

# County Government's Manual for Commercial Financing of the Water and Sanitation Sector of Kenya

November 2015



The Water and Sanitation Program is a multi-donor partnership, part of the World Bank Group's Water Global Practice, supporting poor people in obtaining affordable, safe, and sustainable access to water and sanitation services. WSP's donors include Australia, Austria, Denmark, Finland, France, the Bill & Melinda Gates Foundation, Luxembourg, Netherlands, Norway, Sweden, Switzerland, United Kingdom, United States, and the World Bank.

The Water Services Regulatory Board (WASREB) is a non-commercial State Corporation established in March 2003 as part of the comprehensive reforms in the water sector. The mandate of the institution is to oversee the implementation of policies and strategies relating to provision of water and sewerage services. WASREB sets rules and enforces standards that guide the sector towards ensuring that consumers are protected and have access to efficient, affordable and sustainable services.

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# Contents

|   |           |
|---|-----------|
| <b>Acknowledgements.....</b>  | <b>5</b>  |
| <b>Abbreviations.....</b>   | <b>6</b>  |
| <b>Section 1: How to Use this Toolkit.....</b>  | <b>7</b>  |
| 1. How to Use this Toolkit.....   | 7         |
| 1.1 Introduction .....  | 7         |
| 1.2 Forms and Guidance Materials provided in this Toolkit.....  | 8         |
| <b>Section 2: Introduction to the WSS sector and role of Counties .....</b>   | <b>9</b>  |
| 2. How the Water Sector is Organized in Kenya .....   | 9         |
| 2.1 Introduction to the water sector .....  | 9         |
| 2.2 The Current Institutional & Regulatory Arrangements .....   | 12        |
| 2.2.1 Water Sector Reforms of 2002.....   | 12        |
| 2.2.2 Regulatory Framework.....   | 14        |
| 2.3 Devolution in the Water and Sanitation Sector .....   | 15        |
| 2.3.1 Role of County Governments in the Water Sector .....  | 15        |
| 2.3.2 WSS Planning at County Level.....   | 16        |
| <b>Section 3: Role of County Governments in WSPs Management .....</b>   | <b>20</b> |
| 3. Role of Counties in Management of WSPs in Kenya .....  | 20        |
| 3.1 How WSPs Operate in Kenya.....  | 20        |
| 3.2 How Water Service Providers are Managed in Kenya.....   | 21        |
| 3.2.1 Corporate Governance .....  | 21        |
| 3.2.2 Organizational & Management Structure .....   | 22        |
| 3.3 Understanding the Key Performance Indicators for WSPs in Kenya.....   | 23        |
| 3.4 Role of counties in Tariff Setting for WSPs in Kenya.....   | 27        |
| 3.4.1 Types of Tariffs .....  | 27        |
| 3.4.2 The Tariff Structure.....   | 28        |
| 3.4.3 Tariff Preparation and Application Process .....  | 29        |
| 3.4.4 How Counties can Support WSPs in Tariff Setting.....  | 30        |
| 3.5 Social Connection Policy .....  | 31        |
| 3.5.1 Introduction .....  | 31        |
| 3.5.2 Roles and responsibilities of County/Water Service Boards<br>and WSPs and the criteria for Selecting Beneficiaries..... | 32        |
| <b>Section 4: The Role of Counties in Commercial Financing of WSS sector .....</b>  | <b>33</b> |
| 4. The Role of Counties in Commercial Financing of WSS Sector .....   | 33        |
| 4.1 How the Sector Has Been Financed .....  | 33        |
| 4.1.1 Budgetary Allocation.....   | 33        |
| 4.1.2 Equalization Fund .....   | 34        |
| 4.1.3 County Allocation.....  | 34        |

