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TOPIC:

**KENYA'S PETROLEUM EXPLORATION AND PRODUCTION LAW: CHALLENGES
FOR INVESTORS, THE GOVERNMENT AND LOCAL COMMUNITIES.**

**SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS OF THE
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BY

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DECLARATION

I, **MUTUMA DENNIS KIBANGA**, do hereby declare this thesis to be my original work and that it has not been submitted elsewhere or is not due for submission for a degree in any other university.

Signature _____

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This dissertation has been submitted with my approval as the University supervisor.

Signature _____

DR. JANE DWASI

DEDICATION

This thesis is dedicated to my dear wife and my entire family for their unceasing love and support.

ACKNOWLEDGEMENT

I thank the God almighty for the care, protection and guidance thus far. I also wish to thank my supervisor Dr. Jane Dwasi for guidance and constructive criticism in writing this thesis. I specially thank my family for support and understanding during my studies. Lastly, I thank all the many people including my classmates, lectures and friends who supported me in the course of my Master of Laws studies. All the errors and omissions are mine.

LIST OF STATUTES

Kenya Law

1. Constitution of Kenya,
2. Foreign Investment Protection Act, Chapter 518, Laws of Kenya.
3. Investment Disputes Convention Act, Chapter 522, Laws of Kenya.
4. Investments Promotion Act, Act No. 6 of 2004, Laws of Kenya
5. Petroleum (Exploration and Production) Act, Chapter 308, Laws of Kenya.
6. Companies Act, Cap 481, Laws of Kenya.
7. Energy Act No. 12 of 2006, Laws of Kenya.
8. Energy Bill, 2012.
9. Mining Act, Cap 306, Laws of Kenya.
10. Mining Bill, 2012.
11. Environmental Management and Co-ordination Act, Act No. , Laws of Kenya.

ABREVIATIONS

BP

British Petroleum

CNOOC	China National Offshore Oil Company
EAC	East African Community
EMCA	Environmental Management and Co-ordination Act
ERC	Energy regulatory Commission
FDI	Foreign Direct Investment
KAM	Kenya Association of Manufacturers
KenInvest	Kenya Investment Authority
KEPSA	Kenya Private Sector Alliance
KNCCI	Kenya National Chamber of Commerce and Industry
KRA	Kenya Revenue Authority
LDCs	Least-Developed Countries
MNEs	Multinational Enterprises
NEMA	National Environment Management Authority
NEP	National Energy Policy of 2004
NOCK	National Oil Corporation of Kenya
PSA	Production Sharing Agreements
SAPs	Structural Adjustment Programmes

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INTRODUCTION

1.1 Background

The study analyzes the legal, policy and institutional challenges in the regulation of oil exploration and production in Kenya. In this regard, it analyses the existing legal, policy and institutional framework for regulating oil exploration and production in Kenya to determine whether it is adequate and effective to protect the social, economic and environmental interests of the local community, the investor and the government, and to make recommendations as necessary, including proposals for legal reform in the sector.

Petroleum is Kenya's major source of commercial energy and is mainly used in the transport, commercial and industrial sectors as well as for domestic purposes. The country imports crude oil for national consumption in monthly installments¹. The government has over the years made efforts to explore and produce oil by entering into production sharing agreements (PSA) with oil companies willing to invest in that sector and to encourage the prospectors to train Kenyans to acquire knowledge in exploration and production.²

The investments in oil exploration and production in Kenya are done by both local and foreign-based companies. However, in most cases, where the oil companies are foreign multinationals, the possibility is that they operate a locally registered subsidiary company for tax benefits purposes. An example is the Tullow Oil Company which has a Kenya branch, namely Tullow (K) Limited.

By and large, oil exploration efforts in Kenya had remained unsuccessful before and after independence. While oil exploration dates as far back as 1954, there had been little to show for the exploration efforts expended over the years. Thus, although some of the wells drilled since 1954 showed traces of oil and gas, much of it did not prove to be commercially viable.³ But the government and the oil exploration investment community did not tire or give up.

¹ The system of obtaining oil in monthly installments is called Open Tender System (OTS) where oil marketing companies bid to import oil at the most competitive prices. See, Caroline Katisya- Njoroge, '*Oil and Gas: The Challenge of Protectionism in Kenya*', <http://www.liverpoollawsociety.org.uk/userfiles/file/Society%20News/Oil%20and%20Gas%20The%20Challenge%20of%20Protectionism%20in%20Kenya.pdf> (Accessed on 17th November, 2011)

² Training Kenyans is a standard clause in Production Sharing Agreements under section 6 of the Petroleum (Exploration and Production) Act, Chapter 308, Laws of Kenya.

³ National Oil Website, "*History of Oil Exploration in Kenya*", <http://nockenya.co.ke/content.asp?ctid=3&title=Upstream+Activities> (accessed on 10/03/2011).

Rather, exploration efforts were intensified in the hope of finding commercially viable deposits.

Exploration for oil in Kenya has been inspired by the understanding that discovery would create many benefits including economic benefits resulting from reduction in oil imports and accruing income from locally produced oil. This would yield further benefits in the way of use of locally available energy resources and reduction in oil import bills. It would also trigger faster development of commercial and manufacturing activities in the country, owing to reduction in energy costs. Additionally, it would result in increased agricultural productivity especially through irrigation. Locally produced oil would also reduce dependency on foreign oil and the economic vulnerability that this arrangement yields as it would be cheaper and more cost effective to maintain national oil reserves.⁴ Additionally, government revenue would increase.

The exploration efforts in Kenya were boosted by the success in the oil exploration efforts in Northern Uganda with the discovery of commercial petroleum resources in 2006. Four oil fields namely Mputa, Waraga, Nzizi and Kingfisher were discovered and a minimum of three hundred (300) million barrels of oil are estimated to be in place in the Kaiso Tonya area, which covers less than 5% of the entire prospective belt. A significant level of investment continues to be made to undertake seismic surveys together with exploration and appraisal drilling in the country, and therefore the country's reserves are expected to increase as further exploration work is undertaken.⁵ The success of Kenya's neighbour Uganda to establish Uganda's oil and gas potential and the finding that the country has commercial reserves of oil in the Northern Region which geographically lie parallel to Northern Kenya led to speculation that the same stream likely flowed into Kenya.

Thus, in recent days oil exploration companies have intensified their exploration for oil and gas in the northern and coastal regions of Kenya which are believed to have oil and gas deposits.⁶ As a result, in the period following discovery of oil in Uganda, Kenya experienced

⁴ Kiremu Magambo, "Renewable Energy Resources Exploitation in Kenya" available at: <http://unfccc.int/ttclear/presentations/Kenya/KM.ppt>. (accessed on 10/09/2010).

⁵ Ministry of Energy and Mineral Development (Uganda), *The National Oil and Gas Policy for Uganda* (Government of Uganda, Kampala, 2008).

⁶ Zeddy Sambu, 'Kenya: Big Companies Scramble for Stake on Oil Exploration' available at <http://allafrica.com/stories/20110110103.html> (accessed on 17/11/11)

her highest levels of investment in oil exploration especially in its North Eastern frontier.⁷ This saw thirteen companies divide the country's north and east, particularly Turkana District, Lamu District and parts of the North Eastern Province and intensify the drilling exploratory wells.⁸ These areas are the Turkana Basin in Turkana County and Lamu Basin in Lamu County. These companies include Dominion Petroleum, BG Group PLC and Tallow Oil PLC, all from the United Kingdom.⁹ Others are Total SA of France, Simba Energy of British Columbia, Anadarko of America and China National Offshore Oil Company (CNOOC).¹⁰

Eventually, the oil exploration efforts in Turkana County paid dividends with discovery of commercially viable oil in the county by Tullow Oil PLC. The oil was discovered following the concerted exploration for oil in Turkana by Tullow Oil Plc. The Ngamia structure is the first prospect to be tested as part of a multi-well drilling campaign in Kenya and Ethiopia and many leads and prospects similar to Ngamia have been identified and following this discovery the outlook for further success has significantly improved. Indeed, Tullow has proposed to the Government an increase in 2D seismic acquisition and the sourcing of an additional rig to increase drilling activities.¹¹

Nevertheless, even as much as exploration for oil has proved successful, it has also posed challenges to the investors, local communities and the government. One of the problems has been resistance by local communities to the exploration exercise. For example, when CNOOC set out to begin exploration in Isiolo in October, 2009, this activity was met with protests by residents of Merti Division, Isiolo District. One of the complaints by the residents was that the company did not consider them for employment.¹² The protests caused the exploration exercise to be launched by satellite from Nairobi.¹³ The fact that protests by residents can potentially hinder the activities of such a venture is a matter of concern. This is

⁷ Alex Taylor, "Kenya starts drilling for oil", available at: <http://www.bushdrums.com/news/index.php?shownews=520> (accessed on 01/03/2011).

⁸ Zeddy Sambu, 'Kenya: Oil Search in Kenya Shifts to top Gear as Gas Deposits found' available at <http://allafrica.com/stories/201005260109.html> (accessed on 17/11/11).

⁹ *Ibid.*

¹⁰ *Ibid.*

¹¹ Booker Ngesa Omole, "Ngamia-1 oil discovery in Kenya Rift Basin", <http://www.kenyaengineer.co.ke/news/2-news/188-ngamia-1-oil-discovery-in-kenya-rift-basin> (accessed on 17/11/11).

¹² Hassan Huka, 'Kenya: Oil Exploration Could Hit Snag as Locals Protest' available at <http://allafrica.com/stories/printable> (accessed on 17/11/11).

¹³ *Ibid.*

a problem caused by lack of clear statutory guideline on how to cater for the social, economic and environmental interests of the local communities concerned. It is prudent to anticipate that such protests can recur. This is, therefore, the ideal time to evaluate and review the law, policy and institutions responsible for exploration and production of petroleum to make recommendations with a view to strengthening the legal, policy and institutional framework in oil exploration and production in Kenya.

1.1.1 International Trade and Investments Aspect of the Study

This study is anchored in international trade and investments law for a number of reasons. In the first place, oil exploration and production sector has been affected by globalization in a number of respects. As a matter of fact, globalization has given rise to a number of industries, changing the overall scenario of the world market. In turn, this has affected the relationship between countries, which creates a huge impact on international trade. Now big companies can import and export products and services without any hassles. This allows them to open several branches at multiple locations all over the world.¹⁴

Oil and gas drilling companies are not an exception. Oil manufacturers and producers have started to obtain mining and drilling rights worldwide. While oil drilling has been into existence for many decades now, the possibility of oil drilling companies operating worldwide has only become possible because of globalization. In any case, earlier internationalization of oil exploration was restricted only to some countries due to the international laws. However, these days many countries have successfully acquired and implemented latest oil drilling and mining facilities. They have shared their knowledge with other oiling giants to make sure that everyone in oil and gas industry is on a single platform.¹⁵

It has also become necessary to critically review the regulatory environment, government policies on energy investments and public private partnerships. This study seeks to achieve this objective by analyzing how the oil exploration and production law, policy, and institutions in Kenya vis-à-vis the interest of the government to achieve optimum regulation, the quest of the investors to safeguard the security of their investments and the need to ensure

¹⁴ Paul Collier and Anthony J. Venables, "International rules for trade in natural resources", This paper appears in the WTO working paper series as commissioned background analysis for the World Trade Report 2010 on "Trade in Natural Resources: Challenges in Global Governance", available at: http://www.wto.org/english/res_e/reser_e/ersd201006_e.pdf (accessed on 12/07/2012).

¹⁵ David L Greene, "The Effects of Globalization on Oil Drilling Operations Worldwide", available at: <http://ezinearticles.com/?The-Effects-of-Globalization-on-Oil-Drilling-Operations-Worldwide&id=6806657> (accessed on 12/07/2012).

the best public interest objectives are captured and upheld especially with respect to the immediate community.

This research, therefore, falls within the international trade and investment law thematic area in that it investigates the scope for the Kenyan law, policy and institutions for oil exploration and production to address market failures in trade in natural resources and the associated international transactions of prospecting and investment in resource exploitation. The underpinning argument is that unless adequate and effective regulation is guaranteed, market failures will occur which may translate into substantial costs. Indeed, the study seeks to make a case, however subtle, for the shift from *ad hoc* approaches in addressing market failures resulting from oil exploration to a more systematic and comprehensive approach in the regulation of trade and development of natural resources in WTO member countries.

1.1.2 Theoretical Framework of the Study

The theoretical framework adopted in the study is the utilitarianism theory. The theory argues that the ability of the law to create ‘the greatest happiness for the greatest number’ is the ideal approach for evaluating law.¹⁶ In this regard, ‘the interest of the community is comprised of the all the interests of the stakeholders who comprise the community.’¹⁷

Essentially, utilitarianism is strongly associated with two historical figures, Jeremy Bentham and John Stuart Mill. While Mill’s views are important, Jeremy Bentham, however, provides a wonderful entrée into the world of utilitarian jurisprudence and philosophy. According to Bentham, the common law was a disorganized body of archaic and dysfunctional rules. Common-law judges irrationally worshiped historical pedigree and had an immoral disregard of the consequences of legal rules.¹⁸

In jurisprudence, the most common and highly appealed to form of utilitarianism is the ‘ideal rule-utilitarianism’. Essentially, ideal-rule utilitarianism stipulates that an action is right if required by a rule which passes the criteria of being an “ideal rule”. Similarly, a rule is an ideal rule if once it is obeyed by all or at least a majority of whom it applies, it will have

¹⁶ J. W Harris, ‘Legal Philosophies’ Second edition (Oxford University Press), page 40.

