, capital investment is intensive, and project risk is acute.⁶¹ Therefore the extent to which the relevant public sector entity undertakes to protect the investment would be at the center of both the negotiation of a specific contractual regime and the proper design of a project structure.⁶² The author looks at this discourse in the context of PPPs in Sri Lanka and analyses the constitutional, legislative, regulatory and policy safeguards that have been in place by the Government of Sri Lanka to shield private actors in PPPs from the effects of political risks.

Closer home, there is literature on general issues arising from PPPs by government and/or government agencies in Kenya and in neighbouring countries, some of which will inform the research issues arising from the study herein. In this regard, **Prof. Migai Akech** in his book, *Privatization and Democracy in East Africa: The Promise of Administrative Law*,⁶³ focuses on democratization of the privatization processes in East Africa. Prof. Migai explores the role of democracy and public law in privatization processes in the three East African Countries of Kenya, Uganda and Tanzania. In particular, the book recommends the creation of strongly institutionalized Administrative Law frameworks to facilitate meaningful democratization of privatization processes in these countries. The book anticipates that such reforms would enhance the day-to-day accountability of and public participation in the privatization processes in the three countries. The book further seeks to contribute to

⁵⁸ *ibid* at 6

⁵⁹ *ibid*

⁶⁰ Asanga Gunawansa, 'The Legal Consequences of Breach of Government Undertakings to Investors'

(Dauphine University Paris 2010)

http://www.rics.org/site/download_feed.aspx?fileID=8043&fileExtension=PDF accessed 30th August 2011.

⁶¹ *ibid* at 9

⁶² *ibid*

⁶³ *ibid*

the study of the relationship between Public Law, markets and democracy in African Countries. Its particular contribution is the argument that privatizations can only be efficient fair, and legitimate if they are democratic, that is participatory and accountable.

Prof. Migai states that the processes of privatization typically involve the exercise of immense power, which can be unaccountable and can impact adversely on the liberties and livelihoods of citizens.⁶⁴ For example, privatization processes entail a power to decide which private entity will be favoured with the privilege of performing functions that were previously the domain of public agencies. It also confers upon such private entities power to decide which citizens will benefit from their services and the conditions under which such services will be offered.⁶⁵

Relating to Prof. Migai's book, this report will seek to present the argument that lack of democratic processes in PPPs by LAs has contributed to challenges by LAs' councils' of PPPs entered by their predecessors.

Harriet Naitore in the article *Study on Local Council Oversight Role and Social Accountability in Kenya*⁶⁶ examines the main aspects of local council oversight of elected councillors in planning, overseeing service delivery and their involvement in public financial management with a view of assessing the degree of their involvement in these processes (formally and informally) and the extent to which such involvement helps to reflect local preferences in the planning and implementation of their LA's activities and programmes.⁶⁷

In respect to the involvement of local councillors in the planning processes and public financial management, the study by Naitore has recognised *inter alia*, that decision -making power in local councils is vested in councillors corporately as the policymakers.⁶⁸ Councillors make decisions that guide development planning, priority setting, allocation and management of resources and the selection, implementation and monitoring of projects/programmes in the context of council committee and the full council deliberations.⁶⁹ The author observes that due to the structure of LAs, councillors have been known to make decisions that are pegged on personal rather than public interest.

⁶⁴ *Ibid* at 1

⁶⁵ *Ibid*.

⁶⁶ Harriet Naitore 'Study on Local Council Oversight Role and Social Accountability in Kenya ' prepared for the African Development Group (2008) www.siteresources.worldbank.org accessed 4th July 2011.

⁶⁷ *Ibid* at 45

⁶⁸ *Ibid*

⁶⁹ *ibid*

Naitore also points out that there is no legal provision for involving citizens in the decision-making process of a LA in the Local Government Act but also points out that under the provisions in the Local Authority Service Delivery Action Plan (LASDAP) Regulations and Guidelines, issued under the Local Authority Transfer Fund (LATF) Act, LAs are required to involve the community and other stakeholders in project identification, prioritization and monitoring of implementation.⁷⁰ Naitore states that the process has been faulted for not being comprehensive enough and all inclusive because the citizens and other stakeholders are not involved beyond the selection of projects/activities included in the resource envelope and the responsibility for identifying and inviting the stakeholders to the consultative forums remain just that.

In line with Naitore's study, this thesis will analyse the effect of the concillors decision making power on PPPs entered by LAs.

Wilfred Uronu in his article *Making Effective Private Public Partnership in Local Government*⁷¹ addresses general issues arising from PPPs by the local government in Tanzania. He addresses the reasons for the local government adopting PPPs, the criteria that can be used in determining the potentials of the local government entering into PPPs, the problems faced by the local government in entering into PPPs and recommended solutions and the benefits of stakeholder involvement in PPPs.

Uronu points out that the PPP mechanism is relevant for local government due to the limited budget and staff with enough technical skills, monitoring, designing and construction as well as management techniques that the private sector can bring in through partnership.⁷² He also avers that private sector involvement on the other hand can bring great improvement of quality and bring cost effectiveness, economic efficiency through operating performance and capital investment, access to capital market, directing subsidies to less served group and managerial expertise.⁷³

Uronu identifies several causes of problems in PPPs by the local government in Tanzania⁷⁴ which may aid the author in analysing the challenges to PPPs in Kenya. Uronu says that lack of specific goals of partnership can be a problem and recommends that to avoid unclear goals, the broad goal should be broken into more

⁷⁰ *Ibid* at 47

⁷¹ Wilfred Uronu " Making Effective Private Public Partnership in Local Government' *Research Journal of Social Sciences*, (2009)ISInet Publication 4: 57- 60

⁷² *Ibid* at 58

⁷³ *Ibid*

⁷⁴ *ibid*

specific goals to eliminate a room of some actors creating other goals for personal interest or for realizing hidden agenda.

Another problem according to Uronu may arise in sharing resources, cost and benefits and balance of powers. Thus it is important that social costs and benefits are shared by all partners. For the issue of balancing powers, it is important that there is a clear regulation on sharing of resources and benefits.

Ngowi, yet another author writing on the Tanzanian PPPs experience in LAs also touches on some aspects that will assist the author herein in recommending solutions to the challenges to PPPs in Kenya. Ngowi in his article *Public –Private Partenership in Service Delivery: Application, Reasons, Procedures, Results and Challenges in Tanzania Local Government Authorities*⁷⁵ argues that a number of challenges have arisen from use of PPPs by LAs in Tanzania due to the relative newness of PPPs in Tanzania.⁷⁶ Challenges include lack of proper understanding of the concept and its operationalisation by those in various positions in the public and private sector; lack of the needed support, commitment and endorsement by various stakeholders in a PPP arrangement, partly as a result lack of the needed readiness to change and depart from the orthodox ways of doing things.⁷⁷ All these challenges may lead to opposition in the use of the concept and where it is applied it may be wrongly applied hence failures.⁷⁸

⁷⁵ Ngowi: *Public –Private Partenership in Service Delivery: Application, Reasons, Procedures, Results and Challenges in Tanzania Local Government Authorities* www.unpan.un.org last accessed on 4th August 2011.

⁷⁶ *Ibid* at 33

⁷⁷ *ibid*

⁷⁸ *ibid*

10 CHAPTER BREAKDOWN

We have in chapter one introduced the study and set out its background. We have also explained the problem statement and set out the justification of the study. We have also set out the theoretical and conceptual framework, objectives of the study, hypothesis, research questions and the methodology of research. We have in the reviewed the literature relating to this study.

In Chapter two, shall discuss the nature and concept of PPPs and will in this regard set out its Key attributes connected to this study key among them will be the long term nature of PPPs. We will also analyze the interface between PPPs, privatization and procurement as the three components are related and sometimes intertwined service delivery mechanisms. We will then explain some of the main reasons for use of PPPs by government and government agencies and will finally set out the legal and regulatory framework for PPPs in Kenya.

In chapter three, we will analyze selected case studies of PPPs by LAs in Kenya with the main focus being placed on PPPs by the City Council of Nairobi and the Municipality of Mombasa. We will in this regard discuss the PPPs experience by the City Council of Nairobi in the provision of water and sewerage services, solid waste management and provision of public toilets. We will then analyze the two main case studies forming the basis of the study, to wit, the PPP between City Council of Nairobi and Adopt-A-Light Limited in the provision of advertising and lighting services and PPP between the Municipal Council of Mombasa and Kenya Airports Parking Services Limited in the provision of parking services. We will complete this chapter by analyzing the case studies and discussing the trends in PPPs by LAs in Kenya

As for Chapter we will delve onto the nature and concept of political risk and its interplay on PPPs. In the context of the theme of this study, we shall analyze the political risk in PPPs by LAs in Kenya. We shall also by way of a comparative analysis mechanisms that have been adopted in other jurisdictions to confront the issue of political risk arising out of PPPs

This chapter five shall sum up the study set out in chapters 2, 3 and 4 conclude the research and recommend ways to deal with the challenges identified from PPPs in Kenya and formulate lessons for the benefit of county governments

CHAPTER TWO: THE CONCEPT AND NATURE OF PUBLIC PRIVATE PARTNERSHIPS.

1. A general overview of Public Private Partnerships

Many citizens around the world and especially in developing countries including Kenya face an 'infrastructural deficit', as evidenced by congested roads, poorly-maintained transit systems and recreational facilities, street and lighting facilities, deteriorated schools, hospitals, and water and water treatment systems, and other infrastructure assets which are either non-existent or in urgent need of repair. These problems in turn impose huge costs on governments from lessened productivity and reduced competitiveness, to an increased number of accidents, health problems and lower life expectancy.

Many governments have come to realize that the tax base alone cannot fund the huge needs for infrastructure. In many African countries there is an acute need to rehabilitate existing infrastructure that, was built decades ago. To alleviate this problem, many countries including Kenya have in the recent past involved the private sector in order to bridge the budget deficit.

The renewed interest on PPPs can be traced, at least partially, to the ideas of the "new public management", the "governance" paradigm, and the "reinventing government" movement, all of which stress harnessing of private sector expertise and resources to assist in the accomplishment of public policy goals.⁷⁹

Immediately after independence in most developing countries including Kenya, the state was generally seen as the agent of development and it was thought that only the state could provide public goods to citizens.⁸⁰ This was informed by the fact that provision of public good would not only require huge financial resources but also power to determine how those resources would be raised and spent.⁸¹ In that respect, throughout the 1970s in many countries, public services were acknowledged to be the responsibility of central governments—not only as a moral commitment but also to produce the infrastructure for national economic growth.

State-led development largely failed as evidenced by the fiscal crises of the many African countries in the late 1970s, partly because of mismanagement of public enterprises.⁸² It is the failure of state-led development that motivated the World Bank

⁷⁹ United Nations Economic Council for Europe: 'Guide Book on Promoting Good Governance in PPPs' (2008) http://www.undp.ro/download/UNECE_ppp.pdf accessed 15th May 2011.

⁸⁰ Migai Akech *Privatization and Democracy in East Africa: The Promise of Administrative Law* (East African Educational Publishers Limited, 2009) at 10.

⁸¹ *ibid*

⁸² *ibid*

and the International Monetary Fund to "roll back" the state in Africa by implementing the Structural Adjustments Programmes (SAPS).⁸³

Conceptualization of the state's responsibility for and role in providing public services has thus undergone a notable reversal since 1980.⁸⁴ Since the early 1980s, that role has been shifted to the operation of the market and the lower tiers of government. The current neoliberal perspective expects the private sector to pursue, more effectively and efficiently, the development of infrastructure and the provision of public services, while the state monitors its activities.⁸⁵ Recent national administrations have viewed government as changing "from doing to ensuring" and have abandoned its redistributive political role in favor of a technical managerial role.⁸⁶

The adoption of large-scale privatization programmes gained considerable momentum worldwide in the wake of the British experiment of the early 1980s.⁸⁷ This phenomenon has changed the respective roles of the public and private sector worldwide. Projects and activities in sectors which were formerly government monopolies, including physical infrastructure and social services, are being increasingly financed and/or managed by private firms under negotiated programmes and contracts.⁸⁸

From the early 1990s, there was a push from donor agencies in developing countries through SAPs requiring the involvement of the private sector in service delivery and the replacement of public monopolies by private competition. SAPs had with it as a component the objective to unleash the markets so that competition can help improve the allocation of resources and this required market liberalization, introduction of competition, privatization and a significant reduction in the role of the state in economic affairs.⁸⁹

SAPs emerged out of a diagnosis by international development policy institutions that the policies that African states had been pursuing were responsible for their poor economic performance. In this respect, the World Bank observed that "the main factors behind the stagnation and decline were poor macroeconomic and sectoral

⁸³ *ibid*

⁸⁴ Faranak Miraftab, 'Public Private Partnership: The Trojan Horse of Neoliberal Development?' (2004) *Journal of Planning Education* 24: 89 – 101 (Association of Collegiate of Schools of Planning) at 93.

⁸⁵ *ibid*

⁸⁶ *ibid*

⁸⁷ United Nations 'Public-Private Partnerships: The Enabling Environment for Development' presented at the Group Experts of the United Nations Programme on Public Administration and Finance 13th Meeting held on 27th May to 4th June 1997 at 2 www.unpan.un.org accessed on 10th July 2011

⁸⁸ *ibid* at 3

⁸⁹ Migai *supra* note 80 at 2.

policies emanating from a development paradigm that gave the state a prominent role in production and in regulating economic activity".⁹⁰ SAPs were therefore inspired by the perceived failures of the state-led development paradigm.

By the late 1990s, however, it had become clear that market-led development advocated under SAPs by the International Financial Institutions (IFIs) was not working either. The IFIs therefore moved from the minimalist state or night watchman state they had advocated under SAPs. As a result the policies such as liberalization, privatization, deregulation etc were now to be matched with good institutions, democracy, a good bureaucracy, corporate governance and such like policies.⁹¹ It is in this context that PPPs have since the early 1990s gained prominence in both the developed and the developing world.

The long-term development blueprint for Kenya Vision 2030 seeks to transform the country into a "globally competitive and prosperous country with quality life by 2030."

⁹² An analysis of medium term plan reveals that 65% of the functioning of the implementation of the vision of a total of 3.9 trillion is expected from the private sector through the implementation of PPPs.⁹³ Infrastructural development has been identified as a foundation to the three pillars of Kenya Vision 2030 (political, social and economic) with the Five year Medium Term Plan for Kenya Vision 2030 projecting expenditure to the tune of US\$ 25 billion to finance infrastructural requirements and related services.⁹⁴ The Kenya government is expected to fund Government to fund US\$ 7.5 billion and the bulk of the balance is to be achieved through use of PPPs.⁹⁵

In its draft on "Privatization of State Corporations and investments",⁹⁶ the Government of Kenya reiterated its role of being a facilitator for private sector which favoured economic growth and investment⁹⁷. Its proposed privatization strategy was, therefore, stated to be an integral part of the public sector reforms that are to be implemented by Government to spur the recovery of the Kenyan economy, improve the social economic indicators and help Kenya to move toward the Millennium Development Goals (MDGs)⁹⁸.

⁹⁰ As quoted by Migai *supra* note 80 at 2

⁹¹ Migai *supra* note 80 at 21

⁹² See www.vision2030.go.ke last accessed on 22nd August 2011

⁹³ *ibid*

⁹⁴ See www.vision2030.go.ke last accessed on 22nd August 2011

⁹⁵ *ibid*

⁹⁶ Sessional paper No 2 of 2005

⁹⁷ *ibid*

⁹⁸ *ibid*

2. Meaning of PPPs

In policy perspectives, PPP means cooperation between actors in the public and private sector for the mutual benefits and mobilization of the coalition of interest drawn from different sectors for the purposes of organizing the agreed strategy for development.⁹⁹

The underlying logic for establishment of PPPs is that both the public and private sector have unique characteristics that provide them with advantages in specific aspects of service delivery or project delivery. PPP is a viable option with a great potential which by combining skills, expertise and other resources from different entities can help achieve outcomes that are unattainable by independent action.

There are various types of PPPs, established for different reasons, across a wide range of market segments, reflecting the different needs of governments for infrastructure services. Although the types vary, two broad categories of PPPs have been identified by scholars: the institutionalized kind that refers to all forms of joint ventures between public and private stakeholders; and contractual PPPs¹⁰⁰ The first category consists of PPPs of an institutional nature, involving cooperation between the public and the private sector within a distinct entity and secondly PPPs a purely contractual nature, in which the partnership between the public and the private sector is based solely on contractual links.¹⁰¹

PPPs in Kenya are principally governed by the Public Procurement and Disposal Act of 2005 (herein after referred to as the "PPDA") and the regulations made there under.

A PPP is defined by the Public Procurement and Disposal Regulations 2006 and Public Procurement and Disposal (Public Private Partnerships) Regulations 2009 (2009 PPPs regulations) as an agreement between a procuring entity (defined as a public body under the PPDA) and a private party under which;¹⁰²

- (a) The private party undertakes to perform a public function on behalf of the procuring entity;
- (b) The private party receives a benefit for performing the function, either by way of;
 - (i) compensation from a public fund;

⁹⁹ Wilfred Uronu " Making Effective Private Public Partnership in Local Government' *Research Journal of Social Sciences*, (2009)ISInet Publication 4: 57- 60 at 57.

¹⁰⁰ Garsse Steven 'Public –Private Partnerships, Concessions and Procurement Law' 3rd International Public Procurement Conference Proceedings 28th- 30th August 2008 www.ippa.ws/proceedings last accessed on 9th August 2011 at 223

¹⁰¹ *ibid*

¹⁰² See Regulation 2 of both Regulations.

(ii) charges or fees collected by the private party from the users of a service provided to them; or

(iii) a combination of such compensation and such charges or fees.

(c) the private party is generally liable for the risks arising from the performance of the function depending on the terms of the agreement.

3. Key attributes of Public private partnerships

We have seen that in legal literature, the definition of a PPP covers all forms of long term co-operation between public authorities and the private sector.¹⁰³ The main characteristics of a PPP include: the relatively long duration of the relationship, involving cooperation between the public partner and the private partner on different aspects of a planned project; the method of funding the project, in part from the private sector, sometimes by means of complex arrangements between the various players; the important role of the economic operator, who participates at different stages in the project (design, completion, implementation, funding), the public partner concentrates primarily on defining the objectives to be attained in terms of public interest, quality of services provided and pricing policy, and it takes responsibility for monitoring compliance with these objectives and the distribution of risks between the public partner and the private partner, to whom the risks generally borne by the public sector are transferred.¹⁰⁴

Under PPPs, public and private sectors are expected to work together on the implementation of projects. They are expected to collaborate on the basis of a clearly defined sharing of tasks and risks to achieve benefits of added value and increased efficiency. Project related risks are largely transferred to the private entity. In a PPP, the focus of the government should ideally shift to policy, strategy and monitoring role rather than service delivery. In the short run a PPP may shift a financing requirement from the public to the private sector, or may defer the costs incurred on the budget but does not increase the quantum of services that the economy can accommodate.

PPPs thus usually involve the investment of private capital by a private entity to design, finance, construct, operate, and maintain a project for public use for a specific term during which a private entity is able to collect revenue from the users of the facility. When the limited term of ownership expires, title to the project usually reverts to the government at no cost and this is particularly the case for a Build-Own-Operate-Transfer (BOOT) type of a PPP. By then, the private entity is expected to have collected enough revenue to recapture its investment and turn a profit on the investment.

¹⁰³ Garsse *supra* note 100.

¹⁰⁴ *ibid*

Further, PPPs often involve complex planning and sustained facilitation. Infrastructure projects such as roads and bridges, water supply, sewerage and drainage involve large investment, long gestation period, poor cost recovery, and construction, social, and environmental risks. When infrastructure is developed as PPPs, the process is often characterized by detailed risk and cost appraisal, complex and long bidding procedures, difficult stakeholder management, and long-drawn negotiations to financial closure.

A look at the various forms of PPPs will demonstrate the, long term and complex nature envisioned in most PPPs.

There are many types and forms of PPPs, both in theory and in practice. The range of PPP models allocate responsibilities and risks between the public and private partners in different ways.¹⁰⁵ The following terms are commonly used to describe typical PPP agreements: .¹⁰⁶

Buy-Build-Operate (BBO): Transfer of a public asset to a private or quasi-public entity usually under contract that the assets are to be upgraded and operated for a specified period of time. Public control is exercised through the contract at the time of transfer.

Build-Own-Operate (BOO): The private sector finances, builds, owns and operates a facility or service in perpetuity. The public constraints are stated in the original agreement and through on-going regulatory authority.

Build-Own-Operate-Transfer (BOOT): A private entity receives a franchise to finance, design, build and operate a facility (and to charge user fees) for a specified period, after which ownership is transferred back to the public sector.

Build-Operate-Transfer (BOT): The private sector designs, finances and constructs a new facility under a long-term PPP contract, and operates the facility during the term of the PPP after which ownership is transferred back to the public body upon completion of the project. In fact, such a form covers BOOT (above) and BLOT (below) with the sole difference being the ownership of the facility.

Build-Lease-Operate-Transfer (BLOT): A private entity receives a franchise to finance, design, build and operate a leased facility (and to charge user fees) for the lease period, against payment of a rent.

¹⁰⁵ United Nations Economic Commission for Europe *supra* note 79 at 2 and 3.

¹⁰⁶ *ibid*

Design-Build-Finance-Operate (DBFO): The private sector designs, finances and constructs a new facility under a long-term lease, and operates the facility during the term of the lease. The private partner transfers the new facility to the public sector at the end of the lease term.

Finance Only: A private entity, usually a financial services company, funds a project directly or uses various mechanisms such as a long-term lease or bond issue.

Operation & Maintenance Contract (O & M): A private operator, under contract, operates a publicly owned asset for a specified term. Ownership of the asset remains with the public entity.

Design-Build (DB): The private sector designs and builds infrastructure to meet public sector performance specifications, often for a fixed price, turnkey basis, so the risk of cost overruns is transferred to the private sector.

According to the Task Force on Devolved Governments (TFDG), the following modes of PPPs set out in the Public Procurement and Disposal Regulations 2009¹⁰⁷ can be adopted by the county governments for the delivery of county infrastructure¹⁰⁸:

- a. **Management contracts (MCs).** MCs are short term PPP arrangements under which the public sector procuring entity entrusts private companies with operating infrastructure or providing management services according to contract for a period not exceeding five years. The public sector retains ownership and control of facilities, capital assets and properties.
- b. **Leases:** when public and private sectors engage in a lease agreement, the private party pays rent to the procuring entity and manages, operates and maintains the facility in exchange of fees or charges from consumers in exchange of services for a specified period of time.
- c. **Concessions:** concessions, just like BOOT agreements (see below) are long term PPP arrangements. The contract covers a period not exceeding 30 years under which the private party maintains, rehabilitates upgrades and enhances the facility under consideration in the course of the concession.
- d. **Build –Own-Operate-Transfer (BOOT):** BOOT contracts are long term PPPs contracts in which private companies invest, build, operate and own

¹⁰⁷ Regulation 3

¹⁰⁸ Task Force on Devolved Governments(Kenya), *Interim Report nterim Report on Devolved Governments*, (April 20 2011).
http://www.communication.go.ke/documents/INTERIM%20REPORT_ON_DEVOLVED_GOVERNMENT.pdf accessed 16th May 2011, at 284

infrastructure until capital is recovered through fees under a concession from the county, and the facility in question is then transferred back to the county government.

- e. **Build Own Operate (BOO):** contracts where the private sector invests, builds and permanently owns assets under the contractual terms that secure public interest under the county supervision.

Other types of PPPs that county governments can utilize are: Design-Build Maintenance, (DBM), Design Build- Operate (DBTO), Design –Build-Finance-Operate (DBFO) also called Private Finance Initiative (PFI) in Britain and Purchase – Upgrade- Operate (PUO).¹⁰⁹

The huge financial risk looking at the forms of PPPs is borne by the private entity and due to this PPPs envision a long- term relationship to enable the private party recoup its investments.