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|  |           |
|--|-----------|
| 4.1.4 Donor Funding.....   | 35        |
| 4.1.5 Water Services Trust Fund .....  | 35        |
| 4.1.6 Consumer Contribution (WSS system generated revenue) .....                                       | 35        |
| 4.2 What are the Current Financing Needs .....   | 36        |
| 4.2.1 Available Sector Funding and Deficit .....   | 36        |
| 4.2.2 Bridging the Funding Deficit .....   | 39        |
| 4.3 Why Counties should Support WSPs in Borrowing.....   | 41        |
| 4.4 Challenges facing WSPs in accessing Commercial Finance<br>Affordability Constraints.....           | 46        |
| 4.5 Required County and Other Stakeholders Support & Approvals<br>for Commercial Financing.....        | 47        |
| 4.5.1 Overview.....  | 47        |
| 4.5.2 The Applicable Legal Framework .....   | 47        |
| 4.5.3 The Borrowing Restriction.....   | 47        |
| 4.5.4 The Role of Key Stakeholders in borrowing by WSPs.....   | 48        |
| 4.5.5 Checklist of Required Approvals & Documentation.....   | 50        |
| <b>Section 5: The Borrowing Process .....</b>  | <b>52</b> |
| 5. Introduction to Commercial Borrowing for WSPs.....  | 52        |
| 5.1 Project Appraisal: Understanding how WSPs develop<br>financeable projects.....                     | 52        |
| 5.1.1 Overview.....  | 52        |
| 5.1.2 Project Appraisal - Due Diligence Checklist .....  | 52        |
| 5.2 Borrowing Process for WSPs.....  | 55        |
| 5.2.1 Borrowing cycle .....  | 55        |
| 5.2.2 Pre-Application Process.....   | 56        |
| 5.2.3 Application, Approvals & Acceptance Process .....  | 57        |
| 5.2.4 Post-Acceptance .....  | 60        |
| <b>Section 6: Appendices .....</b>   | <b>63</b> |
| 6.1 Appendix 1: Roles & Responsibilities of Water Sector Institutions.....                             | 63        |
| 6.2 Appendix 2: Water Service Providers in Kenya .....   | 64        |
| 6.3 Appendix 3: Request for Funding Proposal Template .....  | 65        |
| 6.4 Appendix 4: Sample WSP Memorandum & Articles of Association.....                                   | 71        |
| 6.5 Appendix 5: Sample Memorandum of Understanding between<br>County Government, WSB, WSP & WSTF ..... | 96        |
| 6.6 Appendix 6: County Government Approval Template for Borrowing .....                                | 102       |
| 6.7 Appendix 7: Water Service Provider Approval Template for Borrowing<br>by Board of Directors .....  | 104       |
| 6.8 Appendix 8: Water Service Board Approval Template for Borrowing<br>by WSB .....                    | 107       |
| 6.9 Appendix 9: WSP Capacity Diagnostic Assessment Tool .....  | 109       |

