




This newsheet is designed to inform our clients of recent developments in the law in Kenya, Uganda and Tanzania. If you would like us to e-mail it direct to any specific persons in your organisation please contact: Pamela Nabwire  
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## Doing Business in Kenya: New Proposals to Reform Trade and Business Licensing Regulations

The complicated and cumbersome licensing regime in Kenya has significantly remained an obstade to the country's competitiveness as an attractive investment destination. Currently, there are an estimated 600 licences that govern different aspects of trade and investment in Kenya.

In line with the much publicized policy of the Government of Kenya (the "Government") of improving the business environment for both local and foreign investors, the Government has proposed the abolition of certain trade licenses as set out in the Statute Law (Miscellaneous Amendments) (No. 2) Bill, 2005 (the "Bill"). The purpose of the Bill is to refine the legal framework of the licensing regime governing the conduct of business activity in Kenya and more importantly to abolish several licenses whose compliance requirements have significantly increased the cost of doing business in Kenya. These licenses are either outdated or impose higher costs to users as compared to the anticipated benefits. This note highlights the key changes proposed to be made to the licensing regime which include:

### Local Government Licenses

The Bill proposes to amend the Local Government Act with a view to reducing the number of business permits that a distributor of goods or provider of services is required to obtain in order to distribute goods or provide services. In a marked departure from the current situation, whereby a trader is required to obtain a licence from every local authority where he distributes goods or provides services, a permit granted by one local authority for distribution of goods and provision of services would be effective for carrying out a similar activity in the jurisdiction of another local authority.

### Factory Licenses

In what is dearly seen as an incentive to enhancing growth and development of small and medium enterprises ("SMEs"), the Bill proposes to amend the Factories and Other Places of Work Act (the "Factories Act") in order to exempt SMEs with employees not exceeding fifty from the provisions of the Factories Act.

### Other Licenses

In what is welcome relief to foreign investors, the Bill is set to amend the Investment Promotion Act ("IPA") in order to give foreign investors the opportunity to choose whether they need an investment certificate or not. Presently, under the IPA, which has not yet come into force, a foreign investor is obliged to obtain an investment certificate before the investor can invest in Kenya. In addition, the Bill proposes to repeal the Trade Licensing Act effectively dispensing with the requirement for licenses that are not related to the regulatory aspects of a business. The Bill also proposes to amend the Hotels and Restaurants Act by dispensing with the requirement of a hotel manager's licence before one can set up a business in the hospitality industry. Further, if the proposals of the Bill are enacted into law, no licence would be required for the purpose of dealing in hide, skin and leather.

### Asset Leasing in Kenya

Asset leasing is increasingly being recognized by businesses in Kenya as a tax and cash efficient method of financing the "acquisition" of assets such as plant and machinery, IT equipment, motor vehicles and other non-core assets without having the need to own such assets.

Essentially, an asset lease is a contract of bailment, where the owner of an asset (the bailor or lessor) leaves his asset in the possession of another person (the bailee or lessee) for a specific purpose and period.

The essence of the relationship between a lessor and the lessee include:

- legal ownership of the leased asset remains with the lessor throughout the period of the lease;
- the lessee being entitled to use the leased asset for a specified period;
- the lessee paying the lessor rental payments for the use of the leased asset – the lessor may also require the lessee to make other payments to the lessor or to a third party relating to the asset (for example, the lessor may require the lessee to pay to the lessor an amount equivalent to the cost incurred by the lessor in insuring the leased asset).

Almost any class of asset is capable of being leased provided possession of the asset is capable of being transferred by physical delivery. The duration of a lease can vary from a few minutes (for example, the hire of a tennis racket at a sports club) to many years (for example, the lease of an aircraft by an airline company).

### *Asset Leasing In Kenya– Continued*

#### Entry into Leases - Acquisition of assets by the lessor

The method by which a lessor acquires the assets which are the subject of a lease can vary. The following are some of the principal ways of acquisition.

#### (i) Direct purchase by lessor from supplier

An intended lessee having selected certain assets he wishes to lease can sign a lease agreement with an intended lessor by way of offer. The order for the relevant assets is then placed with the supplier and on delivery the lessee certifies to the lessor that the assets have been received in good order. The lessor then signs the lease by way of acceptance and pays the supplier.