To illustrate this important attribute of PPPs, we examine the investment made in one of the recent PPPs by the national government viz the RVR concession. The 25 years concession's investment is estimated at more that US\$ 300 in Kenya and US\$ 54 in Uganda¹¹⁰¹¹¹. The governments required the concession fee structure to entail, Upfront fee of US\$3 million in Kenya and US\$2 million in Uganda; Variable annual fee for each Concession for 25 years being 5% of annual gross revenues for the first five years and 7% of annual gross revenues thereafter; fixed annual fee for each Concession for each of the 25 years: amounts may vary from one year to the other; fixed annual concession fee for each of the 7 years for the Kenya passenger services (the amounts vary each year)¹¹².

PPPs thus imply a common understanding of shared goals, a willingness to repartition responsibilities for their achievement, a continuing public-private dialogue on what needs to be done to promote their realization, and a supportive policy and institutional framework.¹¹³ This means that PPPs are critically dependent on sustained and explicit support of the sponsoring government. To deal with these procedural complexities and potential pitfalls of PPPs, governments need to be clear, committed, and technically capable to handle the legal, regulatory, policy, and governance issues.¹¹⁴ PPPs are long lived contracts and their viability depends on the legal environment and the protection both of property rights of the private firm

¹⁰⁹ *ibid*

¹¹⁰ D. O Ongolo 'Public Private Partnerships in Kenya' prepared for The Institute of Economic Affairs, Kenya (7th July 2006) at 9. www.ieakenya.or.ke/documents/Public%20Private%20Partnerships.pdf accessed on 20th June 2010 at 23

¹¹¹ *ibid*

¹¹² *ibid*

¹¹³ United Nations *supra* note 87.

¹¹⁴ *Ibid*

and of the rights of the public. This aspect has been shown to be wanting in PPPs by LAs in Kenya

4 The Interface between PPPs, Public Procurement and Privatization.

Not all government projects with the private sector participation are PPP projects. Although closely related, PPPs are different from privatization and public procurement.

A PPP is in the real sense a component of public procurement. Prof. Migai Akech has in fact defined privatization to include PPPs. He gives the definition of privatization as follows *"the transfer of ownership or control of public assets and/or functions from public to private entities. Privatization embraces measures such as divestiture, commercialization or corporatization, commodification, contracting out and public private partnerships"*¹¹⁵

The Privatization Act ¹¹⁶ defines privatization as a transaction or transactions that result in a transfer, other than to a public entity of assets of a public entity including the shares in a state corporation or operational control of assets of a public entity or operations previously performed by a public entity. Thus, while PPPs involve private management of public service through a long-term contract between an operator and a public authority, privatization involves outright sale of a public service or facility to the private sector.¹¹⁷ Unlike a full Privatization scheme, in which the new venture is expected to function like any other private business, the government continues to participate in certain ways in PPPs.¹¹⁸

According to Prof. Migai, PPPs are seen as a way of involving the private sector in government projects while avoiding the problems associated with the more extensive methods of privatization.¹¹⁹ While privatization represents a take-over of a publicly owned entity, PPPs, are more like mergers, with both sides sharing the risks and benefits. For the state, the main attraction is that the private sector can bear part of the financial burden of investing in infrastructure.¹²⁰

Public procurement on the other hand is the supply by the private sector of works goods or services as defined by a public entity. According to the PPDA, "Procurement" means the acquisition by purchase, rental, lease, hire purchase,

¹¹⁵ Migai *supra* note 80, iv and 5.

¹¹⁶ Act No. 2 of 2005

¹¹⁷ United Nations *supra* note 87

¹¹⁸ D. O. Ongolo *supra* note 110 at 5

¹¹⁹ *Supra* note 80 at 6.

¹²⁰ United Nations *supra* note 87.

license, tenancy, franchise, or by any other contractual means of any type of works, assets, services or goods including livestock or any combination.¹²¹

PPPs fall within the purview of public procurement and should be seen as one of the types of public procurement. Simpler forms of procurement are chosen because of the simplicity of goods or services desired the possibility to choose from numerous providers, and the intention to contain costs. PPPs on the other hand are more complex, frequently larger in financing requirements, and are long-term as opposed to one-off relationships.

As such, PPPs presents as a middle case between public procurement and privatization and operate at the boundary of the public and private sectors, being neither nationalized nor privatized assets and services. Politically, they represent a third way in which governments may deliver some public services. Public procurement and full privatisation thus lie at the opposite ends of a continuum defined by the extent of service obligations imposed, and ultimate ownership of assets.¹²²

Public procurement, PPPs and privatization are thus related and sometimes intertwined institutional relationships undertaken by governments in streamlining the provision of public services and goods. This thesis will however differentiate the three concepts and will focus on PPPs but reference will be made to privatization and public procurement in applicable contexts.

5 Reasons for use of PPPs by government and government agencies

Generally, some of the key reasons for considering PPPs include the need to benefit from increased efficiency, shorter implementation time, greater innovation and ultimately better value in the delivery of services brought about by increased competition between private firms or between the private and public sectors.¹²³ Other benefits of PPPs include the benefits of cost savings, risk sharing, improvement of levels of service and enhancement of revenue.¹²⁴

According to Jutting, there are three general and main reasons for use of PPPs by governments.¹²⁵ First, due to fiscal pressures governments have to reallocate resources with the utmost effectiveness. In this respect various studies have shown,

¹²¹ Section 2.

¹²² D. O Ongolo *supra* note 110

¹²³ Ministry of Municipal Affairs, British Columbia 'Public Private Partnership: A Guide for Local Government' at 11 the www.marh.gov.bc.ca accessed on 14th March 2010.

¹²⁴ *Ibid.*

¹²⁵ Jutting 'Public-private partnerships and social protection in developing countries: the case of the health sector' at 5-6 Paper presented at the ILO workshop on "The extesnion of social protection" Geneva 13-14 December www.oecd.org/dataoecd/32 accessed on 5th August 2010

that there is a large potential for gains in efficiency in the social sectors. Secondly, private providers, both non-profit or for-profit oriented play an important role in social service provision; a role which has been largely neglected by governments. Third, given the intrinsic, albeit different strengths and weaknesses of the state, for-profit and non-profit institutions the question arises as to what extent a complementarity can be organised in the provision of social services.¹²⁶

We will delve into more details on some of the main reasons for governments adoption of PPPs.

a. Reduction of the government budget deficit

Globally, governments are increasingly constrained in mobilizing the required financial and technical resources and the executive capacity to cope with the rising demand for provision of essential services. Rapid economic growth, growing urban population, increasing rural–urban migration, and all-round social and economic development have compounded the pressure on the existing infrastructure, and increased the demand–supply gap in most of the developing world.¹²⁷

Countries in the developing world, are especially experiencing increasing pressure from their citizens, civil society organizations, and the media to provide accessible and affordable infrastructure and basic services. The pressure has also come from the international impact on Millennium Development Goals (MDGs), under which country progress in terms of access to essential services is being monitored.

While the infrastructure gap is rising, government budgetary resources are increasingly constrained in financing this deficit. More importantly, the private sector can generate revenue through the third parties by for example disposing surplus assets which normally can help in running project when there is no cash flow from the government.¹²⁸

Since neither the public sector nor the private sector can meet the financial requirements for infrastructure in isolation, the PPP model thus has come to represent a logical, viable, and necessary option for them to work together.¹²⁹

¹²⁶ *ibid*

¹²⁷ Asian Development Bank (ADB): PPP Preparatory Work

<http://www.adb.org/Documents/Handbooks/PublicPrivatePartnership/Chapter6.pdf> accessed on 30th

August 2010 at 20 to 21

¹²⁸ *ibid* at 72 and 73

¹²⁹ *ibid* at 20 to 21

As such, the primary rationale for privatization and PPPs for that matter in Kenya is that the state or state agencies including the LAs have been incapable or have neglected to provide the essential services to the citizens. In the context of LAs which form the focus of this study, PPPs have been fuelled by the "weak" LAs which lack institutional capacity to perform the essential services.

Finances in the LAs in Kenya have been scarce and the Local Authorities Transfer Fund (LATF) not being adequate to cater for infrastructural needs. The LAs debt burden consumes a substantial amount of the annual LATF allocation at the expense of development projects and service delivery. The limited resources available to the council are further rendered ineffective by virtue of fragmentation through sharing it equally among the electoral Wards.¹³⁰ This has called for participation of the private sector and hence the need for PPPs.

Relatedly, it is argued that government and government agencies could better generate essential community services if it were freed of the burden of publicly owned infrastructure assets. The essence of this argument is that as long capital and other needs of government commercial and business enterprises continued to exhaust scarce financial resources, spending on welfare activities would suffer.¹³¹ The state can thus focus on its core business of providing good governance, enhancing knowledge and skills, and providing basic needs for its citizens.

PPPs thus usually reduce budget deficits – a significant advantage since governments typically face severe budgetary constraints and off-balance sheet borrowing is not an attraction in its own right.¹³²

b. The efficiency argument

This argument has been theoretically developed by the public choice theory, mainly arguing that it cannot be assumed that politicians and bureaucrats always act in the public interest, but either pursue their own interests or those of powerful interest groups.¹³³ The embracing of PPPs was driven by the argument that the hierarchical bureaucracy is inherently inefficient and that the introduction of market mechanisms will substantially enhance the efficiency of public service delivery.¹³⁴ Private contractors may also be able to offer cost savings by providing access to skills,

¹³⁰ Harriet Naitore 'Study on Local Council Oversight Role and Social Accountability in Kenya ' prepared for the African Development Group (2008) www.siteresources.worldbank.org accessed 4th July 2011.

¹³¹ Brian Dollery, 'Public Private Partnerships and Local Government Infrastructure' http://www.lgsa-plus.net.au/resources/documents/dollery-ppps-and-local-government-infrastructure_2005.pdf accessed 2nd August 2011.at 5 to 6

¹³² *ibid*

¹³³ Jutting *supra* note 125 at 4 -5

¹³⁴ *ibid*

equipment, technology and scale economy advantages that derive from specialisation.¹³⁵

The public sector is typically less efficient than the private sector in delivering infrastructure services and empirical evidence seems to support this proposition.¹³⁶ Linked to improved efficiency is the notion that private sector involvement in the provision of government infrastructure invigorates competition in the economy and it is argued that public organizations are not subject to the rigours of a competitive market and this lack of competition may induce inefficiencies.¹³⁷

PPPs are however not an unqualified success. Despite the growing interest in and adoption of PPPs, they have been facing criticism from civil society organizations, public interest groups, media, and other stakeholders. Wide publicity of some of the problematic PPPs has raised concerns about the role of the private sector in public services.¹³⁸ Lack of trust in the private sector with public service, tariff increases, layoffs, and poor stakeholder management have contributed to these concerns. The detractors also accuse PPPs of high procurement costs, which deter small companies and curtail competition.¹³⁹

However, many PPP experts attribute the failure of some of these projects to faulty, rushed, noncompetitive, and nontransparent application of the PPP principles. The PPP approach is growing and evolving globally, as more countries move from state-owned and operated services to the private provision of infrastructure.¹⁴⁰ Regardless of the problems, there are potential long-term benefits of PPPs which should be embraced by the local/county governments in Kenya. Despite that Kenya as a country has embarked on this path, the PPP mechanism has not been properly endorsed by the LAs in Kenya. This study has identified some of the arising issues from the LAs' approach to PPPs.

6. The legal and regulatory framework for PPPs in Kenya.

There was no specific legislative and regulatory framework for PPPs in Kenya prior to 2005. PPPs are now principally governed and regulated by the Public Procurement and Disposal Act of 2005 (herein after referred to as the "PPDA") and the specific regulations made there under viz, the Public Procurement and Disposal (Public-Private Partnership) 2009. There is also in place the Public Procurement

¹³⁵ Dollery *supra* note 131 at 5 to 6.

¹³⁶ Hodge, G. A. *Privatization: An International Review of the Evidence*, (Westview Press, Boulder 2000).

¹³⁷ Dollery *supra* note 131 at 5.

¹³⁸ ADB *supra* note 127 at 20 to 21

¹³⁹ *ibid*

¹⁴⁰ *ibid*

and Disposal (Regulations) 2006 which set out the procedure for public procurement of goods and services.

There are also some provisions in the Privatization Act 2005 which apply to PPPs.

PPPs are indeed a unique kind of public procurement and hence the need to have specific regulations relating to PPPs made under the PPDA. Traditional procurement law would not suffice to govern PPPs.

In consideration of the unique characteristics, the United Nations Commission on International Trade Law (UNCITRAL) has recognised the fact that international experience in the award of privately financed infrastructure projects has in fact revealed some limitations of traditional rules on private procurement and that these would be unsuitable for PPPs.¹⁴¹ In this respect, it is not surprising that UNCITRAL itself nowadays has a different set of “model provisions” for public procurement contracts and for Build Own Transfer (BOT) projects. After having adopted a Model Law on Procurement of Goods, Construction and Services, it adopted, a Model Legislative Provisions on Privately Financed Infrastructure Projects on 7 July 2003.¹⁴²

Constitutional framework

Regarding the constitutional under pinning for PPPs, there are provisions on procurement of public goods or services¹⁴³ which states that when a State Organ or Public Entity contracts for goods and services, it must do so in a fair, equitable, transparent, competitive and cost effective manner. It is arguable that this article does not only apply to traditional short term procurement of services but also extends to long term PPPs. This provision mirrors the objectives of the PPDA under section 2 of this Act which is to establish procedures for procurement and the disposal of unserviceable, obsolete or surplus stores and equipment by public entities to achieve the following objectives –

- a. To maximise economy and efficiency.
- b. To promote competition and ensure that competitors are treated fairly.
- c. To promote the integrity and fairness of those procedures.
- d. To increase transparency and accountability in those procedures; and
- e. To increase public confidence in those procedures.
- f. To facilitate the promotion of local industry and economic development.

¹⁴¹ Garsee *supra* note 100

¹⁴² *ibid*

¹⁴³ Section 227

Article 227 of the constitution further details that an Act of Parliament shall prescribe a framework for procurement and asset disposal and may provide for all or some of the following:

- a. Categories of preference of allocation of contracts
- b. Protection of categories of persons previously disadvantaged by unfair competition or discrimination.
- c. Sanctions against contractors who have not performed in accordance with laid down procedures and their contractual obligations.
- d. Sanctions against persons who have defaulted in their tax obligations, have been guilty of corrupt practices or have been in violation of fair employment laws and practices.

Some of these provisions are already present in the PPDA. For instance section 39 of the PPDA allows the Minister of Finance to prescribe preferences and or reservations in public procurement and disposal on the basis of inter alia citizenship so that Kenyan citizens are given exclusive preferences in certain circumstances.¹⁴⁴

Relevant to this study are also the provisions on leadership and integrity under chapter 6 and values and principles of public service under chapter 13 of the Constitution.

The statutory and regulatory framework

a. Public Procurement and Disposal Act

The principal statutory framework for PPPs in Kenya is set out in the PPDA, Act No 3 of 2005 assented on 26th.October 2005.

The purpose of the Act is to establish procedures for procurement and the disposal of unserviceable, obsolete or surplus stores and equipment by public entities.

With specific regard to PPPs, this is recognized by the Act under Sec. 92 (1), which states that *"A procuring entity may use a procurement procedure specially permitted by the Authority which may include concessioning and design competition"*. Section 92 (2) (a) defines *"concessioning"* to mean *"a procurement that encourages the mobilization of private sector resources for the purpose of public financing, construction, operation and maintenance of development projects and may include build-own and operate, build-own-operate and transfer, build-operate and transfer or similar types of procurement procedures"*

¹⁴⁴ Section 39(8). The subsidiary legislation for this provision are found at regulation 28.

Section 92(4) of the PPD Act states that the Public Procurement Oversight Authority shall issue detailed guidelines for concessioning or PPPs.

Subsidiary legislation relating to PPPs have been made vide the Public Procurement and Disposals (Public-Private Partnership) Regulations 2009 pursuant to the powers vested in the Minister of Finance under section 140 of the Act. The Regulations set out procedures for entering into PPPs and related provisions. There is also established a PPP Steering Committee whose function include spearheading the PPP process and promoting the understanding and awareness of PPPs among key stakeholders and reviewing the challenges constraining participation or realization of full benefits expected from PPPs and formulate time bound solutions to address the challenges and to create an enabling environment¹⁴⁵

The Privatization Act

The Act defines privatization to include all transactions that result in the transfer to a private entity the assets, operational control and operations of all public assets.

PPPs are given due recognition in the description of the methods of privatization under section 2 (1) which provides that privatization includes transfer of operational control of assets of a public entity as well as operations previously performed by a public entity;

Sec 25 (b) defines as one of the methods of PPP to include, “*concessions, leases, management contracts and other forms of public-private partnerships*”.

A comprehensive policy, legislative and institutional framework has already been passed in Kenya to serve the needs of the Government’s privatization programme. Among other things this framework provides for implementation of non-privatization transactions, such as PPPs, under the Privatization Commission and the established legal framework and process if the Government considers it necessary. In this respect it is possible to blend a framework for PPPs into that for the privatisation programme with suitable enhancements to cater for the formal and institutional needs of a PPP programme. Specifically there will be need to provide for strong post closure contract management.

The English common law

Section 2 of the Law of Contracts Act, ¹⁴⁶ provides that “ save as may be provided by any written law for the time being in force, the common law of England relating to contract, as modified by the doctrines of equity, by the Acts of Parliament of the United Kingdom applicable by virtue of subsection (2) of this section and by the Acts

¹⁴⁵ Regulation 5.

¹⁴⁶ Chapter 23 of the Laws of Kenya

of Parliament of the United Kingdom specified in the Schedule to this Act, to the extent and subject to the modifications mentioned in the said Schedule, shall extend and apply to Kenya.” This section thus provides for the application of the English Common Law to contracts in Kenya including PPPs.

CHAPTER THREE: CASE STUDIES ON SELECTED PPPS BY LOCAL AUTHORITIES IN KENYA

1. INTRODUCTION

Effective and efficient infrastructure and services provision are important in delivering major benefits in economic growth, poverty alleviation, environmental sustainability and sustainable development. The key services include water, sanitation, waste management, transport infrastructure and health services. Better service delivery of these services is crucial for sustainable growth, development and poverty reduction as well as increasing people's standards of living and contributes to sustainable development.

Most of these services in Kenya are provided by Local Authorities (LAs) and most of these functions will be taken over by the county governments set out under the current Constitution once the county governments are established.

The UN Habitat has noted that the existing facilities in most LAs in developing countries including in East Africa were planned to cater for much smaller demands.¹⁴⁷ The expansion in demand in commerce and industrial development has added to the existing high population growth in towns without any commensurate rise in the quality and quantity of public infrastructure and services.¹⁴⁸ As a result of the rising demands, service delivery by LAs has deteriorated over the years to an extent that even the most basic services have not been easily available.

Services provided in Kenya were and in some cases still currently are of inferior quantity and quality compared to those in more developed parts of the world.¹⁴⁹ Where some services infrastructure are in place, their maintenance and repair is inadequate.¹⁵⁰ These problems are exacerbated by rapid urbanisation in most countries.¹⁵¹

The UN-Habitat has also pointed out that the factors that have affected service delivery include insufficient resources (both collection and allocation), mismanagement, weak

¹⁴⁷ UN- Habitat, 'Local Democracy and Decentralization in East and Southern Africa: Experiences from Uganda, Kenya, Botswana, Tanzania and Ethiopia' www.unhabitat.org accessed on 3 August 2011 at 16

¹⁴⁸ *ibid*

¹⁴⁹ Ngowi: *Public –Private Partnership in Service Delivery: Application, Reasons, Procedures, Results and Challenges in Tanzania Local Government Authorities* www.unpan.un.org last accessed on 4th August 2011.

¹⁵⁰ *ibid*

¹⁵¹ UN-Habitat *supra* note 147 at 47

technical and institutional capacities to increase service coverage and lack of planning and foresight.¹⁵²

The poor state of service delivery in LAs can also be attributed to , *inter-alia*, the nature of the public sector faceted with closely inter-linked and self-reinforcing characteristics of the sector like political interference; unclear objectives; limited operational autonomy; inadequate managerial skills *vis a vis* technical, human, conceptual and design skills; inadequate accountability and transparency; heavy and cumbersome bureaucracy; poor workers' morale; inappropriate economic settings; inadequate capital and lack of appreciation of the free inter-play of the market forces of supply and demand.¹⁵³

The UN Habitat has further pointed out that financial sustainability of any LA in Kenya has been to a large extent dependant on the central government /LAs' relationships.¹⁵⁴ The LAs' capacity to fulfill their functions is also largely dependent on their financial resources and their efficiency in generating revenue from these sources and further supplementary resources they can derive from the central government ¹⁵⁵ The control system in place also affects the timelines of expenditures (exchequer releases being controlled), their level of activities and the range of services they can offer or development projects they can embark on.¹⁵⁶

In view of the state of service delivery in LAs, there has been a move in the last two decades to adopt a *modus operandi* that draws on resources, experiences and capacity of various actors including private entities and citizens to complement their ability and to encourage a feeling of ownership, promote public awareness, strengthen LAs management instruments and promote transparency in the process.¹⁵⁷ Towards achieving the social, economic and political government's blue print enshrined in the Vision 2030, LAs in Kenya have embraced and continue to embrace the PPP mechanism.

This study will focus on PPPs by the Local Government in Kenya with the intention of formulating recommendations and lessons which will be useful for PPPs by the County Governments established under the Constitution promulgated in 2010. With the coming into force of the Constitution, we now have in place a two tier devolved Government system which will somewhat change the structure of the local authorities. Hitherto, the

¹⁵² *ibid*

¹⁵³ Ngowi *supra* note 149.

¹⁵⁴ *ibid* at 42

¹⁵⁵ *ibid*

¹⁵⁶ UN-Habitat *supra* note at 147 at 42.

¹⁵⁷ *ibid* at 44.

structure of government has constituted the central government, the provincial government and the local government.

The idea behind the devolution of government was to bring development and public participation at the grass roots. This was at the backdrop of intending to correct the deficiencies in the governance structure of the country. A central objective was the restoration of power to local communities to manage their affairs particularly in matters of local development. The two tier government under the current Constitution is believed if properly implemented will achieve the desired goal of grass root development and public participation.

The Task Force on Devolved Government (TFDG) established under the auspices of the Local Government Ministry was set up in October 2010 to propose ways in which the devolved government as envisaged in the constitution of Kenya can be operationalized.

The relationship between the 47 counties established under the Constitution¹⁵⁸ and the 175 Local Authorities¹⁵⁹ was somewhat uncertain with the coming into force of the Constitution. Article 18 of the transitional provisions under the new Constitution provides that civic bodies will continue existing subject to any laws that may be enacted. However the transitional clause that touches on elections¹⁶⁰ does not mention anything on election of councilors and it is expected that wards will form electoral units for county assemblies.¹⁶¹

The chairman of the TFDG, Mr Mtakha Kungu has taken the position that Article 18 of the transitional provisions under the new Constitution was included to provide for the existence of the LAs pending enacting of legislation to pave way for the collapse of LAs and integrate into the two tier government.¹⁶²

It is reported by The Institute for Social Accountability (TISA) that the Minister for Local Governments has had discussions with members of the Association of Local Government Authorities of Kenya on the effect of the new Constitution on the Local

¹⁵⁸ Part 2 of Chapter 11 of the Constitution.

¹⁵⁹ See the Association of Local Government's website: www.localafrica.org/associations accessed on 6th May 2011.

¹⁶⁰ Article 9 of the sixth schedule.

¹⁶¹ Stephen Makabila 'The fate of councillors remains uncertain' *The Standard* (Nairobi 16th October 2010).

¹⁶² Statement made during the Law Society Conference at Leisure Lodge and Golf Club in Diani Mombasa under the theme: 'One Year into the Implementation of the Constitution: Taking Stock' (17th to 21st August 2011).

Government structure.¹⁶³ It is further stated that there will be two tiers of government; the national government and the county governments and that some LAs will continue to exist, others will be merged, others scrapped and some handed over to the counties through the amendment of the Local Government Act.¹⁶⁴

In view of the provisions of the Constitution, it has been proposed that county governments would combine both the present districts and smaller LAs that are to be merged. County assemblies will consist of members elected by the registered voters of wards, each member consisting of a single member constituency.

