

Real Estate

Contributing editor
Joseph Philip Forte



2018

GETTING THE
DEAL THROUGH

GETTING THE
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Real Estate 2018

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Kenya

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General

1 Legal system

How would you explain your jurisdiction's legal system to an investor?

Kenya's legal system is largely based on English common law and comprises private and public law. The primary sources of law in Kenya are the Constitution 2010 (the supreme law binding on all persons and state organs), statutes and case law. The laws relating to land are codified and have a national application.

In determining matters, the courts of Kenya are guided by the Constitution, statutes and the doctrines of equity, and the statutes of general application in force in the United Kingdom on 12 August 1897.

Injunctions can be granted in court once a claim preventing an action is lodged in court. A temporary or permanent injunction preventing the action can be granted.

The Law of Contract Act (Cap 25) provides for both oral and written contracts. However, contracts relating to a disposition of an interest in land must be in writing and oral contracts are not admissible.

2 Land records

Does your jurisdiction have a system for registration or recording of ownership, leasehold and security interests in real estate? Must interests be registered or recorded?

Kenya has a well-codified land registration system. The Land Act, the Land Registration Act and the National Land Commission Act, all enacted in the year 2012, consolidated all laws in Kenya relating to land.

Dealings in land, whether leases, charges, easements or other encumbrances, must be registered at the relevant land registries. Registration vests the interest and confers the rights appurtenant thereto. A non-registered instrument does not confer the interest but, to the extent possible, operates as contract interparty.

Unregistered land in Kenya is not recorded.

3 Registration and recording

What are the legal requirements for registration or recording conveyances, leases and real estate security interests?

Before registration the following must be done:

- the instrument to be registered, and transfers or leases must be properly prepared and executed;
- all land rates and land rents (if applicable) must be paid and clearances obtained;
- consents such as Land Control Board Consent, National Land Commission consent should be procured;
- in the case of a sale, the vendor should compute the capital gain and pay the relevant capital gains tax; and
- the instrument must be presented for assessment of stamp duty and the stamp duty paid.

Having satisfied the above, the documents can be booked for registration.

- The following fees and taxes are payable in a dealing with property: stamp duty: a tax payable to the government on any instrument listed in the stamp duty act, including transfers, leases and security instruments. the type of instrument and the transaction value determines the stamp duty payable;
- land rates: a tax payable to the county government in accordance with the valuation for rating act (Cap 266);
- land rent: the rent payable to the head lessor on leasehold property.
- capital gains tax: a tax payable by the seller of a property, being 5 per cent of the difference between the excess of the transfer value of the property over the adjusted cost of the property at the point of transfer; and
- value added tax (VAT): VAT is payable by the buyer of a commercial property. it is computed at 16 per cent of the sale value.

Parties to a transaction structure the transaction in a myriad of ways to minimise tax obligations or avoid an otherwise illegality. This can be achieved either by the parties choosing the right entity or entities to transact through or by acquiring the property through a shares purchaser rather than a direct purchase of the property.

4 Foreign owners and tenants

What are the requirements for non-resident entities and individuals to own or lease real estate in your jurisdiction?

What other factors should a foreign investor take into account in considering an investment in your jurisdiction?

Generally, foreigners and non-resident entities can own land in Kenya. There are, however, certain restrictions to ownership and dealing with land by foreigners as follows:

Foreigners and local companies with foreign shareholding may only hold land on the basis of leasehold tenure for terms not exceeding 99 years.

Dealings in agricultural land in Kenya are controlled under the Land Control Act. The consent of the Land Control Board must be obtained for any transaction involving the sale, transfer, lease, mortgage, exchange, partition or other disposal of, or dealing with, agricultural land. Consent will not be given to non-Kenyan citizens for any such transactions (save for a mortgage or charge created in favour of a non-Kenyan lender). Non-citizens may, however, apply for a presidential exemption from the application of the Land Control Act.

Any of the following land will not be transferred to non-Kenyan, a government other than the government of Kenya, or a body corporate that has non-Kenyan citizens as shareholders without the prior written approval of the cabinet secretary responsible for matters relating to land:

- within a zone of 25km (kilometres) from the inland national boundary of Kenya;
- within the first and second row from high water mark of the Indian Ocean; and
- any other land declared as controlled land under any law or Statute.

Save for the foregoing, no special licences, tax forms or permits are required from foreigners when dealing with land.