#### (ii) Novation

Novation is used when a proposed lessee has entered into a contract with a supplier for the purchase of assets. Before payment is made to the supplier, the lessor and lessee can enter into a lease agreement, and thereafter, the supply contract is novated to the lessor. The original contract between the lessee and the supplier is discharged and a new contract between the lessor and the supplier is created.

#### (iii) Agency

A lessee can be appointed as agent for the lessor to acquire the goods from the supplier. The agency relationship may or may not be disclosed to the supplier. The agency relationship is not disclosed if the lessor and/or the lessee do not wish the supplier to know of the underlying lease transaction or if the lessee wishes to have a direct contractual relationship with the supplier.

#### (iv) Sale and leaseback

If the lessee owns certain goods, such goods can be sold to the lessor. Thereafter, the lessor would lease such goods to the lessee.

#### Key documents utilised in leasing transactions

The main documents in asset leasing transactions include the Master Lease Agreement, Lease Agreement, Purchase Agreement, Maintenance Agreement, Buy-back Guarantee and Other Miscellaneous documents (such as an Agency Agreement or Novation Agreement).

#### Taxation considerations of asset leasing in Kenya

In Kenya, asset leasing is governed by the Income Tax (Leasing Rules) 2002 (the "Leasing Rules") enacted by the Minister of Finance under the Income Tax Act (the "ITA") and the Value Added Tax Act (the "VAT Act"). Lease payments are deductible against the income of the Lessee. It should also be noted that asset leasing is a taxable service under the VAT Act, and as such, VAT is chargeable on lease payments made by the lessee. These VAT payments are however, claimable as input VAT by a registered lessee. As for the Lessor, he will be entitled with the approval of the Commissioner of Income Tax to claim deductions for wear and tear in respect of the leased assets and any other expenditure incurred.

wholly and exclusively in the production of the lease payments. VAT paid by the Lessor on the original purchase of leased assets will be claimable as input VAT, albeit over a longer period of time than the lessee as VAT on the assets purchased is payable upfront while VAT charged on the lease payments is spread over the lease period.

#### Certain legal advantages of leasing in the East African context

In an East African context there could potentially be certain legal advantages to leasing, particularly with regard to financial institutions

Traditionally, banks in East Africa have lent against security such as charges/ mortgages over immovable property, directors' personal guarantees, specific charges (sometimes called specific debentures) over identified movable assets or all-asset debentures over all or substantially all the assets of borrowing companies.

It is the case that courts in East Africa have been prepared to issue orders preventing lenders from enforcing security by granting, for example, injunctions vacating the appointment of receivers thus interfering with the exercise of statutory powers of sale under charges or mortgages. Banks have therefore found themselves in the invidious position of having large outstandings and non-performing loans that are not being properly serviced but with security they are unable to enforce. Although such injunctions are issued on an interim basis, the inevitable delays in the court process often mean that for the foreseeable future a bank that is at the wrong end of such a court order is unable to do much to enforce its rights and obtain repayment of the amounts that it claims are due to it.

There is also the general concern (as evidenced by the Donde Legislation in Kenya) of the risk of the rate of interest or at least default interest being controlled by the regulations.

With this backdrop of what seems to many as judicial activism targeted against the enforcement of traditional forms of bank security, leasing is an attractive alternative to lending, principally for the following reasons:

- Legal title to the assets which a bank is leasing remains with the bank;
- Subject to compliance with statutory requirements in each jurisdiction, the courts in each country have generally not so far interfered with the principal remedy of a lessor when a lessee is in breach of the terms of a lease agreement, namely forfeiture and repossession of the leased assets and the right to sell such leased assets to recover what is due under the lease;
- It may be possible for proposed lessees to quite properly circumvent limitations imposed by existing bankers against incurring additional borrowings and for new bankers to develop relationships with such lessees without being subject to any security that existing bankers may hold; and

*Asset Leasing In Kenya— Continued*

- It may be possible for bankers to lend to companies (proposing to act as lessor) that they may otherwise not consider lending to, when actual credit risk lies with the proposed lessee (whose credit risk the Bank is willing to accept) as it may be possible to secure in favour of the Bank the receivables due from the lessee to the lessor.

(Anjarwalla and Khanna, Advocates has been recognized by Chambers International Law Directory of the world's leading lawyers as "having a niche in Asset Leasing in Kenya").