The intention to change the structure of LA is supported by the Task Force on Devolved Government (TFDG) in its interim report released on 20th April 2011¹⁶⁵ which takes the view that many government structures including LAs, Provincial Administration, line ministries, regional authorities are all embedded in counties under the Constitution and they shall have to conform to Constitutional provisions.¹⁶⁶

The 47 County governments established under article 6(1) of the Constitution are specified under the First Schedule. Article 184 which falls under Chapter 11 on Devolved governments provides that the national government shall provide for governance and management of urban areas and cities. This according to the TFDG implies that cities and urban areas, except for the cities of Nairobi and Mombasa will operate under county governments.¹⁶⁷ ¹⁶⁸Both the City of Nairobi and Mombasa are also counties and will directly relate to the national government.

One of the terms of reference of the TFDG is to prepare drafts of such new legislation on urban areas and cities under Article 184 of the Constitution and review the local Government Act (Chapter 265 of the Laws of Kenya) or the Local Government Bill, 2009 which enactment was halted after the promulgation of the constitution in 2010.¹⁶⁹

In this respect, the TFDG has identified six pieces of legislation to help guide the running of the newly created 47 counties that will *inter alia* bring certainty to the fate of

¹⁶³ www.tisa.or.ke accessed on 6th May 2011.

¹⁶⁴ *ibid*

¹⁶⁵ Task Force on Devolved Governments(Kenya), *Interim Report nterim Report on Devolved Governments*, (April 20 2011).
[http://www.communication.go.ke/documents/INTERIM%20REPORT_ON_DEVOLVED_GOVERNMENT.p](http://www.communication.go.ke/documents/INTERIM%20REPORT_ON_DEVOLVED_GOVERNMENT.pdf)
df accessed 16th May 2011.

¹⁶⁶ *Ibid* at 54.

¹⁶⁷ *Ibid* at 47

¹⁶⁸ This position is clearly set out in the Urban Areas and Cities Act 2011 which provides inter alia that Municipal Councils shall be accountable to the County Executive Committees. See section 14(b) which creates an agency relationship between municipal councils and county governments.

¹⁶⁹ *Supra* note 158 at 2

local authorities. The drafts are the Devolved Government Bill, Urban Areas and Cities Bill (already enacted), Intergovernmental Relations Bill, Intergovernmental Fiscal Relations Bill, County Government Financial Management Bill and Transition to County Government Bill.

The system of Local Government in Kenya is established under the Local Government Act¹⁷⁰. The system is composed of four categories of local governments, namely: a City Council, Municipal Councils, Town Councils and County Councils. It is worth noting that the Act defines “the City of Nairobi” as follows: “*the City of Nairobi*” means the area of the City Council of Nairobi incorporated by Royal Charter dated the 20th March, 1950, and any reference in this Act or any written law to a municipality or municipal council shall be construed as including a reference to the City of Nairobi or the City Council of Nairobi, as the case may require”. Thus, the City Council of Nairobi is vested with the same powers and has the same functions and responsibilities as a municipal council.

Town and County councils are largely rural in nature and provide minimal basic services such as markets, parks and gardens, sanitary inspection and refuse disposal; burial grounds and crematoria; fire services and brigade; public transport and social welfare services, basic environmental services, roads and drains, water supply and basic planning and development control among others. Other services are offered by line ministries which have administrative structures originating from the central government, through the provincial to district administrative system. The City Council of Nairobi and other larger Municipalities such as Mombasa and Kisumu undertake all the above services and other higher level functions such as health, education and engineering works.

The Local Government Act¹⁷¹ sets out a wide range of powers and duties bestowed upon local authorities. These include the provision of sewerage services, water, health, parking, garbage collection among others.¹⁷² Some of these functions constitute some of the areas that some LAs have partnered with private entities under the PPP regime. Section 143 of the Local Government Act¹⁷³ expressly allows LAs to enter into contracts necessary for the discharge of their functions.

The powers of LAs under the Local Government Act¹⁷⁴ are similar as those bestowed upon County Governments under Part 2 of the Fourth Schedule to the Constitution. The

¹⁷⁰ Chapter 265 of the Laws of Kenya.

¹⁷¹ Chapter 265 of the Laws of Kenya.

¹⁷² See sections 154, 155, 160, 161, 162 and 163 which set out some of the powers and duties vested upon local authorities.

¹⁷³ Chapter 265 of the Laws of Kenya.

¹⁷⁴ *ibid*

areas that County governments can partner with the private sector under the PPP regime include physical infrastructure, entertainment and recreations facilities, educational facilities, health amenities, commercial centres and agricultural facilities.¹⁷⁵

The government intends to use PPPs as one of the modes of achieving the development agenda by the county governments. Most of the functions hitherto performed by LAs will now be taken up by county governments with the operationalization of the devolved government as envisaged under the constitution of Kenya 2010.

The TFDG has recognized the devolved government interface with LAs in the context of PPPs and has taken the view that counties should draw lessons from infrastructure and service delivery approaches currently being practiced by the current local authorities.¹⁷⁶ In this regard, the TFDG has for instance referred to the concessioning of security and street lighting within the CBD in Nairobi and from JKIA to Gigiri to Adopt-A-Light under contractual arrangements involving concessions on billboard advertising by corporate entities helped in keeping the streets and adjacent areas well lit and relatively safe.¹⁷⁷

The TFDG has categorized the options for county public partnerships in Kenya.¹⁷⁸ For the local area activity, it is proposed PPPs are expected to cover issues such as neighborhood cleanup and NGO/Municipal Nature Conservancy. For the outsourced functions, PPPs may cover contracted waste service, outsourced billing function, urban improvement partnership and management contract for stadia. For cross-county wide full service, PPPs may be entered for water concession to a private company or privatization of county government.

Some of the envisaged infrastructure under county governments' functions set out in the fourth schedule will require huge capital outlays and it will not be possible to finance them from the normal budgetary allocations. This is how PPPs will come into play.

According to the TFDG, the following table shows county infrastructure that can be commercialized or developed through PPPs:¹⁷⁹

	INFRASTRUCTURE CATEGORY	TYPES OF INFRASTRUCTURE
1.	Physical infrastructure	<ul style="list-style-type: none"> Roads

¹⁷⁵ Interim report on Devolved Governments *supra* note 158 at 288

¹⁷⁶ Interim report on Devolved Governments at *supra* note 158 at 284

¹⁷⁷ *ibid*

¹⁷⁸ *ibid* at 135, Adapted from Robbins, Glen (2008)

¹⁷⁹ *Ibid* at 228

		<ul style="list-style-type: none"> • Offices and housing • Gas and electricity reticulation • Water and sewerage • Refuse yards and dumps • Streets and security lighting • Ferries and harbours • Cemeteries, funeral parlours and crematoria. • Fire stations, vehicles, plant and equipment.
2.	Entertainment and recreational	<ul style="list-style-type: none"> • Museums • Sports and cultural facilities • County parks and beaches
3	Educational facilities	<ul style="list-style-type: none"> • Libraries • Pre-primary education • Village polytechnic • Home-craft centers and • Childcare facilities
4.	Health amenities	<ul style="list-style-type: none"> • Dispensaries, clinics • Ambulances service and • Pharmacies
5.	Commercial centres	<ul style="list-style-type: none"> • Markets • livestock sale yards

6.	Agricultural facilities	<ul style="list-style-type: none"> • cooperative buildings and facilities • fish ponds • abattoirs
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2. PPPS BY LOCAL AUTHORITIES AND COUNTY GOVERNMENTS IN KENYA

While this thesis will draw from known and reported experiences from PPPs by LAs in Kenya generally to demonstrate the adoption of the PPP mechanism by LAs, its legal analysis will be confined to the two case studies of the PPPS between KAPs and the Municipality of Mombasa, and Adopt-A-Light and the City Council of Nairobi.

The choice of the two PPPs is motivated by several factors. First, this thesis adopts this approach as the two case studies are drawn from the two largest LAs in the country. Secondly, the two PPPs have faced similar challenges by councils after change of administration following civic elections and it was felt vital to focus on this two in order to identify reasons for the challenges and recommend solutions.

Further the two PPPs are the most publicized due to the fact that the disputes between the parties have been taken to court. Lastly, provision of parking services and lighting and advertisement services are public goods that have were up to early 1990s not seen as vital functions of the LAs yet they should be provided by the local authorities. With increased urbanization and the resultant population growth, these services have increased in demand and can be seen as component of the achievement of the Governments blueprint set out in the Vision 2030.

For the avoidance of doubt and in view of the pending court cases/ and arbitration relating to some of the PPPs forming the subject matter of this study, this thesis would not delve or focus onto whether or not the LAs in question were entitled to terminate the PPPs and/or challenge them, so as to comply with the rule of sub-judice. The thesis will therefore restrict to the rulings delivered and decisions made in interlocutory applications and interviews with the relevant parties.

This thesis will thus use the main PPPs entered by the major LAs in this country that is to say, the City Council of Nairobi and the Municipal Council of Mombasa as illustrations to analyze and study the arising research issues and recommend the best approaches

to be taken to ensure the entering of PPPs by LAs and/or county governments that will be effective to both the private party, the public body and the public, being the consumer of the services.

The focus of LAs is motivated by various reasons. First, with the coming into effect of the current constitution, the structure of LAs is expected to change to suit into the two tier devolved government structure. The service delivery and other functions being undertaken currently by LAs will be carried out by the county governments established under the current constitution. Second, PPPs have been identified as one of the mechanisms to be used by the county governments in performance of their functions as well as the implementation of the Government's economic blue print, vision 2030. It is thus vital to study the legal issues that have arisen from the use of PPPs by the LAs and analyse the current PPPs legislation to confirm whether they are sufficient to deal with the arising legal and policy issues arising from the PPPs by local authorities.

The choice of the case studies on PPPs by the City Council of Nairobi and the Municipal Councils is premised by the fact that they are the largest LAs and have also embraced the use of PPPs more than the smaller LAs. The PPPs to be analyzed in this research are some of the most publicized and thus material available on them.

3. PPPS EXPERIENCE IN NAIROBI

The City Council of Nairobi is one of the LAs in Kenya that has been shown to embrace the PPP mechanism the most for service delivery including infrastructural development. It is therefore vital to analyse some of the notable PPPs to demonstrate the embrace of the PPP mechanism by LAs in Kenya before specifically and critically analysing the two PPPs forming the key arguments for this study.

a. PROVISION OF WATER SERVICES IN NAIROBI

LAs in Kenya are authorized by the Local Government Act to undertake the supply of, establish acquire and maintain works for the supply of water within their area of operation.¹⁸⁰ The City Council of Nairobi (the Council) however faces numerous challenges like rapid urban growth and development, limited financial capacity and infrastructure development that lag behind urban growth amongst others¹⁸¹.

While Kenya needed to reform its water and sanitation sector due to deficiencies in public water systems it adopted a different approach to reform in the water sector from

¹⁸⁰ Section 178 of Local Government Act

¹⁸¹ Nairobi Town clerk Mr. Philip Kisia

the approaches taken by the neighboring countries in East Africa such as Tanzania which has privatized the water sector.¹⁸²

There was public resistance on forms of privatization such as lease contracts in Nairobi for example a proposed lease contract with a subsidiary of Vivendi collapsed after public raised concerns that the company had not been sourced competitively and yet it would make substantial profits from installing a new billing system while investing nothing during the duration of the contract and as such ,Kenya opted for the commercialization/corporatization model, underpinned by an overhauled regulatory framework established by the Water Act, 2002.¹⁸³

The Water Act establishes various regulatory agencies principle of which include the Water Resources Management Authority and the Water Services Board. The functions of the Water Resources Management Authority relate to the general management and regulation of water to ensure sustainable utilization of water¹⁸⁴ while the Water Services Board are vested with functions such as issue of licences for provision of water.¹⁸⁵

The Water Act envisages that the Minister will establish Water Services Boards¹⁸⁶ which will then be licences by the Water Services Regulatory Board to provide water services.¹⁸⁷ The Act further envisages that the Water Services Board will instead of providing these services directly, contract them out to Water Service Providers.¹⁸⁸

We have seen that LAs in Kenya which are empowered under section 178 of the Local Government Act to “undertake the supply of ,and establish, acquire and maintain works for the supply of Water” revamped their roles to suit into the regulatory framework provided under the Water Act.¹⁸⁹

It should be noted that the Water Services Boards are corporate bodies and have powers to be sued and sue in their corporate names, and, in the exercise and

¹⁸² Migai Akech *Privatization and Democracy in East Africa: The Promise of Administrative Law* (East African Educational Publishers Limited, 2009) at 78.

¹⁸³ *ibid*

¹⁸⁴ Section 8

¹⁸⁵ Section 47

¹⁸⁶ Section 51

¹⁸⁷ Section 53 (1).

¹⁸⁸ Sections 53(2) and 55.

¹⁸⁹ It is however arguable to state that by the Water Act not repealing section 178 of the Local Government Act, a conflict was created in that both the LAs and the Water Services Board can legitimately claim that they have a legal mandate to provide water services. Perhaps to reconcile this will be to adopt the rule on the interpretation of statute that provisions of a later statute (in this case the Water Act) overrides any conflicting provisions in former legislation.

performance of its powers and functions, to do and permit all such things as may lawfully be done or permitted by a body corporate in furtherance of its objects.¹⁹⁰

The idea behind establishing the water companies partly owned by LAs is to ensure managerial autonomy while equally facilitating managerial accountability.¹⁹¹ These companies are wholly owned by local authorities, even though in order to satisfy the requirements of the Companies Act the Mayor, and Town clerk each hold one share on behalf of the local authority as it is the case in the Nairobi City Water and sewerage Company Limited.¹⁹²

The City Council of Nairobi has thus chosen not to formally partner with the private sector in providing water services. It provides water in Nairobi through the Nairobi City Water and Sewerage Company's (NCWSC) whose formation arose from the enactment of the Water Act of 2002, which sought to delineate water infrastructure management and service provision in Kenya. This approach has however not been free from challenges. For example, the Nairobi Water and Sewerage Company Limited (NWSC) is private company wholly owned by the City Council of Nairobi which is appointed an agent of the Athi Water Services Board to provide water services within the City of Nairobi of the local council and has been known to be subject to interference by both the councillors and appointed officers.¹⁹³

The NWSC has however informally partnered with private actors in the provision of water in the city. An example of such informal arrangements is the PPP with Maji Bora Kibera (hereafter referred to as MBK), a type of private enterprise representing hundreds of small scale water vendors in Kibera and serving approximately 500,000 inhabitants¹⁹⁴. These two players in the water sector had an acrimonious relationship, which worsened the situation of water supply, for a long time before they entered into a partnership in 2004¹⁹⁵.

¹⁹⁰ Section 51 (3)

¹⁹¹ Migai supra note 182 at 78

¹⁹² *Ibid* at 24

¹⁹³ Harriet Naitore 'Study on Local Council Oversight Role and Social Accountability in Kenya ' prepared for the African Development Group (2008) www.siteresources.worldbank.org accessed 4th July 2011, at 48

¹⁹⁴ John Momanyi Birongo And Nhi Quyen Le 'An Analysis of Water Governance in Kibera Kenya' (Roskilde University Center : International Master of Science in Environmental Policy and the Global Challenges' 2004/2005) at 17
<http://www.environmentalexpert.com/Files%5C0%5Carticles%5C20194%5Cwaterproject.pdf> accessed on 10th July 2011

¹⁹⁵ *ibid*

The PPP was launched in July 2004 when MBK made the initiative of forming the partnership and approached the NSWC with their ideas on improved water provision in Kibera ¹⁹⁶. With the intention of boosting revenue collection following MBK's acceptance to police the water network and report illegal connections, the board of NWSC endorsed the partnership. The partnership was entered after a 'give and take' discussion. On its part, MBK asked for several concessions from NWSC including legalizing all illegal connections of MBK members, subsidizing the water prices, involving MBK in license issuance for new water vendors, installing meters (without payment) for MBK members whose connections lacked meter, issuing notices whenever NWSC planned to introduce water rationing and launching a reliable and efficient billing system.¹⁹⁷

NWSC in principle agreed to all of MBK's demands and tabled its own including the fact that MBK shall agree to have all the water sold metered and there shall be no connections by-passing meters, MBK to report regularly, any suspicious connections to NWC's hotline, MBK members to cease forthwith, dealing with any other party other than the official water meter readers, MBK members to pay all bills at the NWC's cashier office located at County Hall, Nairobi only and have a receipt of payment issued; and that MBK shall police the water network against tampering.¹⁹⁸

An examination of the the MBK-NSWC partnership against the background of the principles of PPPs reveals that in as much as it is not a formal PPP, it is characterized with some attributes of PPPs. For instance, the partnership brought together representatives from the NSWC and representatives from the MBK around the shared goal of water provision in Kibera.¹⁹⁹ On the other hand, an analysis of the same partnership reveals inadequacies relating to some core aspects of PPPs. To illustrate this is the fact that MBK and NWSC do not have clear guidelines that determine decision-making and neither are management responsibilities shared among these partners.²⁰⁰ Further, it is important that decisions are jointly made by partners in any PPP. This is made possible through the sharing of management responsibilities. In the case of MBK and NWSC, this important feature PPP is absent.²⁰¹ In such a scenario then, unity of purpose is compromised and this can be a catalyst for challenge to the PPP²⁰² which issue touch on the research issues the subject of this study.

¹⁹⁶ *ibid* at 74 and 75

¹⁹⁷ *ibid*

¹⁹⁸ *ibid*

¹⁹⁹ *ibid* at page 75 and 76

²⁰⁰ *ibid*

²⁰¹ *ibid*

²⁰² *ibid* at 77

The legitimacy and legality of the partnership itself is questionable because despite the exchange of memoranda, the partnership seems to be based on a 'gentlemen's agreement'.²⁰³

Due to the manner in which the partnership was entered into, it seems that the necessary principles for PPP namely transparency, accountability, legitimacy and legality, equity, inclusiveness, and competition were not on its agenda. The partnership was sought in essence to lock out competitors operating as independent water vendors.²⁰⁴ This in itself goes against the principle of competition.

It has already been pointed out that the MBK is the party that approached NWSC and offered to enter into the PPP arrangement. It is therefore worth noting that this constitutes unsolicited bids a kind of PPP envisaged by the 2009 PPP Regulation. Regulation 30 of the 2009 PPPs Regulations provide that unsolicited bids shall be authorized where – (a) innovative and related intellectual property associated with the proposed project's design and engineering costs incurred in developing the design has been considered and recognized; and (b) a feasibility study has been carried out and there is presently little interest in the private sector in the proposed project. The Regulations²⁰⁵ also state that the Minister for the time being in charge of finance should establish place rules setting out guidelines for authorization of unsolicited bids.

There is therefore need to ensure that the rules relating to unsolicited bids when enshrined, take into consideration the issue of anti-competition as well as take into account recommendations that will be set out in chapter 5 of this study regarding the challenges arising from PPPs identified in this study.

It is reported that the NWSC, is facing growing water scarcity and a non-revenue water ratio (NRW) of 45%, resulting from a combination of illegal connections, poor revenue management and decaying infrastructure.²⁰⁶ NRW covers, for example, leaks and spills in the network, faulty meters, which means the utility under-bills actual consumption, or fixed fees where the cost of actual consumption is far higher than the fee).²⁰⁷ It is vital that the utility seeks to reduce losses in the informal settlements where the majority of Nairobi's residents live and where most illegal connections take place. These issues raise the question of whether the decision of not embracing formal PPPs by the City

²⁰³ *ibid* at 77 to 78

²⁰⁴ *ibid*

²⁰⁵ Regulation 30

²⁰⁶ IRC symposium: *Sanitation for the urban poor partnerships and governance*, www.irc.nl last accessed on 25th August 2011.

²⁰⁷ *ibid*

Council of Nairobi is something that needs to be investigated further. There is certainly more potential for the Council and for that matter the NWSC to enter into PPPs to deal with the challenges arising from the experiences so far.

b. SOLID WASTE MANAGEMENT IN NAIROBI

There is no much literature on the Kenyan solid waste management sector except for the city of Nairobi. Generally, the collection of garbage ration is not proportionate to the waste generated.²⁰⁸ It is estimated that only 25 % of waste generated is collected.

²⁰⁹Until mid-1970-s, the Nairobi City Council singly collected over 90 per cent of the waste.²¹⁰ In mid 1980s, the appalling performance by the Council demand for municipal solid waste management services attracted private sector providers.²¹¹ Most of the private companies were and still are contracted by the residents independent of the Council. There are also a number of Community Based Organisations, ethnic associations, welfare societies, village committees, self help groups and residential and neighborhood associations which account of a substantial part of waste management in Nairobi.²¹²

The Council has no capacity to collect and dispose of the waste generated resulting into widespread and indiscriminate dumping on illegal dumpsites and waste pickers litter the city with unusable waste material without control. There is only one official dumpsite which is Council owned and operated which is full and located in the densely populated Dandora area. Until recently, there have been no deliberate and active processes by the council to enter into PPPs for waste management in the city.

The only formal PPP in the city's solid management sector to date was the pilot one year service contract awarded in 1997 to one of the private companies in Kenya, Refuse Handlers Limited.²¹³ The contract involved the daily sweeping of streets, roads, lanes, pavements and markets in the City's CBD, solid waste collection and transportation from the same area to the Dandora dumpsite at a fee agreed between the parties.²¹⁴

It is reported that the PPP worked very well in the initial years and the CBD became noticeably clean but payment problems from the Council's side led to poor performance

²⁰⁸ National Environmental Management Authority (NEMA) 'Over view of solid waste management in Kenya' http://www.nema.go.ke/index2.php?option=com_docman&task=doc_view&gid=28&Itemid=35 accessed on 25th August 2011

²⁰⁹ *ibid*

²¹⁰ *ibid*

²¹¹ NEMA *supra* note 208

²¹² *ibid*

²¹³ *ibid*

²¹⁴ *ibid*

particularly due to sit-ins by unpaid workers.²¹⁵ The contract which ended in 1999 was majorly financed by the Council as the revenue collected from waste chargers was inadequate.²¹⁶

In early 2011, a total of 33 companies have expressed interest in an extensive waste management programme, which is promising to transform the waste management in Nairobi the main component consisting of the transformation of the current Dandora dumpsite into a leisure park.²¹⁷

While 16 companies have expressed interest in the closing down of the notorious eyesore, 17 others are interested in entering into a PPP with the Council to collect, transport, treat and dispose of solid waste at a sanitary landfill at Ruai.²¹⁸ The Contractor is expected to innovate ways of managing harmful chemicals such as heavy metals - lead, mercury, cadmium, copper and chromium and dangerous gasses -like Methane that various studies have shown are found at or are being emitted from the 32-acre dumpsite.²¹⁹ The project leading to the closing down of the Dandora site is expected to take five years and projected to cost approximately Ksh3 billion.²²⁰

On the other hand, the successful bidder among the 17 is expected to design, construct and manage solid waste a sanitary landfill site at Ruai, which should also accommodate technology on recycling and that of energy recovery such methane gas for electricity generation.²²¹ The successful bidder is also expected to construct a solid waste recycling plant under the project which is projected to cost Ksh5 billion. The company will also collect and transport waste from public places for disposal, conduct mechanical/manual cleaning of public areas, develop on site solid waste management storage facilities and manage waste intermediate treatment.²²² It will also develop programmes for mobilization of community participation in Integrated Solid Waste Management (ISWM)²²³ including community awareness on waste minimization.²²⁴

The two projects are the latest efforts to privatize waste management in the city after previous attempts failed. For instance, the Ministry of Local Government signed a

²¹⁵ *ibid*
²¹⁶ *ibid*
²¹⁷ Justus Ondari 'Firms Seek to be filthy Rich From Garbage' *Daily Nation*, (10th January 2011)
²¹⁸ *ibid*
²¹⁹ *ibid*
²²⁰ *ibid*
²²¹ *ibid*
²²² *ibid*
²²³ *ibid*
²²⁴ *ibid*

Memorandum of Understanding with Italian corporation, Jacorossi, in 2004 to tackle the problem but it fell through.