¹⁷ Ibid, page 41.

¹⁸ Ibid.

better consequences or at least good consequences compared with any other rule governing the same act.¹⁹

The immediate alternative to ideal rule-utilitarianism is act-utilitarianism. This form of utilitarianism applies to the effect that a decision maker considers or views his decision as a single act whose relevant consequences affect only a limited number of persons. For instance, if the decision maker is a judge, in a case involving liability for damages, in determining whether to award damages and how much to award, he or she is expected to have the relevant circumstances of the defendant in question. Clearly, the act-utilitarianism is best suited in private law matters where the number of affected actors are limited. On the other hand, the ideal rule-utilitarianism is more suited to public law issues with many stakeholders involved are diverse and varied and with many considerations involved.

As a result, the ideal rule-utilitarianism is the approach used to analyze whether or not the National Energy Policy (NEP), the Constitution of Kenya, the Environmental Management and Co-ordination Act (EMCA), the Mining Act and the Energy Act and Petroleum (Exploration and Production) Act and the various institutions established under them are adequate and effective for their purpose, which is in broad terms to ensure optimum and sustainable utilization of natural resources, including oil for the benefit of all the parties earlier stated.

The theory of utilitarianism is particularly useful in the light of the fears voiced by the local communities that oil exploration and production may not be of immediate or direct benefit to them.²⁰ In this regard, utilitarianism affords the best tool for evaluating the ability of the law, policy and institutions for regulating oil exploration and production in Kenya by determining which rule or policy would, if applied across board, guarantee the best consequences for the majority of the community members involved. Further, the theory provides criteria that prioritize community interest in comparison with other interests unlike approaches which tend to put the government and investors on the frontline to the detriment of the community, who engender the majority. The community stands to benefit from adequate and effective regulation of the oil exploration and production sector in that it ensures that benefits trickle down to the community and unnecessary economic rents are avoided.

¹⁹ Ibid.

²⁰ Supra, note 11.

The objectives of this study are, firstly, to analyze the legal, policy and institutional framework for regulating the exploration and production of petroleum in Kenya in addressing the challenges facing the key stakeholders in the sector, namely, the government, the investors and the communities. In this regard, the study analyses whether the available law, policies and institutions for exploration and production of petroleum in Kenya are adequate and effective to ensure optimum regulation of the industry, guarantee the security of the investors and safeguard the community interest in oil and natural resources. Finally, the study seeks to make recommendations on the amendment or review of the policies, law and institutions regarding exploration and production of oil in Kenya.

To achieve the objectives stated above, the following questions are considered: Firstly, what are the legal, institutional and policy frameworks for regulating oil exploration and production? Secondly, are the laws, policies and institutions adequate and effective for addressing the challenges facing the government, investors and the relevant community as stakeholders in the oil exploration and production sector? Thirdly, in the light of the foregoing, is there need to reform the policies, laws and institutions regulating petroleum exploration and production in Kenya?

1.2 Statement of the Problem

This thesis investigates whether Kenya's laws governing petroleum exploration and production is capable of adequately and effectively ensuring the government realizes optimum regulation of the oil exploration and production industry in the country. Secondly, it analyses the extent to which the policies, laws and institutions on petroleum exploration and production in Kenya guarantee the security of the investor both commercially and physically to ensure return on investment. Lastly, the study considers how the policies, laws and institutions safeguard the local community's and the general public's interest in sustainable and transparent exploitation of the oil resources in the country. The study is only limited to the adequacy and efficacy of the law and, thus, detailed analysis of incidental matters may be lacking.

1.3 Literature Review

The purpose of literature review is to determine what has been written on the law regulating petroleum exploration and production in relation to the social, economic and environmental

interests of the investors, the local communities and the government in Kenya. This review therefore seeks to establish the extent to which prior studies and research in the area have covered this subject and specifically the findings of the authors about the adequacy of the law in protecting the interests of the parties mentioned above. In order to gain insight into what other writers have said on this subject and to identify the gap to be filled it is intended to review some relevant writings.

The literature reviewed in the study includes UNEP's "*Compendium of Environmental Laws relating to Chemicals and Waste Legislation of Selected Countries of Africa*"¹ which discusses African legal framework on exploitation and production of chemical natural resources including oil. The book concludes that legislation on minerals extraction especially is fragmented and scattered in various pieces of legislation. Bede Nwete in a study titled "*The Challenges and Opportunities of Using Africa's Petroleum and Mineral Resources for Poverty Alleviation*"² argues that although African countries are endowed with oil and petroleum mineral resources, structural deficiencies in the regulatory and economic framework in African countries provide a leeway for corruption and lack of transparency over revenues accruing from these resources. Karanja Kabage's thesis on "*The interface between Foreign Direct Investment and Corruption in Kenya*",³ concludes that no particular attention is paid on the importance of ensuring that investment agreements in Kenya take into account the possible future changes that may work against the investor. Lastly, Wycliffe Nyachoti Otiso thesis '*Examining the Bias in Kenya's Investment Law and Policy in Relation to Foreign Direct Investment and Local Investor*'⁴ argues that there is need for legal and policy reforms on how the government relates with local and foreign investors especially in sectors requiring large capital outlay like petroleum exploration and production. The Kenya Vision 2030 and the Kenya Energy Policy of 2004 both address the need for Kenya to promote cheap sustainable and environmentally friendly sources of energy in general terms.

The gap that emerges from the literature review is that the laws, policies and institutions do not adequately address the social, economic and environmental challenges facing the

¹ United Nations Environment Programme, "Compendium of Environmental Laws relating to Chemicals and Waste Legislation of Selected Countries of Africa" UNEP/Env.Law/2009/2, Nairobi, 2009; available at: <http://www.unep.org/Law/PDF/CompendiumAfricaChemicalsWastesLaws.pdf> (accessed on 20/10/2010).

² Bede Nwete, "The Challenges and Opportunities of Using Africa's Petroleum and Mineral Resources for Poverty Alleviation" A paper presented at International Institute for Justice and Development (IIJD)'s International Conference on the State of Affairs of Africa (ICSAA) October 26th, 27th, and 28th of 2006.

³ Karanja Kabage, "*The interface between Foreign Direct Investment and Corruption in Kenya*"; (University of Nairobi, Unpublished LL.M Thesis, 2005), p. 32.

⁴ Wycliffe Nyachoti Otiso, '*Examining the Bias in Kenya's Investment Law and Policy in Relation to Foreign Direct Investment and Local Investor*', (University of Nairobi, Unpublished LL.M Thesis, 2008).

investor, the local community and the government, respectively, when oil exploration and production is undertaken. It also emerges that the sector has not received adequate research attention aimed at identifying the difficulties and propose recommendations for improvement. The current study which explores issues relating on the adequacy of the legal, policy and institutional framework in addressing the challenges facing the government, investors and local community in regulating petroleum exploration and production in Kenya is, therefore, timely and in order to fill the lacuna.

1.4 Chapter Breakdown

This thesis is presented in five chapters. Chapter one identifies the challenges in petroleum exploration and production. The challenges are stated briefly with reference to the three main players in the industry, namely, the investor, the local community and the state. Each of these stakeholders in oil exploration and production in Kenya, namely, the state, the investor and the local community, has unique challenges. In particular, the three stakeholders coincide with the three challenges, namely, ensuring optimum exploration and production, security for the investor and advancement of community interests which are discussed at length in this study.

Chapter Two discusses the main challenge facing the State in regulating the oil exploration and production sector in Kenya, namely, ensuring optimum exploration and production. Thus, the chapter analyses the oil exploration and production legal, policy and institutional framework in place in Kenya to determine whether the same allows for optimum exploration and production of oil in Kenya. This chapter, therefore, attempts to answer the question whether the existing policy, legal and institutional frameworks adequately and effectively ensures that there is optimum regulation of the oil exploration and production sector in Kenya.

Chapter Three analyses the extent to which the existing legal, policy and institutional framework for oil exploration and production in Kenya guarantees security of the investor. It seeks to highlight the gaps and needs in this important aspect of attracting investment in the sector.

Chapter Four discusses whether the current legal, policy and institutional framework on oil exploration and production is capable of safeguarding the social, economic and environmental welfare of the local community in the area of exploration and production. The

aim is to determine whether the public interest is generally protected through the state in so far as revenue collection and allocation are concerned.

The last chapter contains conclusions and recommendations arrived at the end of the study. It is hoped that the recommendations made will be of use to the policy makers and contribute positively to the development of the law in this area.

CHAPTER ONE

CHALLENGES OF PETROLEUM EXPLORATION AND PRODUCTION IN KENYA

2.1 Introduction

The world over, potential or real ownership of petroleum resources by a state is a big asset for the State and its people. It affords the country great opportunities for economic, technical and social development.¹ In Kenya, the commercial discovery of hydrocarbon resources will have a profound impact on the domestic economy, particularly in addressing the trade imbalance, which the country has continued to experience over the last three decades.² Additionally, Government revenue will increase considerably.

Regulation of exploration and production of petroleum is based on the fact that all the natural resources, including petroleum, existing in their natural state, are vested in the Government. As such, the government is the body responsible for the conduct of petroleum operations in the country including licensing, exploration and production. It has, however, emerged that the management of petroleum resources, especially exploration and production, poses great challenges for the state, investors local communities. These challenges are of technical, political, regulatory, environmental, social and economic character.³ Before outlining the challenges, it is proposed to briefly state the history of petroleum exploration in Kenya.

2.2 History of Petroleum Exploration in Kenya

Petroleum exploration in Kenya began in the 1950s. In 1954, the British Petroleum (BP) and Shell began exploring in Kenya in Lamu where they drilled ten wells. None of the wells were fully evaluated or completed for production despite several indications of oil staining and untested zones with gas shows.¹ By 1981 fourteen wells had been drilled in the sedimentary basins in the coastal region. Although some of these wells showed oil and gas traces, none of them had any commercial deposits. These early petroleum exploration works were

¹ Melvin Yalapan, Legal Nature of the Papua New Guinea Petroleum Arrangement 6 MLJ 117 [2003].

² Kenya National Energy Policy, Sessional Paper No. 4 of 2004, (GOK, Nairobi, 2004), p. 25.

³ A. Suleiman, *The Oil Experience of the Middle East*, 6 *Journal of Energy and Natural Resources Law*, 1, 3(1988).

¹ National Oil Website, "History of Oil Exploration in Kenya", <http://nockenya.co.ke/content.asp?ctid=3&title=Upstream+Activities> (accessed on 10/03/2011). Gas shows refer to mud extracted during drilling that contains gas bubbles. See <http://www.glossary.oilfield.slb.com/Display.cfm?Term=gas%20show> for definition.

undertaken under a royalty based licensing system provided for under the Mining Act, Cap 306.²

In 1975, several consortia acquired acreage in upper part of Lamu Basin led by Texas Pacific Company. In 1976 Chevron and Esso drilled for oil in the southern part of Anza Basin. The tests done in both cases indicated presence of hydrocarbons and microfossils that contaminated the geochemical and cuttings respectively, which gave an indication of some oil deposits. An interest in the offshore portion of the Lamu Basin resulted in the drilling of three deep wells by a consortium of Cities Services, Marathon and Union in 1982.³ In 1982 the Petroleum Exploration and Production Act, Cap 308 was enacted to govern petroleum exploration and improve incentives to companies involved in exploration in Kenya. The period beginning in 1983 saw significant exploration activities with five of the offered blocks taken up by oil companies.⁴ In 1986, the petroleum exploration and production legislation in Kenya was revised to provide further incentives and flexibility to attract increased international exploration interest in the country. In the same year, the Government of Kenya entered into a joint venture exploration programme with Petro-Canada International Assistance Corporation.⁵

A group of companies led by Amoco and Total drilled ten (10) wells, 8 of them in Anza Basin and 2 in Mandera Basin between 1985 and 1990. The wells were dry but with indications of oil and gas. While none of these wells showed commercial reserves, fluorescence and gas shows were reported in Hothori, Endela, and Ndovu wells. Biostratigraphic studies suggest that these wells may not have penetrated deep to the source reservoir, and seal within Sudan rift basins.⁶

In 1991, National Oil initiated an in-house study of the Lamu Basin as part of a long-term strategy to re-evaluate the existing geological, geophysical and geochemical data relating to each of the sedimentary basins in Kenya. The Lamu Basin study was completed in 1995. Based on the above reports Kenya subdivided the Lamu embayment (both onshore and

² Kenya National Energy Policy, Sessional Paper No. 4 of 2004, (GOK, Nairobi, 2004), p. 25.

³ National Oil Website, "History of Oil Exploration in Kenya", <http://nockenya.co.ke/content.asp?ctid=3&title=Upstream+Activities> (accessed on 10/03/2011).

⁴ *Ibid.*

⁵ National Oil Website, "History of Oil Exploration in Kenya", <http://nockenya.co.ke/content.asp?ctid=3&title=Upstream+Activities> (accessed on 10/03/2011).