5 Exchange control

If a non-resident invests in a property in your jurisdiction, are there exchange control issues?

There are currently no exchange control restrictions or laws in Kenya. However, the Central Bank of Kenya regulates transactions with foreign entities by requiring all monies to be paid through an authorised bank in Kenya.

6 Legal liability

What types of liability does an owner or tenant of, or a lender on, real estate face? Is there a standard of strict liability and can there be liability to subsequent owners and tenants including foreclosing lenders? What about tort liability?

Various liabilities attach to the owners and occupiers of land. These include:

- utilities charges: the owner or occupier must pay for utilities (eg, electricity and water consumption on the property), land rent and land rates, and maintain the property;
- occupier's liability: this is a liability on the occupier of premises for damage any done to visitors to the premises. This liability is not transferable to the owner or lender;
- liability under the Public Health Act of Kenya (Cap 242): under this Act, owners of buildings or land bear the liability for compliance with environmental obligations; and
- the Environmental Management and Coordination Act (EMCA) (Cap 387): there is a liability on the owner and occupier of a parcel of land to comply with the prescribed environmental quality standards, including proper handling and disposal of waste and dangerous substances, pollution and the use of pesticides and toxic substances.

7 Protection against liability

How can owners protect themselves from liability and what types of insurance can they obtain?

Generally, risk and liability passes to the new owner on the handing over of possession and title of the property from the seller. To ensure that any liability (environmental or otherwise) remains with the seller, buyers usually protect themselves through negotiated warranties in the sale contract, conditions precedent and indemnities from the seller.

Having acquired the property, owners take on insurance to shield themselves from liability. The most common property insurance covers are taken to cover the occupier's liability and against risks of loss or damage by events such as:

- fire;
- storm and tempest;
- earthquake;
- lightning;
- explosion;
- riot and civil commotion;
- malicious damage;
- flood; and
- damage by bursting or overflowing of water pipes and tanks.

8 Choice of law

How is the governing law of a transaction involving properties in two jurisdictions chosen? What are the conflict of laws rules in your jurisdiction? Are contractual choice of law provisions enforceable?

It is trite law that where parties have agreed the terms of contract, including a consensus on the choice of law to the extent that the validity of the contract is not in contest, the courts cannot interfere with the decision of the parties. In case of a dispute regarding the choice of law clause, the dispute resolution authority agreed upon in the contract will interpret the said clause in order to determine the intention of the parties or decide on the most suitable system of law that will apply to the contract.

However, Kenya applies the doctrine that the law governing dealings with immovable property is that of the jurisdiction in which the property is situated. Thus, in a transaction involving properties in

different jurisdictions the laws of the different jurisdictions will apply to each of the properties separately to the extent possible.

9 Jurisdiction

Which courts or other tribunals have subject-matter jurisdiction over real estate disputes? Which parties must be joined to a claim before it can proceed? What is required for out-of-jurisdiction service? Must a party be qualified to do business in your jurisdiction to enforce remedies in your jurisdiction?

The Environment and Land Court and the Magistrate Courts have jurisdiction to hear and determine disputes relating to the environment, land and contracts, choses in action or other instruments conferring any enforceable interests in land. Further, the Rent Restriction Tribunal and the Business Premises Rent Tribunal have the jurisdiction to determine rent payment disputes where the rent payable or term of tenancy is standardised by law.

For a suit to proceed, the persons against whom any right to relief is sought or who will be affected by a claim for relief ought to be joined as parties.

To affect out-of-jurisdiction service, when the subject matter of a suit is immovable property situated outside Kenya and where the relief is sought against a person domiciled or resident outside Kenya, leave from the court must be sought. The process to be served is sealed by the High Court and thereafter served through diplomatic channels.

10 Commercial versus residential property

How do the laws in your jurisdiction regarding real estate ownership, tenancy and financing, or the enforcement of those interests in real estate, differ between commercial and residential properties?

The legal frameworks in Kenya regarding commercial properties and residential properties are fundamentally the same. There are, however, some slight differences in respect of the consents required, taxes, and nature of obligations of parties. These include:

- spousal consent: an estate or interest in matrimonial property may not be alienated without the consent of the spouse; and
- VAT: as noted earlier, VAT is payable on disposal of a commercial property, but not on a residential property.

11 Planning and land use

How does your jurisdiction control or limit development, construction, or use of real estate or protect existing structures? Is there a planning process or zoning regime in place for real estate?