C. PROVISION OF PUBLIC TOILETS WITHIN THE CITY COUNCIL OF NAIROBI

Human excreta are a major threat to public health and the environment in Nairobi. Unless properly managed, human waste is the source of both widespread disease and loss of civic and personal dignity and value. Less than 50 percent of Kenya's population has access to basic sanitation services.²²⁵ In Nairobi, the government has not invested in facilities in more than 30 years.²²⁶ For many years, existing public toilets were inaccessible or are overcrowded, unhygienic and poorly lit, and lack privacy and security.²²⁷

The World Bank's Water Sanitation Program (WSP) has in the past labeled Nairobi's the then 138 public toilets as unhygienic and barely functional.²²⁸ The problem was particularly dire in Nairobi's slums where many residents use plastic bags or "flying toilets" as a substitute for toilet facilities after dark. Others are forced to use unhygienic pit latrines that lack privacy and security.²²⁹

Until very recently, it would not be surprising to see human excreta lying on major streets within the Central Business District. Despite improvement in this sector over the years, the author has recently witnessed the presence of human waste in some of the lanes joining some streets such as River Road and Kirinyaga Road.

The 138 public toilets were built during the colonial era or soon thereafter and they are under the control of the Council but for a variety of reasons they for a long time received little or no management attention.²³⁰ The Council had for a long time no policy in place regarding the management and development of public toilets in the city and only constructed or rehabilitated the public toilets in emergency situations such as disease epidemics or special demands from the central government.²³¹

²²⁵ Acumen Fund 'Quality Sanitation Facilities for the Urban Poor' www.acumenfund.org accessed on 15th august 2011.

²²⁶ *ibid*

²²⁷ *ibid*

²²⁸ Water and Sanitation Program-Africa (WSP) 'From Hazard to Convenience: Towards Better Management of Public Toilets in the City of Nairobi' (2004). www.wsp.org accessed on 20th August 2011.

²²⁹ *ibid*

²³⁰ *ibid*.

²³¹ *ibid*

Public toilets suffered from low priority in the budgetary process. A study carried out by the WSP in 1995 revealed that the management and rehabilitation of public toilets required approximately Kshs. 4. 5 million but only Kshs 100,000/- (2.2 % of the required funds) were allocated to public toilets rehabilitation by the Council.²³²

The Water and Sanitation Program-Africa (WSP-AF) , a subsidiary group of the WSP Group Plc, a global business providing management and consultancy services particularly in relating to water and sanitation,²³³ at the instance of the Council conducted a study of the refurbishment, management and operation of public toilets in Ghana, Burkina Faso, Uganda and India and concluded that there was considerable potential for private sector participation in public toilet management in Nairobi.²³⁴ The study presented two variants of a Build Finance and Operate (BFO): one a fully private sector commercial operation for toilets within the CBD and the other involving community based organizations from the surrounding residential neighbourhoods.²³⁵

As a result of implementing some of the recommendation by WSP, the Council has in the recent past partnered with the private sector in the rehabilitation, management and provision of public toilets. This is a departure from the past where provisions and maintenance of the toilets depended wholly on the Council.

A notable PPP with the Council is the one entered with Ecotact Limited (Ecotact) resulting into what is commonly known as Iko toilets.

Before partnering with Ecotact to construct Iko toilets, Council has in the past collaborated and presently continues to collaborate with the Nairobi Central Business District Association (NCBDA) to renovate and maintain public toilets within the city centre. The NCBDA is made up of private businesses operating within the central business district.

The NCBDA was and still is tasked with the responsibility to rehabilitate the toilets, hire security personnel, attendants, and cleaners, and supervise day-to-day operation. The public toilets monitored by the NCBDA and users are required to pay a small fee for this service.²³⁶ NCBDA levies Ksh 5 and Ksh 10 for short and long call, respectively. The use of the public toilets after this rehabilitation and security improvement has increased considerably and currently more people are reported to be visiting the toilets than

²³² *ibid*

²³³ See www.wsp.org last accessed on 20th August 2011.

²³⁴ WSP *supra* note 221

²³⁵ *ibid*

²³⁶ *ibid*

before.²³⁷ However, lack of unequivocal support from the NCC and the government for this new arrangement is a major challenge for the NCBDA and the public toilets suffer from regular water and electricity cuts.²³⁸

The idea behind Iko toilets was to build pay-for-use toilets in Nairobi's urban centers while providing clean and affordable toilets in inter alia the CBD, residential place and slums using a cross-subsidy model. Customers pay Ksh 5 per use of the toilets and Ksh20 per use of the showers.²³⁹ Additional revenue comes from a) advertising inside the facilities b) rental of space for third-party vendors providing shoeshine services, and c) kiosks selling items such as newspapers and beverages, and providing mobile funds transfers (commonly known as MPESA).²⁴⁰

The project implementation strives to achieve objectives such as providing convenient, highly hygienic and sustainable water and sanitation services to urban centres; creating employment opportunities for youth; conserving diminishing natural resources as well as conserving public health; influencing a policy shift in the governance of municipalities in relation to the provision of water and sanitation services; transforming, restoring and ensuring sustainability of social dignity in the growing urban populations; and revolutionizing people's perceptions towards toilets as well as environmental and sanitation awareness.²⁴¹

Further, pollution from human waste in the surrounding areas to Iko toilets has decreased leading to a positive environmental footprint. As recognition, Ecotact has won several awards including *Africa Social Enterprise of the Year 2009* at the World Economic Forum and the *2010 Public Service Award* from the African Ministers' Council on Water.²⁴² In April 2011, Iko toilets founder was recognized for his effort and was awarded as the winner in that category by The Dubai International Best Practice Award to Improve the Living Environment.²⁴³ The company has also received similar awards including Guinness Book of World Record, the Clinton Global Initiative and African Council Ministers on Water among others.

The importance of the Iko toilets PPP is even more pronounced in Nairobi's slums where there is a dire need of management of human excreta. There are two *Ikotoilets* in

²³⁷ *ibid*

²³⁸ *ibid*

²³⁹ *ibid*

²⁴⁰ *ibid*

²⁴¹ www.ecotact.co.ke last accessed on 25th August 2011

²⁴² *ibid*

²⁴³ Harold Ayodo 'Iko-toilet' wins global recognition' *The Standard*, (Nairobi 16th May 2011) at 3.

Kawangware and Mathare operating in partnership with local committees who hold responsibility for operations.²⁴⁴ Under this approach, Ecotact's role is to provide management assistance to the committee for a percentage of revenue. Customers pay subsidized rates of either Ksh 3 for single use or Kshs 100 for a monthly family package.²⁴⁵ With an average of over 1200 customers a day, many residents have abandoned unsanitary latrines for *Ikotoilets*.²⁴⁶

To date, Ecotact Limited has invested over US\$1.2 Million in partnering with 20 municipalities in Kenya in respective PPPs to construct toilets in the municipalities countrywide including 12 in Nairobi serving 6.2 million people in 2010 up from 3.8 million in 2009 and creating a pool of 100 employees.^{247 248}

The PPPs are 5-year contracts with the respective municipalities to build and exclusively operate toilet facilities on government owned land. Under this Build-Operate-Transfer (BOT) model, Ecotact maintains operational rights for 5 years, at the end of which the contract would either be renewed or the facility be transferred to the municipality.²⁴⁹ The partnership ensures cost recovery for Ecotact as well as the development of management capabilities to sustain high quality service after the handover.²⁵⁰

In 2010, Ecotact launched the *Ikotoilet* for Schools project, financed by the government, with the vision of building 1000 *Ikotoilet* in schools by 2020.²⁵¹ The initiative is expected to transform school sanitation by improving hygiene and reducing incidences of waterborne diseases.²⁵² Ecotact has already built 7 *Ikotoilets* in Kenya's Kikuyu constituency with the total expected to reach 60 by year-end.²⁵³ In schools, *Ikotoilets* are built with biodigesters designed to convert waste to energy, producing biogas for cooking meals or electricity for lighting.²⁵⁴

²⁴⁴ *ibid*

²⁴⁵ *ibid*

²⁴⁶ *ibid*

²⁴⁷ *Ibid.*

²⁴⁸ Khuram Hussain. 'Providing Adequate Sanitation to the Base-of-the Pyramid in Kenya' <http://www.johnson.cornell.edu/Portals/0/PDFs/2nd%20place.pdf> accessed on 15th August 2011.

²⁴⁹ *ibid*

²⁵⁰ *ibid*

²⁵¹ *ibid*

²⁵² *ibid*

²⁵³ *ibid*

²⁵⁴ *ibid*

The Iko toilets concept has stimulated demand across East Africa and it is reported that there are proposals to adopt similar models in Tanzania and Uganda.²⁵⁵

4. PPP BETWEEN CITY COUNCIL OF NAIROBI AND ADOPT-A-LIGHT

By an agreement dated 28th March 2002 supplemented by another agreement dated 19th November 2002, Adopt-A-Light Limited (Adopt-A-Light) entered into a PPP agreement with the City Council of Nairobi (the Council) for the provision of advertising and lighting services on some approved streets on the City of Nairobi.²⁵⁶ In accordance with the terms of the contract, Adopt-A-Light was granted exclusive right to use the street light poles on the approved streets for advertisement services provided to members of the public at a fee. The contract at the first instance granted Adopt-A-Light permission to place advertisements on some streets and subsequently on all "other streets to be approved by the city engineer on written application".²⁵⁷

Under the PPP, the company partners with the City Council of Nairobi to sell advertising space on street lamps on public roads. Companies in turn contract with Adopt-A-Light Limited to "adopt" highway, street and slum lights, traditional billboard to place their advertisement. Adopt-A-Light also provides high mast lighting as well as advertising services in slums. Local companies including banking and financial institutions, manufacturing companies as well as such large scale multinationals as AIG, Colgate and LG have also been seen "adopting" the lights.

Adopt-A-Light has won many awards for its business model, including the 2009 UN Habitat Business Award, which rewards organizations for best practices regarding sustainable infrastructure, affordable housing and the like.²⁵⁸ One of the immediate gains from the Adopt-A-Light model are said to be better lit roads which has enhanced security in the areas which have received the lights under the Adopt-A-Light initiative. Proper lighting also means that the population and especially those in slums who have received the benefits are able to work longer in once darkened corridors. These and other benefits of the Adopt-A-Light initiative are documented in a 2006 report conducted by the Steadman Group.²⁵⁹

The Late Honourable Karisa Maitha the then Local Government Minister is on record as having recognized the benefits derived from the Adopt-a-Light/City Council of Nairobi

²⁵⁵ *ibid*

²⁵⁶ This information was obtained by perusing the pleadings and other papers filed in in the court file in Court of Appeal Civil Appeal Number 159 of 2009 , *Adopt –A- Light Limited v Magnate Ventures Limited and 3 Others(unreported)*

²⁵⁷ *ibid*

²⁵⁸ 'Public –Private Partnership Meets advertising' www.americancity.org last accessed 12th August 2011.

²⁵⁹ Accessible from Adopt-A-Light's website www.adopt-a-light.co.ke last accessed on 12th August 2011.

arrangement as a classical example of a PPP for the common good of the City of Nairobi.²⁶⁰

Under the terms of the contract, the Council was barred from directly or indirectly competing with Adopt-A-Light or permitting other third parties to place any form of advertisement on the designated street poles.

In return for advertising services ceded to Adopt-A-Light's control, Adopt-A-Light is obliged to maintain the lamps, a service that it was clear the Council did not hitherto have the capacity nor the resources to carry out. In further consideration of the use of the street poles for the advertising services, Adopt-A-Light agreed to finance the initial project set up costs including the creation of the necessary awareness of the project thus enabling advertisers to be drawn to the project.²⁶¹ Adopt-A-Light was also obliged to finance the repairs and maintenance by provision of all materials for the adopted street light. Adopt-A-Light contends that it has to date invested huge amounts of money to the tune of hundreds of millions of Kenya Shillings towards the implementation of the PPP.²⁶²

At the time of entering into the PPP, advertising on street lights was a relatively new phenomenon and Adopt-A-Light appear to have pioneered this. Adopt-A-Light indeed claims that they instigated the idea of advertisement on street lighting in Nairobi.²⁶³

In 2006, Adopt-A-Light claims that the City Council of Nairobi officials started removing advertising media from the designated street poles in breach of the contract.²⁶⁴ A litany of suits has been filed by both parties against each other as well as by or against third parties from the advertising industry revolving around the PPP.

One such suit was by Adopt-A-Light in High Court Civil Case No. 637 of 2006 (*Adopt-A-Light Limited v the City Council of Nairobi*) in which it sought interim measures of protection pending referral of the dispute to arbitration in view of the existence of an arbitration clause.²⁶⁵ An injunction was granted barring the Council from removing the advertisement media pending referral to arbitration. The suit was eventually stayed pending the resolution of the dispute by arbitration after the Chartered institute of

²⁶⁰ Luke Mulunda 'Adopt-A-Light Contract Clean, Declares Govt' *Financial Standard* (Nairobi 20th May 2003)

²⁶¹ *Supra* note 256

²⁶² *Supra* note 256

²⁶³ www.adopt-a-light.com accessed on 12th July 2011.

²⁶⁴ *Supra* note 256

²⁶⁴ *ibid*

²⁶⁵ *ibid*

Arbitrators appointed an arbitrator in terms of the provisions of the contract, the City Council having declined to agree on the appointment of an arbitrator.²⁶⁶

Some of the other stakeholders in the advertising industry had at the same time started questioning the validity and legality of the contract between Adopt-A-Light and City Council of Nairobi. Amongst them were Magnate Ventures Limited and Outdoor Advertising Association of Kenya who sought to be joined in High Court Civil Case No. 637 of 2006 as well as in the arbitration which request was declined.²⁶⁷

Their request to be joined in the arbitration was also made vide High Court Civil Case No. 708 of 2008 (*Magnate Ventures Ltd and Others v Adopt-A-Light Limited and Others*) which application was allowed by Khaminwa J in ruling delivered on 10th March 2009.²⁶⁸ Adopt-A Light has appealed against this decision in Court of Appeal Civil Appeal No 254 of 2009 which appeal is pending for resolution, objecting that third parties should not have been allowed to participate in the arbitration.²⁶⁹ At the time of writing this paper, the arbitration had been halted as a result of the pending court of appeal case and as such no resolution of the dispute has been made. It is public knowledge that there is a huge backlog of appeals before the Court of Appeal and unless the current judicial reforms deal with this issue, it will be after a couple of years that the dispute will be resolved.

The crux of the challenge of the contract by the other advertising players in the suits filed including High Court Civil Case No. 637 of 2006 and High Court Civil Case No. 708 of 2008 has been that the contract was illegal for *inter alia* failure to comply with the provisions of the Public Procurement Act, 2005 of the Exchequer and Audit (Public Procurement) Regulations 2001.²⁷⁰ The parties also contended that Adopt-A-Light had been granted a monopoly in the provision of advertising and lighting services under the PPP.²⁷¹

The basis of the challenge of the contract by Magnate Ventures Limited and Outdoor Advertising Association of Kenya in the suits filed in court has been that, as stakeholders in the advertising industry and rate payers in the City Council of Nairobi, they are entitled to and the Council is accountable to them as well as to any other interested businessmen and ratepayers in the City of Nairobi on how revenue is

²⁶⁶ *ibid*

²⁶⁷ *ibid*

²⁶⁸ *ibid*

²⁶⁹ *ibid*

²⁷⁰ This information was obtained by perusing the pleadings and other papers filed in the court file in the respective cases.

²⁷¹ *ibid*

collected and utilized by the Council of Nairobi and how services and goods are procured.²⁷²

In most of the suits filed in court, the Council supported the position that the contract was illegal as contended by Magnate Ventures Limited and Outdoor Advertising Association of Kenya. For instance in High Court Civil Case No. 708 of 2008, the Council stated that it had repudiated the contract “*and or/terminated the unlawful agreement upon discovering that it was tainted with illegalities in the extreme*”²⁷³ Adopt-A-Light has maintained that the contract subsists and is renewable after every five years as it has not fell into breach.

The author has observed that it appears Magnate Ventures appears to currently have a huge market share in the street pole lighting and advertising industry. The City Council of Nairobi has indeed confirmed that it has contracted other contracted other companies to provide the advertising and lighting services within the city.²⁷⁴

Other than damages or losses said to have been incurred by Adopt-A-Light as a result of the challenges, third parties who had contracted Adopt-A-Light to place adverts on the street poles have also been reported to have suffered loss and damage as a result of the challenges to the PPP.

One such instance is reported in the case of *Republic v Nairobi City Council & 3 Others Ex-parte Barclays Bank of Kenya*.²⁷⁵ It is reported that as a result of the dispute between the Council and Adopt-A-Light, a litany of suits has been filed against Adopt-A-Light and its customers including Barclays Bank, the Applicant herein. Barclays bank in this suit sought to prohibit the hearing of criminal proceedings instituted against it in the subordinate court at the City Courts.

The criminal proceedings had been instituted by the Council after issuing enforcement notices under the Physical Planning Act²⁷⁶ demanding the payment of advertising revenue to the Council. Barclays Bank was aggrieved as it maintained that it had paid advertising charges to Adopt-A-Light. The Court found that, by instituting the criminal proceedings the Council was actuated by malice and further had an ulterior motive which actions the Court could not allow through the criminal proceedings. In the

²⁷² This information was obtained by perusing the pleadings and other papers filed in the court file in High Court Civil Case No. 637 of 2006 at the Milimani Commercial Courts.

²⁷³ A perusal of the defence filed by the City Council of Nairobi from the court file in High Court Civil Case No. 708 of 2008.

²⁷⁴ *ibid*

²⁷⁵ [2011] eKLR.

²⁷⁶ Chapter 228 of the Laws of Kenya.

circumstances the court issued the prerogative order of prohibition to stop further proceedings in the criminal proceedings.

It is very vital to note for purposes of this study that the PPP with Adopt-A-Light was entered into in March 2002 and there was a change in office of the Council after the general elections comprising civic elections in December 2002. It is noteworthy that the challenge to the contract was harnessed and heightened after the new councilors took office after the civic elections.

5 PPP BETWEEN MUNICIPAL COUNCIL OF MOMBASA AND KAPS PARKING SERVICES LIMITED

Kenya Airports Parking Services (KAPS) is a company incorporated in Kenya which operates the business of provision of car parking services, access control and revenue management.²⁷⁷ The Company states that it has made several innovations including world-class parking systems, audio and video automation and data capture solutions.²⁷⁸ KAPS has installed such systems for municipalities, major facilities, parking lots and shopping malls.²⁷⁹ The analysis in this study will however be restricted to the arrangement between KAPS and the Municipality of Mombasa.

By an agreement 28th June 2008 between KAPS and Municipal Council of Mombasa (the Council), the parties entered into a PPP for provision of parking services within the Municipality of Mombasa including the following services:²⁸⁰

- Street pay and display ticketing;
- Park management and revenue collection for private vehicles;
- Management of *matatu* parking and revenue collection;
- Management of bus parking and revenue collection;
- Collection of enforcement charges;
- Advertising and information services on parking equipment and systems;
- Quality of service support.

The PPP was designed to be implemented through KAPS Municipal Parking Services Limited, incorporated by the parties as a joint venture company between to act as the

²⁷⁷ http://www.kaps.co.ke/modules/about_us/?sid=lpgrhvh3q7snbiohb5s6a56j3 accessed on 24th August 2011.

²⁷⁸ *ibid*

²⁷⁹ *ibid*

²⁸⁰ This information was obtained from perusing the pleadings and papers filed in court in High Court Civil Case Number 434 of 2009 *Kenya Airports Parking Services & Another v The Municipal Council of Mombasa*

special purpose vehicle for the actualization of the PPP.²⁸¹ Both parties have shareholding in the special purpose vehicle company with KAPs owning 75% and the Municipal Council of Mombasa, 25% of the shares.²⁸²

One of KAP's obligations under the agreement is the installation of equipment and construction of such structures and facilities so as to enhance the provision of the Parking Services.²⁸³ KAPS contends that it has invested colossal amounts of monies to the tune of over 36 million into the joint venture.²⁸⁴

It is a term of the contract that KAPs remits an advance share of profits in the sum of Kshs 1,000,000/- every month in arrears for the first three years of the contract and thereafter increasing at the rate of 10% per annum at the end of each calendar year.²⁸⁵

In High Court Civil Case Number 434 of 2009 (*Kenya Airports Parking Services Ltd and Another v The Municipal Council of Mombasa*) KAPs sought interim measures of protection pending resolution of a dispute that had arisen between the parties by arbitration²⁸⁶. The dispute arose after the Municipal Council of Mombasa had resolved to terminate the PPP. KAPS disputed the termination.

The interim measures of protection were granted on 17th June 2009 and were in the nature of an injunction restraining the Municipal Council of Mombasa from collecting parking fees or in any other manner in contravention of the agreement between the parties. The suit has since been stayed pending resolution of the dispute by arbitration which was ongoing as at the time of writing this paper.²⁸⁷

The Municipal Council of Mombasa has maintained that it was entitled to terminate the agreement on *inter-alia*, the ground that no resolution was passed by the Council's tender committee to authorize the entering into the PPP.²⁸⁸

Notwithstanding that a suit was pending and an injunction having been issued to restrain the Council from collecting parking fees in contravention of the PPP, the Council entered into another PPP with another company, Summit Cove Lines Company

²⁸¹ *ibid*

²⁸² *ibid*

²⁸³ *ibid*

²⁸⁴ *ibid*

²⁸⁵ *ibid*

²⁸⁶ See the Ruling dated 24th March 2010 by Kimaru J on an application for disobedience of an injunction order [2010] eKLR.

²⁸⁷ Interview with Lawrence Madialo, Legal Officer KAPs (Nairobi 20th September 2011).

²⁸⁸ *ibid*

to provide the same parking services.²⁸⁹ This according to KAPS legal officer Mr. Lawrence Madialo was tantamount to undermining and breaching the PPP with KAPS as Summit Cove Lines Company was granted the power to carry out the same parking services in the areas allocated to KAPS under the PPP.²⁹⁰ Indeed it was a term of the contract that the agreement related to existing car parks as at the date of the commencement and other new car parks subsequently developed by the Council were to be managed by KAPS.²⁹¹

A constitutional petition was filed by the Kenya Transport Association and by a ruling delivered on 20th May 2011, the Honourable Justice Ojwang annulled the PPP between the said Summit Cove Lines Company and the Municipality of Mombasa for *inter alia*, failure to comply with the Public Procurement and Disposal Act.²⁹² KAPS did not participate in these proceedings.²⁹³

Similar to the Adopt-A-Light PPP with the City Council of Nairobi, the KAPS PPP was entered into in 2006 and the challenge to it commenced in or about 2009 after new councilors took office following the 2007 general elections.

A further similar issue as that arising from the Adopt-A-Light arrangement in the potential of third party liabilities claims against KAPS as a result of the dispute with the Council. It has been reported that the Council has collected parking fees from motorists who had paid the parking fees to KAPS and some motor vehicles were clamped forcing various motorists to make second payments of parking fees to the Council.²⁹⁴

6. ANALYSIS OF THE CASE STUDIES: TRENDS IN PUBLIC PRIVATE PARTNERSHIPS BY LOCAL AUTHORITIES IN KENYA

The above analysis of the main PPPs entered by LAs in Kenya illustrate the fact the LAs are increasing adopting the PPP mechanism in Kenya for service delivery. There are however certain traits that bear a common strand across most of the PPPs entered by the LAs.

LAs have not been keen in implementing PPPs and most of PPPs have been subjected to political interference by the councilors with each elected council seeming to prefer a

²⁸⁹ *Kenya Transport Association v Municipal Council of Mombasa* [2011] eKLR.

²⁹⁰ Interview with Lawrence Madialo, Legal Officer KAPS (Nairobi 25th September 2011).

²⁹¹ *Supra* note 260

²⁹² *Supra* note 289.