⁶ *Ibid.*

offshore) into ten (10) exploration blocks, each with a specific exploration play. Two (2) more exploration blocks have been created since the year 2001.⁷

However, the period between 1993 and 1999 registered low exploration activities mainly due to depressed international crude oil prices which made it unattractive for prospecting companies to venture into areas perceived to be marginal. Thus, most of the exploration activities undertaken during this period largely consisted of collection and analysis of primary data by National Oil Corporation of Kenya (NOCK).⁸ Promotion efforts generated new interests in the offshore Lamu Basin, and resulted in the signing of seven (7) Production Sharing Contracts between 2000 and 2002. In August 2000 the Corporation commissioned the Tertiary Rift Study, which was completed in March 2001. Tertiary rift study led to quantification of potential source and reservoir rock units in the study area as well as the petroleum system at play in the sub-basins.⁹

National Oil has a Data Centre for storage of seismic data, well logs, well reports, other oil exploration reports and aeromagnetic as well as gravity data which has been obtained in this country to date through petroleum exploration activities. In addition, National Oil has set up cores and drill cuttings storage facility in which the rock samples retrieved during petroleum exploration in this country from 1960 to date are stored for use by those carrying out exploration.¹⁰

On 26 March 2012, Tullow Oil discovered that Ngamia-1 had encountered in excess of 20 metres of net oil pay. This was the first time Kenya discovered commercially viable oil in the country. The well has now been deepened from 1,041 metres to 1,515 metres. Oil samples with an API greater than 30 degrees have been recovered to surface from the newly drilled section with similar properties to the light waxy crude encountered in the upper reservoir zone. Experts have hailed the discovery thus:

“The net pay encountered so far in Ngamia-1 is more than double that encountered in any of our East African exploration wells to date. We...look forward to the drilling and evaluation of the deeper potential of this well and the acceleration of our seismic and drilling campaigns in the region.”¹¹

⁷ National Oil Website, “History of Oil Exploration in Kenya”, <http://nockkenya.co.ke/content.asp?ctid=3&title=Upstream+Activities> (accessed on 10/03/2011).

⁸ *Ibid.*

⁹ *Supra*, note 26

¹⁰ *Supra*, note 26.

2.3 Challenges in petroleum exploration

Each of the key players in oil exploration and production, that is the state, the investor and the local community, has unique challenges. One of the challenges facing the state is to maintain control of the resource to ensure optimum exploration and production. The risk of over exploitation is a key consideration. Without proper control, the investor could produce more oil than is favourable to the long term existence of the resource and its preservation for the benefit of future generations. It is the state's responsibility to ensure sustainable exploitation of oil¹. The other challenge is the ability of the state to ensure that it remains the lawful owner of the resource in accordance with its sovereign powers. In this regard, the government should retain the right to terminate the exploration and production at any time if it appears that its sovereign right to the natural resource is being endangered, for example, by an investors claim to the resource permanently. The government is interested in safeguarding the best interest of its citizens especially with respect to the right to property and the environmental right to clean, safe and healthy environment. In most cases, therefore, this interest is safeguarded by outlining the minimum terms and conditions for petroleum exploration and production.² Also of concern to the state is the question of how much revenue it could generate make from the resource. Another critical challenge to the state is the government's ability to explore and produce petroleum products by itself³. The state and local investors do not seem to possess the technical capability to undertake this exercise.

As stated in the introduction to this work, foreign companies have in recent years intensified their exploration for oil and gas in the northern and coastal regions of Kenya which are believed to have oil and gas deposits. As a result, Kenya has experienced one of the highest levels of investment in oil exploration. The intention of an investor is to make profits. It follows therefore that the commercial, social and political environment in which an investor is operating must be conducive to good business. A primary challenge facing an investor in oil exploration and production is whether there is sufficient social, political and commercial

¹¹ Ben Harrington, "Tullow Oil shares rise on Kenya oil find", available at: <http://www.telegraph.co.uk/finance/newsbysector/energy/oilandgas/9251434/Tullow-Oil-shares-rise-on-Kenya-oil-find.html> (accessed on 10/03/2012).

¹ Article 69 (1)(a) of the Constitution of Kenya makes it the state's responsibility to ensure sustainable exploitation of natural resources.

² Energy Regulatory Commission Website, "Energy Sub-sector: Petroleum", http://www.erc.go.ke/erc/energy_sub_sectors/?ContentID=2#(accessed on 10/03/2012).

³ The contents of the Petroleum (Exploration and Production) Act generally reflect the state's inability to undertake this exercise by itself.

security⁴ to their investment. An investor cannot put up business in an environment where the law does not ensure the investor's security against an uprising by the local community or arbitrary (or unpredictable) government decisions negatively affecting the investment. It was probably in recognition of these difficulties that when, in June, 2011 two companies, Tullow Oil and Africa Oil, started exploration in the Kerio Valley Basin, the local District Commissioner assured the residents of employment and environmental safety by the companies.⁵

Given that past explorations in Kenya have not yield fruits, most foreign investors seeking to invest in exploration of oil in Kenya sought incentives to ensure that they do not incur undue loss in case of failure to discover viable oil reserves.⁶ The way the state handles these challenges is decisive for the ability of a State to attain sustainable development of the petroleum resources and adequately address the interests of the foreign investors, the local communities and the government.⁷

Regarding local communities, it is their concern to seek to make the most of the exploration opportunity by agitating for preferential access to employment and training opportunities availed by the oil-exploration companies, minimal disruption to the cultural and communal way of life, access to their environmental right to clean, healthy and safe environment and public participation in the decision to explore and produce oil within the community's area of occupation.⁸

The issues arising from the challenges outlined above are, firstly, whether the law relating to oil exploration and production ensures the social, political and commercial security of the investor in so far as the actual exploration and production of oil is concerned. Secondly, whether the law adequately safeguards the social, economic and environmental welfare of the local community in the area of exploration and production. Thirdly, whether the public interest are generally protected through the state in so far as revenue collection and allocation⁹ are concerned. Lastly, whether the state's interest in maintaining sovereignty over the natural resource is upheld.

⁴ The word security as applied here is intended to mean the security of the investment from interference by the local community or even the government itself in a manner making it difficult for the investor to continue with the operations.

⁵ 'Oil Firms Set to Drill Oil in Turkana', *Daily Nation*, 30th June, 2011, page 16.

⁶ *Supra*, note 32.

⁷ 'Oil Firms Set to Drill Oil in Turkana', *Daily Nation*, 30th June, 2011, page 16.

⁸ *Ibid*.

⁹ Article 69(1)(a) of the Constitution requires the state to share the accruing benefits equitably.

2.4 Conclusion

The next three chapters will analyze the existing policy, legal and institutional framework in petroleum exploration and production in Kenya to find out whether and to what extent they offer protection to the three players. In particular, whether and how the laws, policies and institutions address the challenges of each of the stakeholder will be discussed in the following chapters.

Noteworthy, each of the stakeholders in oil exploration and production in Kenya, namely, the state, the investor and the local community, has unique challenges. Each of the three stakeholders coincide with three challenges, namely, ensuring optimum exploration and production, security for the investor and advancement of community interests which are discussed in the next part of the study.

CHAPTER TWO

FRAMEWORK FOR ENSURING OPTIMUM EXPLORATION AND PRODUCTION OF OIL IN KENYA

3.1 Introduction

As already noted, the key challenge for the state is how to ensure optimum exploration and production of the oil resources while maintaining commercial incentive for the investors. This is brought to bear on the risk of over exploitation and environmental management and sustainability issues. Without proper control, the investor could produce more oil than is favourable to the long term existence of the resource and its preservation for the benefit of future generations. Under the Constitution, one of the state's responsibilities is to ensure sustainable exploitation of oil as a natural resource.¹

In most countries, petroleum exploration and production is envisaged to be undertaken under a legal regime that fixes in advance, conditions under which rights to explore for and produce petroleum are granted. Such legal regime is set out in the legislation which outlines the terms and conditions of the respective petroleum agreements entered into in respect of each exploration licence.² Other countries do not use the legislation to set out the terms and conditions of petroleum development. In such a country, if there be a petroleum exploration and production law, it is of a general nature. For example, in Indonesia the government grants exploration and production titles on the basis of individually negotiated agreements.³ Other countries take the middle ground by using a hybrid system of fixing the terms of petroleum exploration and production, partly by legislation and partly by agreements.⁴

Petroleum agreements are used in many countries as the main policy instruments, to set the scope of, and govern, petroleum exploration and production. These agreements are used exclusively or in association with petroleum legislation.⁵

¹ Article 69 (1)(a) of the Constitution of Kenya makes it the state's responsibility to ensure sustainable exploitation of natural resources.

² Countries with such regime include Australia, United States, Canada and most of the EEC countries. Kamal Hassain, *Law and Policy in Petroleum Development*, (1979) France Printer (Publishers) Ltd, London, 100.

³ *Ibid*, 101. Indonesia and Bangladesh are examples of such countries.

⁴ *Ibid*, 101 and 102. Norway, New Zealand, Britain, Trinidad and Tobago are examples of countries that have a hybrid petroleum regime.

⁵ Melvin Yalapan, "The Legal Nature of the Papua New Guinea Petroleum Agreement" available at : <http://www.paclii.org/journals/MLJ/2003/6.html> (accessed on 10/06/2012).

This chapter discusses the legal, policy and institutional framework in place in Kenya analysing whether the same allows for optimum exploration and production of oil in Kenya. In this regard, optimum exploration and production is understood as such exploitation of oil resources that has regard for environmental concerns and sustainability and serves to yield maximum economic benefit to the country. The various legal, policy and organizational instruments in place in the country will therefore be analysed to discern whether or not they guarantee for optimal oil exploration and production in Kenya or they deserve to be overhauled or amended or re-oriented.

3.2 The Constitution and Optimum Exploration and Production of Oil in Kenya

The Constitution in the preamble underlines the need to use our natural resources and the environment sustainably for the benefit of future generations.¹ Further, the constitution vests sovereign power directly in the hands of the people of Kenya and it is to be exercised in accordance with the Constitution.² This is relevant to optimum petroleum exploration and exploration because it falls under the purview of permanent sovereignty which has hitherto been vested and exercised by the executive arm of the government. The implication is that any future petroleum exploration and extraction contracts must be in the interest of the people of Kenya or otherwise be unconstitutional and therefore null and void.

Further, the Constitution provides for environmental right to the effect that every person has the right to a clean and healthy environment. This right includes the right to have the environment protected for the benefit of present and future generations through legislative and other measures and to have obligations relating to the environment fulfilled.³ The Government is also enjoined to ensure sustainable exploitation, utilization, management and conservation of the environment and natural resources, and ensure the equitable sharing of the accruing benefits.⁴ In connection with this, the government's responsibility is, inter alia, to ensure that the oil exploration investors comply with environmental impact assessment requires and adhere to the environment management laws and regulations.

¹ Preamble to the Constitution of Kenya.

² Section 1(1) of the Constitution of Kenya.

³ Article 42 of the Constitution.

⁴ Article 69 of the Constitution.

3.3 Energy Policy Framework and Optimal Oil Exploration and Production

The relevant policy framework for petroleum exploration is the National Energy Policy of 2004 (NEP) which has a number of broad objectives relevant to optimal exploration and production of oil in Kenya. These include ensuring the adequacy, reliability, cost effectiveness and affordability of energy to meet development needs, while protecting and conserving the environment. These objectives are to be achieved by enhancing access to affordable energy services, promote development of indigenous energy resources and promote energy efficiency and conservation as well as prudent environmental, health and safety practices.¹ The NEP also requires enhancing explorations for oil through subdivision of exploration acreage into smaller blocks and collection of additional geological agrochemical and geophysical data to attract more oil prospecting companies.²

Further, at the overall level, the National Energy Policy adopts key approaches which are critical for enhancing optimal oil exploration in the country. These include: increasing transparency and room for debate; increasing consultation in policy formulation; encouraging participation through parliamentary committees; creation of local ownership and commitment to policy and budgetary process; and strengthening the voices of different stakeholders. Other significant benefits that resulted from the NEP included the enactment of the Energy Act while by involving greater political commitment and legal backing for planning process and public participation. Nevertheless, analysts have pointed some gaps which need to be filled in the NEP and have proposed, inter alia, the development and adoption of policies that address harmful economic, social and environmental impacts. Such policies may include targeted income subsidies to the poor or marginalized, and micro-enterprises (SMEs), and differential taxation to encourage or discourage certain oil exploration and production practices. The research community can also assist by identifying and developing innovative and cost effective methods of assessment and research into appropriate oil exploration and production technologies. In addition, private sector organizations such as KAM and non-governmental organizations (NGOs) can also spearhead sustainable development, energy conservation and efficiency and transparency and accountability.³

¹ Sesssional Paper No. 4 on Energy, 2004, page 4. This document contains Kenya's national energy policy.

² *Ibid.*

³ Kenya: Integrated assessment of the Energy Policy (UNEP, Nairobi, 2006) p. viii.