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# Abbreviations

|                |  |               |  |
|----------------|--|---------------|--|
| <b>AWSB</b>    | Athi Water Services Board                                    | <b>OBA</b>    | Output Based Aid                                   |
| <b>CAAC</b>    | Catchment Area Advisory Committees                           | <b>PCG</b>    | Partial Credit Guarantee                           |
| <b>CBEF</b>    | County Budget and Economic Forum                             | <b>PFMA</b>   | Public Finance Management Act                      |
| <b>CBK</b>     | Central Bank of Kenya  | <b>PPP</b>    | Public – Private Partnership                       |
| <b>CGA</b>     | County Government Act of 2012                                | <b>SPA</b>    | Service Provision Agreement                        |
| <b>CIDP</b>    | County Integrated Development Plans                          | <b>T-Bill</b> | Treasury Bill                                      |
| <b>CRB</b>     | Credit Review Board  | <b>T-Bond</b> | Treasury Bond                                      |
| <b>DA`</b>     | Deed of Assignment   | <b>USAID</b>  | United States Agency for International Development |
| <b>DCA</b>     | Development Credit Authority                                 | <b>WAB</b>    | Water Appeals Board                                |
| <b>EBIT</b>    | Earnings Before Interest and tax                             | <b>WASREB</b> | Water Services Regulatory Board                    |
| <b>EBITDA</b>  | Earnings before Interest, Tax, Depreciation and Amortization | <b>WB</b>     | World Bank   |
| <b>EIA</b>     | Environmental Impact Assessment                              | <b>WCA</b>    | Water Catchment Areas                              |
| <b>EWASCO</b>  | Embu Water and Sanitation Company                            | <b>WRUA</b>   | Water Resource User Associations                   |
| <b>GDP</b>     | Gross Domestic Product                                       | <b>WSB</b>    | Water Service Boards                               |
| <b>GoK</b>     | Government of Kenya  | <b>WSP</b>    | Water Service Provider                             |
| <b>GPOBA</b>   | Global Partnership on Output Based Aid                       | <b>WSS</b>    | Water Supply & Sanitation                          |
| <b>HFB</b>     | Housing Finance Bank   | <b>WSTF</b>   | Water Services Trust Fund                          |
| <b>KBRR</b>    | Kenya Bank’s Reference Rates                                 |               |  |
| <b>KCB</b>     | Kenya Commercial Bank  |               |  |
| <b>KEWI</b>    | Kenya Water Institute  |               |  |
| <b>KIWASCO</b> | Kisumu Water and Sewerage Company                            |               |  |
| <b>KPI</b>     | Key Performance Indicators                                   |               |  |
| <b>MWI</b>     | Ministry of Water and Irrigation                             |               |  |
| <b>NCWSC</b>   | Nairobi City Water and Sewerage Company                      |               |  |
| <b>NEMA</b>    | National Environment Management Authority                    |               |  |
| <b>NGO</b>     | Non – Governmental Organization                              |               |  |
| <b>NRW</b>     | Non – Revenue Water  |               |  |
| <b>NWCPC</b>   | National Water Conservation & Pipeline Corporation           |               |  |
| <b>O&amp;M</b> | Operations and Maintenance                                   |               |  |

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# I. How to Use this Toolkit

- How to use this Toolkit

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## 1. How to Use this Toolkit

### 1.1 Introduction

This toolkit is designed to give the County Governments useful insights into how WSPs can utilize commercial financing to fund their infrastructure projects. It provides a standardized procedure for loan application and appraisal for investments in water and sanitation projects.

Developed by a team of industry experts, this toolkit is a resource for County Governments. Other stakeholders in the sector such as Lenders and Water Service Providers (WSPs) will also be provided with similar toolkits.

While much of this manual is applicable to other markets, the toolkit is specifically designed for the Kenyan market.

The toolkit is divided into six sections focusing on:

- **Section 1: How to use the Toolkit** - This section provides an overview of the tool kit and how it can be applied.
- **Section 2: Introduction to the WSS sector and the need for Commercial Financing** - This section provides a high level overview of the current operations in the Water Supply and Sanitation Sector in Kenya. The section also discusses how the sector has been traditionally financed and its current financing needs.
- **Section 3: Role of County Governments in Water Utility Management** - This section discusses an overview of the operations of a typical WSP in Kenya as well as a review of key performance indicators for the sector. It covers the role of counties in tariff setting for WSPs and introduces the concept of social connection policy.
- **Section 4: The Role of Counties in Commercial Financing of WSS Sector** - This section builds the case for County Government helping their WSPs access commercial financing. It also covers the challenges facing WSPs in accessing commercial financing and ends with the required County and other Stakeholder approvals to enable WSP access to loans.

- **Section 5: The Project Appraisal & Borrowing Process** - This section provides tools to assist county governments conduct an effective project appraisal. It also expounds on the borrowing process indicating the required stakeholder involvement at every stage.
- **Section 6: Appendices.** This provides further elaborations on roles and responsibilities and provides pro-forma forms, and management diagnostic tool kits e.t.c.

This toolkit aims to provide County Governments with effective decision making support in assisting their WSPs undertake sustainable and well-considered projects through commercial financing.