**Troubling Court Decision for Manufacturers of Consumer Goods**

Uganda's Court of Appeal recently handed down a worrying decision in the case of *Ssendi Edward v M/S Crown Beverages Ltd*, the facts of which are very similar to a famous English case which most lawyers will fondly remember having come across during their law school days. In this case the defendant Crown Beverages ("Crown") was found liable for injuries caused to Ssendi who had consumed a soft drink produced by Crown that was found to contain foreign substances. Ssendi alleged that he had suffered a number of minor and serious ailments as a result of consuming the soft drink and sued Crown for general damages. The trial judge dismissed Ssendi's case for failure to prove that Crown had breached the duty of care owed to Ssendi.

On appeal, Ssendi succeeded. The Appellate Court found that when Ssendi bought the soft drink it was still intact and that the soft drink had left the factory with no external intervention until Ssendi consumed some of its contents. The Court found that Crown's failure to adduce evidence to contradict Ssendi's testimony was an admission that the bottle was contaminated when it left the factory and that this was therefore a breach of duty on Crown's part.

The Appellate Court also found that although Ssendi had not proved that the consumption of the adulterated soft drink had caused the serious illnesses alleged, there was ample evidence that Ssendi had suffered pain. It awarded Ssendi general damages. The Court held that there was a "serious laxity and dereliction of the duty of care owed to the unsuspecting consumer by Crown".

In reaching this decision, the Court made reference to the famous English cases of *Donoghue v Stevenson* and *Bonnington Castings Ltd v Wardlaw*. The ratio in both these cases is that in an action for damages in common law, the onus of proving that the fault complained of caused, or materially contributed to, the injury complained of, as well as of proving the negligence or breach of duty lies with the Plaintiff. Interestingly, although purporting to follow the *Donoghue* decision, the Court made no finding at all on the issue of Crown's negligence as a matter of fact but rather seems to have presumed that this was the case.

The Ssendi decision appears to have been based on the premise of strict liability and arguably creates strict liability in such "consumer" cases. We can only presume that this was not the intention of the Court of Appeal as the repercussions of such a decision would be enormous for all manufacturers and suppliers of consumer goods. The decision has been appealed against and hopefully the law will be clarified on the outcome of the Supreme Court's decision. In the meantime manufacturers of "consumer" goods must take cognizance of the decision in Ssendi's case.

**Rights and Duties of a Mortgagee upon sale of Mortgaged Asset**

In the recent case of *African Textile Mills Ltd [In Liquidation] v Co-operative Bank Ltd (In Liquidation)* the High Court ruled on the rights and duties of a mortgagee upon realisation of an asset by that mortgagee.

African Textile Mills Limited ("ATML") mortgaged its property to the Co-operative Bank (the "Bank") to secure certain banking facilities. ATML subsequently defaulted on its repayments to the Bank and after proceedings were filed the case was settled with ATML accepting the debt and undertaking to pay in certain stage payments. When threatened by execution of the resulting Court decrees, ATML placed itself in voluntary liquidation. This action was intended to frustrate the execution process. The Bank then seized possession of the mortgaged property acting under its contractual powers set out in the mortgage deed and its statutory powers under the Mortgage Act.

ATML contended that the Bank as secured creditor should be restrained from realising its security on account of the voluntary liquidation of ATML. In ATML'S view, the sale of the mortgaged property should have been left to the Liquidator with the Bank receiving first claim to the proceeds of assets disposed of by the Liquidator. ATML contended further that if the mortgaged property was sold on a piece meal basis by the Bank and not as a whole by the Liquidator, the property would effectively be sold at a price below its actual value and ATML would suffer loss.

The judge ruled that the Bank as mortgagee was a secured creditor and was entitled to stand outside the liquidation process and realise its security. The judge further held that a sale by a mortgagee must be a genuine one to an independent purchaser at a price honestly arrived at. The mortgagee is liable in damages to the mortgagor for negligence either of the mortgagee or his agent in the conduct of the sale. The Judge held that a mortgagee has a duty to take reasonable steps to obtain the proper price in the interests of the mortgagor and in this regard followed the principles enunciated in *Cuckmere Brick –v- Mutual Finance (1971) 2 All ER 633*. While the *Cuckmere Brick* decision has been the law in England for sometime now, it had not to our knowledge been cited in a local decision of the Courts.

Mortgagees selling mortgaged property should take every precaution to ensure that the property is properly advertised with all material information and facts regarding the property being brought to the attention of prospective purchasers. Where the property has a specialised use, particular care must be taken to bring the sale to the attention of users of such property. An advertisement including, amongst other information, a picture of the property with a good description of it, its current and possible uses, and right of access is recommended.