The Kenya Vision 2030 (Vision 2030) also makes policy pronouncements on energy which are relevant to oil exploration and production. It is clear that the development projects recommended under Vision 2030 and overall economic growth will increase demand on Kenya's energy supply. Currently, Kenya's energy costs are higher than those of her competitors and, therefore, the country has to generate more energy and increase efficiency in energy consumption. Vision 2030 envisages continued institutional reforms in the energy sector, including a strong regulatory framework and private generators of power.⁴

Given the recognition of energy as an infrastructural enabler of the three "pillars" of Vision 2030,⁵ proposals are made to meet the energy needs although focus is on petroleum and electricity as the prime movers of the modern sector of the economy.⁶ However, Vision 2030 does not give special attention to the need to ensure optimum oil exploration and production and only mentions this sector in passing. The blueprint moots the inauguration of an 'exploration initiative' to undertake an accurate and detailed geological mapping of the country to provide information that may lead to the discovery of new natural minerals of commercial value.⁷ This initiative entails intensifying ongoing exploration for minerals and crude oil in the country and has since borne fruits for the country with discovery of commercial oil deposits in Turkana.

In this regard, the Vision 2030 is deficient in that it gives no particular attention to oil exploration and production and does not particularly address itself to oil production in the country. The reforms it envisages in the energy sector are not expressly stated to affect the exploration or production of oil. Therefore, it suffices to say that Vision 2030 as a policy document does not adequately address the interests of the key players in oil exploration and production and in particular does not cater for the interest of the government to ensure optimum exploration and production of oil in Kenya. This is attributable to the fact that the current oil find was not anticipated at the time of coming up with Vision 2030 after hitherto oil exploration activities had not borne fruits. Further, much of the policy-making efforts seem to be focused on oil exploration to the detriment of oil production.

⁴ Republic of Kenya, *Kenya Vision 2030* (Government Printer, Nairobi, 2007) p. viii.

⁵ The three pillars are social, economic and political.

⁶ Ibid.

⁷ Ibid., p. 132.

With respect to the energy policy framework, the key weakness is that having been executed at the time when oil had not been discovered in Kenya, it is focused on attracting investors. Thus, the NEP notes the perception of Kenya's marginality as a potential of hydro carbons which has meant the country has attracted only a limited number of oil exploration companies. The strategy for success in attracting oil exploration companies is anchored on ensuring flexibility of the production-sharing model contract embedded in the Petroleum (Exploration and Production) Act. This has meant that every term in the model contract is negotiable including sharing of cost oil, profit oil, surface fee, training levy and Government participation.⁸

However, while this flexibility approach has suited the country in the effort to attract oil explorers in the country, it is not sustainable in the long term. It means that oil exploration and production investors are likely to have a field day at the expense of the government especially the former has stronger bargaining power. There is need to review the model contract to provide for more legal certainty as well as guarantee optimum exploration of the oil resources in country.⁹

3.4 The Environmental Management and Co-ordination Act

The Environmental Management and Coordination Act¹ (EMCA) address environmental matters relevant to sustainable oil exploration and production in Kenya by making provisions relevant to regulation of environmental issues arising during exploration and extraction of petroleum in Kenya. In the first place, the Act establishes national environmental principles to provide guidance and coherence to good environmental management.² The Act also makes provisions dealing with issues that cut across all sectors of environmental protection and management including environmental policy, environmental planning, protection and conservation of the environment.³

Further, EMCA provides for the duty to safeguard and enhance the environment.⁴ In other words, every person entitled to enjoy the right to a clean and healthy environment has a duty to protect the environment and promote sustainable development. This, in essence, is

⁸ Supra, note 12.

⁹ *Ibid.*

¹ The Environmental Management and Coordination Act (EMCA), Act No. 8 of 1999

² *Ibid.*, Section 3.

³ *Ibid.*

⁴ *Ibid.*, section 3(1)

important in that it binds the government and foreign investors seeking to explore or produce petroleum in Kenya to protect the environment. The Act compels the government to ensure that all natural resource exploitation agreements it enters into safeguard and protect the environment of Kenya.

3.5 Petroleum (Exploration and Production) Act and Optimum Oil Exploration and Production

The Petroleum (Exploration and Production) Act is the primary statute governing the legal relationship between the investor and the government on matters touching on oil exploration and production in Kenya. The Act, adopted in 1984, regulates the negotiation and conclusion by the government of petroleum agreements relating to exploration for, development, production and transportation of petroleum.¹

The Act defines "petroleum" to mean mineral oil including crude oil, natural gas and hydrocarbons. Petroleum operations are defined as all or any of the operations related to the exploration for, development, extraction, production, separation and treatment, storage, transportation and sale or disposal of, petroleum up to the point of export, or the agreed delivery point in Kenya or the point of entry into a refinery. The Act regulates all aspects of petroleum operations with exception of petroleum refining operations.²

Importantly for optimum exploration and production, the Act vests all petroleum existing in natural condition in strata lying within Kenya and the continental shelf in the Government. This is subject to any rights under any written law which have been or are granted or recognized as being vested, in any other person.³ This provision acknowledges the permanent sovereignty of the Government of Kenya over its natural petroleum resources.⁴ The implication is that the Government enjoys unfettered powers of management and control of petroleum development. It also implies that the entire bundle of rights that govern petroleum

¹ See Preamble to the Act.

² Section 2 of the Petroleum (Exploration and Production) Act.

³ *Ibid.*, section 3.

⁴ The doctrine of permanent sovereignty over natural resources became popular in the 1950s with increased concerns of governments with regard to ownership and control of the natural resources within the states' territories under the International Law. As a result, the 1962 *UN Resolution on the Permanent Sovereignty over Natural Resources* was passed to reflect the assertion of sovereignty, particularly by the newly independent third world governments, to natural resources within their territories.

development vests in the government which is entitled to contract them to the oil companies upon good bargain.⁵

To ensure optimum exploration, the Act requires the Government to ensure oil exploration and production investor it contracts has the financial ability, technical competence and professional skills necessary to fulfil their obligations under the petroleum agreement.⁶ The Act in section 9 sets out implied terms to apply to every petroleum exploration and production agreement in Kenya. The Government is also enjoined to ensure the contractor adequately compensates for any private land appropriated for oil exploration and production.⁷

3.6 Institutional Framework for Petroleum Exploration and Production in Kenya

In order to achieve optimum petroleum exploration and production of oil, there must be in place requisite institutional framework to oversee the implementation and enforcement of the policy and legal frameworks respectively. In a word, neither the law nor policy can succeed in achieving optimum petroleum exploration and production of oil without strong and capable institutions.

The institutions tasked with regulation of oil exploration and production in Kenya are mainly players in the energy sector and environment management and conservation. These include the Ministry of Energy, National Environment Management Authority Provincial Administration and Local Authorities. The role of the provincial administration and local authorities will soon be taken over by devolved governments of the respective counties where oil resources are situated. The main institutions under the Ministry of Energy in Kenya whose role is relevant to oil exploration and production are National Oil Corporation of Kenya and Energy Regulatory Commission (ERC).

3.6.1 National Oil Corporation of Kenya

Although the initial role of National Oil was to coordinate oil exploration (upstream) activities, since 1988 it has focused more on downstream activities involving importing crude oil, into the country.¹ At first, the company was mandated to supply 30% of the country's

⁵ Petroleum (Exploration and Production) Act, section 3.

⁶ *Ibid*, section 8.

⁷ Petroleum (Exploration and Production) Act, section 10

¹ National Oil Website, "Upstream Activities", <http://nockenya.co.ke/content.asp?ctid=3 &title=Upstream+Activities>(accessed on 10/03/2011).

crude oil requirements to be sold to oil marketing companies for refining and onward sale to consumers. After de-regulation of the oil industry in 1994, the company lost that mandate, and had to formulate new survival strategies that saw its entry into downstream operations.²

Nevertheless, National Oil Company still has an important role to play with respect to petroleum exploration and production which includes spearheading of petroleum exploration on behalf of the Kenya government. Specifically, the role of National Oil in petroleum exploration includes:

- a) Overseeing the fulfilment of petroleum exploration companies' obligations in accordance with contracts signed with the Kenya Government.
- b) Providing and disseminating exploration data from various exploration activities in form of reports and promoting the same to oil companies in order to attract them to do exploration in Kenya.
- c) Undertaking various exploration works in various basins in accordance with available capital outlay, technical expertise and equipment available. Due to limitations of risk capital from government, to date some exploration activities such as exploration drilling have been left mostly to international oil companies.
- d) To manage on behalf of the government storage and disposal of government's share of oil after discovery.³

The key limitation is that National Oil lacks the capacity having focused its resources mainly on downstream petroleum services. This has mainly been as a result of the fact that no commercial discovery has been made to date despite the numerous exploratory activities that have been carried. Indeed, the strategy of National Oil now appears more focused on its being the premiere regional energy company in Africa in providing a full range of downstream services. The management of National Oil merely sees its role in petroleum exploration and production as merely supporting active exploration program in Kenya. For instance, in the period ending 2013, National Oil's strategic plan is, inter alia, to achieve market leadership in commercial operations in Kenya.⁴ Noteworthy, National Oil initiated active exploration⁵ which has borne fruits with the oil finds in Turkana but much remains to be done in terms of

² *Ibid.*

³ Memorandum and Articles of Association, National Oil Corporation of Kenya Limited.

⁴ National Oil Website, "Strategic Intent, National Oil Corporation of Kenya", <http://nockenya.co.ke/content.asp?ctid=3&title=Upstream+Activities> (accessed on 10/03/2011).

⁵ *Ibid.*

building the institution's capacity to manage and oversee optimal oil exploration and production in the country.⁶

3.6.2 Energy Regulatory Commission

The Session Paper No. 4 of 2004 on Energy recommended review of the Petroleum Act Cap 116 and other energy sector statutes culminating in the introduction of a new energy sector legislation to cover petroleum, electricity and renewable energy, namely, the Energy Act No. 12 of 2006.¹ The policy paper also recommended a single energy sector regulator to regulate electricity, downstream petroleum, renewable energy and other forms of energy. The Act transformed the Electricity Regulatory Board to the Energy Regulatory Commission (ERC) to regulate petroleum and renewable energy sectors in addition to electricity.²

The functions of ERC include regulating the importation, exportation, transportation, refining, storage and sale of petroleum and petroleum products. The ERC is, thus, relevant only with respect to petroleum exploration and production for the purposes licensing of petroleum import, export, transport, storage, refining and sale. These functions are relevant where exploration is successful and the need for production of the locally produced petroleum arises. ERC's petroleum department deals with matters touching on production and regulation of petroleum in Kenya. The functions of the Petroleum Department include:

- a) Review of government policy on petroleum;
- b) Governing the petroleum sector with focus on licensing, issuing of construction permits, developing standards for bulk petroleum transportation and petroleum costs and prices monitoring;
- c) Take the lead in the formulation, review and enforcement of rules, regulations and codes for the petroleum sector.³

⁶ [Mwakilishi](http://www.mwakilishi.com/content/articles/2012/03/26/oil-discovered-in-kenya%E2%80%99s-turkana-county.html), "Oil Discovered in Kenya's Turkana County", <http://www.mwakilishi.com/content/articles/2012/03/26/oil-discovered-in-kenya%E2%80%99s-turkana-county.html> (accessed on 10/06/2012).

¹ Kenya National Energy Policy, Sessional Paper No. 4 of 2004, (GOK, Nairobi, 2004), p. 10.

² Section 4 of the Energy Act, Act No. 12 of 2006.

³ Energy Regulatory Commission Website, "Energy Sub-sector: Petroleum", http://www.erc.go.ke/erc/energy_sub_sectors/?ContentID=2#(accessed on 10/03/2011).

Section 102 empowers the Minister to make regulations upon recommendation by the Commission on petroleum related activities including importation, exportation, and landing, open tender systems for importation, minimum operational stocks, and determination of retail prices for petroleum products among others. Regulations which were developed under the repealed Petroleum Act Cap 116 are deemed to be in force until repealed or revoked under the provisions of the Energy Act No. 12 of 2006.

As far as optimum petroleum exploration and production is concerned, there is no single dedicated institution with a clear mandate to oversee the interests of the government. National Oil Corporation, the body with the mandate has to a large extent abandoned its mandate to deal with exploration and production, leaving the parent ministry to deal with the matter directly. There is need for institutional reform to build the capacity of the body to bargain for best terms with oil investors and also enforce the terms conditions entered thereof to guarantee optimum exploration and production of oil in Kenya.

3.7 Conclusion

It emerges from the analysis made above that the legal and the policy and institutional frameworks are not adequate to ensure optimum exploration and production of oil in Kenya. Save for the fundamental principles on the management of natural resources by the state under article 69 to 72 of the Constitution, the examined statutes have no provisions specifically targeting the interests of the concerned parties. It is important to note, however, that EMCA contains comprehensive provisions on safeguarding the environment. It may be argued that local communities have their environmental concerns well addressed by EMCA.

As noted in the introduction and the previous chapter, environment is not the only legal concern of local communities. Issues of employment in priority and general community welfare also arise. The Petroleum (Exploration and Production) Act is the statute specifically dealing with exploration and production of oil. This statute, however, does not address these concerns. Regarding employment, the act only states that the investor has an obligation to ‘give preference to the employment of and training of Kenyan nationals in petroleum operations’.¹ It is worth noting that the act does not give any special preference to local communities in terms of employment. This leaves it open for the investor to employ Kenyans from other parts of the country and could in fact, employ no locals. The current state of this

¹ Section 9(1)(g) of the act.

law does not help in resolving one major challenge to petroleum exploration and production, that is, ensuring employment for local communities.