²⁹³ Interview with Lawrence Madialo, Legal Officer KAPS (Nairobi 20th September 2011).

²⁹⁴ *Supra* note 459.

different player in the PPP. Some of these challenges have resulted in litigation as seen in the Adopt-A-Light and KAPs case studies and the common theme has been that the councils have taken unilateral decisions to cancel the PPP arrangement without there being any protection accorded to the private sectors to recoup their investments.

In the two main case studies of KAPS and Adopt-A-Light, there has been outright challenge to the PPPs by the respective councils resulting in litigation. Even in PPPs where no litigation has ensued, it is reported that the LAs have interfered with the running and implementation of the PPPs. Problems have also been reported in the informal PPP arrangement by the NSWC and by an NGO in Kibera. The lack of support accorded NCBDA relating to the rehabilitation and management of public toilets is also instructive to point out in this regard. The analysis of the previous attempts to privatize the solid waste management by the City Council of Nairobi is also a case in point. We have already pointed out that the only formal PPP with the City Council of Nairobi in solid waste management collapsed due to lack of commitment from the Council.

In all case studies whether there has been litigation or not, there are no safeguards that have been put in place to guard the private actors from the effects of political risks. That means that those PPPs in which no challenge has been reported such as the Iko toilets arrangement are not immune from the effects or political risk inherent in PPPs.

This failure to adequately shield the private sector from the effects of political risk is not unique in Kenya. A similar trend in local government has been identified in other jurisdictions as well.²⁹⁵ The experience of Northern Electricity in Namibia is a case in point.²⁹⁶ Contracted by the Namibian Ministry of Regional and Local Government and Housing (MRLGH) in 1996 to operate a set of state-owned assets in the more densely populated northern region of Namibia, Northern Electricity provided a reliable and profitable service in a rural area where the LAs had been losing approximately N\$10 million (US\$1 million) annually.²⁹⁷ Despite Northern Electricity's success in managing the business of electricity provision, their management contract was not renewed by the newly created Electricity Control Board following change of administration and the contract was awarded instead to a joint venture between the national utility company NamPower and several local and regional governments.²⁹⁸

²⁹⁵ D. O. Ongolo 'Public Private Partnerships in Kenya' prepared for The Institute of Economic Affairs, Kenya (7th July 2006) at 9. www.ieakenya.or.ke/documents/Public%20Private%20Partnerships.pdf accessed on 20th June 2010 at 33

²⁹⁶ Peter Farlam: *Accessing Private- Public Partnership in Africa*, (Nepad Policy Focus Series SAIIA 2005).

²⁹⁷ *ibid*

²⁹⁸ *ibid*

It is recognised that the main channel of influencing council decisions in support of locally identified needs and preference should be through relevant motions and effective articulation of citizen needs in the council meetings leading to entering of PPPs that are for the benefit of the residents of the LAs. It has however been observed that this channel is not effectively utilised as decisions in the council are influenced by factional interests, personal agenda, local social and political environment.²⁹⁹ Further it has been noted that the capacity of local councillors to understand and interpret the juridical attributes of a PPP are at best limited.³⁰⁰

It is quite clear from the two case studies of KAPs and Adopt-A-Light in Mombasa and Nairobi that the sanctity of contracts has not been adequately provided under the laws as well as adequately enforced by the judiciary. For instance, we have pointed out that Lady Justice Khaminwa allowed third parties to the PPP who were competitors to the Adopt-A-Light (and who had in conjunction with the Council challenged the PPP) to participate in the arbitration proceedings between the Council and Adopt-A-Light Limited

³⁰¹

We have seen in chapter 2 of this study that PPPs by their very own nature envision a long term relationship between the public entity and the private actor. One of the reasons for this semi-permanent nature of PPPs is that PPPs are usually very capital intensive and a considerable period of time should be allowed so as to enable the private actor recoup the investment made in the embryonic formation and initial installation of the infrastructure needed for the implementation of the PPPs.

We have pointed out in setting out the components of the various case studies the enormous amounts of monies that the private actors have been said to have invested in towards the implementation of the PPPs and the arrangements were expected to last for periods ranging from 5 years to 25 years and some have renewal clauses for further terms.

If we look at the two main case studies, the Adopt-A-Light contract was to last for an initial period of 5 years renewable every other five years unless Adopt-A-Light fell into breach.³⁰² The KAPs arrangement was to run for an initial period of 15 years and thereafter to be renewed for a further ten years unless the contract was terminated in

²⁹⁹ Naitore *supra* note 193 at 48

³⁰⁰ *ibid*

³⁰¹ This information was obtained by perusing the pleadings and other papers filed in in the court file in High Court Civil Case No. 708 of 2008 *Magnate Ventures Limited and another v Adopt –A- Light Limited and 2 Others* (Unreported)

³⁰² *Supra* note 256

accordance with the provisions of the contract.³⁰³ Adopt-A-Light was to finance the repairs and maintenance by provision of all materials for the adopted street light while KAPS is obliged to inter alia provide and maintain infrastructure necessary for provision of parking services. Both private parties in the two PPPs contend that they have invested huge amounts of money to the tune of hundreds of millions of Kenya Shillings towards the implementation of the PPPs.³⁰⁴

It is therefore not in consonance with this unique attribute of PPPs for the PPPs to be halted before the private parties have recouped their investments or without there being an entitlement to compensation.

This unique feature of PPPs as long term partnerships has not been appreciated by LAs in Kenya. Unless good and legally justifiable grounds exist for challenge of the PPPs by the LAs, it would be unfair to the private actors and illegal for PPPs to be challenged early in the term before they start recouping their investments.

The trend to challenge PPPs and political interference has not been seen in central government, line ministries or parastatals that have partnered with private actors under the PPP mechanism. We have not seen, for instance reluctance by these bodies to implement PPPs when there is a succession of office either through general elections, by-elections or a change of the board members for state corporations or line ministries. We will briefly analyse the privatization of Kenya Airways Limited and the RVR Railways Concession as illustrations in this regard.

i. The privatization of Kenya Airways .Looking at Kenya Airways Limited as a way of illustration, the airline was until its privatization in 1996 a state corporation controlled by the Government of Kenya.³⁰⁵ The Corporation was set up with very little equipment, without adequate technical expertise, competent employees and effective management and had virtually no financial base.³⁰⁶ A host of other managerial problems also contributed to the airline's decline in service provision. From its inception in 1977 until 1995, the airline had ten different government-appointed chief executives and therefore, each successive holder of the office had insufficient time to develop and implement effective strategies.³⁰⁷

³⁰³ *Supra* note 280

³⁰⁴ *Ibid*, *supra* note 256.

³⁰⁵ Yaw A. Deborah and Oliver K Toroitich 'The Making of an African Success Story: The Privatization of Kenya Airways' *Thunderbird International Business Review* Vol 47(2) 205-230 March –April 2005 at 212

³⁰⁶ *Ibid*

³⁰⁷ *Ibid* at 213

Moreover, because the board of directors consisted mainly of political appointees with no specific experience either in managing a business, in general, or an airline in particular, the airline lacked clear strategic direction.³⁰⁸ Further, despite the fact that the airline had the largest market share of East and Central Africa regional routes and a fair share of international routes from Nairobi (e.g., Nairobi–London, Nairobi–Rome, Nairobi–Dubai), the airline was losing customers, particularly in the tourist segment, mainly due to substandard flight services and persistent late arrival and departure times.³⁰⁹

By 1991, Kenya Airways was unable to pay its debts, which had run into millions of U.S. dollars. Hence, the government continually had to bail the company out of bankruptcy by paying its foreign loans (which the government had guaranteed).³¹⁰ In fact, by 1992, the airline was technically bankrupt, and, hence, the government was searching for a way to improve Kenya Airways' messy balance sheet and bring it to profitability.³¹¹ This was achieved by commercialization and privatization following adoption of recommendations of the Probe Committee under the chairmanship of Isaac Omolo Okeru.³¹²

In January 1996, the government sold 26% of its shareholding to KLM for U.S.\$26 million and currently owns only 23 % .³¹³ The other shareholders are drawn from other members of the public majorly from East Africa.

Government administration has changed several times since 1996 following elections held in 1997, 2002 and 2007. No attempts to challenge KQ's operations has been taken by the successive governments. The government has on the other hand been greatly propmoted and marketed the airline as the " pride of Africa" and has continually supported its operations.

It is indeed reported that one of the factors that has greatly influenced the successful privatization of KQ has been lack of interference from political decision makers in the affairs of the company.³¹⁴ The same cannot be said of LAs in Kenya. For instance the PPP entered by the Municipal Council of Mombasa and KAPS is very unique in the author's view as it does not make legal sense for the Council to challenge the

³⁰⁸ *ibid*

³⁰⁹ *ibid*

³¹⁰ *ibid*

³¹¹ *ibid*

³¹² *ibid*

³¹³ *ibid* at 217

³¹⁴ *ibid* at 227.

operations of a company in which it has equity ownership and going further ahead to allow its competitors to engage in the same business the subject matter of the PPP between them. This would be for instance tantamount to the government of Kenya setting up a competing airline against Kenya Airways in which it has equity ownership.

ii. The RVR Concession. By 2006, the Kenya Railways Corporation had been relegated to an insolvent rail utility with \$280 million in outstanding debt, massive investment needs required to upgrade a rail service dependent on poorly maintained track, wagons and locomotives averaging 40 years in age, 4,000 to 5,000 unnecessary employees, colossal revenue leakages, rampant theft, and two government owners, with all of the associated political and regulatory complications.³¹⁵ Prior to this, by 1992 the Kenyan government, responsible for most of the stretch of rail infrastructure, employed 22,000 workers to look after it, probably at least 15,000 more than necessary.³¹⁶ In the 2004–05 fiscal year, the annual cargo tonnage had slipped to 1.9 million, less than 20% of total east-west shipping. By June 2004 Kenya Rail had accumulated \$277 million in debt.³¹⁷ The monthly cash deficit was around \$3.2 million, with annual losses running at about \$39 million.

By 2005 the Kenya rail was spending more on salaries and wages than it was on maintenance and equipment accounting to about 40% of total revenue. Months before entering into the concession, the corporation employed 9,500 workers, down from a high of 22,000 in 1992, but still 4,000 to 5,000 too many for even a reasonably efficient operation.³¹⁸ In Uganda the labor force at 1,500 seemed three times more than what was needed.

The need to do something about the rail line was recognized in the late 1990s at about the same time in both countries. The Kenyan Finance Minister, Musalia Mudavadi, announced in June 1998 that Kenya Rail would be concessioned.³¹⁹ International consultants were hired, but they advised that a concession was not practical unless the Uganda side of the line was brought into the deal.³²⁰ In August 1999 Uganda asked the Public-Private Infrastructure Advisory Facility (PPIAF) for funding to survey

³¹⁵ Public Private Infrastructure Advisory Facility (PPIAF) 'A PPP against the Odds: The Kenya Uganda Rail Concession Fights for Survival' (2010) at 3
<http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/publication/Kenya-Uganda%20Rail%20Case%20Study.pdf>
accessed on 9th September 2011 at 1

³¹⁶ *ibid*

³¹⁷ *ibid*

³¹⁸ *Ibid* at 3

³¹⁹ *ibid* at 2

³²⁰ *ibid*

opportunities for expanding private participation in the country's infrastructure services. The resulting Country Framework Report put rail concessioning high on the list of quick-win possibilities.³²¹ Uganda confirmed this via a second PPIAF-funded study in July 2000, which looked specifically at the rail sector.³²² The study recommended a joint rail concession with the Kenyan government. In June 2002 the Kenyan government also requested PPIAF funding to assess the kind of regulatory framework needed for transport in general, and a rail concession in particular. Shortly after the initiation of that study the government hired the International Financial Corporation (IFC) advisory team to begin work on a transaction structure and tender documents. The PPIAF research on the regulatory framework, completed in April 2003, was closely coordinated with the IFC advisory work.³²³

Later in 2003 the Kenyan President Mwai Kibaki and Ugandan President Yoweri Museveni announced at a meeting hosted in Kampala that a joint concession would be prepared.³²⁴ Procurement. In late October 2005 after two years of deal structuring and procurement, a consortium led by Sheltam Rail (Pty) Ltd (Sheltam) was named the preferred bidder for what had become a 25-year concession. Sheltam was an affiliate of the Sheltam Grindrod group, which included Comazar (Pty) Ltd, the biggest private railway operator in Africa, which in turn had links to South Africa's largest transport and logistics enterprise, Transnet. Comazar had already been active in Burkina Faso, Cameroon and Madagascar. Through its local consortium, Rift Valley Railways-Kenya (RVR-Kenya), Sheltam edged out the Magadi Soda Consortium, led by Rail India Technical and Economic Services Ltd (Rites). The two groups reportedly spent as much as \$1.5 million each on their bids. The joint concession is structured legally as two separate 25-year concession contracts signed by each government with the subsidiary company in each country of the RVR Investments (Pty) Ltd ("RVR"), which acts as the overall concession holding company.

In spite of seven years of preparation, and ground-breaking efforts to manage key political and government risks, the deal came perilously close to collapse on October 30, 2006, just a day before RVR was scheduled to take over the railway.³²⁵ A key member of Sheltam's consortium pulled out, meaning that the equity was no longer in place and the financial closing with lenders scheduled for later that day, had to be called off. Collapse of the deal with RVR would have meant starting the procurement process

³²¹ *ibid*

³²² *ibid*

³²³ *ibid*

³²⁴ *ibid*

³²⁵ *ibid* at 5

over and Sheltam would have lost millions in project preparation costs as well as over \$3 million in operating costs already incurred.³²⁶

Sheltam was given 45 days by the two governments to rebuild its consortium with a new set of credible investment partners and source the \$24 million equity required by the lenders as a precondition to financial close of the debt facility.³²⁷ In a whirlwind series of meetings and negotiations, three new shareholders were recruited.³²⁸ The new partners included Trans-Century, a Kenyan institutional investor (20%), global infrastructure company Babcock & Brown (10%), and the Industrial and Commercial Development Corporation Investment Company, (10%).³²⁹

On December 14, 2006, the respective governments were paid their one-time entry fees (\$2 million for Uganda and \$3 million for Kenya), and the deal was finally closed.³³⁰

Before and after closure of the deal, experts predicted that within three years, the rail line would be able to carry five million tons of cargo, sharply increasing revenues for the private operators.³³¹ Economic benefits to both countries were expected to include a reduction in the costs of carrying goods within the economies by an estimated \$42 million a year.³³² The governments also expected millions of dollars each year in new corporate tax revenues, and equally large savings in road maintenance and fuel costs.³³³

Unfortunately, three years later the predictions of experts proved to be off the mark, and the deal was once again on the verge of collapse. The concessionaire had effectively defaulted on payment of concession fees and agreed investments and improvements in cargo haulage and the two governments of Kenya and Uganda had given notice of terminating the concession³³⁴³³⁵. In a bid to inject more capital to forestall the cancellation of the concession, Sheltam, the majority shareholder sought to bring in a new entrant, Ambience with the intention of the former acquiring major shareholding.³³⁶ Trans-Century and the other shareholders countered with a lawsuit to block Ambience's

³²⁶ *ibid*

³²⁷ *ibid*

³²⁸ *ibid*

³²⁹ *ibid*

³³⁰ *ibid*

³³¹ *ibid*

³³² *ibid*

³³³ *ibid*

³³⁴ *ibid*

³³⁵ A. M Kitolo 'Kenyan Experience on PPPs' www.unescap.org accessed on 24th September 2011.

³³⁶ PPIAF *supra* note 315 at 5

entry into the consortium.³³⁷ In March 2010 the International Financial Corporation hosted shareholder negotiations in London, which resulted in a joint statement indicating agreement had been reached on a shareholder injection of Sh19 billion (\$250 million) to restructure RVR.³³⁸ The new investments would translate into a 51% shareholding for Ambience, with Trans-Century expanding its shareholding from 20% to 34% and an unnamed Ugandan investor would hold the remaining 15%.³³⁹

As will be pointed out below,³⁴⁰ the concessionaires' huge investment in the concession was protected by a synergy of uniquely designed protective safeguards against political risk. The investment was protected with one mechanism for precisely documenting the amortized value of the improved conceded assets, and another mechanism to strengthen the ability of the two governments of Kenya and Uganda to make good on any end-of-contract commitments vide investment guarantees issued by IDA.³⁴¹

The potential profitability of this rail line is difficult to miss. At the eastern most point on the rail line, cargo handling at Mombasa port reached 17 million tonnes in 2009 and as the operations of the port become more efficient, that total will continue to increase..³⁴² Currently, most of that tonnage is transported west over an inefficient and poorly maintained road network. To the west, as Uganda's oil resources are fully exploited, they eventually will need a reliable means of transporting crude oil to the nearest refinery or port.³⁴³

In economic and financial terms, the future of the rail operation are certainly vital. It is arguable that a recognition of this economic reality has caused all the major stakeholders including the two governments motivated to make this deal work and hence the ugly face of political risk has not been a hurdle to the concessionaires. This should be seen in the context of the fact that the hurdles faced by the concessionaire were opportunities that would have attracted politics into it and bring the PPP to a stop. As such, the PPP's continued survival is evidence of the commitment of many actors including the two governments in carefully preparing the transaction and devising innovative risk mitigation measures for the project the project. This kind of commitment has is not present in LAS in Kenya.

³³⁷ *ibid*

³³⁸ *ibid*

³³⁹ *ibid*

³⁴⁰ See Chapter 4 at pages 88 to 89.

³⁴¹ PPIAF *supra* note 315 at 5

³⁴² *ibid*

³⁴³ *ibid*

Conclusion

The above trend by LAs therefore demonstrates a problem that needs to be resolved. The ugly head of politics has found its root in PPPs by LAs due to lack of adequate legal and policy framework. The analysis of the PPP experience by LAs in Kenya thus demonstrates certain unique problems that need to be addressed. The dominant indicator for political risk is that councils are not willing to be bound by PPPs entered by their predecessors after change of administration following civic elections and have taken steps to annul them or refuse to be bound and have stated to have committed breaches of the provisions of the contracts governing the PPPs. Another common strand in the PPPs experience by LAs has also been the fact that other than challenging the PPPs, the Council's have entered into other PPPs in competition with the PPP entered by their predecessors.

It has also been illustrated by the two main case studies that the victims of challenges to PPPs by LAs are not restricted to the private entities partnering with LAs. Members of the public have been seen to have suffered. There has as such been collateral damages that arise from challenges to PPPs in that third parties who have entered into arrangement with the private entities are affected by the actions of the Councils as a result of the dispute and there is also a potential for a litany of suits being filed against the private entities for breach of contract arising from commitments made to third parties.

It is therefore vital that the issues identified are addressed so that future and ongoing PPPs by the LAs such as the iko toilets initiative, the rehabilitation of the Dandora dumpsite and the construction the Ruai dumpsites by the City council of Nairobi are not subjected to the same challenges.

CHAPTER FOUR: POLITICAL RISK IN PUBLIC PRIVATE PARTNERSHIPS

1. Introduction

The prevailing idea among development circles is that PPP arrangements, particularly in infrastructure, allow governments and government agencies to shift risks to the private sector. We have seen that a PPP entails a contractual arrangement whereby a private party performs a departmental function on behalf of the national or local government for a specified amount of time. This often includes a substantial risk transfer to the private party.

In an ideal situation, a PPP does not necessarily mean that the private partner assumes all the risks, or even the major share of the risks linked to the project. The precise distribution of risk is determined case by case, according to the respective ability of the parties concerned to assess, control and cope with this risk.³⁴⁴ The ideal objective is to allocate risks in such a way that both the private and the public sector benefit and consumers are well served.³⁴⁵

It is usually advisable that risks are allocated to the party that can most efficiently and manage them at the lowest cost.³⁴⁶ As such, the public sector transfers risks to the private sector for more efficient management of costs since the private sector has an incentive to manage risks as efficiently and innovatively as possible in order to control costs³⁴⁷.

There are various types of risks arising from in PPPs. The major ones identified by the 2009 PPPs Regulations include; design, construction, site, operation, demand/revenue, tariffs, collection, credit, force majeure and political risks.³⁴⁸ Others not identified by the Regulations include currency and land risks.³⁴⁹

³⁴⁴ Garsse Steven 'Public –Private Partnerships, Concessions and Procurement Law' 3rd International Public Procurement Conference Proceedings 28th- 30th August 2008 www.ippa.ws/proceedings last accessed on 9th August 2011.

³⁴⁵ *ibid*

³⁴⁶ Najja Bracey and Sonia Moldovan, 'Public Private Partnerships: Risks to the Public and the Private Sector' a paper presented under the auspices of the Louis Berger Group Incorporated, 6th Global Conference on Business and Economics (2006), www.louisberger.com at 4 accessed on 29th August 2011.

³⁴⁷ *Ibid* at 4.

³⁴⁸ See the second schedule

³⁴⁹ Najja *supra* note 344 at 5

It has emerged in practice that the private companies that have partnered with LAs in Kenya have borne the brunt of political risks resulting into challenges to the PPPs. Research has shown that the legal and regulatory framework relating to PPPs has not been adequate to mitigate the effects of political risk in LAs.

2. THE CONCEPT AND NATURE OF POLITICAL RISKS AND THE INTER PLAY WITH PUBLIC PRIVATE PARTNERSHIPS

a. The concept and nature of political risk in PPPs.

Regulation 2 of both the Public Procurement and Disposal (Public Private Partnership) Regulations 2009 and the Public Procurement and Disposals Regulations 2006 provides *inter alia* that in a PPP, the private party is generally liable for the risks arising from the performance of the function depending on the terms of the agreement.

The Second Schedule to the PPPs 2009 Regulations states as follows concerning political risk *“Political risk include events or circumstances arising from an action or inaction of the government or any Governmental authority exercising authority over a party which adversely affect the public private partnership such as blockade, embargo, riots, discriminatory change in law, expropriation and non renewal or revocation of project licenses without default on the part of the private party. The political risks shall be best placed with the Government”*

Political risks can arise from changes in government, changes in public policy, corruption and favouritism, lack of sanctity of contract, and arbitration difficulties.³⁵⁰ Political risks also extend to consequences and likelihood of changes in government and circumstances when the new government withdraws support to a PPP.³⁵¹

The political risk resulting from frequent changes in government can lead to confusion, poor communication, and a poor exchange of information.³⁵² An incoming government/administration as we have seen in the Adopt-A-Light and KAPS above may have a different opinion of the concessionaire than the outgoing government had, and thus, its perception or opinion of the project may change or they may prefer different actors for their own personal benefits.³⁵³

³⁵⁰ *ibid*
³⁵¹ UNDP, 'Public –Private Partnerships for Service Delivery – Toolkit for Pro-Poor Municipal PPPs' www.undp.org accessed on 29th August 2011
³⁵² Najja supra note 344 at 6
³⁵³ *ibid*

In many economies, the political temptation to reverse policy after privatization is steep because areas traditionally under public ownership (utilities and infrastructure) were historical monopolies with major fixed sunk investments, which produce a long term steady cash flow of revenues.³⁵⁴ Thus the profits represent considerable rents or quasi rents, which may arouse strong political opposition.³⁵⁵ Private investment in such industry has always been reluctant because of this heightened risk of de facto expropriation by ex post policy shifts.³⁵⁶

If the rule of law is not firmly entrenched in governments and government agencies, officials have been known to renege on contracts signed by previous administrations and thus fail to uphold the sanctity of contracts.³⁵⁷ An example is given in Hungary relating to a road construction PPP.³⁵⁸ The new government that came into office after the PPP was entered into was opposed to PPPs and private sector funding of public projects in general resulting into re-nationalization of the project.³⁵⁹

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Political risk can also arise indirectly, without the government's instigation. A case decided by the Supreme Court of Sri Lanka involving the "Waters Edge" Project³⁶³ is ideal to examine in this regard. The petitioners representing public interest complained of violation of their fundamental rights, due to the alienation of a land by the Urban Development Authority of Sri Lanka (UDA) to an investment project approved by the BOI under Section 17 of the BOI Law.³⁶⁴ The basis of the complaint was that the said

³⁵⁴ *ibid*

³⁵⁵ *ibid*

³⁵⁶ *ibid*

³⁵⁷ *ibid* at 12

³⁵⁸ *ibid* at 10 and 11.