#### Stamp Duty Exemption for Transfer of Property between Associated Companies

Associated and group companies in Tanzania involved in various sectors of the economy such as real estate, manufacturing, media, agriculture, tourism, banking and insurance are, in our experience, increasingly looking at restructuring their operations to ensure that associated companies concentrate their operations on areas of strength. This process could usually entail transferring or shifting non-core assets and property from one associated company to another company. It will be appreciated that as a result of such restructuring, the associated companies could potentially incur considerable costs, one particular case which could be as much as 1% if a transfer of land was involved in stamp duty clearly and as such, if the transactions were exempt from the payment of stamp duty, then the restructuring costs could be significantly reduced.

In Tanzania, transfers or conveyances of property between associated companies are not chargeable to stamp duty provided that it is shown that the effect of the transaction is to convey or transfer the beneficial

interest (and not, therefore, the legal interest only) in property from one company to another company and that either:

- one of such companies is the beneficial owner of not less than ninety per cent. (90%) of the issued share capital of the other company; or
- not less than ninety per cent. (90%) of the issued share capital of each of the body corporates is in the beneficial ownership of a third body corporate.

In addition, in order for entities to obtain the benefit of the stamp duty exemption, the relevant instrument must be executed in pursuance of or in connection with an arrangement where either:

- the consideration for the conveyance or transfer is to be provided directly or indirectly by a company which at the time of execution of the instrument was associated with either the transferor or transferee; or
- the beneficial interest in the property was not previously conveyed or transferred directly or indirectly by such person (that is a non-associated person who is providing the consideration).

A company for the purposes of this exemption shall only be deemed to be associated with another company if, either one of them is the beneficial owner of not less than ninety per cent. (90%) of the issued share capital of the other or not less than ninety per cent. 90% of the issued share capital of each of them is in the beneficial ownership of a third company.

#### Business Competition in Tanzania: The Regulatory Regime

The Tanzanian legislature enacted in 2003 the Fair Competition Act (the “FCA”) to provide a foundation for the establishment of competition policy and law in Tanzania. The major objects of the FCA are to promote and protect effective competition in trade and commerce and to protect consumers from unfair and misleading market conduct. It also addresses other related matters in order to increase efficiency in the production, distribution and supply of goods and services, promote innovation and maximize the efficient allocation of resources.

The conduct of all private or public enterprises engaged in business falls within the ambit of this law. If a company is engaged in activities outside Tanzania, its conduct may also be regulated by the FCA as it applies to the following:

- a citizen of Tanzania or a person ordinarily resident in Tanzania;
- a body corporate incorporated in Tanzania or carrying on business within Tanzania;
- any person in relation to the supply or acquisition of goods or services by that person into or within Tanzania; or
- any person in relation to the acquisition of shares or other assets outside Tanzania resulting in the change of control of a business, part of a business or an asset of a business in Tanzania.

#### Restrictive trade practices under the FCA

These includes acts performed by persons engaged in production or distribution of goods or services which prevent others from effective participation in the distribution of goods or services and which reduces or eliminates the opportunities of others to acquire those goods or services

#### Abuse of dominant position

The FCA forbids abuse of a dominant position in the market if by conduct the object or effect of the conduct is to prevent, restrict or distort competition unless the Fair Competition Commission has granted an exemption. A person has a dominant position in a market if in acting alone the person

can profitably and materially restrain or reduce competition in that market for a significant period of time and if the person's share of the relevant market exceeds thirty five per cent.

#### Monopolies and concentration of economic power

If a company is engaged in any merger or seeks to acquire businesses and assets in Tanzania, the FCA seeks to control the rise of monopolies and concentration of economic power through rules on mergers and acquisitions. A merger is prohibited if it creates or strengthens a position of dominance in the market

#### Consumer protection

For the protection of Tanzanian consumers from business practices that injure their welfare, the FCA expressly forbids:

- misleading or deceptive conduct such as misleading representations and misleading conduct in relation to goods and services;
- unfair business practices such as advertising of goods and services at a price that is different from what the supplier intends to supply them at and accepting payments without intending to supply the goods or services; and
- exclusion or modification of the application of the provisions of the FCA in consumer contracts (any term of a contract that purports to exclude, restrict or modify them shall be void).

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