Complying with Business Regulation in Kenya


by
The REME De-regulation Study Team
Peter K'Obonyo
Gerrishon K. Ikiara
Winnie Mitullah
Charles Abuodha
Grace Ongile
Dorothy McCormick

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Executive Summary

The Government of Kenya (GoK) has recognised a need to remove or reduce unnecessary regulatory barriers affecting Small and Micro Enterprises (SMEs) since there are a number of restrictive regulations that affect their operation. In an effort to address the restrictive environment, the GoK with the support of the British government's Department for International Development (DFID) set up the De-regulation Section (DS) within the Ministry of Planning and National Development. The DS is one of the DFID projects being researched, evaluated and monitored by the University of Nairobi, Institute for Development Studies (IDS) Research, Monitoring and Evaluation (REME) Project.

The DS aims at the removal of superfluous and unnecessarily restrictive regulations which inhibit economic activity. The DS has been examining laws and regulations that impact on the growth and development of SMEs. Their work revealed that the licensing laws and by-laws which were set up to control, prohibit or regulate various business activities are the single greatest deterrent to entry into and growth of business in the private sector in Kenya.

The benchmark study of the Trade Licensing and Registration of Business Names Acts conducted by IDS, REME Project aimed at understanding the policy and regulatory framework within which SMEs operate. The study sought to establish compliance rates and the costs of compliance and non-compliance. The research also sought to know the perception of both policy makers and the general public on the activities of SMEs. Samples (for analysis) were drawn from six towns: Nairobi, Nakuru, Kakamega, Siaya, Nyeri and Kajiado. The six were purposively selected for the benchmark survey on de-regulation. The selection was guided largely by considerations of the nature of the regulatory environment rather than a need for geographical representation. The sample covered a total of 300 entrepreneurs and 54 suppliers, consumers and people staying near SMEs.

The majority (73.7%) of enterprises were sole proprietorships, and most entrepreneurs started doing business in 1980. There was no difference in when men and women started doing business. Enterprises were mostly trading in the sectors of manufacturing (20.7%), commerce and trade (21.3%), hotel and restaurants (10.3%), repairs (11.7%), food and food processing (11.0%). Others included construction and building (8.7%), transport (8.0%) and fish trade (8.3%). Most (32.0%) of the enterprises covered in the survey were operating within the central business districts (CBDs) of urban areas. This was followed by roadside/highway (17.0%), open air markets (16.7%) and residential shopping centres (15.3%).

The study determined the extent to which small-scale entrepreneurs are in
compliance with government regulations. Trade licensing and registration of business names received most attention, but the investigation also included questions about other regulations. Despite the fact that the Registration of Business Names Act (Cap 499, Laws of Kenya) is very clear about who is required to register, the study found that there was confusion about registration. When asked if their business was registered, 123 entrepreneurs (42.0%) out of 300 replied in the affirmative. Only 73 of these, however, gave the Attorney-General’s Chambers as the body with whom they had registered. The others named agencies such as the Ministry of Social Services, Ministry of Health and Fisheries Department. Such registrations have nothing to do with business name, yet the fact that the enterprises lumped all together is an indication of the confusion surrounding the term registration.

The Trade Licensing Act (Cap 497, Laws of Kenya) requires that all business activities be licensed. Of the 300 firms in the enterprise survey, 89 were engaged in trading activities requiring a licence. Of these, 73 (82.0%) reported having the required licence, 15 (16.9%) said they had no licence and one respondent (1.1%) did not reply to the question. Those with licences seem to keep them up-to-date. Nearly all (95.3%) of those who have licences said that they were current. Those without licences tend to be traders without fixed premises, operating in open air markets and along the roadside.

The sample data were used in conjunction with data from Kenya’s national baseline studies of small and micro-enterprises (Parker 1994, Daniels et al 1995) to estimate the number of enterprises in compliance in the country as a whole. The estimates are a direct extrapolation from the sample percentages. Over 480,000 businesses are in compliance with the Registration of Business Names Act, and over 350,000 are in compliance with the Trade Licensing Act.