As with any toolkit, periodic updating will be needed. As policies and regulatory framework evolve, the procedures for commercial borrowing should also change to accommodate the new environment. For example, as discussed in Section 2, the legal and regulatory framework is in a transition period with a number of functions in the process of being devolved to the Counties. As the regulatory framework becomes clearer with the anticipated enactment of Water Bill 2014, some aspects of this manual may need to be revised.

It is hoped that this toolkit provides County Governments with the appropriate understanding of commercial financing in order to enable their WSPs develop appropriate projects for commercial financing.

### 1.2 Forms and Guidance Materials provided in this Toolkit

Throughout the document, the toolkit provides relevant materials for commercial borrowing, references, interactive tools, and links to web sites cited. Some of the templates and links provided within the chapters for easy reference include the following:

| Section   | Document and relevance   | Link/Reference  |
|-----------|--|---|
| Section 2 | National Water Master Plan   | <a href="http://www.wrma.or.ke/index.php/projects/nwmp-2030.html">http://www.wrma.or.ke/index.php/projects/nwmp-2030.html</a> |
|           | National Water Sector Strategy (including Water Act 2002) and policy to guide water investment in the sector | <a href="http://www.wasreb.go.ke/policy-instruments">http://www.wasreb.go.ke/policy-instruments</a>                           |
|           | The Constitution of Kenya  | <a href="http://kenyalaw.org/kl/index.php?id=398">http://kenyalaw.org/kl/index.php?id=398</a>                                 |
|           | Sector Investment Plan   | Ministry of Water and Irrigation  |



| Section          | Document and relevance   | Link/Reference  |
|------------------|--|---|
|                  | Sector Regulation (including licensing, NRW standards, Sample of an SPA, service regulations, enforcement of standards, appointment criteria, corporate governance,  | <a href="http://www.wasreb.go.ke/regulatory-tools">http://www.wasreb.go.ke/regulatory-tools</a>                           |
|                  | Water Act 2002   | <a href="http://wasreb.go.ke/policy-instruments">http://wasreb.go.ke/policy-instruments</a>                               |
| <b>Section 3</b> | The criteria appropriate for the services to be provided by the WSP<br><a href="http://www.wasreb.go.ke/regulatory-tools/wsp-appointment-criteria">http://www.wasreb.go.ke/regulatory-tools/wsp-appointment-criteria.</a>        |   |
|                  | WASREB sector regulatory tools can be found in   | <a href="http://www.wasreb.go.ke/regulatory-tools">http://www.wasreb.go.ke/regulatory-tools.</a>                          |
|                  | Corporate Governance documents issued by WASREB<br><a href="http://www.wasreb.go.ke/images/Downloads/Corporate%20Governance%20Guideline.pdf">http://www.wasreb.go.ke/images/Downloads/Corporate%20Governance%20Guideline.pdf</a> |   |
|                  | The guidelines and various roles in tariff setting   | <a href="http://www.wasreb.go.ke/regulatory-tools">http://www.wasreb.go.ke/regulatory-tools</a>                           |
|                  | The reporting requirements   | <a href="http://www.wasreb.go.ke/regulatory-tools">http://www.wasreb.go.ke/regulatory-tools</a>                           |
|                  | Past Sector Impact reports   | <a href="http://www.wasreb.go.ke/impact-reports">http://www.wasreb.go.ke/impact-reports</a>                               |
| <b>Section 5</b> | Water Services Trust Fund (WSTF) Subsidy mechanism   | <a href="http://www.waterfund.go.ke/">http://www.waterfund.go.ke/</a>   |
|                  | The Impact Reports that contains technical and operational performance of the utilities.   | <a href="http://wasreb.go.ke/impact-reports">http://wasreb.go.ke/impact-reports</a>                                       |
|                  | Financing Urban Water Services in Kenya: Utility Shadow Credit Ratings <sup>1</sup>  | <a href="http://wasreb.go.ke/publications/credit-rating-report">http://wasreb.go.ke/publications/credit-rating-report</a> |
| <b>Section 6</b> | <b>Templates &amp; forms</b>   |   |
|                  | Roles and Responsibilities per the 2002 Water Act  | Appendix 1  |
|                  | List of Water Service Providers  | Appendix 2  |
|                  | Request for Funding Proposal Template  | Appendix 3  |
|                  | Sample WSP Memorandum & Articles of Association  | Appendix 4  |
|                  | Sample Memorandum of Understanding between County Government, WSB, WSP & WSTF  | Appendix 5  |
|                  | County Government Approval Template for Borrowing  | Appendix 6  |
|                  | Water Service Provider Approval Template for Borrowing by Board of Directors   | Appendix 7  |
|                  | Water Service Board Approval Template for Borrowing by WSB   | Appendix 8  |
|                  | WSP Capacity Diagnostic Assessment Tool  | Appendix 9  |