Besides employment, the act does not make it obligatory to provide any other benefits to the local communities. While the constitution requires equitable sharing of the accruing benefits², the Petroleum (Exploration and Production) Act does not state whether there would be any benefits directly accruing to the local community. This act appears to have been enacted only to ‘regulate the negotiation and conclusion by the Government of petroleum agreements relating to the exploration...’³

Policy cannot address the issues raised in this thesis in the absence of supporting legal framework to balance the social, environmental and commercial interests of the local community, the investor and the government as the case may be. The institutional framework is also imbalanced because too many powers are vested in the Minister for Energy who is merely a political appointee. The Energy Regulatory Commission has no role in regulation of exploration of petroleum in Kenya and the National Oil Corporation plays a mere supportive role and has since shifted to downstream petroleum projects. Furthermore, no institution seems to be specifically mandated with the responsibility of addressing the issues raised in this thesis.

² Article 69(1)(a)

³ See preamble to the act.

CHAPTER THREE

FRAMEWORK FOR GUARANTEEING SECURITY OF THE INVESTOR

4.1 Introduction

This chapter analyses the extent to which the existing legal, policy and institutional framework for oil exploration and production in Kenya offers security to the three players, including the investor. This chapter seeks to highlight the gaps and needs in protecting the investor in order to attract investment in the sector. On the one hand, the discussion will highlight the key legal, policy and institutional documents and how they address the security of investors in the oil exploration and production in Kenya. On the other hand, the chapter will analyze the state of rule of law in the country and how it enhances or undermines the security of investors in oil exploration and production sector in Kenya.

In order to ensure the security of the investor, the legal, policy and institutional framework for oil exploration has to capture the economic rent attributable to petroleum as well as exhibit the attributes of a strong legal system capable of safeguarding and upholding private property rights. In other words, in addition to the relevant petroleum exploration and production laws, there should be in place an independent judiciary, separation of powers and strict observance of the rule of law to guarantee unfettered enforcement of the rights of the investors if need arise. The licensing framework in place should also accommodate the requisite legal certainty to ensure that the investors are guaranteed the security of their investments given the capital intensive nature of petroleum exploration and production ventures.¹

4.2 Role of the Government and Security of Investors in Oil Exploration and Production

One of the key approaches in guaranteeing the security and interest of the investor is to ensure minimalist government role in petroleum resource development and exploitation. In this case, the focus of the government should be on attracting investors to the petroleum sector.¹ Once the investors are on the ground, the role of the government shifts to promotion

¹ Tina Hunter, "The Legal Regulatory Resources for the Sustainable Extraction of Australian Petroleum Offshore Resources: A Critical Functional Analysis", available at: http://epublications.bond.edu.au/cgi/viewcontent.cgi?article=1353&context=law_pubs&sei-redir=1&referer (accessed on 10/06/2012).

¹ *Ibid.*

of efficient and competitive petroleum exploration and production industry and safeguarding community interest.² Overall, the government's interest should be to maximize the contribution of the petroleum industry in advancing its economic goals while staying out of the way of the investors to realize sustainable return on investment.³

The current petroleum exploration and production law and policy in Kenya focuses on the attraction of investments into the petroleum exploration industry.⁴ However, the government still exercises more than minimalist role in that it is intimately involved in the process of oil exploration and production. The Petroleum Exploration and Production sector is tightly held and controlled by the Ministry of Energy on behalf of the Government of Kenya. The Government also has a commercial interest in the sector through the National Oil Corporation of Kenya (NOCK) which liaises with international oil exploration investors interested in participating in the oil and gas exploration in Kenya. The conditions for exploration of petroleum states that the Government may elect to participate in any development area and the percentage of participating interest is negotiable. The Ministry of Energy and the NOCK also represent the government in negotiations with companies intending to explore oil in Kenya.⁵

National Oil Corporation of Kenya Limited is a company incorporated under the Companies Act (Cap 486) whose main objective with respect to petroleum exploration in Kenya is to coordinate oil exploration (upstream) activities. From 1984, when National Oil became operational, one of the major activities has been the spearheading of petroleum exploration on behalf of the Kenya government. There has been no commercial discovery to date, but the company has accumulated a lot of data showing positive prospects.⁶

Thus, in the interest of security of the investor, there is need to adopt a policy for government participation in petroleum exploration that reflects complete liberalization of the petroleum sector. The role of the government ought to be limited, as far as possible, to that of the

² Department of Primary Industries and Energy, *Offshore Strategy: Promoting Petroleum Exploration Offshore Australia* (1990), p. 1.

³ Peter Voser, "Energy: The Oxygen of the Economy", available at: <http://reports.weforum.org/energy-for-economic-growth-energy-vision-update-2012/> (accessed on 10/06/2012).

⁴ *Supra*, note 1, p.1.

⁵ National Oil Company of Kenya (NOCK), "Conditions for Oil and Gas Exploration" available at: <http://nockkenya.co.ke/upstream/?flag=upstream&ust=9> (accessed on 20/05/2012).

⁶ Mbendi, "Oil and Gas in Kenya: Overview" available at: <http://www.mbendi.com/indy/oilg/af/ke/p0005.htm> (accessed on 15/05/2012).

regulator in the sector. Further, the relevant government institutions should have jurisdiction to police the investors to safeguard the interest of the country in its natural resources. The government may be involved in the sector to guarantee that community projects tied to oil exploration and production and environmental management prerogatives are adhered to by the investor. Beyond that, the government ought to take decisive steps to give investors in the oil exploration and production sector ample leverage to realize their investment in the best investment climate.⁷

The Government of Kenya is in the process of implementing economic recovery programmes that will ease the process of doing business in Kenya while relegating the role of government in commercial undertakings to the minimum.⁸ With discovery of oil with potential for commercial exploitation, the government has also renewed its commitment to promote an efficient and competitive petroleum exploration and production industry.

The government is, thus, in the process of setting up a taskforce to review the obtaining policy, legal and institutional framework and make recommendations for reforms. This process should be guided by the following broad principles:

- a) Private decision makers should be allowed to manage risk in a regulatory framework that is predictable, transparent, equitable and timely.
- b) Energy resource developments should be required to comply with standards of environmental performance which are commensurate with those imposed on other sectors of the economy.
- c) Commercial decisions should determine the nature and timing of energy resource developments, with government interventions being transparent and allowing commercial interests to seek least - cost solutions to government objectives (e.g. environment, safety or good resource management objectives).
- d) Government objectives should generally be driven by sector - wide policy mechanisms rather than impose inconsistent requirements on individual projects/private investors.⁹

⁷ Tina Hunter, "The Offshore Petroleum Regulatory Frameworks of Australia and Norway", 8(4) *Oil, Gas & Energy Law Intelligence*; available at: <http://epublications.bond.edu.au/cgi/viewcontent.cgi?article=1351> (accessed on 20/04/2011).

⁸ Kenya National Energy Policy, *Sessional Paper No. 4 of 2004*, (GOK, Nairobi, 2004), p. 40.

⁹ Energy Task force, *Securing Australia's Energy Future* (Department of Premier and Cabinet, Canberra, 2004) p. 51-3.

Further, there is need to develop a policy framework for oil exploration and production that boasts the following five key objectives:

- a) Offer high levels of certainty to investors and other stakeholders about their rights and responsibilities and the process of decision – making;
- b) Provide a highly competitive operating environment, in an economic sense;
- c) Support the industry's efforts to achieved sustained wealth generation through growth, innovation and enhancement of the value of its output before export, including the role of the government in collecting and disseminating pre – competitive geo-scientific data to assist in attracting investment;
- d) Ensure good stewardship of the environment and community interests; and
- e) Allow industry to respond confidently to international challenges and seize international trade and investment opportunities.¹⁰

4.3 Policy Framework and Security of Oil Exploration and Production Investor

The NEP outlines as one of the objectives of the Government as to enhance the enabling environment through which petroleum exploration and associated resources development activities can be undertaken in an environmentally sound manner. This was considered as important given the prevailing dismal success of past exploration efforts and the need to promote investments in oil exploration in the country. Thus, it seems much of the effort was focused on promoting security of the investor at the expense of other stakeholders such as government interest and the community.¹

Thus, as part of the strategy to improve the enabling environment to promote oil exploration activities by the private sector, Government undertakes to carry out the minimum needed exploration works in areas designated for licensing. This is aimed at minimizing financial risks to help to attract more oil prospecting companies.² Further, the Government commits to undertake the following additional activities to reduce risk in exploring for oil in Kenya, namely:³

- i. collection and analysis of primary data so as to reduce the exploration risk by private explorers;

¹⁰ Warwick Parer, “Delivering National Prosperity”, *Address to the 1998 APPEA Conference 9 March 1998* in Canberra, Australia.

¹ Kenya National Energy Policy, *Sessional Paper No. 4 of 2004*, (GOK, Nairobi, 2004), p. 40.

² *Ibid.*

³ *Ibid.*, p.41.

- ii. making available additional funds to finance data collection and analysis. Sources of such funds will include levies on licensees for surface rights, training and royalties during the production period and the exchequer. External assistance will also be sought from Kenya's development partners to augment these funds;
- iii. reducing the size of the exploration blocks in order to attract small exploration companies;
- iv. enhancing the existing regional cooperation in data acquisition and exchange so as to reduce cost of exploration;
- v. building internal capacity to undertake oil exploration to complement external efforts
- vi. introducing services contracts to enhance exploration; and,
- vii. ensuring that licensees comply with the licensing provisions including minimum works programme schedule.

Nevertheless, there are glaring policy limitations in the provision of security for investors in oil production and exploration in Kenya. In the first place, this owes to focus of the National Energy Policy on the hydro-electric power as the core form of energy. Only recently has the government embarked on directing itself to exploiting locally available alternative sources of energy such as coal and oil.⁴ The problem with this is that the incentive structure does not capture the economic rent attributable to petroleum exploitation.⁵ Thus, investors looking to explore and produce oil in Kenya and East Africa generally allude to high risk which threatens to water down the expected return on investment in the sector if not checked and addressed in time. An independent report on investing in oil exploration and production sector in East Africa highlights the problem thus:

“...there are considerable risks specific to the East Africa region that must be recognized and mitigated by exploration and production (E&P) companies operating in the region. Although recent material exploration success in Uganda [and in Kenya] has renewed interest in East Africa, overall the region has had a disappointing history of exploration activity resulting in little commercial development. Beyond the exploration and geological uncertainty, above-ground risks can be country-specific and could potentially include political instability, corruption, active militant groups, limited infrastructure and access to a skilled labor force.”⁶

⁴ *Ibid.*

⁵ Department of Industry, Science and Resources, *Australian Offshore Petroleum Strategy: a Strategy to Promote Petroleum Exploration and Development in Australian Offshore Areas* (1999), p. 4.

⁶ David Beddis, Will Hares and Brent Watson “Untapped Oil Frontier-Hunting Elephants in East Africa”, *Oil & Gas East Africa Report*, February 2011.

Further, the investor enjoys limited bargaining power as against the government which tends to view exploration and production of oil merely as a second best investment project. This state of affairs may change with the discovery of commercially viable oil in the country but it will take more than mere statements of commitments to include policy review and overhaul.⁷

The Government of Kenya can take the opportunity to align the existing policy and legal framework on petroleum exploration and exploitation in Kenya. This is important to correct the anomaly owing to the fact that the policy was implemented in 2004, about twenty years after the Petroleum (Exploration and Production) Act was enacted. Indeed, what passes for policy framework on petroleum in Kenya is patchwork of documents which although addresses the petroleum sector does not specifically deal with petroleum exploration and production at length.⁸ The petroleum policy needs to be reviewed to give emphasis on attracting oil exploration and production investors to undertake petroleum exploration and production. Further, the policy should focus on the promotion of an efficient and competitive petroleum exploration and production industry and maximizing the contribution of the petroleum industry in advancing economic development in Kenya.⁹

These forgoing steps are necessary for Kenya to capitalize on the renewed oil investor interest in the region. It is also necessary to take advantage of the overriding factors that make Kenya and East Africa in general a preferred oil exploration and production investment destination. The Oil & Gas East African Report, 2011 prominently highlighted the increased regional interest and the revamping of the exploration activity in East Africa as follows:

The region stands out as offering large resource potential, a substantial amount of underexplored exploration acreage, close proximity to markets, limited competition, and several potential high impact exploration catalysts within the next two years. As a result, we believe the possibility exists for companies and investors to look toward East Africa to generate attractive investment returns in the near term.¹⁰

⁷ *Ibid.*

⁸ Kenya National Energy Policy, Sessional Paper No. 4 of 2004, (GOK, Nairobi, 2004), p. 1.

⁹ Department of Primary Industries and Energy, *Offshore Strategy: Promoting Petroleum Exploration Offshore Australia* (1990), p. 1.

¹⁰ *Supra*, note 18.