Most firms in the sample (68.3%) are in compliance with the requirements of the Registration of Business Names Act. Of the 205 complying firms, 73 were actually registered. For those not required to register, the only cost of compliance is that of obtaining information on the act. Registered businesses, however, have additional costs: the direct cost of registration, travel time and the cost of displaying the registration certificate.

The survey examined three broad types of costs of non-compliance. The first are the money costs of preventing the authorities from taking punitive action as a result of the enterprise’s failure to comply. The most common item in this category is the payment of “public relations” money to the enforcement officers. The second group includes the financial consequences of punitive action actually taken by the authorities. The authorities are known to close businesses, evict firms from their premises, demolish premises and confiscate goods. Such actions have direct costs. Finally, both preventive measures and dealing with the consequences of the punitive action take time, a costly commodity in the business world.
Businesses out of compliance with the Registration of Business Names Act pay an estimated KSh 273 million in public relations (bribe) money to protect themselves from punitive action. Firms whose names are unregistered also suffer from evictions, arrests, demolitions and confiscation of goods. These costs are estimated at KSh 356 million annually. Finally, firms whose names are not registered spend time valued at KSh 128 million dealing with the consequences of their non-compliance. The total cost for the estimated 224,000 out-of-compliance firms is estimated to be KSh 757 million. Unlicensed trading firms pay an estimated KSh 23 million in public relations money to prevent the authorities from taking punitive action against them. Firms without trade licences also incur costs when they are evicted or arrested and when their premises are demolished or their goods confiscated. These costs are estimated to amount to KSh 141 million annually. The most costly part of non-compliance with trade licensing is not the direct payments but the lost time. The estimated 77,000 entrepreneurs who do not comply with the Trade Licensing Act lose an estimated KSh 236 million annually as a result of the time needed to cope with actual or threatened punitive action.

The study assessed the perceptions of the public and policy makers on the importance and benefits of regulation and de-regulated environment for SMEs and the government’s ability and commitment to de-regulation. The members of the public—suppliers, consumers and those staying near SMEs—felt that they faced a number of problems in running their operations. These problems included lack of business development facilities, inadequate infrastructure, poor location and access to services, inadequate shelter, insecurity, lack of markets, pollution, health risks, noise and unfair competition from large licensed businesses. Despite the positive aspects of employment opportunities and income generation from SMEs, the public had mixed reactions about the importance and benefits of regulations, with the majority pointing out that regulations encouraged corruption and only large businesses should be subjected to registration and licensing. Evidence from discussions with members of the public and with government officials supports the general need for making the regulatory framework simpler and more fair. The main concern was in the area of public health, where members of the public wanted strict and well-enforced regulations to ensure that they are not exposed to health hazards.

Discussions with policy makers revealed that they were aware of the local government circular about the need for de-regulation. They acknowledged the fact that procedures of licensing are tedious and cumbersome and that de-regulation is necessary. Some councils had begun re-organising departments involved in licensing in preparation for the de-regulation programme requirement of a one-stop-shop office for handling all matters of licensing. Policy makers at the Ministry of Trade indicated that the implementation of the one-stop-shop policy would create unemployment for the many officers who had been dealing with
issuing licences.

The benchmark study found a high level of compliance with both the Trade Licensing Act and the Registration of Business Names Act. The study found that enterprises could benefit substantially from streamlining the regulation process. Time was found to be the largest single cost of complying with the Registration of Business Names Act. This is because all registration is done in Nairobi, forcing business owners located elsewhere to take considerable travel time. De-centralising the registration process would substantially reduce the costs to the enterprises without interfering with government revenue. The study found that non-compliance is also costly, especially to enterprises suffering from punitive measures taken by the Central Government or Local Authorities. It is not surprising, therefore, that many businesses choose to make “public relations” payments to avoid these costs.

Evidence supports the need for continued effort to reduce the regulatory burden. The study noted that de-regulation as a concept is recent in Kenya, and many members of the public are still not aware of it. Furthermore, members of the public have lost faith in government performance and are therefore not sure that the de-regulation programme will be put in place. There is need for information and awareness campaigns.