Planning and land use are controlled mainly through the:

- conditions of title;
- Land Act, 2012;
- Physical Planning Act (Cap 286);
- EMCA (Cap 387); and
- Land Control Act (Cap 302).

The National Museums and Heritage Act 2006 deals with identification, protection and conservation of the cultural and natural heritage of Kenya. Under this Act, a building, area or zone can be declared a national monument and be preserved.

Prior to undertaking a development, approval must be sought from the relevant county government, the Physical Planning Authority, the National Construction Authority and the National Environment Management Authority.

12 Government appropriation of real estate

Does your jurisdiction have a legal regime for compulsory purchase or condemnation of real estate? Do owners, tenants and lenders receive compensation for a compulsory appropriation?

There are no laws in Kenya on compulsory condemnation of property. The law, however, allows for compulsory acquisition by the government

for a purpose in the interest of the public, subject to fair and prompt compensation. The process is effected by the National Land Commission, which accords the owner and all persons with legitimate interests an opportunity to present their cases. Once the Commission ascertains the legitimacy of the alleged interests, it proceeds to award evaluated compensation before taking possession of the land in question.

One can dispute the amount awarded and where such dispute arises the Commission is required to place the compensation awarded in a special account, which will earn interest at prevailing bank interest rates, before taking possession of the land when the dispute is resolved.

Publication of the intention to acquire is done through the Kenya Gazette and County Gazette.

13 Forfeiture

Are there any circumstances when real estate can be forfeited to or seized by the government for illegal activities or for any other legal reason without compensation?

Ordinarily, land cannot be seized by government without adequate compensation. The government, however, can reclaim land that was either illegally or procedurally obtained. Additionally, since 2016, the Land Laws (amendment) Act enables the National Land Commission to receive, admit and investigate all historical land injustice complaints and make recommendations for appropriate redress.

The recommendations by the National Land Commission may include:

- restitution;
- compensation;
- orders for revocation; and
- reallocation of land among others, which can lead to land being seized by the government without compensation.

14 Bankruptcy and insolvency

Briefly describe the bankruptcy and insolvency system in your jurisdiction.

Bankruptcy and insolvency of natural persons and incorporated and unincorporated bodies are governed under the Insolvency Act No. 18 of 2015. Of significance, the Act provides for alternatives to bankruptcy procedures by allowing for the redemption of insolvent bodies, incorporated and unincorporated, and natural persons as opposed to their liquidation or declaration of bankruptcy.

The concept of involuntary bankruptcy or insolvency applies where a creditor applies for the winding up of the entity or where the court orders the same.

If the creditor is a holder of execution or other process in respect of debt on a judgment, or an order of court, that execution or process must have been returned wholly or partly unsatisfied.

One of the wins of the Insolvency Act is that it emphasises assisting insolvent natural persons, unincorporated bodies and corporate entities to a redeemable financial position and restore sound financial standing.

Investment Vehicles

15 Investment entities

What legal forms can investment entities take in your jurisdiction? Which entities are not required to pay tax for transactions that pass through them (pass-through entities) and what entities best shield ultimate owners from liability?

Investment entities can take the following forms:

- branch offices;
- real estate investment trusts (REITs);
- general partnerships;
- limited liability partnerships (LLPs); and
- limited liability companies (LLCs).

General partnerships and LLPs are not required to pay taxes and are often considered pass-through entities. To a large extent, REITs can also be considered as pass-through entities because of the tax exemptions currently afforded to them. This, however, may not always be the case.

Regarding liability, REITs, LLCs and LLPs provide for limited liability of the owners, and thus offer the best shielding from liability.

16 Foreign investors

What forms of entity do foreign investors customarily use in your jurisdiction?

The preferred entities of foreigners are LLCs and LLPs, owing to the limited liability on the owners.

17 Organisational formalities

What are the organisational formalities for creating and maintaining the above entities? What requirements does your jurisdiction impose on a foreign entity? Does failure to comply incur monetary or other penalties? What are the tax consequences for a foreign investor in the use of any particular type of entity, and which type is most advantageous?

LLCs

LLCs are created through an online governmental portal. To incorporate, a person logs into the government's e-citizen portal and goes to the office of the Attorney General and Department of Justice tab. An application is made there. The application is a step-by-step procedure that requires certain information to be input as one goes along. The corporation tax for a resident LLC is 30 per cent, and the withholding tax on dividends is 5 per cent for residents and 10 per cent for non-residents.