³⁵⁹ *ibid*

³⁶⁰ *ibid*

³⁶¹ *ibid*

³⁶² *ibid*

³⁶³ SC/FR Application 352/2007 as cited by Asanga *supra* note 60 at 6.

³⁶⁴ *ibid*

alienation of land to a private investor was against public policy, as the land had been acquired for a “public purpose”.³⁶⁵

Having examined the material submitted for their consideration, their lordships of the Supreme Court of Sri Lanka concluded that the fundamental rights of the Petitioners had been violated by several of the Respondents, including the former President, Chandrika Bandaranaike Kumaratunge. In the circumstances, their Lordships decreed that the entire Waters Edge Project be reverted to the ownership of the UDA. The Supreme Court also ordered the UDA to pay the investor a sum representing the cost of construction of the buildings as at the date of construction, excluding all other development on the said land, within 4 months of the judgment.

At the international level, we have Multilateral Investment Guarantee Agency (MIGA) which is an organ established under the auspices of the World Bank Group whose main duty is the provision of political risk insurance guarantees to private sector investors and lenders. Its shareholding is drawn from 175 member countries constituting of 150 from developing countries including Kenya and 25 from the industrialized nations.³⁶⁶ MIGA focuses on several political risk indicators including, losses relating to: currency inconvertibility and transfer restriction, expropriation, war, terrorism, and civil disturbance, breach of contract and non-honoring of sovereign financial obligations.

MIGA points out that investors worldwide, whether from developed or developing countries, consider political risk to be the most important constraint for investment in emerging markets today.³⁶⁷ It is said that investors are primarily worried about adverse government intervention rather than overt political violence even in conflict-affected and fragile economies.³⁶⁸ It is also noted that most risk is centered on regulatory concerns, government interference, and transparency issues.³⁶⁹ Political risk perceptions thus play an important role in influencing investment by the private sector in PPPs.

The relative stability of key investment conditions responsible for the economic and financial performance of an investment venture is at the heart of investor concerns when negotiating an investment contract with a public sector entity. It is particularly so

³⁶⁵ *ibid*

³⁶⁶ See <http://www.miga.org/whoweare/index.cfm?stid=1789> last accessed 13th September 2011.

³⁶⁷ See MIGA, 'MIGA Sees Gradual Recovery in Foreign Direct Investment' <http://www.miga.org/news/index.cfm?aid=2749n> accessed on 12th September 2011

³⁶⁸ See MIGA: 'Spreading the Word on Investment in Conflict-Affected and Fragile Countries' <http://www.miga.org/news/index.cfm?aid=2956> accessed on 12th September 2011.

³⁶⁹ *ibid*

for projects like PPPS where duration and risk exposure are long, capital investment is intensive, and project risk is acute.³⁷⁰ Therefore the extent to which the relevant public sector entity undertakes to protect the investment would be at the center of both the negotiation of a specific contractual regime and the proper design of a project structure.³⁷¹ Other relevant factors include investment recovery, the ability to maintain contractual and proprietary rights.³⁷²

State decentralization arguments that lay the groundwork for advocating PPPs reveal contradictory expectations that through them the government both enables and regulates the market.³⁷³ Successful partnerships require strong commitment and political will by the state to develop detailed regulations that level the playing field amongst unequal partners.³⁷⁴

Governments and the private sector especially in the developing world often underestimate the extent and effect of political risk to privatisation initiatives.³⁷⁵ As such there is no focus on legal reform to shield private actors from the effects of political risk.³⁷⁶ As a result the law does not make any or any adequate provisions for dealing with effect of political risks to PPPs. This study has identified political risk to be more dominant in LAs than in the national government.

For there to be political will to perform the steering role in and to synergize the interests of different rowers, the state or state agency/institution has to be willing as well as able to use its financial, legislative/regulatory, and institutional resources to this end. This is lacking in LAs in Kenya. Weak governments and other state actors with inadequate will or resources in any of those areas cannot effectively negotiate to lead partnership processes or guide their outcomes.³⁷⁷ Yet the state's important role is necessary to

³⁷⁰ Asanga Gunawansa, 'The Legal Consequences of Breach of Government Undertakings to Investors' (Dauphine University Paris 2010) http://www.rics.org/site/download_feed.aspx?fileID=8043&fileExtension=PDF accessed 30th August 2011 at 9

³⁷¹ *ibid*

³⁷² *Ibid*

³⁷³ Faranak Miraftab, 'Public Private Partnership: The Trojan Horse of Neoliberal Development?' (2004) *Journal of Planning Education* 24: 89 – 101 (Association of Collegiate of Schools of Planning) at 94

³⁷⁴ *Ibid*

³⁷⁵ D. O Ong'olo *Public Private Partnerships in Kenya* prepared for The Institute of Economic Affairs, Kenya. www.ieakenya.or.ke/documents/Public%20Private%20Partnerships.pdf accessed on 20th June 2010 at 33.

³⁷⁶ See also Peter Farlam: *Accessing Private- Public Partnership in Africa*, (Nepad Policy Focus Series SAIIA 2005)

³⁷⁷ Faranak *supra* note 373 at 93.

strengthen the capacity of weaker partners and to establish a level playing field.³⁷⁸ But it is usually local governments that are found in PPP local development projects, and their limited resources as well as the propensity of officials to foster political interests do not bode well for their leadership unless their decision making is backed by macro-level strategies of the central government.³⁷⁹

The United Nations Economic Commission for Europe (UNECE) has recognised that Legal processes in many jurisdictions are insufficient, overly complex and fail to provide sufficient security and incentives to investors in PPP arrangements.³⁸⁰ The UNECE has recognised that investors in PPPs need predictability and security in legal frameworks, which means fewer, simpler and better rules. In addition, the legal framework needs to take account of the beneficiaries and empower them to participate in legal processes, protecting their rights and guaranteeing them access in decision-making.³⁸¹ There is need for a secure, predictable, stable, consistent and commercially-oriented framework of law and regulation, so that PPPs can flourish.

Generally, in view of the relationship between political risk and PPPs, it is indeed correct to state that privatization and by extension PPPs are an ideal test for political commitment to market-oriented reforms, as it severely tests the determination of policymakers to resist the political backlash after the transaction is completed and implemented as it involves a retreat of political forces from the governance of economic activity.³⁸² As a consequence, politicians used to discretionary control over firms' activities see their capacity to reallocate resources sharply curtailed.³⁸³

b. Political risk in PPPs by Local Authorities in Kenya

In the context of LAs in Kenya, the executive or administrative arm of a LA in Kenya is made of departments. The number of departments depends on the size and the functions and services being undertaken by a LA. Large LAs, especially urban ones, usually have more departments. Under the law, councillors have no executive powers. A councillor can only act in the context of his/her participation in the corporate decisions

³⁷⁸ *ibid.*

³⁷⁹ *ibid*

³⁸⁰ *Ibid* at 29

³⁸¹ *Ibid.*

³⁸² Perotti, Enrico C & van Oijen, Pieter, 'Privatization, political risk and stock market development in emerging economies' (2001) *Journal of International Money and Finance*, Elsevier, vol 20 (1) pages 43-69 (February) at 48.

³⁸³ *Ibid*

of the LA. It is only at a committee or full council meeting that a councillor can voice issues concerning the citizens that he/she represents, either by tabling a motion or generally during deliberations in those fora.

A councillor has no direct authority over local service producers and his/her influence on them will depend on his/her influence in the relevant committee and, ultimately, in the full council. Experience has however shown that factionalism plays a prominent part in the decision making dynamics of a local authority.³⁸⁴ If a councillor is not within the loop of the dominant faction in a local authority, he/she may not be able to significantly influence decisions affecting the people he/she represents.³⁸⁵ This is how politics appear to play a major role in PPPs implementation in LAs resulting with the challenges that have been identified in this study.

This unique structure of LAs in Kenya has a likelihood to create basis for challenge to PPPs that may not find favour with councillors sitting in the relevant committees including the committee that is mandated to oversee PPP projects. This is indeed the genesis of the political risk inherent in PPPs entered by LAs. The councillors keep changing after elections and thus the risk that the PPPs by predecessors may be challenged.

The general view relating to privatization and by extension to PPPs has been that state actors and officials, in this context councillors have tended to eschew the law to ensure that privatization and PPPs have not been implemented in a way that will achieve the desired objective of delivery of services to the citizens in an efficient manner.³⁸⁶

It is said that one of the causes of political risk at the LA level is that councils typically do not understand the nature of PPPs and further the fact that contracts are binding on the LAs independent of them as councillors.³⁸⁷ This is a possible explanation of the challenges to PPPs by some LAs in Kenya. It is arguable that councils do not understand or rather ignore the corporate principle and end up personifying the LAs and thus prone to challenge PPPs entered during the previous administration and in turn enter into

³⁸⁴ Harriet Naitore 'Study on Local Council Oversight Role and Social Accountability in Kenya' prepared for the African Development Group (2008) www.siteresources.worldbank.org accessed 4th July 2011

³⁸⁵ *ibid*

³⁸⁶ Migai Akech *Privatization and Democracy in East Africa: The Promise of Administrative Law* (East African Educational Publishers Limited, 2009) at 8.

³⁸⁷ Brian Dollery, 'Public Private Partnerships and Local Government Infrastructure' http://www.lgsa-plus.net.au/resources/documents/dollery-ppps-and-local-government-infrastructure_2005.pdf accessed 2nd August 2011 at 5

other PPPs that would favour them personally as opposed to the LA as a corporate entity.

Human capital to implement and explain PPP legislation is lacking in most developing countries and as a result, creating and enforcing contracts becomes a strenuous and costly process.³⁸⁸ Public governance where individuals do not have the necessary skills to enforce and monitor contracts has led to cancellation or renegotiation of contracts.³⁸⁹

In France, which has the longest experience of such concessions to build roads, water works and other infrastructure, an official report observed that the system left elected councilors on their own, without support, to deal with conglomerates wielding immense political, economic and financial power.³⁹⁰

Due to the failure to understand the fundamental aspects of PPPS, it has been reported that some LAs in other jurisdictions have suffered pecuniary losses in astronomical amounts. For instance, problems with the Oasis Project involving the Liverpool City Council in the New South Wales prompted an inquiry that led to general recommendations concerning PPPs in local government³⁹¹. Four main general recommendations emerged from the Inquiry: The Local Government Act 1993 to be amended to make regulations for PPPs in local government; the Act to require the Minister's consent to any PPP; the Act to oblige councils to undertake tendering and guidelines to be provided outlining processes and procedures to be followed.³⁹² Some of the recommendations were enacted under the Local Government (Public Private Partnership) Act 2004.³⁹³

Prof. Migai has attributed this state of affairs in government³⁹⁴ to two concepts: neopatrimonialism and development assistance.³⁹⁵ Neopatrimonialism entails the

³⁸⁸ Najja *supra* note 346 at 11

³⁸⁹ *ibid*

³⁹⁰ David Hall: *PPPS: A critique of the Green Paper*, (Public Services International Research Units 2004) <http://www.epsu.org/IMG/pdf/PSIRUonECPPPGP2.pdf> accessed on 9th September 2011.

³⁹¹ Dollery *supra* note 387 at 8 See also Liverpool City Council Public Inquiry (2004), 'Lessons from the Public-Private Partnership Liverpool City Council Experience: Recommendations for Local Government' NSW DLG, Sydney.

³⁹² Dollery *supra* note 387 at 8

³⁹³ *ibid*

³⁹⁴ Which view is applicable to Local Authorities in Kenya.

³⁹⁵ According to Prof. Migai, development assistance (which is not directly relevant in this study) comes forms such as financial aid such as subsidized credits and loans and commodity assistance. While development assistance is based on the moral idea that developed countries should support development initiatives in poor developing countries, it is noted that much foreign aid is given to further the interests of the donor countries. According to Prof. Migai, development assistance considering that it *inter alia*

usurpation of public resources by political elites which they then use to dispense political patronage for purposes of keeping political power.³⁹⁶ As such, while formal structures and rules exist in theory in a neo-patrimonialism rule, there is virtually no separation of the private and public sphere in practice.³⁹⁷ ³⁹⁸Accordingly, the patrimonial penetrates the legal-rational system and twists its logic, functions and effects. In practice, neopatrimonialism manifests itself through the practice of clientism and patronage.³⁹⁹ Clientilism refers to the exchange or brokerage of specific services and resources for political support in the form of votes.⁴⁰⁰ On the other hand, patronage involves the distribution of favours to individuals but essentially to groups based on ethnic or tribal lines.⁴⁰¹

The neopatrimonial regime therefore gives the political actors who control it flexibility in the sense that they have a certain degree of choice as to which logic they want to employ to achieve their goals and achieve their interests best.⁴⁰² As a result political actors who wield power are able to straddle the patrimonial –legal national divide and base their decisions on rules that best fit their interests.⁴⁰³ As a result of the state of affairs, PPP by LAs have been implemented in a context characterized by weak institutions as well as weak regulatory and legal frameworks.⁴⁰⁴

Neopatrimonialism is thus undesired since it abhors the establishment of effective state institutions, as these would greatly undermine the dispensation of clientelism and patronage. As such, while there can be legal systems in place so that the state appears to possess all trappings of a “Weberian rational-legal system” with a clear distinction between the public and the private, this official order is constantly subverted by patrimonial logic, in which office bearers, and in this context councilors, systematically exploit the PPPs/privatization projects for their own good.⁴⁰⁵

further the donor countries, is troubling when it comes to privatization because it undermines institution building thereby reinforcing the neopatrimonial tendencies. Development assistance is not directly relevant to this study and will not be delved into any greater detail.

³⁹⁶ Migai *supra* note 386 at 8.

³⁹⁷ *Ibid* at 23.

³⁹⁸ This has been an important conclusion arrived at by the author looking at PPPs experience by LAs in Kenya as will be seen above..

³⁹⁹ Migai *supra* note 386 at 24

⁴⁰⁰ *ibid*

⁴⁰¹ *ibid*

⁴⁰² *ibid*

⁴⁰³ *ibid*

⁴⁰⁴ *Ibid* at 8

⁴⁰⁵ *Ibid* at 25

Neo-patrimonialism has indeed played a great role as cause for challenges to PPPs entered by LAs in Kenya as the councilors have in practice acquired the same personality as the LAs in violation of the principle of corporate and distinct personality of LAs. In this regard the UN- Habitat has recognized the fact that LAs in Kenya have not been exuding their independent corporate entity as stipulated in the Local Government Act⁴⁰⁶ as a result of which several challenges have arisen.⁴⁰⁷ It is observed that LAs in Kenya have been associated with administrative as well as professional problems this being in contrast with the separate legal personality bestowed upon LAs.⁴⁰⁸

PPP as a unique kind of public procurement has been accorded special treatment as a result of which specialized Regulations governing PPPs quite apart from the general regulations governing other simpler forms of procurement, have been made vide the Public Private Partnership (Public Procurement and Disposal) Regulations, 2009.

However, the current PPP legal framework governing PPPs is not sufficient and even appropriate to deal with the challenges to PPPs identified in this study. The main area of inadequacy has been the lack of sufficient provisions to deal with political risks arising from PPPs by LAs.

However, after the promulgation of the current Constitution in 2010, we now have some constitutional provisions that may aid in addressing political risks arising from PPPs by county governments. Article 227 of the Constitution providing for public procurement lays focus on protection of government interests for instance by providing that legislation should be enacted to sanction against contractors that have not performed according to professionally regulated procedures, contractual agreements or legislation. Regarding protection of private actors, reliance for purposes of redress by private actors against county governments may be placed upon Article 227 (1) which requires a state organ or any other public entity when contracting for goods and services, to do so in accordance with a system that is fair, equitable, transparent, competitive and cost effective. Further, it is strongly arguable that they can find redress by virtue of Article 227(2)(b) which provides that an statute should be enacted to provide for the protection or advancement or persons and categories or groups of persons previously affected by unfair competition or discrimination.

⁴⁰⁶ Chapter 265 of the Laws of Kenya.

⁴⁰⁷ Migai *supra* note 386 at page 43

⁴⁰⁸ UN- Habitat, 'Local Democracy and Decentralization in East and Southern Africa: Experiences from Uganda, Kenya, Botswana, Tanzania and Ethiopia' www.unhabitat.org accessed on 3 August 2011 at 43

Other relevant provisions of the constitution which can be used to address political risks effects to PPPs are found in chapter 13 and specifically article 232 which has provisions on values and principles of public service under which state actors are *inter alia* uphold the following principles and values; high standards of professional ethics, efficient, effective and economic use of resources, accountability for administrative acts.

It should be noted that article 232 (2) of the Constitution states that the principles of public service apply to all state organs in both levels of government. Parliament is required by article 232 (3) to enact legislation to give full effect to the principles of public service.

The provisions of Chapter 6 of the Constitution on leadership and integrity are also important to point out. Leading with integrity is perhaps the most important quality of leadership, but it is also one of the great challenges of leadership. Leaders who enter office with genuine intentions usually find themselves faced with ethical dilemmas when their personal interests are brought into competition with official authorities and discretions. It is on this backdrop that the Constitutional provisions in chapter 6 were perhaps promulgated.

The Constitution dedicates the whole chapter 6 on Leadership and Integrity. The chapter concerns with the conduct, ethics and integrity of State officers, defined to include members of the county assemblies. A most important provision of chapter six is Article 73 (1) which declares the authority of a State officer to be a public trust which must be exercised in a manner that is consistent with the purposes and objects of the constitution, demonstrates respect for the people, brings honour to the nation and dignity to the office, and promotes public confidence in the integrity of the office. By virtue of article 73(b), the authority vests in State officers the responsibility to serve the people, rather than the power to rule them.

We have already pointed out that after the general elections in 2012, the LAs will be subsumed in county government structure to align to the devolved government under the Constitution. The roles of LAs will be taken over by county governments. It is expected that county governments will adopt the PPP mechanism in development of infrastructure.

The political arm of the county government is the county assembly which shall constitute of *inter alia* members elected by the registered voters of the wards.

The boards of cities and municipalities established under the Urban Areas and Cities Act, No. 13 of 2011 are empowered by section 33 of the Act to enter into PPPs for purposes of delivery of services and performance of works within their jurisdiction. Such power is however subject to the approval of the county assembly.

Unless the current legal and regulatory framework is reformed to buttress the Constitutional provisions, there is a potential risk that PPPs entered by county assemblies as well as by the urban areas and cities may be riddled by political interference from county assemblies.

It is therefore important to examine how political risk has been dealt with in other jurisdictions in order to formulate the way forward for county governments.

3. WAYS OF MINIMIZING POLITICAL RISK IN PPPS: A COMPARATIVE ANALYSIS

a. Use of investment guarantees and protection

i. Nature of investment guarantees

In order to attract foreign direct investments through PPPs,⁴⁰⁹ developing country governments provide various investment protection undertakings. Firms ask for guarantees so they can unload risks arising from PPPs⁴¹⁰. Legal consequences of breaching such undertakings can be severe as it is well established in international investment law that states should not breach promises made concerning the stability of investments.⁴¹¹ However, sometimes developing country governments take decisions that adversely affects the interests of the investors, without due consideration of the legal consequences and regard to the interests of the private sector.⁴¹²

At the international front, the context of this study necessitates a little more detailed analysis of some of the political risk indicators over which MIGA offers investment guarantees to wit, expropriation, breach of contract and non-honoring of sovereign financial obligations.⁴¹³

⁴⁰⁹ This should be taken to mean PPPs with a contractors drawn from foreign countries. The PPDA as well as the PPPs 2009 Regulation envisage international PPPs and specifically by Regulation 16. For instance the rehabilitation of the Dandora Dumpsite as well as the construction of a new dumpsite by the City Council of Nairobi has been said to have drawn interest from foreign bidders.

⁴¹⁰ Angel, Fischer and Galetovic, 'Public Private Partnerships: When and How' www.cowles.econ.yale.edu accessed on 29th August 2011.

⁴¹¹ Asanga *supra* note 370.

⁴¹² *ibid*

⁴¹³ See <http://www.miga.org/investmentguarantees/index.cfm> last accessed 12th September 2011.

As for expropriation, MIGA points out that it offers protection against losses arising from certain government actions that may reduce or eliminate ownership of, control over, or rights to the insured investment.⁴¹⁴ In addition to outright nationalization and confiscation, "creeping" expropriation, a series of acts that, over time, have an expropriatory effect is also covered. Coverage is available on a limited basis for partial expropriation such as confiscation of funds or tangible assets.⁴¹⁵

As for breach of contract, MIGA protects against losses arising from the government's breach or repudiation of a contract with the investor such as a concession or a power purchase agreement.⁴¹⁶ Breach of contract coverage may be extended to the contractual obligations of state-owned enterprises in certain circumstances.⁴¹⁷ In the event of an alleged breach or repudiation, the investor is required to invoke the dispute resolution mechanism such as arbitration set out in the underlying contract. If, after a specified period of time, the investor has been unable to obtain an award due to the government's interference with the dispute resolution mechanism (denial of recourse), or has obtained an award but the investor has not received payment under the award (non-payment of an award), MIGA would pay compensation.⁴¹⁸ If certain conditions are met, MIGA may, at its discretion, make a provisional payment pending the outcome of the dispute and before compensation for non-payment of an award is paid. For non-payment of an award, MIGA would pay the investor's interest in the award.⁴¹⁹ For denial of recourse, MIGA would pay the investor's interest in the amount which, according to MIGA's claims determination, the host government would have to pay to the investor pursuant to the contract.⁴²⁰ In either case, MIGA's compensation would be capped by the amount of guarantee stated in the guarantee contract.⁴²¹

As for non-honouring of sovereign financial obligations, it is pointed out that MIGA offers protection against losses resulting from a government's failure to make a payment when due under an unconditional financial payment obligation or guarantee related to an eligible investment.⁴²² It does not require the investor to obtain an arbitral award. This coverage is applicable in situations when a sovereign's financial payment

⁴¹⁴ *ibid*

⁴¹⁵ *ibid*

⁴¹⁶ *ibid*

⁴¹⁷ *ibid*

⁴¹⁸ *ibid*

⁴¹⁹ *ibid*

⁴²⁰ *ibid*

⁴²¹ *ibid*

⁴²² *ibid*

obligation is unconditional and not subject to defenses. Compensation would be based on the insured outstanding principal and any accrued and unpaid interest.⁴²³

It is noted that MIGA recorded a gradual recovery in foreign direct investment (FDI) to the effect that it issued \$1.5 billion in investment guarantees (insurance) for 19 projects in developing countries during the fiscal year ending June 30, 2010.⁴²⁴ The results bring total guarantee coverage issued since MIGA's inception in 1988 to \$22.4 billion. This growth in the provision of political risk cover for investments by MIGA has also been witnessed in Africa and particularly in Kenya, Senegal and Ethiopia.⁴²⁵

The project in Ethiopia which involves the production of tropical fruit juices, is expected to create over 900 jobs in five years. It is reported that in April 2009, africaJUICE Tibila Share Company, a joint venture between africaJUICE BV of the Netherlands and the Ethiopian government, took operational control of Tibila Farm in Ethiopia's Upper Awash Valley.⁴²⁶ MIGA is supporting the investment by providing \$10 million in guarantees to africaJUICE BV and to the Industrial Development Corporation of South Africa, a lender to the project.

In Kenya, it is reported that MIGA has supported the design, construction, and operation of a 48 MW geothermal power plant, and the construction and operation of the first modern bulk handling and storage facility for imported grains and fertilizers in the port of Mombasa.⁴²⁷ It also reported that, MIGA has demonstrated its commitment to helping Kenya generate jobs and reduce rural poverty by supporting the rejuvenation of an ailing sugar industry that has failed to keep up with demand.⁴²⁸

ii. Investments guarantees by Local Authorities and the National Government in Kenya. As for PPPs in Kenya, regulation 11(1) of the 2009 PPPs Regulations has provision on Government Investment Protection. The Regulation provides that

⁴²³ *ibid*

⁴²⁴ See MIGA, 'MIGA Sees Gradual Recovery in Foreign Direct Investment' <http://www.miga.org/news/index.cfm?aid=2749n> accessed on 12th September 2011

⁴²⁵ *ibid*

⁴²⁶ See MIGA 'Tropical Fruit Juice Project Helping to Spur Economic Revival in Ethiopia' <http://nazret.com/blog/index.php/2011/05/12/tropical-fruit-juice-project-helping-to-spur-economic-revival-in-ethiopia> accessed on 12th September 2011

⁴²⁷ See <http://www.miga.org/news/index.cfm?aid=680> accessed on 12th September 2011.