<sup>1</sup> WASREB Shadow Credit Rating Report 2011

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# II. Introduction to the WSS sector and role of Counties

- Introduction to the water sector
  - The current, institutional & regulatory arrangements
  - Devolution and the Role of Counties in the Water Sector
- 

## 2. How the Water Sector is Organized in Kenya

This section provides an overview of how the WSS sector is currently organised in Kenya. It provides a brief summary of the key sector players and how they interact. With the devolution of water service provision and the establishment of County Governments in 2013, this section seeks to provide an overview of the role of county governments in the sector. Finally, this section will provide an overview of how the sector has been traditionally financed and the current financing needs.

The country's vision is to have 100% access to safe water and sanitation services in Kenya by 2030

- Water coverage stands at 53% in areas covered by Water Service Providers in Kenya. Sewerage coverage stands at 16%.
- Investment requirements to reach this goal dwarfs the current financing sources
- With inadequate allocation from central budgets and development partners, the sector needs to rely more on new sources of raising finances and is looking for the private sector and commercial lending to finance some of the projects

### 2.1 Introduction to the Water Sector

Water coverage stands at 53% in areas covered by Water Service Providers in Kenya. Sewerage coverage stands at 16%.<sup>2</sup> This is against the Vision 2030 targets of 100% coverage making this development target a significant challenge for the Government. For the country to reach the 100% coverage, substantial investment in Water Supply and Sanitation (WSS) infrastructure is required both for rehabilitation of existing infrastructure, as well as for expanding water supply and sewer connections to unserved areas.

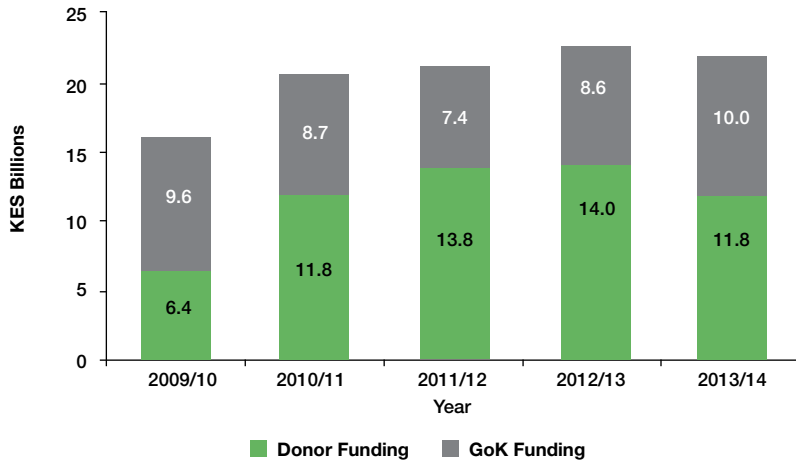
In recent years, the sector has benefited from a large number of technical studies, improvement plans, and re-organisations. However, the investment has not been adequate. This underinvestment will inevitably lead to deteriorating and insufficient infrastructure and poor services.

Traditionally, most of the financing for investments in the WSS sector has been sourced from Government budgetary resources and development partners (as shown in Figure 1).