Branch offices

Like LLCs, branch offices are created through the government online portal. Corporation tax for branch offices is 37.5 per cent. There are no dividend payouts for branch offices. Branch offices are common, but due to the high rate of corporation tax they are only preferred where the branch office is largely a cost centre or very little revenue-earning business is carried out in Kenya.

LLPs

These too are registered through the government online portal. LLPs are not taxed, but the drawings made by the partners are taxed. Where a partner is an individual, they are taxed at the individual tax rate; if companies, they are taxed at the corporate tax rate.

General partnerships

These are registered by way of registration of business name of the government online portal. The tax treatment of general partnership is similar to that of LLPs.

REITs

These are a fairly new investment concept in Kenya, and are formed through an application to the Capital Markets Authority. REITs are exempt from income taxes, except for the payment of withholding tax on interest, income and dividends.

Where an investor has lent money to an entity, the withholding tax on the interest is 15 per cent.

Acquisitions and Leases

18 Ownership and occupancy

Describe the various categories of legal ownership, leasehold or other occupancy interests in real estate customarily used and recognised in your jurisdiction..

Ownership of land in Kenya takes one of two forms:

- freehold tenure: an absolute ownership of an interest in land and subject only to the laws relating to land use; and
- leasehold tenure: an interest in land for a specific period, subject to payment of a fee to the grantor.

Other rights and interests such as head lessor, right of possession and occupancy are recognised under Kenyan laws.

Benefits and burdens on land attach either through being registered against the title or recognised by law as overriding interest.

Registerable interests include:

- charges;
- easements;
- caveats; and
- inhibitions.

Unregistered interests include:

- trusts;
- rights of way, water and profits;
- natural rights to light, air and support;
- charges on unpaid rates, electric supply lines, telephone lines and poles.

Communal ownership of land is also guaranteed and protected. Communal land is registered in favour of the community concerned. Any unregistered communal land is held in trust by the county government on behalf of the community.

There is no differentiation on the lease space for different types of properties (eg, multifamily, retail, industrial and office).

19 Pre-contract

Is it customary in your jurisdiction to execute a form of non-binding agreement before the execution of a binding contract of sale? Will the courts in your jurisdiction enforce a non-binding agreement or will the courts confirm that a non-binding agreement is not a binding contract? Is it customary in your jurisdiction to negotiate and agree on a term sheet rather than a letter of intent? Is it customary to take the property off the market while the negotiation of a contract is ongoing?

Parties to an intended transaction ordinarily execute letters of offer before executing a binding agreement for sale. Whether or not a letter of offer is binding depends largely on the drafting and the content of the document. Courts will interpret them as per the document.

Vendors will ordinarily pull a property out of the market where the purchaser executed the letter of offer. Even in this instance, the letters of offer often limit the timelines within which the prospective purchaser must execute the agreement for sale, failing which the property may be returned to the market. After execution of the agreement for sale, the property is taken off the market.

20 Contract of sale

What are typical provisions in a contract of sale?

A standard contract of sale will contain clauses on the following, among others:

- a description of the parties and the property;
- transaction cost and payment arrangements. (This is usually 10 per cent on execution of the agreement and 90 per cent on completion date. The purchase price is ordinarily held by the vendor's advocates on a stakeholder basis.);
- conditions precedent;
- if the property is sold with vacant possession;
- completion period (typically 60 to 90 days);
- completion documents to be provided by the seller in exchange of money;
- apportionment of prorations, which ordinarily entails the apportionment of land rent and land rates as at the completion date;
- risk allocation clauses. Risk ordinarily transfers to the purchaser on either taking possession or registration of the property in the name of the purchaser (whichever occurs earlier);
- warranties disclosure and limitation of warranties;
- dispute resolution clauses;
- capacity of the parties (when necessary);
- interest rate in respect of default; and
- what happens on breach by either party.

Investigations of genuineness of title done by the purchaser are done at the purchaser's expense, including conducting a search.

Typical warranties and representations in contract for sale of land include the following:

- the vendor has not received a notice of compulsory acquisition or repossession, and does not know of any intention to compulsorily acquire or repossess;
- the use of the property is lawful;
- no building or other structure on the property encroaches on adjoining property;
- each dividing fence and wall is on the boundary of the property;
- the property is not on a buffer zone, road reserve or public land;
- the property is not subject to any actual, pending or threatened litigation or other proceedings;
- the seller is the beneficial owner of the property; and
- the seller is not engaged in any negotiations and has not agreed to transfer, charge or alienate the property to a third party.