4.4 Legal Framework and Security of Oil Exploration and Production Investor

The legal system on oil and exploration in Africa has been described as being “governed by rules, regulations, and other command-and-control mechanisms that stipulate what people can do and what they cannot do.” These legal systems take the concessionary or contractual form being customised to address, as far as possible, the rights and obligations of host governments and of private investors. In this regard, the legal framework is expected to outline the conditions and requirements on the use of oil and gas resources and also establish sanctions for non-compliance with the same.¹

In Kenya, exploration and production of petroleum is governed by the Constitution, Petroleum (Exploration and Production) Act and other mining and environmental management laws. The main objective of the Petroleum (Exploration and Production) Act is to regulate the negotiation and conclusion by the Government of Petroleum Agreements relating to the exploration, development, production and transportation of petroleum.² The Act provides guidelines upon which the Government shall enter into contract with a contractor for oil exploration. Further, the Act stipulates the minimum conditions upon which the Kenyan government is to contract for oil exploration and production.³

The Kenyan Constitution gives regulatory powers over natural resources to the central government. Article 70 of the Constitution tasks the government with ensuring sustainable exploitation, utilization, management and conservation of the environment and natural resources and ensure the equitable sharing of the accruing benefits. This provision of the constitution is yet to be implemented through an Act of Parliament. Thus, as matters stand, in Kenya, the petroleum exploration and production sector is still regulated through the system which was in place under the old constitution.⁴

The terms and conditions of petroleum exploration contracts are subject to negotiation and are governed by the Petroleum (Exploration and Production) Act, the Petroleum (Exploration and Production) Regulations, the Income Tax (Amendment) Act made to specify the fiscal regime applicable to petroleum operations. However, like in the case of other African countries, the enforcement of these rules, regulations, and mechanisms has been insufficient

¹ Africa Development Bank and African Union, *Oil and Gas in Africa: Supplement to African Development Report*, (Oxford University Press, New York, 2009), p. 182.

² Preamble to the Petroleum (Exploration and Production) Act, cap 308, Laws of Kenya.

³ Section 9 (1) (g) of cap 308

⁴ Reference to the old constitution means the constitution which was replaced by the Constitution of Kenya (2010), now in force.

and ineffective. The statement on the inadequacy of the legal and policy framework on oil and exploration as expressed in the Oil and Gas Supplement to the African Development Report is very relevant for Kenya. In any case, Kenya as a country has “...inadequate policies and legal frameworks for managing oil and gas resources.” The available laws “do not meet the requirements of international organizations in terms of transparency, accountability, and other good governance criteria.”⁵ Further, it suffices to state that:

“...lack of modern oil and gas exploitation policies is a severe drawback to the development of the sector. These include policies guiding contracts, documentation of exploitation, code of conduct and exploitation practice, training and development of local staff and community members, oil and gas research, financial guidelines, and environmental regulations.”⁶

There is need to overhaul the law to reflect the change and especially give county governments a role in vetting application and licensing petroleum exploration and production in Kenya. This will not only guarantee public participation, but will also facilitate equitable distribution of resources to the people close to where petroleum resources are located. The Australian system which reflects a balance in powers between the federal and state governments offers a viable option in consideration the best legal framework for Kenya to adopt in regulating petroleum exploration and production as shown above.

4.5 Rule of Law and Security of Investors in Oil Exploration and Production in Kenya

Article 40 of the Constitution is important in that it guarantees the right of every person, either individually or in association with others, to acquire and own property of any description in any part of Kenya. Further, the article bars the Parliament from enacting laws that permits the State or any person (a) to arbitrarily deprive a person of property of any description or of any interest in, or right over, any property of any description; or (b) to limit, or in any way restrict the enjoyment of the rights under the article. The state is also barred from depriving a person of property of any description, or of any interest in, or right over, property of any description except as stipulated under the article. Such acquisition has to be for a public purpose or in the public interest and be carried out in accordance with this Constitution and any Act of Parliament. In any event, the Government is required to effect

⁵ *Ibid.*

⁶ *Ibid.*

prompt payment in full, of just compensation to the person. Any person has an interest in, or right over, such property has right of access to a court of law.¹

In addition, the Constitution of Kenya buttresses the independence of the judiciary by establishing a strong Judicial Service Commission,² enhancing the independence of the Chief Justice and the individual courts,³ creating the office of Chief Registrar of Judiciary,⁴ and promoting the place of the legal profession as a key stakeholder in the justice system. The Judiciary in Kenya has benefited a great deal and is now able to attract qualified judicial staff through transparent and open recruitment process. The Vetting process in the judiciary which is ongoing is expected to restore the integrity of the judiciary by removing judicial officers whose integrity and performance record is wanting.

The constitution also establishes the Environment and Land Court as an independent division of the High Court of Kenya to attract qualified and specialised judicial officers with the requisite expertise and experience to hand environment and natural resource disputes including those relating to oil exploration and production in Kenya. The independent Environment and Land Court is also envisioned to fast-track land and environmental disputes to ensure investors are not bogged down by costs and delays occasioned by litigations.⁵

The Constitution enshrines additional rights to secure the rights of local and foreign investors. Article 47 guarantees the right of every person to administrative action that is expeditious, efficient, lawful, reasonable and procedurally fair. Further, if a person has been or is likely to be adversely affected by administrative action, the person has the right to be given written reasons for the action and the parliament is enjoined to enact a legislation to give effect to these rights.⁶

Article 48 binds the State to ensure access to justice for all persons and, if any fee is required, it shall be reasonable and shall not impede access to justice. This is an important assurance for investors are guaranteed affordable and unimpeded recourse to the justice system to enforce their rights against the government and any other third party if the need arises.⁷ The right to fair hearing is also a constitutional prerogative under Article 50 of the Constitution.

¹ Article 40, Constitution of Kenya.

² *Ibid.*

³ *Ibid.*, Article 160 & 167.

⁴ *Ibid.*, Article 161 (1)(c).

⁵ *Ibid.*, Article 162(2)(b).

⁶ *Ibid.*, Article 47.

⁷ *Ibid.*, Article 48.

Every person whether Kenyan or foreign entity has the right to have their dispute decided in a fair and public hearing before a court or, if appropriate, another independent and impartial tribunal or body.⁸

However, the Constitution also has a number of weaknesses which may serve to limit the security of investors. Article 61 defines public land as including all minerals and mineral oils as defined by law. The public land containing minerals and mineral oil vests in and is to be held by a national government in trust for the people resident in the county and is to be administered on their behalf by the National Land Commission. The Constitution limits the disposal and use of such Public land except in terms of an Act of Parliament specifying the nature and terms of that disposal or use. The new Land Act has mainly served to buttress the constitutional position regarding public land.⁹

The Constitution also limits the rights of non-citizens to hold land in Kenya. Thus, a person who is not a citizen may only hold land on the basis of leasehold tenure only, and any such lease, however granted, may not exceed ninety-nine years.¹⁰ In case of a body corporate, the provisions are stringent in that it can only be regarded as a citizen only if it is wholly owned by one or more citizens. Where a property is held in trust, it is to be regarded as being held by a citizen only if all of the beneficial interest of the trust is held by persons who are citizens.¹¹

The Constitution also affords the State the discretion to regulate the use of any land, or any interest in or right over any land. Such regulation is permissible if it is in the interest of defence, public safety, public order, public morality, public health, or land use planning.¹² This clause is a major impediment to the security of investors in that it gives the government a near *carte blanche* where it seeks to impose undue regulation to private investments in land and natural resources such as oil exploration and production. The Parliament is also tasked to enact legislation ensuring that investments in property benefit local communities and their economies.¹³ This may likely to undermine the security and interest of investors given that Parliamentarians as representatives of the community may be motivated to enact stringent laws and regulations for safeguarding the interest of the respective communities which have

⁸ *Ibid.*, Article 50.

⁹ Act No. 6 of 2012.

¹⁰ *Ibid.*, Article 65(1).

¹¹ *Ibid.*, Article 65(3).

¹² *Ibid.*, Article 66(1).

¹³ *Ibid.*, Article 66(2).

the overall impact of undermining the returns on investments in oil exploration and production in Kenya.

Given the emergence of aggressive public interest litigation and advocacy in Kenya in the recent days, these provisions of the Constitution, although well-intended may emerge to be major impediments to the security of investors in oil exploration and production sector in the country. The provisions also anticipate a very elaborate and arduous legal and institutional infrastructure which may end up imposing undue costs to the investors in navigating the bureaucracy.

4.6 Conclusion

The key finding of this Chapter is that although the Government has taken major steps to create a framework that guarantees the security of investors in oil exploration and production sector, the resultant framework is far from adequate and efficient. One of the key principles underscored in this Chapter is that to guarantee security of investors, the oil exploration and production framework should be such as allows private decision makers to manage risk in a regulatory framework that is predictable, transparent, equitable and timely. Further, the government regulation should ensure energy resource developments comply with standards of environmental performance. The institutional framework for oil exploration and production should also limit government participation in oil exploration by adopting a minimalist intervention approach to the development of petroleum resources.

The regulatory framework for oil exploration and production in Kenya is therefore deficient in that it is not focused on reaping maximum benefits from petroleum resources for the benefit of the country. While the framework avails government the opportunity to exercise the permanent sovereignty over natural resources, this goes beyond the threshold of licensing and collecting royalties from oil investors. The Constitution, for instance, anticipates an expanded role for the Government in regulating the oil exploration and production sector which may lead to undue bureaucracy and red-tape. Overall, the resultant government participation in petroleum sector is more than minimalist and goes beyond the traditional role of regulating and licensing private sector interests. It is also yet to be seen how balancing of the national and county government interests in the sector will be undertaken as it stands to impact the security of investors if it is not handled well and efficiently. There is need to ensure that there is no tension and maximum efficiency is guaranteed in execution.

The relevant policy on oil exploration and production in Kenya does not lay emphasis or focus on oil exploration and production while the relevant institutional framework dwells on energy generally, denying exploration and production of oil adequate and specific attention. The policy framework also does not specifically address how the interests of government, the investor and the local communities in so far as exploration and production is concerned are to be reconciled. As a result, while the Constitution lays a strong rule of law structure to safeguard the interests of investors in the country, there is still legal uncertainty as to the impact of the provisions of the constitution that run counter to the rights and interests of investors as highlighted above. This matter deserves to be addressed comprehensively in the future by clearly outlining how the provisions of the new Constitution of Kenya affect the energy industry and in particular the oil exploration and production sector.

CHAPTER FOUR

ADVANCEMENT OF COMMUNITY INTERESTS IN OIL EXPLORATION AND PRODUCTION IN KENYA

5.1 Introduction

The community interests in oil exploitation and production in Kenya is based on the community rights over the affected land and the need to safeguard the interest of future generations. The government has a public interest in safeguarding the best interest of its citizens especially with respect to the right to property and the environmental right to clean, safe and healthy environment. In most cases, therefore, this interest is safeguarded by outlining the minimum terms and conditions for petroleum exploration and production.¹ Also of concern to the state is the question of how much revenue would trickle down to the community.

The immediate concern of local communities is how to make the most of the exploration opportunity by agitating for preferential access to employment and training opportunities availed by the oil-exploration companies². For instance, in the case of the recent oil find in Turkana County, the community would be interested to realise improved standard of living by tapping the resources accruing from the oil exploration and production activity. Further, communities are interested in guaranteeing minimal disruption to the cultural and communal way of life, access to their environmental right to clean, healthy and safe environment and public participation in the decision to explore and produce oil within the community's area of occupation.³

The recent discovery of oil in Kenya has resulted in intensified exploration for oil and gas in the Northern and Coastal regions of Kenya and the possibility for discovery of exploitable oil and gas deposits⁴. As a result, Kenya is experiencing one of the highest levels of investment in oil exploration in its North Eastern frontier.⁵ Thirteen companies have divided the

¹ Energy Regulatory Commission Website, "Energy Sub-sector: Petroleum", http://www.erc.go.ke/erc/energy_sub_sectors/?ContentID=2#(accessed on 10/03/2011).

² Mazera Ndurya, 'Residents Expectations Raised Sky High', the Daily Nation, 29th March, 2012, page 5.

³ *Ibid.*

⁴ Zeddy Sambu, 'Kenya: Big Companies Scramble for Stake on Oil Exploration' available at <http://allafrica.com/stories/201110110103.html> (accessed on 17/11/11)

⁵ Alex Taylor, "Kenya starts drilling for oil", available at: <http://www.bushdrums.com/news/index.php?shownews=520> (accessed on 01/03/2011).

country's North and East, particularly Turkana District, Lamu District and parts of the North Eastern Province and are drilling exploratory wells.⁶ These areas are the Turkana Basin in Turkana County and Lamu Basin in Lamu County. These companies include Dominion Petroleum, BG Group PLC and Tallow Oil PLC, all from the United Kingdom.⁷ Others are Total SA of France, Simba Energy of British Columbia, Anadarko of America and China National Offshore Oil Company (CNOOC).⁸

This intensified exploration activity presents a challenge for the government in safeguarding the interest of the local communities. On the one hand, there is the problem of resistance by local communities to the exploration exercise. For example, when CNOOC set out to begin exploration in Isiolo in October, 2009, this activity was met with protests by residents of Merti Division, Isiolo District. One of the complaints by the residents was that the company did not consider them for employment.⁹ The protests caused the exploration exercise to be launched by satellite from Nairobi.¹⁰ The fact that protests by residents can potentially hinder the activities of such a venture is a matter of concern.

On the other hand, there is the question of whether the public interest is generally protected through the state in so far as revenue collection and allocation are concerned.¹¹ This Chapter discusses whether the current legal, policy and institutional framework on oil exploration and production is capable of safeguarding the social, economic and environmental welfare of the local community in the area of exploration and production.