⁴²⁸ *ibid*

“Where it is necessary to support private sector investments and reduce premiums factored for political risks, the Government where it is not a signatory to the agreement, may issue binding letters of comfort to private sector investors and their lenders to acknowledge the investment by the private sector, assure investors that they will be provided with reasonable assistance with acquiring authorizations and guarantee against risks arising from Government actions or omissions “(emphasis added)

A similar provision is present under section 3(1) of the now repealed Guarantee (Loans) Act ⁴²⁹ which provides that:

“The Government may, with the prior approval of the National Assembly, guarantee in such manner and upon such conditions as it may think fit the due performance of any covenants on the part of a local authority or a body corporate under the terms of any legal instrument to which such local authority or body corporate is a party” (*emphasis added*).

The Guarantee (Loans) Act has been replaced with the National Government Guarantee Loans Act 2011 whose object is to ensure that the authority conferred on the national government to guarantee loans under is exercised in a transparent, prudent and equitable manner, consistent with Article 213 of the Constitution.⁴³⁰ It is noteworthy that there is no similar provision as section 3(1) in the repealed Guarantee Loans Act which we understand extended beyond guaranteeing loans as it also provided for national government's guarantee of performance of covenants by LAs which in our view would include obligations under a PPP contract. It is not understood why such a vital provision was repealed.

Perhaps the failure to retain section 3(1) of the now repealed Act was informed by the fact that county governments are autonomous from the national government contrary to the case for LAs which operate under the auspices of the ministry of Local Government and hence answerable to the national government. Perhaps it was thought not appropriate for the national government to guarantee the county government's covenants as this may have impeded the autonomy created by article 6 (2) of the Constitution which provides that the governments at the national and county levels are distinct and inter-dependent and shall conduct their mutual relations on the basis of consultation and co-operation. It is however still difficult to understand with certainty why section 3(1) of the repealed Act was not saved.

⁴²⁹ Chapter 461 of the Laws of Kenya.

⁴³⁰ Section 2 of the National Government Loans Guarantee Act, 2011.

The existing statutory provisions and regulations on investment guarantees have not been sufficient to deal with political interference of PPPs by LAs. Succeeding administrations in LAs have found it easy to withdraw support from existing PPPs leaving the private sectors naked regarding safeguarding their investments.

The provision of investment guarantees in the PPPs 2009 Regulations is left to the discretion of the Government and there is no empirical evidence that the discretion has been exercised to govern PPPs by LAs. No such guarantees were given by the Government in the PPPs analyzed in case studies in chapter three above.

Perhaps the reason for this could be that the PPPs were entered into before the enactment of the PPPs 2009 Regulations. However, there does not appear to be much focus on the provision as is required. The Steering Committee is yet to recommend to the Minister of Finance “the principles, procedures and standards for making decisions on investment protection and letters of comfort on PPPs projects based on Cost Benefit Analysis, national priorities and available Government resources” as is required by Regulation 11(2).

There is also no express Constitutional provision on investment guarantees by the national government as is present in other countries such as Sri Lanka as shown below. The provision relating to guarantees by national government is in relation to loans guaranteed by national government.⁴³¹

There is however evidence to show that the national government has given investment guarantees to investors in PPPs. The RVR rail concession is vital to analyse in this respect. It is important to give a brief understanding of mechanisms that have been adopted to shield against political risks that have arisen in rail concessions especially in sub-Saharan Africa in order to understand the approach taken in the RVR concession.

The general view in railway construction is that, due to the long life expectancy of the rail assets conceded to a concessionaire (often 40-50 years), it makes it impossible for private companies to pay for them and recoup this investment over the 20-30 year life spans of normal concession agreements.⁴³² The traditional approach for dealing with

⁴³¹ Article 213.

⁴³² Public Private Infrastructure Advisory Facility (PPIAF) 'A PPP against the Odds: The Kenya Uganda Rail Concession Fights for Survival' (2010) at 3 <http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/publication/Kenya-Uganda%20Rail%20Case%20Study.pdf> accessed on 9th September 2011.

this problem is for concessionaires to finance initial investment, with governments committing to compensate concessionaires for unamortized investment at the end of the concession period.⁴³³ But this approach has never been popular with operators because they question the willingness and/or ability of governments to make good on potentially large commitments made decades earlier by other officials no longer in government.⁴³⁴

As a consequence of this perceived risk, concessionaires have increasingly insisted that governments also pay for some or all of the initial investment, usually by securing “soft” loans from donors or multi-lateral development financing institutions and on-lending these funds to concessionaires.⁴³⁵ Most new rail concessions in Africa are of this kind. In effect, governments are becoming financiers for their own concessions, raising questions about the extent to which they can also monitor contract compliance and effectively represent the rights of service beneficiaries.⁴³⁶ And because even under this newer approach governments must commit to make some end-of-contract payments if called for, the possibility exists that some private operators ultimately will manage the risk of government failure to make good on these commitments by slowing down privately financed track rehabilitation and replacement toward the end of the concession period.⁴³⁷

The Kenya–Uganda concession addressed this problem by adopting a third approach, something hardly before used. The concessionaires were required to make the initial track investment, but the investment was protected with one mechanism for precisely documenting the amortized value of the improved assets, and another mechanism to strengthen the ability of these governments to make good on any end-of-contract commitments.⁴³⁸

First, a “conceded assets account” was created for all of the public assets associated with the concession and assets handed over to the concessionaires were to be accounted for as concessionaire liabilities to the government and amortized accordingly.⁴³⁹ Newly acquired or improved assets, such a rolling stock, were to be amortized under the same account, but treated as credits to the concessionaires.⁴⁴⁰ By auditing the account frequently, the amortization of these investments could be

⁴³³ *ibid*

⁴³⁴ *ibid*

⁴³⁵ *ibid*

⁴³⁶ *ibid*

⁴³⁷ *ibid*

⁴³⁸ *ibid*

⁴³⁹ *Ibid* at 4.

⁴⁴⁰ *ibid*

monitored, and the value added to the railway business by the concessionaires assessed.⁴⁴¹

This conceded assets account was designed to be the basis on which the accounts between the concessionaires and the governments would be reconciled whenever the deal was terminated, or upon its natural expiration.⁴⁴²

Second, the government's willingness and ability to make good on obligations relating to this conceded assets account were supported by two separate International Development Association (IDA) Partial Risk Guarantees (PRGs).⁴⁴³ These were guarantees to the respective concession companies—\$ 30 million for RVR-Kenya and \$15 million for RVR-Uganda.⁴⁴⁴ The PRGs would be triggered by the failure of either government to meet its contract termination payment obligations relating to the Conceded Assets Accounts (or failure to pay any liquidated damages).

In other words, the concession contract was structured so that any breach of contract terms by any party potentially would lead to contract termination, which in turn would lead to a requirement to make good on any obligation documented in the conceded assets account. In the case of a government obligation to pay, such an obligation was guaranteed by the PRG. These mechanisms provided a level of certainty and comfort to governments and concessionaires (including their shareholders and lenders) alike, regarding outstanding obligations at the time of contract termination.

The mechanisms played an important role in maintaining investor interest during the bidding process, attracting lenders to the deal (including both commercial banks and multi-lateral financing agencies), and shifting risk of a very important PPP to the private sector.

iii. Investment guarantees and protection, and their enforcement in other jurisdictions

Research has shown that some countries offer elaborate investment guarantees to the private investors in PPPs through their policies, regulations and laws to protect the private sector from the effects from political risks arising from the government or government agencies including LAs.

⁴⁴¹ *ibid*

⁴⁴² *ibid*

⁴⁴³ *ibid*

⁴⁴⁴ *ibid*

The most straightforward manner is to provide investment protection in the investment agreement itself. However, it is common for countries to offer investment protection by specific statutory provisions and general undertakings, in investment policy statements.⁴⁴⁵

To encourage investors to undertake projects in Sri Lanka, its Board of Investments (BOI) makes the following promises to all investors:⁴⁴⁶

- i. "When you sign an agreement with the BOI, the provisions embodied in the agreement remain valued for the life of the enterprise. Successive Governments cannot change these provisions, ensuring a degree of stability that few other countries can offer or match."
- ii. "The government has never defaulted nor requested rescheduling of any of its international obligations. Significantly this protection extends to foreign investors."
- iii. "The safety of foreign investment is guaranteed through the acceptance by two third majority of Parliament of the Constitutional Guarantee of Investment Protection Agreements."
- iv. "Sri Lanka is also a founder member of the Multilateral Investment Guarantee Agency (MIGA). This provides further safeguards against expropriation and noncommercial risk."
- v. "Bilateral investment agreements supported by a constitutional guarantee provide strong protection for foreign investment for Sri Lanka."
- vi. "Under article 157 of the country's constitution, the agreement enjoys the force of law and no legislative, executive or administrative action can be taken to contravene the provisions of a bilateral investment agreement otherwise than in the interests of national security."
- vii. "A clause in the Sri Lanka's constitution ensures the sanctity of the agreements. These agreements provide the following:
 - a. Protection against nationalisation.
 - b. Prompt and adequate compensation if required.
 - c. Free remittance of earnings, capital and business fees.
 - d. Settlement of disputes under the International Convention for the Settlement of Investment Disputes (ICSID)."

In addition to the aforesaid representations by the BOI, Article 157 of the Constitution of Sri Lanka - which is also referred to in the aforesaid representations of the BOI - provides as follows:⁴⁴⁷

⁴⁴⁵ Asanga *supra* note 370 at 2.

⁴⁴⁶ Asanga *supra* note 370 at 2 and 3.

⁴⁴⁷ *ibid*

“Where Parliament by resolution passed by not less than two-thirds of the whole number of Members of Parliament (including those not present) voting in its favour, approves as being essential for the development of the national economy, any Treaty or Agreement between the Government of Sri Lanka and the Government of any foreign State for the promotion and protection of the investments in Sri Lanka of such foreign State, its nationals, or of corporations, companies and other associations incorporated or constituted under its laws, such Treaty or Agreement shall have the force of law in Sri Lanka and otherwise than in the interests of national security no written law shall be enacted or made, and no executive or administrative action shall be taken, in contravention of the provisions of such Treaty or Agreement”

The effect of Article 157 of the Sri Lankan Constitution is that it pledges constitutional protection to investors coming from countries which have entered into bilateral investment treaties with Sri Lanka⁴⁴⁸. The cumulative effect of this Article, the aforesaid representations by the BOI and the provisions of the BOI Law is that investors are given the assurance that Sri Lanka is a very safe investment destination and that the government facilitates and protects investments. Further, there is assurance that investments will not be taken away without adequate compensation.

Breach of investment guarantees has great ramifications for the government. It is settled law that where governments or state entities unduly interfere with the contractual rights of the investors, the latter should be adequately compensated. This principle flows from the most important United Nations General Assembly (UNGA) resolution on permanent sovereignty, UNGA Resolution 1803 of 1962.⁴⁴⁸ This resolution adopted language declaring that investors "shall be paid appropriate compensation ... in accordance with international law" where their property, including by inference their contract rights, has been taken.

When an investment agreement has been negotiated and agreed by a host state that guarantees contractual stability under some general legislation, the promised stability is a factor taken into consideration in investment dispute arbitrations in ascertaining when compensation is due, and in determining the quantum of compensation, when that state subsequently revokes or ignores its legislative promise⁴⁴⁹. It follows that the unilateral amendment by the state of the contract and/or the guaranteed regulatory and legislative

⁴⁴⁸ www.un.org accessed on 30th August 2011.

⁴⁴⁹ Asanga *supra* note 370 at 10

protection would immediately and directly engage the responsibility of the state to compensate the investor.⁴⁵⁰

In these circumstances, in practical terms, arbitral tribunals and courts would give full effect to the undertakings given to an investor and, at a minimum, order full compensation to investors injured, due to the breach of such undertakings.⁴⁵¹ In this connection it is worth to note that in the *Texaco Overseas Oil Petroleum Co./California Asiatic Oil Co. v. Libyan Arab Republic* oil industry arbitration⁴⁵², which involved an issue concerning the validity of a stabilization clause, the sole arbitrator stated that:

“There is no doubt that in the exercise of its sovereignty a state has the power to make international commitments....There is no value to dwell at any great length on the existence and value of the principle under which a State may within the framework of its sovereignty, undertake international commitments with respect to a private party. This rule results from the discretionary competence of the State in this area....The result is that a State cannot invoke its sovereignty to disregard commitments freely undertaken through the exercise of this same sovereignty, and cannot through measures belonging to its internal order make null and void the rights of the contracting party which has performed its various obligations under the contract.”

In another oil industry arbitration, namely *Aramco v. Saudi Arabia*⁴⁵³, the tribunal came to a similar conclusion with regard to the binding force of the stabilization clause under international law. The decision concluded that:

“By reason of its very sovereignty within its territorial domain, the State possesses the legal powers to grant rights [by] which it forbids itself to withdraw before the end of the concession, with the reservation of the Clauses of the Concession Agreement relating to its revocation. Nothing can prevent a State, in the exercise of its sovereignty, from binding itself irrevocably by the provisions of a concession and from granting to the concessionaire irrevocable rights. Such rights have the character of acquired rights.”

This trend towards arbitral enforcement of state contracts was further confirmed by the 1963 award in *Sapphire International Petroleum Ltd. v. National Iranian Oil Company*

⁴⁵⁰ *ibid*

⁴⁵¹ *ibid*

⁴⁵² 17 I.L.M. 1, 8 (1977) as cited by Asanga *supra* note 370 at 10

⁴⁵³ 27 I.L.R. 117, 168 (1963) as cited by Asanga *supra* note 370 at 11

("NIOC"). On the issue of whether state promises to investors should be recognized as binding, with breaches subject to a duty to compensate, the sole arbitrator left no doubts⁴⁵⁴:

"It is a fundamental principle of law, which is constantly being proclaimed by international courts, that contractual undertakings must be respected. The rule pacta sunt servanda is the basis of every contractual relationship."

In *Libyan Am. Oil Co. v. Gov't of the Libyan Arab Republic*⁴⁵⁵, where the claim alleged breaches of a concession contract by the Libyan government without payment of compensation, the arbitrator concluded that the action of the state party amounted to repudiation of the contract in apparent violation of so-called "stabilization" clauses through which Libya had expressly promised not to change the legal framework in ways adverse to the investors' interests.

In the circumstances, it could be said that it is well established by international dispute resolution forums that investors who have suffered due to breach of investment protection guarantees given by governments are entitled to just compensation. This position can find domestic application if the law is reformed to provide for investment guarantees for contracts by state actors including LAs and County governments.

b. Securing the sanctity of contracts through legislation

The deliberate securing of the sanctity of contracts in legislation is one of the additional ways adopted in a number of jurisdictions for mitigating the effect of political risks to private investors under PPPs. The position in some jurisdictions has been to expressly secure the sanctity of contracts under statute as well as the constitution. For instance the USA's position is found under Article I, section 10, clause 1 of the Constitution which provides that "No State shall ... pass any Law impairing the Obligation of Contracts." This clause has commonly been referred to as "the Contract Clause".

In its early appearances before the Supreme Court, the Contract Clause was given an expansive reading. In *Fletcher v. Peck*,⁴⁵⁶ Chief Justice Marshall, ruled that the clause applied not only to executory contracts, but also to those which had been executed, including grants of property rights; and that it applied not only to contracts between private parties, but also to contracts to which a state was a party. Those conclusions dictated the holding that the clause prohibited a subsequent Georgia legislature from

⁴⁵⁴ 35 I.L.R. 136 (1963) at 172 – 173 as cited by Asanga *supra* note 370 at 11

⁴⁵⁵ 20 I.L.M. 1 (1981) as cited by Asanga *supra* note 370 at 11

⁴⁵⁶ 10 U.S. (6 Cranch) 87 (1810) as quoted and cited by Rodger Bern, 'A Look Back at the Contract Clause' www.lonag.com accessed on 5th September 2011.

annulling an earlier grant of land title made by a previous legislature to private parties who in turn had sold the land to bona fide purchasers. Within the decade the Marshall Court confirmed that the clause applied to all public contracts, whether they be in the form of agreements, grants or charters. In *The Trustees of Dartmouth College v. Woodward*,⁴⁵⁷ Marshall delivered the opinion of the Court holding that the clause prevented the terms of a charter of incorporation from the crown to a private educational institution from thereafter being modified by the state in which such corporation operated.

The application of the Contract clause has over the years certainly cultivated confidence within the business community and has been upheld in many other decided cases. No investor would be interested in taking high risks and developing projects in countries which do not offer a safe investment environment.

Article 3 Chinese Contract Law embodies the principle of sanctity of contracts. It provides that a contract is an agreement between equal parties and that one party is prohibited from imposing its will upon the other. Article 3 is to be understood as meaning that a state authority, as a contracting party, does not have the right to force another natural or legal person to enter into a contract, and within that contract, the parties are equal in their legal status with respect to its formation, performance, obligations and liability for breach.⁴⁵⁸

The sanctity of contracts principle is also expressly recognized under Article 1134.1 of the French Civil Code which recognizes the effectiveness of penalty clauses, whose purpose is to ensure the performance of a contract.

The absence of legal provisions in Kenya securing the sanctity of government contracts have created an environment for councilors to easily challenge PPPs they find in LAs upon their assumption of office following general elections. The common law embodiment of the principle of sanctity of contracts has not been sufficient to deal with this issue as research shows that judicial interpretation of the same has not been in favour of private parties to PPPs.

⁴⁵⁷ 17 U.S. (4 Wheat.) 518 (1819) as quoted and cited by Rodger Bern: A Look Back at the Contract Clause accessed from www.lonag.com last accessed on 5th September 2011.

⁴⁵⁸ Nicole Kornet, 'Contracting in China: Comparative Observations on Freedom of Contract, Contract Formation, Battle of Forms and Standard Form Contracts' *Electronic Journal of Comparative Law* <http://www.ejcl.org/141/art141-1.pdf> last accessed on 30th August 2011.

c. Policy guidelines on PPPs.

Clear policy guidelines designed to guide state actors in the implementation of PPPs have been used in some jurisdictions to *inter alia*, forestall and mitigate the effect of political risks to PPPs.

This approach has been adopted in the province of British Columbia vide the *Public Private Partnerships: A Guide for Local Government*⁴⁵⁹ which *inter alia* sets out the following:

1. A write-up on the legislative authority for PPPs
2. Assistance to LAs in determining when PPPs should be considered in delivery of services
3. Guidelines on how local governments can prepare themselves for delivery of services using PPPs
4. Recommendations for each stage of the partnership building process.

A similar policy guideline has been established for the New South Wales government through the *Guidelines on the Procedures and Processes to be followed by Local Government in Public-Private Partnerships*.⁴⁶⁰

A study of the policy guide in British Columbia shows that there appears to be a misunderstanding of who between the local authority and private entity should control the provision of services.⁴⁶¹ By their very nature, PPPs involve significant investments and risks by the private party and often provide for greater involvement of the private sector in decisions concerning how the services are to be delivered. Perhaps this has been one of the reasons why succeeding council's have tended to challenge PPPs entered by their predecessors in Kenya.

In recognition of the misunderstanding of the powers bestowed upon local authorities, British Columbia has recommended in the policy guide that the issue of control need to be addressed at the time the project is defined and kept in mind when the contract is negotiated.⁴⁶² The issue in Kenya LAs is much bigger. The problem does not appear to

⁴⁵⁹Ministry of Municipal Affairs, British Columbia '*Public Private Partnership: A Guide for Local Government*' at 11 the www.marh.gov.bc.ca accessed on 14th March 2010.

⁴⁶⁰ Available at http://www.dlg.nsw.gov.au/dlg/dlg/home/documents/information/PPP_Guidelines.pdf last accessed on 9th August 2011.

⁴⁶¹ Ministry of Municipal Affairs, British Columbia *supra* note 459 at 15.

⁴⁶² *ibid*

be that the local authorities' feel they have lost control of the service provision since other competitors have been contracted to carry out the same functions. What emerges is that the LAs are not opposed to the PPP mechanism *per se* but rather the specific private sector players.

A similar policy is used in South Africa vide the *Treasury Manual on Public Private Partnerships* which contains guiding tools designed to assist national and provincial government departments to structure successful deals with private partners for improved public service delivery.⁴⁶³ The Treasury Regulations lay down a standardised and specific set of processes which need to be followed before a government department can obtain the necessary treasury approval to enter into a PPP agreement with a private party.⁴⁶⁴

We do not have any guidelines that have been established to aid LAs in Kenya to implement PPPs. PPPs are a relatively new phenomenon and absence of such policy guidelines have fuelled political interference of PPPs by the councillors.

d. Establishment of PPP Units

PPP agencies/Units are a recent phenomenon and as a result, little is known about their origins, functions and global evolution. The term PPP agency/unit refers to any body (either within or connected to government) that provides services related exclusively to PPPs to other governmental bodies, or so-called service agencies. Service agencies are broadly defined to include all governmental entities that may benefit from the services of a PPP agency, including but not limited to municipalities, counties, line ministries, federal agencies, departments, special districts, port authorities and the like.

As developed countries increasingly utilize PPP approaches for procurement of infrastructure assets, they are creating agencies to provide centralized knowledge and a process for approving and implementing large-scale programs of PPP projects to ensure their successful implementation to the benefit of the public as the consumer, the public bodies and the private actors.⁴⁶⁵

For instance in South Africa, the Public Finance Management Act (PFMA) of 1999 was enacted to create a good governance structure for the procurement of goods and

⁴⁶³ Martin Schonteich 'Government Outsourcing: Public Private Partnerships' www.iss.co.ZQ/AF accessed on 20th September 2011.