21 Environmental clean-up

Who takes responsibility for a future environmental clean-up? Are clauses regarding long-term environmental liability and indemnity that survive the term of a contract common? What are typical general covenants? What remedies do the seller and buyer have for breach?

Environmental obligations and liabilities are borne by the property owner. Clauses relating to environmental liability and indemnity are uncommon.

22 Lease covenants and representation

What are typical representations made by sellers of property regarding existing leases? What are typical covenants made by sellers of property concerning leases between contract date and closing date? Do they cover brokerage agreements and do they survive after property sale is completed? Are estoppel certificates from tenants customarily required as a condition to the obligation of the buyer to close under a contract of sale?

Generally no representations are made to a buyer of a property with a tenant in possession. The seller avails the buyer a copy of the executed lease to acquaint themselves with the provisions. No warranties are given regarding brokerage commission.

Contractually, parties agree how the property will be handed over with vacant possession or with tenants in occupation.

Estoppel certificates are not recognised or required under Kenyan law.

23 Leases and real estate security instruments

Is a lease generally subordinate to a security instrument pursuant to the provisions of the lease? What are the legal consequences of a lease being superior in priority to a security instrument upon foreclosure? Do lenders typically require subordination and non-disturbance agreements from tenants? Are ground (or head) leases treated differently from other commercial leases?

The law provides that interests appearing in the land register shall bear priority in the order of which they were presented for registration. Thus a lease ordinarily ranks above a security instrument if it was first in presentation for registration.

Should a lender exercise the rights of sale of property or other remedies available to them, they do so subject to the rights of the lessee.

It is unusual in practice to require a subordination or a non-disturbance agreement.

24 Delivery of security deposits

What steps are taken to ensure delivery of tenant security deposits to a buyer? How common are security deposits under a lease? Do leases customarily have periodic rent resets or reviews?

Security deposits are very common in leases. In a sale transaction, the contract ordinarily provides for the transfer of the deposit to the new owner. Rent escalations are agreed to contractually in the lease instrument and therefore rent resets and reviews are quite uncommon.

25 Due diligence

What is the typical method of title searches and are they customary? How and to what extent may acquirers protect themselves against bad title? Discuss the priority among the various interests in the estate. Is it customary to obtain government confirmation, a zoning report or legal opinion regarding legal use and occupancy?

Conducting an official search at the lands registry against the title is the bare minimum action taken prior to crystallising any land transactions. The government guarantees title, but the same may be subject to challenge (see question 13).

In addition to conducting a search, buyers protect themselves by requiring the sellers to:

- give certain warranties and indemnities;
- engage a surveyor to confirm the status and location of the premises;
- undertake historical searches on the property by reviewing the correspondence files; and
- seeking information relating to the property from other authorities, such as the county government and the survey offices.

Priority of documents is based on the basis of the first to present for registration at the lands registry. However, parties in the contract may agree to a different priority.

26 Structural and environmental reviews

Is it customary to arrange an engineering or environmental review? What are the typical requirements of such reviews? Is it customary to get representations or an indemnity? Is environmental insurance available?

It is not a practice in Kenya to have engineering or environmental reviews conducted.

27 Review of leases

Do lawyers usually review leases or are they reviewed on the business side? What are the lease issues you point out to your clients?

It is within the purview of lawyers to review leases. In review of leases, lawyer seek to establish the scope of liability of their respective clients. Issues such as use, improvement and maintenance of the property, insurance, consequences of default and yielding up of the property are discussed. Lenders rarely require the subordination of management agreements in security instruments in instances where there are leases registered against the title.

28 Other agreements

What other agreements does a lawyer customarily review?

In addition to reviewing leases, advocates review any headleases, easements, caveats and restrictive agreements noted against the title. They also review licences and approvals, service agreements, valuation reports and zoning reports. Lawyers also ordinarily review the Ndung'u Report and Kenya Gazettes to try and ascertain if the property was possibly illegally acquired.

29 Closing preparations

How does a lawyer customarily prepare for a closing of an acquisition, leasing or financing?