5.2 Constitution and Safeguarding Community Interests in Oil Exploration and Production

The Constitution makes provisions with regard to agreements relating to natural resources which are relevant in ensuring optimum exploration and production of oil in Kenya. In particular, article 71 of the Constitution provides that every transaction involving the grant of a right or concession by or on behalf of any person including the national government to another person for the exploration of any natural resource in Kenya shall be subject to

⁶ Zeddy Sambu, 'Kenya: Oil Search in Kenya Shifts to top Gear as Gas Deposits found' available at <http://allafrica.com/stories/201005260109.html> (accessed on 17/11/11).

⁷ *Ibid.*

⁸ *Ibid.*

⁹ Hassan Huka, 'Kenya: Oil Exploration Could Hit Snag as Locals Protest' available at <http://allafrica.com/stories/printable> (accessed on 17/11/11).

¹⁰ *Ibid.*

¹¹ Article 69(1)(a) of the Constitution requires the state to share the accruing benefits equitably.

ratification by Parliament. Parliament is mandated to enact legislation stipulating the classes of transactions subject to ratification.¹

The Constitution binds the state, *inter alia*, to encourage public participation in the management, protection and conservation of the environment. Further, the state has a duty to ensure sustainable exploitation, utilisation, management and conservation of the environment and natural resources, and ensure the equitable sharing of the accruing benefits. The government is also charged to utilise the environment and natural resources for the benefit of the people of Kenya. This last duty is relevant in protecting the interest of the community in that it challenges the constitutionality of any attempt to use natural resources such as oil for personal or non-public benefits.

The Constitution safeguards the right to property which is relevant for compulsory acquisition of private land for petroleum exploration and extraction. Article 40(3) limits the power of the state to deprive a person of property, interest or right in property of any description. One of the justifications for compulsory acquisition of land is acquisition of land for public purpose or in public interest. Such acquisition must be followed by prompt payment in full of just compensation and right of access to a court of law if the party is aggrieved.²

The Government also has a duty under the constitution to take measures to achieve and maintain protection of genetic resources and biological diversity, establish systems of environmental impact assessment, and encourage public participation in the management, protection and conservation of the environment.³ The Government is limited in the exploitation of oil resources in that it can only do so for the benefit of the people of Kenya. Similarly, State organs, investors and the community are required to protect and conserve the environment and ensure ecologically sustainable development and use of natural resources.⁴ Nevertheless, the constitutional provisions are only basic guidelines and principles and envisage operationalization through policy formulations, enactments and regulations.

¹ *Ibid.*, article 71(2).

² *Ibid.*, article 40.

³ *Ibid.*

⁴ Article 69 of the Constitution.

5.3 EMCA and Community Interests in Oil Exploration and Production

The EMCA makes provisions to operationalising the right of every person in Kenya to clean and healthy environment. The right to a clean and healthy environment is defined in the Act to include the access by every person in Kenya to the various public elements on segments of the environment for recreational, education, health, spiritual and cultural purposes.¹ The enforcement of this right is also provided for and where one alleges the contravention or likely contravention of the right to clean and healthy environment; such a person may apply to the High Court for redress.²

Therefore, investors in petroleum exploration and production have a legal duty to ensure that the exercise is carried out in a manner that safeguards the environmental interests of the local community. To this extent, it is fair to conclude that EMCA adequately protects the interests of the local community as far as the environment is concerned.

In order to guarantee enforcement of this right, EMCA gives the High Court comprehensive powers to make orders to prevent and order discontinuation of activities that are potentially harmful to the environment, require environmental audit of ongoing activities, order restoration of environment to its original state and compensation of persons affected by pollution and environmental degradation.³

In particular, the High Court may give orders and as are appropriate to:

- “(a) prevent, stop or discontinue any act or omission deleterious to the environment;
- (b) compel any public officer
- (c) to take measures to prevent or discontinue any act or omission deleterious to the environment;
- (d) require that any on-going activity be subjected to an environment audit in accordance with the provisions of this Act;
- (e) compel the persons responsible for the environmental degradation to restore the degraded environment as far as practicable to its immediate condition prior to the damage; and

¹EMCA, Section 3(2)

² EMCA, section 3(3)

³ *Ibid.*

(f) provide compensation for any victims of pollution and the cost of beneficial uses lost as a result of an act of pollution and other losses that are connected with or incidental to the foregoing.”⁴

5.4 Petroleum Regulations and Community Interests in Oil Exploration and Production

The Petroleum (Exploration and Production) Regulations enacted as section 6 of the Act require all petroleum agreements to conform substantially to the Production Sharing Contract annexed to the Act. The Contract, and in particular Clause 9 thereof, requires the contractor to ‘cause as little damage as possible to the surface of a contractor area and to trees, crops, buildings and other property thereon, shall forthwith repair any damage caused, and shall pay reasonable compensation for any loss suffered’. The Model Agreement also enjoins the contractor to protect and restore the environment to its original state in the event of damage. The contractor is also required ‘where possible’ to employ Kenya citizens in the petroleum operations and also train them.¹

In conclusion, the Act seems to focus more on securing the need to preserve the environment while giving little regard attention to the economic and social interests of the local community. For instance, while the model production sharing contract requires the contractor to employ Kenyans, no special attention is paid to the local community. Additionally, there is nothing compelling the investor to improve infrastructure in the local community or take other measures to improve the social welfare of the community in the area of exploration or production. These shortcomings make a strong case for the review of the law governing petroleum exploration and production in so far as the local community is concerned.

5.5 Safeguarding Community Interests and Role of Parliament

In order to ensure that oil exploration and production eventually benefits the community at large, there is need to ensure that the governance structures in place guarantee transparency, accountability and fairness. Without improving the democratic institutions and administrative capacity, it is unlikely that oil exploration and production in Kenya as in other African countries will bring about economic development and result in poverty reduction. Instead, oil monies are more likely to make matters worse for the poor. There is, therefore, need to support proper democratic management of oil as a natural resource and the implementation of

⁴ *Ibid.*

¹ Clause 13 of the Model Production Sharing Contract, established under section 6 of the Petroleum (Exploration and Production) Agreement.

just development strategies that provide benefits for the poor. In this respect, the first step towards these goals is to build transparency. Secondly, the ownership of oil as a natural resource by all citizens must be enforced and implemented to the letter. Additionally, all aspects of the oil industry in the country must be open to public scrutiny through exercise of the sovereignty of the public in the Parliament.¹

Ideally, successful exploration leading to discovery and production of oil should boost the national income and help to alleviate poverty and create broad-based development and improved standards of living across the country. However, experience around the world points to challenges which are often faced by resource-rich developing countries in translating mineral wealth into peace and prosperity in the interest of larger community. Theorists have called this trend as “resource curse” where such resource finds as oil result in increased conflict and deterioration of the economic and social situation of the immediate community and the beneficiary state. It is possible for developing countries which become reliant on oil and minerals to achieve a deepening of a range of political, economic and social challenges.²

However, to ensure the resource will be used to yield lasting benefits to present and future generations. The legal, policy and institutional framework relevant to oil exploration and production has to address the following:

- The need for a regulatory environment that fosters transparency concerning all revenues and in negotiation and award of contracts;
- The importance of balancing petroleum production with conservation – of the different exploration areas’ unique biodiversities, and wider environmental wellbeing;
- Ensuring other sectors of the economy will withstand fluctuating petroleum prices;
- Enforcing high standards of corporate responsibility and compliance on the part of investing companies;
- Ensuring that the anticipation of wealth from the oil does not intensify land insecurity, sectarian competition and other conflicts; and

¹ Ian Gary and Terry Lynn Karl, “Bottom of the Barrel: Africa’s Oil Boom and the Poor” (Catholic Relief Services, June 2003).

² Africa Development Bank and African Union, *Oil and Gas in Africa: Supplement to African Development Report*, (Oxford University Press, New York, 2009), p. 182.

- Building public participation and capacity to understand the new sector.³

In order to realise the forgoing, there is need to ensure sound policy and legal framework at all stages. This means that in the constitution of stakeholders, community interests should be broadly represented by, inter alia, local government officials, international and national civil society organisations (CSOs), the media, opinion leaders, traditional institutions and religious leaders and the development partners.

The role of the Parliament in policing how oil exploration and production activities factor community interests is also key. The frameworks for oil exploration should allocate the Parliament a clear mandate to guarantee that it plays a pivotal responsibility fulfilling its function of representing its constituents (wider society) in shaping public policy; enacting relevant and effective legislation; providing checks and balances on the executive's performance; overseeing policy implementation; and advocating for Kenyans' long-term interests.⁴

The Constitution makes transactions for oil exploration and production subject to ratification by Parliament in specific instances to protect community interest. In particular, parliamentary ratification is required where it involves the grant of a right or concession by or on behalf of any person, including the national government, to another person for the exploitation of any natural resource of Kenya where the same is entered into on or after the effective date.⁵

Thus, any consequent concession agreements entered after the date of promulgation of the current Constitution, namely 27th August 2010, such agreement has to be subjected to Parliamentary ratification by the relevant committee. This means the current contracts do not fall under the purview of those that are to be ratified by parliament. This presents a problem in that given that oil exploration and production agreements are long-term in nature, the need to have parliamentary oversight in the granting of concession agreements in the oil sector may not be met in the near future.

³ Oystein Noreng, *The Oil Industry and Government Strategy in the North Sea* (London: Croom Helm, 1980), p. 27.

⁴ The Sovereignty of the People of Kenya is chiefly to be exercised through the instrument of Parliament. See Article 1(2) of the Constitution.

⁵ Article 69 of the Constitution of Kenya.

5.6 Institutions to Safeguard Community Interest in Oil Exploration and Production in Kenya

The Constitution also places a duty on to cooperate with State organs and other persons to protect and conserve the environment and ensure ecologically sustainable development and use of natural resources. In this regard, the Constitution establishes several institutions to safeguard community interest in natural resources such as oil including Kenya National Human Rights and Equality Commission, Commission on Revenue Allocation and Commission on Administration of Justice.

The role of the Kenya National Human Rights and Equality Commission includes promoting respect for human rights and promoting gender equality and equity generally and to coordinate and facilitate gender mainstreaming in national development. The mandate of the Commission is to monitor, investigate and report on the observance of human rights in all spheres of life in the Republic. The Commission is also tasked with investigating complaints about alleged abuses of human rights and take steps to secure appropriate redress where human rights have been violated.¹ With respect to oil exploration, the Commission to hear and address the grievances of any community or individual adversely affected or aggrieved by oil exploration in any part of the country.

5.7 Conclusion

The absence of modern laws, standards, and codes governing oil exploration and production in the country and the lack of effective legal and regulatory enforcement mechanisms for such laws, standards, and codes, negatively impact the social, financial, and economic sectors. This in turn augurs badly for the community at large in that it has overall negative effects on the environment, the economy, import and export trade, security, revenue generation and allocation and infrastructure development. The African Development Bank and African Union put it thus:

“Potentially adverse effects are on the environment (pollution); accountability and revenue collection (evasion of taxes, duties, royalties, unjust enrichment, and corruption); trade (smuggling of conflict minerals, unauthorized exports of internationally sensitive materials); populations (displacements, lack of benefits for communities from resources); exports (slow and improper issuance of export

¹ Article 59, Constitution of Kenya.

permits); and revenue generation (suboptimal socioeconomic and financial returns from extractive resources).”¹

Thus, it is necessary to address the ineffectiveness and inadequacies inherent in the law, policy and institutional framework for safeguarding community in order to address the ills above. In addition, the frameworks should be designed to ensure the oil and gas sector contribute to the overall national development. As a matter of fact, increased oil exploration and production will definitely lead to receipt of significant investments by the country. While most of these investments will be for the development of the oil and gas sector, others will be for the resulting opportunities in the other sectors of the economy.²

Overall, it is incumbent to ensure there is legal, policy and institutional framework to use these investments to create as much value as possible in the country. Further, there should be frameworks for guaranteeing national participation through shareholding in licences and provision of goods and services by the country’s entrepreneurs. The extent to which the country’s private sector and its entrepreneurs can participate in oil and gas activities is currently limited by their financial capacity, together with their management and technological skills. It is therefore necessary for the country’s private sector to acquire and develop the skills necessary to participate in this sector of development, and where possible, for it to be provided with the opportunity to participate.

¹ *Supra*, note 21.

² Ministry of Energy and Mineral Development (Uganda), *The National Oil and Gas Policy for Uganda* (Government of Uganda, Kampala, 2008).

CHAPTER FIVE

CONCLUSION AND RECOMMENDATIONS

6.1 Introduction

This is the final chapter of this thesis. The first part of the chapter entails the conclusion of the entire study. The second part of the chapter is dedicated to making recommendations based on the findings of the study to meet the challenges to the various stakeholders as highlighted in the previous chapters.

It is important to note that the analysis in the study was premised on utilitarian theory of law. In this respect, the focus of the analysis in the foregoing chapters is how the laws, policies and institutions help in maximizing the benefit from oil exploration and production in Kenya for all the three stakeholders. Similarly, the recommendations herein will be focused on how the legal, policy and institutional framework for oil exploration and production in Kenya can be reformed to meet the challenges facing the stakeholders in wealth maximization. In other words, the recommendations are geared at highlighting how the state, investors and the communities can optimally regulate exploration and production of oil resources in Kenya.