⁴⁶⁴ *ibid*

⁴⁶⁵ Farrugia, Reynolds and Orr Public Private Partnership Agencies'A Global Perspective: Collaboratory for Research on Global Projects' (2008) at 1.

services by the public sector. It was subsequently decided to regulate the PPP procurement option under the PFMA specific Regulation.⁴⁶⁶ This led to the establishment of the South Africa PPP Unit to create a policy and regulatory framework for PPPs in the country. The goal of the PFMA legislation was to regulate PPPs to ensure that such projects were transparent, equitable and fair.⁴⁶⁷ The South Africa PPP Unit now serves as the regulatory and consulting body for PPPs.⁴⁶⁸ Since its inception in 2000, the South Africa PPP Unit has brought to financial close 20 PPP deals worth a combined \$5.5 billion.⁴⁶⁹

Governments in other countries with successful PPP programs, such as the Philippines, Malaysia, Ireland, and Italy have created PPP Units to provide the skills to take PPPs through the life cycle. This results in stronger projects that have a better chance of being implemented more quickly and successfully.⁴⁷⁰

There are three common arguments for administering PPPs through agencies as opposed to on a one-off, ad hoc, uncoordinated basis.⁴⁷¹ First, the agencies are said to provide a staff of highly-experienced and professional investment banking, legal and infrastructure experts with an ability to negotiate head-to-head with their private sector counterparties in the investment banks, law firms and infrastructure operators. Thereby they are able to ensure a better outcome for the state during the initial negotiations. Next, the agencies are purported to create standardized, consistent tender documents and deal-flow, which makes it possible for the private sector to familiarize itself with the bidding process. This format minimizes transaction costs and attracts many global players to bid, which, in turn, maximizes competition, innovation and value for the state. Finally, the agencies are said to provide institutional memory and an ability to capture best practice and lessons learned so that the state's ability to engage the private sector in infrastructure delivery improves over time.⁴⁷²

International experience strongly indicates that PPPs are likely to be more successful if governments move from an ad-hoc, case-by-case approach to creating a PPP Unit, staffed with professionals with the skills to take PPPs through the entire project life cycle

⁴⁶⁶ Farrugia *supra* note 465 at 21

⁴⁶⁷ *ibid*

⁴⁶⁸ *ibid*

⁴⁶⁹ *ibid*

⁴⁷⁰ D. O Ong'olo *Public Private Partnerships in Kenya* prepared for The Institute of Economic Affairs, Kenya. www.ieakenya.or.ke/documents/Public%20Private%20Partnerships.pdf accessed on 20th June 2010, at 37 and 38

⁴⁷¹ Farrugia *supra* note 465 at 21

⁴⁷² *ibid*

and provide programme support.⁴⁷³ While every project is different, PPP projects share similar features and can benefit from a consistent and structured approach to project identification, design, risk identification and allocation, tendering, evaluation, negotiation and award, which reflect best practices.⁴⁷⁴

A well established and operated PPP unit should help strengthen investor confidence in the government's ability to facilitate responsible private sector participation in key sectors. Any PPP initiatives undertaken without creating an environment conducive for investing in PPP projects could result in a low uptake rate and high perceived risks, both of which can be detrimental to investor confidence.⁴⁷⁵

Typically, in larger countries the national PPP units will not undertake the projects but rather provide the policy, technical, legal and other support mechanisms to LAs and government ministries that have the responsibility of putting the project together. Practically, it can help the relevant procuring authority (particularly one that is new to PPP or if the project is particularly new or complex) more confidently manage the whole process (including external advisors) from the development of the initial project design through to the bid evaluation process and post financial close. Units can achieve this by, for example, providing experienced people to sit on the decision-making boards for individual projects and supporting the public sector at key decision-making points.⁴⁷⁶

There is no established exclusive PPP Unit in Kenya. There is however talk of an intention to establish the same at the national level.⁴⁷⁷ No single PPP unit has been established in LAs to aid in the implementation of PPP projects. PPPs have been implemented through the general tender and procurement committees responsible for the other types of procurement.

PPPs units help in successful implementation of PPPs projects while ensuring the interests of the various actors, viz, the consumers of the services, the public bodies and the private actors are protected and secured. The absence of such dedicated units to aid in implementation of PPPs in LAs have in the author's view been fodder for political intrigues by councillors once they take office.

⁴⁷³ Ongolo *supra* note 470 at 37 and 38

⁴⁷⁴ *ibid*

⁴⁷⁵ Ongolo *supra* note 470 at 6

⁴⁷⁶ United Nations Economic Council for Europe: 'Guide Book on Promoting Good Governance in PPPs' (2008) http://www.undp.ro/download/UNECE_ppp.pdf accessed 15th May 2011 at 24

⁴⁷⁷ D. O. Ongolo *supra* note 463 at 6.

CHAPTER FIVE: THE WAY FORWARD: RECOMMENDATION AND CONCLUSIONS

We have observed above that PPPs represent partnerships in action with huge stakes for both the public sector and private sector agencies to succeed collectively. It is important that the public and private sector work together, keeping the project and outcomes in focus rather than maximizing their own interests, and collaborate for mutually enduring value. PPPs should thus be seen as a new way of doing business, and are not about command and control as has been witnessed in LAs in Kenya.

It has been pointed out that one of the vital things that has emerged from international experience for successful implementations of PPPs include the fact that high level political and institutional support is crucial.⁴⁷⁸ These have been found to be lacking when it comes to PPPs by LAs in Kenya.

The new Constitution has recognized the fact that all laws and institutions which safeguard democracy, justice and development must be underpinned in a philosophy of transparency and accountability for entrusted power. The power belongs to the people, and is held in trust by the leaders. The people are the conveyors of the power as well as the beneficiaries for the exercise of the power. Unlike the independence Constitution, the current Constitution does not give room for any philosophy which would allow service and loyalty to those in power; rather, it is those in power who have a Constitutional duty to serve and be loyal to the will of the collective people of Kenya. We have already pointed out in chapter 4 the specific provisions in the constitution in this regard including the provisions on principles of leadership and integrity in chapter 6 and provisions of public service in chapter 13 of the Constitution.

These Constitutional provisions have not been judicially tested so as to assist private actors who have subjected to the brunt of political risk arising out of PPPs by LAs. The Constitution being the supreme law of the land, the said Constitutional provisions can form the basis for both the central and county governments to enact legislation in order to give full effect to the principles enshrined in the constitution. It is proposed that such legislation should have appropriate provisions for safeguarding private actors from the effects of political risks.

The common law principle of sanctity of contracts has also been shown not to find favour in the implementation of PPPs by LAs. As a result, the rule of law relating to the binding

⁴⁷⁸ D. O Ong'olo *Public Private Partnerships in Kenya* prepared for The Institute of Economic Affairs, Kenya. www.ieakenya.or.ke/documents/Public%20Private%20Partnerships.pdf accessed on 20th June 2010.

nature of contracts has been violated leading to challenges of PPPs by the councilors. New regimes have been seen to withdraw support from PPPs in place and have entered into new but similar PPPs. Lack of sanctity of contracts leading to withdrawal of support of PPPs by state actors is one of the indicators of political risk emanating from PPPs.

It is therefore clear that there are gaps in the current PPP legislative and regulatory framework as a result of which political risk has not been adequately dealt with. As such, the regulatory regime for PPPs need to be changed or newly created in order to lay the basis for successful implementation of PPPs by the county governments. The proposed PPP legislation has to be contrasted with the existing regulatory arrangements and capacity and regulatory gaps should be filled or the PPP structure should be changed⁴⁷⁹.

In order to buttress the Constitutional provisions requiring state actors to act fairly, the following are the proposed main areas that need reform.

1. Legal Reform.

a. Enactment of specific legislation on PPPs by LAs/County Governments

It should be accepted that great steps have been taken towards regulating procurement and specifically PPPs in Kenya. There was no substantive law relating to PPPs prior to 2005. There is however a case for reform when it comes to PPPs by LAs and by extension county governments.

In addition to the existing PPP legislative and regulatory framework, there is need to enact *sui generis* legislation to govern PPPs by county governments in view of the observation that PPPs by LAs have been more prone to be affected by political risks than PPPs entered by the national government as well as other government agencies including line ministries and parastatals.

A well defined legal framework is required that provides clarity, defines contracting authority powers, minimizes procurement costs and timetables, for example, through standard/model contracts, improves dispute reduction, mitigates political risk and accommodates and safeguards the interest of the private actors.⁴⁸⁰

⁴⁷⁹ Asian Development Bank (ADB) 'PPP Preparatory work'<http://www.adb.org/Documents/Handbooks/PublicPrivatePartnership/Chapter6.pdf> accessed on 30th August 2010.

⁴⁸⁰ D. O Ongolo *supra* note 471

Several countries have indeed enacted specific legislation regulating PPPs by LAs quite apart from the general procurement and PPP laws governing procurement and PPPs by national government and other government agencies.

Some countries thus have laws that are specifically tailored to apply to PPPs by the local government taking into account the unique structure of the local government as well as the uniqueness of PPPs. For instance, New South Wales has the Local Government (Public Private Partnership Act).⁴⁸¹ The province of British Columbia in Canada amended its Municipal Act in 1998 to facilitate PPP arrangement by the local government.⁴⁸² The same approach should be adopted for this country so that the proposed legal reform should specifically address the issue of political risks among other issues arising from the use of PPPs by the local government and/or county governments.

In the context of county governments, it is proposed that a County Development Planning & Facilitation Bill be developed and passed to form the basis for integrating economic and spatial planning at the national level and county level.⁴⁸³ The Act may also form the basis for identifying programmes, projects and initiatives which can be the subject matter of PPPs by the county governments. A clear legislative position touching on PPPs by county governments will go a long way in dealing with political risk arising from PPPs by LAs

b. Statutory and regulatory provisions for Investment guarantees and sanctity of contracts

We have observed in chapter 4 of this report that investment guarantees are useful instruments used to protect the private companies and the lenders from the consequences of default by the Contracting Authority or other public authority assuming specific obligations under the project agreement.

We have seen that there is mention of investment guarantees in Regulation 11(1) of the 2009 PPPs Regulation. There are similar provisions under the now repealed Guarantee (Loans) Act which also empowered government to offer investment guarantees to private

⁴⁸¹Brian Dollery, 'Public Private Partnerships and Local Government Infrastructure' http://www.lgsa-plus.net.au/resources/documents/dollery-ppps-and-local-government-infrastructure_2005.pdf accessed 2nd August 2011

⁴⁸² Ministry of Municipal Affairs, British Columbia 'Public Private Partnership: A Guide for Local Government' at 11 the www.marh.gov.bc.ca accessed on 14th March 2010

⁴⁸³ Task Force on Devolved Governments(Kenya), *Interim Report nterim Report on Devolved Governments*, (April 20 2011). [http://www.communication.go.ke/documents/INTERIM%20REPORT ON DEVOLVED GOVERNMENT.pdf](http://www.communication.go.ke/documents/INTERIM%20REPORT%20ON%20DEVOLVED%20GOVERNMENT.pdf) accessed 16th May 2011 at 148

parties contracting with government agencies such as LAs to ensure the performance of LAs covenants. This section has not been saved by the National Governments Loans Guarantee Act, No. 18 of 2011, which repealed the Guarantee (Loans) Act. The current Act came into force on 30th August 2011.

The existing legal provisions on investment guarantees have not been adequate to shield investors partnering with LAs from the effects of political risks.

There is also no evidence that the existing provisions on investment guarantees have been applied in PPPs by LAs. This could be due to absence of guidelines and/or regulations on how the government can assume the projects risks arising from PPPs by LAs.

There is therefore need to have more explicit and elaborate substantive and subsidiary provisions on investment guarantees as has been adopted in other jurisdictions such as Sri Lanka. This will constitute legal reform to clarify and buttress the Government's role under Regulation 11(1) of the 2009 PPPs Regulation as well as making regulations and guidelines that will guide the government on which projects it can assume political risk on behalf of LAs/county governments.

From the analysis of the enforcement of investment guarantees other jurisdictions in chapter 4, it is seen that it is well established by international dispute resolution forums that investors who have suffered due to breach of investment protection guarantees given by governments are entitled to just compensation. Such a concept can find domestic application in Kenya if the law is amended to provide for investment guarantees.

In addition to statutory recognition, there should also be judicial recognition of this concept as has happened in most common law countries. For example, the Supreme Court of India in several cases has recognized the right to property of investors, wherein it has held that just and reasonable compensation should be provided in light of the market value of the property in case of acquisitions by the state.⁴⁸⁴ This is in consonance with the fair and equitable standard in international investment law which has been dealt with above, and thus assures the same protection to the investor as expected in International law.

⁴⁸⁴ See *Bihar v. Kameshwar Singh*, AIR 1952 SC 252; *K Kochhuni v. State of Madras*, AIR 1960 SC 1080; *Sajjan Singh v. State of Rajasthan*, AIR 1965 SC 845 as cited by Asanga *supra* note 41 at 12

There are important provisions in the Constitution that should be enforced through the judicial mechanism to aid private actors. It should be noted that the current Constitution is still in its early stages of existence having been promulgated just a little over a year ago.⁴⁸⁵

County governments are vested with legislative powers and they should enact such provisions in order to buttress the current constitutional provisions so as to secure the sanctity of contracts. County assemblies are vested with legislative authority under article 185 of the constitution. The same article also empowers county assemblies to formulate plans and policies for the management and exploitation of the county's resources and development and management of its infrastructure and institutions.

County government should also expressly legislate to uphold the sanctity of contracts to provide that no PPP shall be arbitrarily revoked. With such guarantees and safeguards in place and protected by clear statutory and constitutional provisions backed up with policy guidelines to educate the stakeholders in the LAs/County governments, private parties would be certain that the principle of sanctity of contracts will be upheld and hence minimize the effects of political risks. On the other hand clear and substantive and regulation on investment guarantees will enable the government to efficiently manage and assess the project risks and determine the level of direct and contingent liabilities it can assume.

Kenya being a member of MIGA, consideration should be given to utilization by county governments of MIGA facilitated investment guarantees to safeguard the interests of the private actors in PPPs. Efforts made to engage MIGA in political risk guarantee that have been made at the national government should trickle down to the county governments.

Closer home, due to the risky nature and huge claims involved, most insurance companies in Kenya have shown little or no interest in political risk insurance. However political risk insurance in Kenya is becoming popular due to the political challenges experienced after the 2007 presidential elections. Some local companies and firms such as Micro Ensure⁴⁸⁶ and African Trade Insurance Agency (ATI)⁴⁸⁷ are now offering political risk insurance and it is recommended that such insurance may be taken to

⁴⁸⁵ The Constitution was promulgated on 27th August 2011.

⁴⁸⁶ See www.microensure.com last accessed 10th October 2011. Mico Ensure is a insurance brokerage firm operating in Kenya.

⁴⁸⁷ See www.ati.aca.org last accessed on 10th October 2011. ATI is a constituent body of the Common Markets for Eastern and Central Africa and Kenya is a founding member.

shield the private sectors partnering with county governments from the effects of political risk.

c. Establishment of PPP Units

It is said that the Government intends to establish a PPP Unit within the ministry of finance.⁴⁸⁸ We recommend that there should be a central PPP Unit for the national government but this should be decentralized to the county government level. These units will oversee policy formulation offering guidance on the understanding of the PPP mechanism and implementation of the PPP projects.

There are several tasks that must be done before the Unit is operational and it has been proposed that the Unit be within the Privatization Commission.⁴⁸⁹ Firstly, there is a need to review, analyze, and recommend draft amendments to existing legislation clarifying the power and authority of local and central governments as well as public enterprises to enter into long-term contractual arrangements with private sector service providers. Secondly, there is a need to develop minimum standards and regulations governing PPP contracts LAs/County governments. The expected PPP framework would then lead to a transparent and successful development of infrastructure projects and services in Kenya. Thirdly, the PPP Unit will need to establish policies and procedures for preparing and packaging projects, and ensure quality control over these activities. Fourthly, capacity building in project planning, coordination and monitoring of PPP projects among public officers is another essential element required to strengthen the implementation capacity. Fifthly, whereas a comprehensive policy, legislative and institutional framework has already been passed in Kenya to serve the needs of the Government's privatisation programme there is need to blend a framework for PPPs into that for the privatisation programme with suitable enhancements to cater for the formal and institutional needs of a PPP programme.

As the set of skills needed to implement a privatisation programme are similar in many respects to that needed to implement PPPs, the PPP programme is likely to benefit from the legal framework which has already been passed by Parliament, the oversight of the Commission and transaction and infrastructure skills available under the Commission.⁴⁹⁰ Meanwhile before the Commission is fully established, it would be possible for the PPP programme to benefit from the transaction and infrastructure development expertise available in the Department of Government Investments and Public Enterprises (DGIPE), which is currently representing the Treasury in matters relating to PPPs. In the long run it would also be possible for the Programme to benefit from capacity created under the Commission once the privatization programme is phased out. Placing the PPP unit under

⁴⁸⁸ D. O. Ongolo *supra* note 478 at 6.

⁴⁸⁹ *ibid*

⁴⁹⁰ *ibid*

the Privatization Commission would also enable the PPP unit to pay reasonable/market rates of remuneration to enable the Unit to attract the required expertise.

A well established and operated PPP unit should help strengthen investor confidence in the government's ability to facilitate responsible private sector participation in key sectors. As a result, the common law position on sanctity of contracts will be integrated within the LAs contracting under the PPP mechanism. Any PPP initiatives undertaken without creating an environment conducive for investing in PPP projects could result in a low uptake rate and high perceived risks, both of which can be detrimental to investor confidence.⁴⁹¹

Public sector as well as private sector capacities should be enhanced, among others through a centrally located core of policy and implementation expertise including guidelines and project evaluation and procurement expertise, and mechanisms to ensure professional management and the purchase of relevant expert advice.⁴⁹²

2. Policy formulation and capacity building

a. Policy guidelines

There is a need for a formal policy to provide guidance to county Governments to understand the dynamics of PPPs. A formal policy adopted by LAs or County Assemblies will set out the broad direction as well as some of the ground rules to guide staff in achieving the LA objectives as they relate to service delivery as well as protect the private entities partnering with LAs/County Governments.

The guidelines as is the case in the province of British Columbia as well as South Africa could also provide clarity from the onset on the control given to the private party under the PPP in the projects.

The guidelines should also address the issue of political risks that the private entities are bound to face. One such recommendation that could also be legislated as recommended above is to specifying who in the LAs/County Governments has the ultimate responsibility of PPPs. It proposed in British Columbia's policy directive that responsibility may vested in one committee or department that may be responsible in formulating a PPP policy.⁴⁹³

⁴⁹¹ *ibid*

⁴⁹² D. O Ongolo *supra* note 478 at 6

⁴⁹³ Ministry of Municipal Affairs *supra* note 482 at 31.

One of the other important reason of the for establishment of policies for PPPs include the fact that a formal policy will allow LAs/County Governments to communicate their position on PPPs to other interested parties, including potential partners, labour unions, other interest groups and the public resulting into a boost of the investor confidence.⁴⁹⁴ A PPP policy will provide accountability and transparency as well as stakeholder involvement that will reduce the chances of challenges to PPPs by councils/county governments.⁴⁹⁵

It is clear from the content of the policy guidelines from the other jurisdictions that PPPs are envisaged to be long term in nature. By having a similar policy guideline in Kenya for county governments/ and or, the long term attributes of PPPs may be preserved as the succeeding councils would be aware of well documented policy guidelines that would be amended as the dynamics change from time to time.

As such a well defined policy framework is required that : (a) sets out clearly the processes, priorities and scope of PPP; (b) drives transparent procurement processes; (c) includes a communication strategy to improve public and private sector understanding of PPPs; (d) provides clarity of long term government obligations that work across federal and provincial levels; (e) includes mechanisms to recognize implicit/explicit government liabilities and public sector balance sheet requirements; and (f) includes mechanisms to deal with incumbents.⁴⁹⁶

Other than legislative measures, we therefore propose that a policy guide be put in place to guide LAs/ county governments in entering into PPPs in order to achieve these objectives.

b. Capacity building and accountability.

Procurement or Supply Chain Management system is an important financial control measure which will require to be enhanced at the county level. Under the ongoing Public Financial Management Reform Programme (PFMR), the legal and policy framework of

⁴⁹⁴ The same objective is given by the province of British Columbia which has formulated specific policy guidelines for PPPs by the local government vide the 'Public Private Partnership; A Guide for Local Government' May 1999, *ibid*

⁴⁹⁵ UN- Habitat, 'Local Democracy and Decentralization in East and Southern Africa: Experiences from Uganda, Kenya, Botswana, Tanzania and Ethiopia' www.unhabitat.org accessed on 3 August 2011, at 45.

⁴⁹⁶ D. O Ongolo *supra* note 478.

the procurement process has promoted transparent and accountable procedures and practices in central and local governments. However, misconduct associated with procurement in the public sector as well lack of investor confidence are still widespread especially in LAs.⁴⁹⁷

To further ensure accountability, it is proposed all appropriations including funds in relation to PPPs by county governments be based on the Integrated County Development Plan (ICDP) that will be one of the key outputs of this and will be the basis of expenditure by county governments.⁴⁹⁸ The ICDP should take into account the national, county and cross-county development parameters.

It is further proposed that the policy guidelines should establish mechanisms under which the members of county assemblies shall be subjected to a judicious application of the following articles of the Constitution in order to promote and ensure sufficiency and optimization of scarce public resources in the development of county infrastructure and the upholding of the rule of law including the sanctity of contracts:

- a. The national values and principles for governance outlines in article 10.
- b. The values and principles of the public service articulated under Article 232(1)
- c. The principles of public finance under Article 201.
- d. The objects of devolution in Article 174.
- e. The principles of devolved government under Article 175 and
- f. The guidelines on procurement of public goods and services (Article 227).

According to the TFDG, public hearings across the country revealed the disgust of citizens with electoral politics. To deal with this issue, further decentralization of functions has been proposed by the TFDG including the formulation of policy decisions on whether the de-concentrated units by County Governments should be purely administrative in order to avoid or minimize political interference. County governments are required by article 176(2) of the Constitution to decentralize their functions and provision of services to the extent that it is efficient and practical to do so.

⁴⁹⁷ Interim report on devolved governments *supra* note 487

⁴⁹⁸ *ibid*

CONCLUSIONS

Recent trends in the provision of infrastructure development indicate that the private sector is playing an increasingly important role in the development of projects within LAs. This trend has mainly arisen out of a necessity for the development of infrastructure to be undertaken at a rate that responds to the modernization needs of countries and growing demand for infrastructure services.

The study has dwelt on the application of the PPPs in service delivery in LAs focussing on PPPs by City Council of Nairobi and the Municipal Council of Mombasa. Some pieces of evidence for the application of the concept in the various LAs have revealed that political risk has not been adequately dealt with under the current policy and legal framework. These have been cemented by a detailed and in-depth case study of the PPPs by the City Council of Nairobi and Adopt-A-Light and the Municipal Council of Mombasa and KAPs.

As procurement reform has been traditionally seen as a technical and administrative process, there are very few studies focusing on its political economy dimension. With regard to procurement and by extension PPPs, political economy issues have been implicitly addressed as part of studies looking at public sector or governance reform more broadly.⁴⁹⁹ Yet, as procurement reform often meets major resistance from vested interests within society there is a growing recognition of the need to understand and address the underlying factors that may undermine political will for reform and more systematically analyse the effects of political risk on PPPs as this study has done.

In our conclusions we state that the issues discussed in the report raise significant challenges to the conduct of successful PPPs by LAs in Kenya. The complexity of such arrangements and the high costs involved is enough cause for the Government to take a careful approach to PPPs.

A number of PPP projects are either on-going or at various stages of project development in LAs under the PPP mechanism. The potential to use PPP projects by LAs and County Governments will be actualized if the existing legal and policy framework are revamped and reformed. This should entail existing laws, regulations, existing PPPs by LAs, and other legal documents that define the characteristics of PPP or those that have to be changed⁵⁰⁰⁵⁰¹. The PPP structure, legal and regulatory

⁴⁹⁹ Transparency International, 'The Political Economy of Public Procurement Reform' <http://www.u4.no/helpdesk/helpdesk/query.cfm?id=202> last accessed on 5th August 2011

⁵⁰⁰ *ibid*

framework has to reflect and take into account such things as would ensure the minimization of damage resulting from political risk and adherence to the independent corporate principle by LA.

In a nutshell, we propose the adoption of better laws and policies that will suit PPPs by LAs/county governments. Better laws and policies are those that are knowable and secure, allowing investors to plan investment decisions and to adopt longer term as opposed to short-term perspectives when entering a market and this factor can attract a better quality of investment to a PPP.⁵⁰² In PPPs better predictable rules have also some other more specific advantages, namely where the need to mitigate risk is such a central feature, predictability can allow lenders to better quantify the risk.⁵⁰³ Lenders and investors will look for a predictable and reliable framework for PPPs for example, on investment laws, tax, security, corporate law, and contracts, and dispute resolution law in the project country. Bearing in mind the limited recourse nature of most concession/PPP based financing, funders look mainly to the legal and contractual framework for protection and need to be reassured as to its long-term stability and predictability.⁵⁰⁴ Here the predictable conditions for investments will include such things as secure legal and enforcement framework for investment guarantees. Better also means better quality legislation that clarifies rights and obligations in PPP processes. The public sector's legal ability to grant concessions and enter into PPPs and the implementation of the projects is in many jurisdictions the most critical uncertainty faced by lenders and investors and it is best removed by a fully-fledged PPP law.⁵⁰⁵

⁵⁰¹ ADB *supra* note 479

⁵⁰² United Nations Economic Council for Europe: 'Guide Book on Promoting Good Governance in PPPs' (2008) http://www.undp.ro/download/UNECE_ppp.pdf accessed 15th May 2011.

⁵⁰³ *ibid*

⁵⁰⁴ *ibid*

⁵⁰⁵ *ibid*

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