Closing a sale, lease and financing are very different. On the completion date for a sale, a typical list of deliverables contains:

- the original title;
- an executed transfer in respect of the property in favour of the buyer;
- spousal consent (if applicable);
- land rent clearance certificate;
- rates clearance certificate;

- consent to transfer;
- colour passport-size photos of the seller or the seller's directors;
- copies of the seller's personal identification number certificate;
- copies of the seller's identity card, certificate of incorporation or certificate of registration (as applicable); and
- a map of the property.

In respect of financing, the above documents are required, save that a duly executed instrument is required in place of a transfer and the photos are not required.

Following completion, valuation and stamping commences and thereafter registration. This process ordinarily takes between two to five weeks from the completion date.

Land rent and land rates are typically apportioned as at the completion date.

30 Closing formalities

Is the closing of the transfer, leasing or financing done in person with all parties present? Is it necessary for any agency or representative of the government or specially licensed agent to be in attendance to approve or verify and confirm the transaction?

The general practice is that completion should occur at the office of the vendor's advocate. In practice, this does not happen. In any event, either party must execute the instrument in the presence of an advocate or other authorised person who witnesses and confirms that the instrument was freely and voluntarily executed.

31 Contract breach

What are the remedies for breach of a contract to sell or finance real estate?

The standard provision in contracts is that completion should occur in the vendor's advocates' offices. This, however, does not ordinarily happen and parties exchange documents via messengers. In any event either party must execute the instrument in the presence of an advocate, or other authorised person, who then witnesses and certifies that the person executing the instrument was present and that they freely and voluntarily executed the instrument.

32 Breach of lease terms

What remedies are available to tenants and landlords for breach of the terms of the lease? Is there a customary procedure to evict a defaulting tenant and can a tenant claim damages from a landlord? Do general contract or special real estate rules apply? Are the remedies available to landlords different for commercial and residential leases?

As a matter of practice, a lease agreement will generally include the remedies that each party is entitled to in case of any default or breach by the other party. A tenant's remedies are mainly:

- termination of the lease;
- a suit for breach;
- injunctive relief against the landlord to
 - compel the landlord to carry out required repairs;
 - to cease entry of the premises at unreasonable times, or
 - to stop an eviction without notice or a court order.

A landlord may, on the other hand, terminate a lease and enter into possession, which results in an eviction of the tenant. To evict the tenant, the landlord has to apply for an eviction order from a court of law. The landlord may also demand interest, or bring an action for recovery of rent arrears and damages or 'distress for rent' (the latter allows the landlord to seize and sell moveable goods on the leased premises for payment of rent arrears due).

An injunction can also be sought to restrain the lessee from committing any breach or further breach of the lease terms.

Update and trends

Kenyan land laws were enacted in 2012 to consolidate and centralise land registration and ownership regimes. Amendments were made in 2016.

Digitisation of services is also being promoted and now services such as obtaining land rent, land rates statements and acquisition of land rent clearance certificates can be undertaken online. There is a push towards digitising the process of conducting land searches.

Finally, foreigners can no longer own property under freehold tenure, but can do so under a leasehold tenure of up to 99 years.

All title to land that was acquired illegally or irregularly is now subject to revocation by the National Land Commission.

The National Land Commission is reviewing and investigating historical injustices complaints and will make recommendations for redress.

Financing

33 Secured lending

Discuss the types of real estate security instruments available to lenders in your jurisdiction.

The main type of security instrument in Kenya is a legal charge. The charge can either be formal or informal.

A formal charge must be in writing and registered. A chargee shall not be entitled to exercise the remedies in the charge unless it is registered.

An informal charge is created where a charge is in writing but not registered or by deposit of documents evidencing title to the land.

Other types of security instruments available to lenders include a deed of assignment of rental income and an all asset debenture over the assets of the borrower where the borrower is a corporation.

34 Leasehold financing

Is financing available for ground (or head) leases in your jurisdiction? How does the financing differ from financing for land ownership transactions?

Ground lease financing is not ordinarily available in Kenya. The only concept akin to ground lease financing is where a lender gives finances to a borrower to make a development. On disposal, the lender partially discharges the land by discharging each of the units separately.

35 Form of security

What is the method of creating and perfecting a security interest in real estate?

To create a security, the borrower makes an application to the lender for a loan and offers the property as security. The lender then performs due diligence over the property and the borrower.