6.2 Conclusion to the Study

This study endeavored to analyze the legal, policy and institutional framework for petroleum exploration and production in Kenya and whether they safeguard the interests of the investor, the state and local communities. In this regard, the thesis investigated whether Kenya's laws governing petroleum exploration and production is capable of adequately and effectively ensuring the government realizes optimum regulation of the oil exploration and production industry in the country, guaranteeing the security of the investor both commercially and physically to ensure return on investment and safeguarding the local community's and the general public's interest in sustainable and transparent exploitation of the oil resources in the country.

Chapter one was an introduction of the study. The Chapter identified the challenges in petroleum exploration and production, namely, the need for the state to ensure optimum exploration and production, the need to guarantee security for the investor and how to advance the interests of the community in the oil exploration and production sector.

Chapter two discussed the challenge facing the State in regulating the oil exploration and production sector in Kenya, namely, ensuring optimum exploration and production. Thus, the chapter analyses the oil exploration and production legal, policy and institutional framework in place in Kenya to determine whether the same allows for optimum exploration and production of oil in Kenya. This chapter, therefore, attempts to answer the question whether the existing policy, legal and institutional frameworks adequately and effectively ensures that there is optimum regulation of the oil exploration and production sector in Kenya.

The Chapter concluded that the legal, policy and institutional frameworks do not offer adequate wherewithal to the government in ensuring optimum regulation of oil and petroleum resources in Kenya. Indeed, save for the fundamental principles on the management of natural resources by the state under article 69 to 72 of the Constitution, the examined statutes have no provisions specifically targeting the interests of the concerned parties. The Energy Policy in place cannot address the issues raised in the absence of supporting legal framework to balance the social, environmental and commercial interests of the local community, the investor and the government as the case may be. The institutional framework is also imbalanced because too many powers are vested in the Minister for Energy who is merely a political appointee. Furthermore, no institution seems to be specifically mandated with the responsibility of addressing and safeguarding the government interest in oil exploration and production in Kenya.

Chapter Three analyzed the extent to which the existing legal, policy and institutional framework for oil exploration and production in Kenya guarantees security of the investor. It seeks to highlight the gaps and needs in this important aspect of attracting investment in the sector. In this regard, the salient and relevant provisions of the constitution, EMCA and the Petroleum (Exploration and Production) Act relating to regulation of exploration and production of petroleum in Kenya were explored to establish whether the existing framework is adequate and sufficient in protecting the interests of the investors.

The key finding of this Chapter is that although the Government has taken major steps to create a framework that guarantees the security of investors in oil exploration and production sector, the resultant framework is far from adequate and efficient. The regulatory framework for oil exploration and production in Kenya is therefore deficient in that it is not focused on reaping maximum benefits from petroleum resources for the benefit of the country. While the framework avails government the opportunity to exercise the permanent sovereignty over

natural resources, this goes beyond the threshold of licensing and collecting royalties from oil investors. Overall, the resultant government participation in petroleum sector is more than minimalist and goes beyond the traditional role of regulating and licensing private sector interests. There is need to ensure that there is no tension and maximum efficiency is guaranteed in execution.

The relevant policy on oil exploration and production in Kenya does not lay emphasis or focus on oil exploration and production while the relevant institutional framework dwells on energy generally, denying exploration and production of oil adequate and specific attention. The policy framework also does not specifically address how the interests of government, the investor and the local communities in so far as exploration and production is concerned are to be reconciled. Finally, the institutional framework for oil exploration and production leaves the government far too much leverage and opportunities for participation in oil exploration which may increase the cost of the development of petroleum resources in the country by creating bureaucracy and red tape.

Chapter Four analyzed how the current legal, policy and institutional framework on oil exploration and production is capable of safeguarding the social, economic and environmental welfare of the local community in the area of exploration and production. The aim was to determine how and whether the public interest is generally protected through the state in so far as revenue collection and allocation are concerned.

The Chapter concluded that the legal, policy and institutional framework establish limited mechanisms for guaranteeing national participation in oil exploration and production. There are also no measures in place to ensure the country's private sector and its entrepreneurs participate in oil and gas activities. Further, there are no mechanisms for enforcing investor commitments to safeguard community interests and/or to ensure the oil exploration and production is carried out in a sustainable and transparent environment and the benefits arising are shared equitably as between the relevant stakeholders.

In other words, the key finding of Chapter Four is that the current legal and institutional framework does not adequately cater for or protect the interests of the communities in the context of oil exploration and production. In the first place, the operative law was enacted before the constitutional framework establishing public participation as a key pillar of natural

resources development was promulgated. Secondly, there are no clear safeguards in the current legal framework to ensure that the scanty public participation mechanisms required are observed as per the law. Thirdly, the institutional framework in place is not adequately devolved to guarantee local and regional community participation in the licensing, auditing and review process of oil exploration and production projects in the country.

Legal Implications of the Oil Discovery in Kenya

The oil discoveries in Kenya is poised to impact the energy industry a great deal in that it has not only created an urgent need for legal reforms it also means that there are numerous institutional challenges and policy complications that will require re-alignment on the part of the national and county governments. The discovery of oil resources if unchecked likely results in major institutional challenges. Indeed, the negative impact of such unexpected discovery as Kenya's is a commonplace scenario for countries with concentrated natural resources and is commonly referred to as resource curse.¹

In simple terms, resource curse is the paradoxical situation in which countries with an abundance of non-renewable resources experience stagnant growth or even economic contraction. The most poignant characteristic of resource curse is a country which channels all of its energies into a single industry, namely the extraction of the relevant resources, at the utter neglects other major sectors. When this happens, the country becomes overly dependent on the price of the commodities, and overall gross domestic product becomes extremely volatile.²

Studies point to a number of factors which trigger resource curse, also known as the Dutch disease, in reference to a situation which occurred in the Netherlands following discovery of large deposits of natural gas. The Dutch disease takes the following elaborate steps: a nation finds ample natural resource reserves, economic focus begins to target this high-income industry, skilled workers from other sectors transfer to the resource sector, higher wages make the national currency less competitive and other industries, especially the

¹ Beatrice Meso, "Discovery of Oil in Kenya: Bane or Boom?" Unpublished article available from the author awaiting presentation at ICPSK Annual Conference 2012 (accessed on 12/07/2012).

² 'The Resource Curse': Why Africa's Oil Riches Don't Trickle Down to Africans *Published: October 31, 2007 in Knowledge@Wharton.*

manufacturing sector, begin to suffer and (especially in Africa) the democratic governance structures take a turn for the worse.³

However, it is highly unlikely that resource curse in the magnitude that has been experienced in other countries such as DRC Congo will occur in Kenya. In my opinion, the oil find in Kenya is very late in the day and the economy of Kenya is already structured towards human resource development, information and communication technology, tourism and hospitality and agriculture and local and informal industry. Nevertheless, oil is recognized as a principal agent of political problems. Oil resources belong to the whole country but managed on behalf of all citizens by their Government.

If adequate measures are not taken, weak institutions that constrain governments and fail in providing accountability may lead to problems such as collusion with large oil companies, rent seeking and corruption, increased political patronage, lower entrepreneurship and lower capacity for investment, increased authoritarianism and even civil conflict in countries that have discovered oil. Further, oil discovered in Kenya lies in the North where conflict has been rife, in form of cattle rustling. As such chances of militancy as observed in Nigeria are highly likely and therefore the community interests should be given a frontline to avoid escalation of violence.⁴

It is also expected that the oil find in Kenya will add impetus on the country's economic growth, speed up reduction of inflation, besides make the local currency stronger hence make cost of imports cheaper. However, measures need to be taken to ensure that the immediate communities also benefit from the oil discovery are not relegated to the periphery. Thus, there is need to enactment of new laws at national level to ensure that community interests are given a front row and measures are instituted to guarantee that the investors deliver on their community commitments.

6.3 Recommendations

The following recommendations are made with regard to legal, policy and institutional framework regarding petroleum exploration and production in Kenya. There is need to:-

³ Ibid.

⁴ Habil Olaka, "Economic Implications of Oil Discovery in Kenya", available at: <http://www.iekenya.com> (accessed on 12/07/2012).

- a. Review the Kenyan legal and policy framework on oil exploration to incorporate and realize the constitutional principles on natural resources management as espoused under the new Constitution of Kenya. The New Constitution is sections 69 and 70 as discussed in the study sets out principles to guide the exploitation of natural resources which must inform the reform of law in the oil exploration and production sector.
- b. Further, the Petroleum (Exploration and Production) Act must be amended to reflect the dynamics of the recent constitutional change in Kenya and particularly cater for the ratification requirement with respect to licensing exploitation of natural resources such as oil as required under the Constitution.
- c. Undertake stakeholder consultation to ensure the resultant oil exploration and production law expressly provides for measures to provide security to investors and safeguard the community by ensuring environmental sustainability of oil exploration in Kenya. In this regard, it is important to also put in place mechanisms for continued review of the law and policy to ensure it is up to date and the industry remains competitive.
- d. Amend the law on oil exploration and production to align it with provisions on environmental protection on the Environment Management and Coordination Act. In particular, there is need to include clear provisions on environmental impact assessment and environmental audit on oil exploration and production projects and also devise clear legal guidelines on how to address issues touching on environmental conservation and preservation during petroleum exploration and production.
- e. In terms of policy reforms, there is need to adopt a clear framework on how the central government should devolve the management of oil resources to the county government without limiting or watering down its sovereignty on natural resources. Further, it is incumbent to institute a policy framework geared at ensuring optimum regulation the country's oil and gas resources contribute to early achievement of poverty eradication and create lasting value to society.
- f. Further, it is necessary to adopt a minimalist government intervention approach in oil exploration and production. The essence of this approach is restricting the role of the government strictly to regulatory and policy-making roles without giving it an opportunity to participate in the market as a commercial player. As such, the private sector is given a free hand to innovate the best approaches to steer the industry forward.
- g. In particular, in order to guarantee security of investors, the oil exploration and production framework should be such as allows private decision makers to manage

risk in a regulatory framework that is predictable, transparent, equitable and timely. The government regulation should also be such as to ensure energy resource developments comply with standards of environmental performance. The institutional framework for oil exploration and production should also limit government participation in oil exploration by adopting a minimalist intervention approach to the development of petroleum resources.

- h. The policy framework for oil exploration and production adopted should be as strong as possible clearly outlining the objectives and goals of the government for the industry and how to achieve them. Additionally, in re-establishing the institutional framework with the discovery of commercially viable oil, it is incumbent to ensure the county government is fully engaged in oil exploration licensing and management as this offers a rare opportunity to infuse public participation in oil and petroleum resources development in Kenya.
- i. In reviewing the legal, institutional and policy framework for oil exploration, efforts should be made to draw input from both the private sector and oil exploration and production stakeholders, the community and public in general and civil society to ensure the final product is inclusive and futuristic in aiming for and facilitating successful oil exploration that will benefit all the stakeholders involved.
- j. The policy framework needs to primarily address exploration and commercial aspects of the petroleum exploration and production, whilst meeting social and economic objectives. In this regard, the petroleum policy should seek to ensure good stewardship of petroleum resources whilst encouraging commercial interests. The exploitation of petroleum resources should occur within a framework that maximizes the wealth from these resources and one that ensures economic sustainability after the resources are exhausted so as to meet the Constitutional objective of using our natural resources and the environment sustainably for the benefit of future generations.
- k. Further, the policy to guide national involvement in the development of petroleum resources whilst focusing on the protection of the environment. Most important, such policy should promote the occupational health and safeties of persons engaged in petroleum operations and develop and implement effective monitoring and enforcement strategies to secure compliance. There is, also, need to ensure the policy specifically addresses the interests of the local community that is affected by oil exploration and production activities to ensure they draw maximum benefits from the investment as is reasonably possible.

- l. As for institution, there is need to put in place a single competent authority with an exclusive mandate to implement government petroleum policy and negotiate and contract with international oil companies since NOCK is no longer focused in exploration of petroleum. Such an authority is important for the efficient and effective exploitation of resources. Thus, it is recommended that the government develop a competent authority with intergovernmental (county and national) and inter ministerial linkages to license, contract and supervise petroleum operations: essentially a 'one stop shop' for the development of petroleum resources
- m. Given that Petroleum is a key component of the energy sector in Kenya, it is necessary to harmonize the law with the Energy Policy and ensure it reflects the current trends in the sector to avoid the industry being shunned by sensitive investors for greener pastures such as South Sudan and Uganda. The government, in this regard, should take steps to ensure oil investors are given adequate incentives to make Kenya their preferred investment destination. The government should also simplify investment registration requirements and formalities and take steps to minimize financial risks and therefore help to attract more oil prospecting companies.
- n. Finally, the Government of Kenya should take steps in improving the rate of oil exploration in a country. The perception of Kenya's marginality as a potential of hydro-carbons should also be attacked with positive exposure of the potential of the industry in international forums in the same lines the tourism sector has taken to market Kenya as an ideal tourism hub. This is because the perception has meant that the country has managed to attract a limited number of oil exploration companies.- need to market the oil sector aggressively. There is also need to take steps to improve the security situation in the country as well as avert any likely negative impacts to economic development that may be occasioned by the oil discovery and commercial exploitation of the resource in the country.

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