The lender also undertakes a valuation to determine the value of the property. Once satisfied, the borrower is issued with a letter of offer setting out the terms on which the facility is to be given. A lawyer is then instructed to create a security instrument. In creating the instrument, a lawyer ought to incorporate certain standards provisions under the Land Act.

Perfection of security entails the registration of the security in favour of the lender at the applicable Lands Registry. Prior to booking the security instrument for registration, the instrument must be assessed for stamp duty, stamp duty paid and the document stamped. Additionally, the consent and clearances required in respect of a property disposal as provided in question 28 must be procured beforehand and presented together with the security instrument at registration.

36 Valuation

Are third-party real estate appraisals required by lenders for their underwriting of loans? Must appraisers have specific qualifications?

Third-party real estate valuations and appraisals are required by lenders. Prior to approving a facility, lenders will require the borrower

to contract the services of a land valuer, from a panel of valuers approved by the lender, to conduct the valuation.

Under the Valuers Act (Cap 532) a valuer/appraiser must be:

- a holder of a bachelor's degree or diploma from a recognised university or college;
- registered as a valuer and issued with a certificate of registration;
- a full member of the Institution of Surveyors of Kenya; and
- a member of the Valuers Registration Board.

37 Legal requirements

What would be the ramifications of a lender from another jurisdiction making a loan secured by collateral in your jurisdiction? What is the form of lien documents in your jurisdiction? What other issues would you note for your clients?

Lenders in other jurisdictions ordinarily give loans to borrowers in Kenya. Such lenders do not require any special licences or qualifications. There is however an obligation on the lender to pay withholding tax at the rate of 15 per cent on interest (unless there is a double tax agreement in place).

The taxes payable in recording a security instrument is stamp duty, typically computed at 0.1 per cent of the value of the security. A registration fee of 500 shillings is also payable on booking the instrument for registration.

A transfer of charge can transfer a security instrument, and is exempt from stamp duty. The debt can also be assigned.

38 Loan interest rates

How are interest rates on commercial and high-value property loans commonly set (with reference to Libor, central bank rates, etc)? What rate of interest is legally impermissible in your jurisdiction and what are the consequences if a loan exceeds the legally permissible rate?

The Banking Act (Cap 488) sets the maximum interest rate on loans at 4 per cent above the Central Bank of Kenya's rate. Lender costs are not generally interpreted as interest in computing the total interest payable.

The Act expressly prohibits persons from entering into agreements or arrangements to borrow or lend at an interest rate in excess of that prescribed by law. A financial institution that contravenes the provisions on interest capping commits an offence. On conviction it is liable for a fine or, if in default, the chief executive officer is liable to imprisonment for a term of no less than one year.

The application of the provision on interest capping is restricted to banks and financial institutions licensed under the Banking Act. This effectively excludes foreign banks and financial institutions and other lender in Kenya not licensed under the Banking Act.

When a loan becomes non-performing, the maximum amount that a bank can recover from a debtor is the sum of:

- the principal owing;
- interest as contractually agreed between the debtor and bank, not exceeding the principal owing when the loan became non-performing; and
- expenses incurred in the recovery of any amounts owed by the debtor.

39 Loan default and enforcement

How are remedies against a debtor in default enforced in your jurisdiction? Is one action sufficient to realise all types of collateral? What is the time frame for foreclosure and in what circumstances can a lender bring a foreclosure proceeding? Are there restrictions on the types of legal actions that may be brought by lenders?

The Land Act 2012 and the Land Registration Act 2012 govern enforcement of charges over land. Where a chargor is in default of their obligations to a chargee for more than 30 days, the chargee is required to serve a notice upon the chargor to remedy the default. If the chargor does not remedy the default within 90 days from the date of service, the chargee may:

- sue the borrower for any money due and owing under the charge;
- appoint a receiver of the income of the charged property;

- lease or sub-lease the charged property;
- enter into possession of the charged property; and
- sell the charged property.

There are no hard-and-fast rules regarding the exercise of one remedy at a time or preferring one over the other, but the lender is restricted to the remedies available in law and in the security instrument.

When selling the chargor's property, the lender must serve the charged with a 40-day notice period, in addition to the notice above.

Lenders are encouraged to exercise all other remedies before suing the borrower for monies owed and courts may stay proceedings for recovery of monies until the charger has exhausted all other remedies available to them.

40 Loan deficiency claims

Are lenders entitled to recover a money judgment against the borrower or guarantor for any deficiency between the outstanding loan balance and the amount recovered in the foreclosure? Are there time limits on a lender seeking a deficiency judgment? Are there any limitations on the amount or method of calculation of the deficiency?

A lender is allowed to recover the difference between the sale value (in exercise of the statutory power of sale) and the loan's balance. This may be done by enforcing any guarantees and indemnity agreements, or bringing a claim in court to have the borrower's assets attached to recover the outstanding loan amount.

There are no prescriptions in law detailing the amount and method of calculation of the deficiency.

41 Protection of collateral

What actions can a lender take to protect its collateral until it has possession of the property?

A lender may appoint a receiver of the income of the charged land or lease the charged land, prior to taking possession of the charged land.

A lender may take possession of the charged land. The right is, however, only exercisable through a court order. A chargor in possession has additional obligations as a land owner, including:

- paying the principal the loan, land rent and land rates;
- keeping and repairing the buildings on the property;
- ensuring appropriate insurance is taken;
- using the land in a sustainable manner; and
- performing and complying with the obligations and covenants of the lease, where the interest is leasehold.

42 Recourse

May security documents provide for recourse to all of the assets of the borrower? Is recourse typically limited to the collateral and does that have significance in a bankruptcy or insolvency filing? Is personal recourse to guarantors limited to actions such as bankruptcy filing, sale of the mortgaged or hypothecated property or additional financing encumbering the mortgaged or hypothecated property or ownership interests in the borrower?

Security instruments, such as debentures and other security instruments, provide for recourse to all of the assets of the borrower. Securities such as charges do not, however, provide for recourse by the lender though secondary instruments, such as guarantees, provide for recourse against individuals and entities.

Recourse to guarantors is not limited in any respect.

43 Cash management and reserves

Is it typical to require a cash management system and do lenders typically take reserves? For what purposes are reserves usually required?

Cash management and reserves are not ordinarily required in Kenya.

44 Credit enhancements

What other types of credit enhancements are common? What about forms of guarantee?

Letters of credits and guarantees, including payment guarantees, are common. In the event of default by the borrower, the guarantor reimburses the lender to the extent of the guarantee enforced by the mutual agreement or the same is affected through civil suits.

45 Loan covenants

What covenants are commonly required by the lender in loan documents?

The covenants common in loan documents relating to property include:

- continuing security clauses and further advance covenants;
- a charging clause and an agreement on the amount ultimately recoverable;
- covenants to pay and perform;
- restrictions and further assurance;
- covenants on the use and maintenance of the property;
- the date of redemption covenants;
- negative pledge not to create other interests over the property without the consent of the lender;



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- restrictions on disposal of the asset charged;
- covenants on tacking and consolidation clause;
- clauses on the remedies available to the lender;
- clause on remedies available to the charge; and
- retention of title covenants.

There are no covenants differentiations between free hold and leasehold financing.

46 Financial covenants

What are typical financial covenants required by lenders?

Financial covenants are based on debt-service coverage ratios. Lenders may require further measures in addition to the provision of collateral, including regular appraisals and valuations depending on the borrower.

Corporate bodies are required to perform periodic appraisals, while, for individuals, an appraisal is only required before financing and not after.

Lenders may also require personal or corporate guarantees and indemnities to further secure the facility to be advanced and shield any loss or default by the borrower.

A lender may also require a borrower to take out insurance for the loan facility that will guarantee full recovery of the facility, especially where recovery on default falls short of the required amount or if the borrower is unable to service the loan for certain reasons.

47 Secured moveable (personal) property

What are the requirements for creation and perfection of a security interest in moveable (personal) property? Is a 'control' agreement necessary to perfect a security interest and, if so, what is required?

A security right over moveable property must:

- be in writing and signed by the grantor;
- identify the secured creditor and grantor;
- describe the secured obligation (except in the case of an agreement that provides for the outright transfer of a receivable); and
- describe the collateral.

Notice of the creation of a security right over moveable property must be lodged at the relevant registry. The main requirements are digital registration via an online portal and an agreement in the form of a moveable property security agreement. A control agreement is not required to perfect the security.

48 Single purpose entity (SPE)

Do lenders require that each borrower be an SPE? What are the requirements to create and maintain an SPE? Is there a concept of an independent director of SPEs and, if so, what is the purpose? If the independent director is in place to prevent a bankruptcy or insolvency filing, has the concept been upheld?

Kenyan lenders do not require a borrower to be an SPE.

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