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<sup>2</sup> WASREB, Impact Report Issue No. 8, Performance Review of Kenya's Water Services Sector 2013 – 2014.

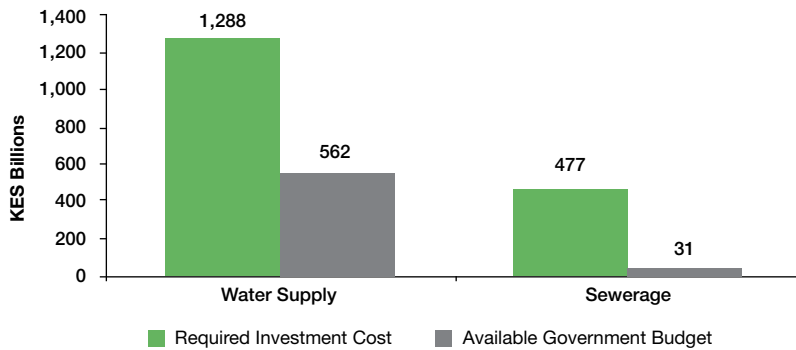
**FIGURE 1: DONOR & GOVERNMENT OF KENYA CONTRIBUTION TO WATER SECTOR BUDGET**



Source: Annual Water Sector Review 2013/14

The National Water Master Plan for 2014 shows that KES 1,765 billion is needed for immediate rehabilitation and for medium term expansion of piped WSS systems in Kenya to achieve the 2030 goals. This is almost 78% of Kenya’s annual expenditure budget of KES 2.246 Trillion. Whilst improved water supply and sanitation services are justifiably high priorities for government, public sector financial resources are insufficient to meet this requirement, even with donor support.

**FIGURE 2: REQUIRED INVESTMENTS AND AVAILABLE FINANCING IN WATER & SANITATION**



Source: NWMP 2030

The financing requirement to cover the investment in new WSS infrastructure and operation of existing facilities are simply too daunting to be met through traditional sources.

With competing needs for Government resources, coupled with changing focus away by the development partners and donors, there are limited financial and other resources available to meet the ever increasing demand for services.

Consequently, the Government is encouraging WSS utilities, as well as other Government entities involved in the WSS services provisions, to look for innovative ways of raising infrastructure financing.

In this regard, the Ministry of Water and Irrigation (MWI) has identified the private sector, through Public Private Partnerships (PPPs) and commercial financing from banks and other lenders, as a key component to financing some of the major Vision 2030 infrastructure projects.

#### KEY REFORMS USHERED BY THE WATER ACT OF 2002

- WSPs became private entity companies, managed independently
- WASREB became the sector's regulator
- WSPs as agents of WSBs
- WSBs have legal ownership of the water and sewerage assets utilised by WSPs
- WASREB has the authority to regulate water tariffs set by WSPs
- Institutionalisation of financing water services through the establishment of the Water Services Trust Fund (WSTF)

## 2.2 The Current Institutional & Regulatory Arrangements

The institutional and regulatory arrangements of the Water Sector in Kenya are currently governed by the Water Act of 2002. However, the adoption of the Constitution of Kenya in 2010 has seen the introduction of the County Governments that has led to the development of functions that were the preserve of the National Government. As a result, the WSS sector is in a state of transition as the current institutional and regulatory arrangements have to be revised to ensure that they are in line with functions and responsibilities as set out in the Constitution.

The paragraphs below discuss the framework under the 2002 Water Act as well as the some of the transitional arrangement that has been so far been effected.

### 2.2.1 Water Sector Reforms of 2002

In 2002, the Kenyan government launched an ambitious programme of reforms for the sector, passing new enabling legislation with clear roles and responsibilities of the key water institutions, increasing public spending to the sector, and pursuing other governance improvements such as the separation of water resources management from water supply services delivery.

Previously, service provision had been the responsibility of a single National Water Conservation and Pipeline Corporation (NWCPC) as well as of a few local utilities established since 1996. After the passage of the Act, service provision was gradually decentralized to 117 Water Service Providers (WSPs).

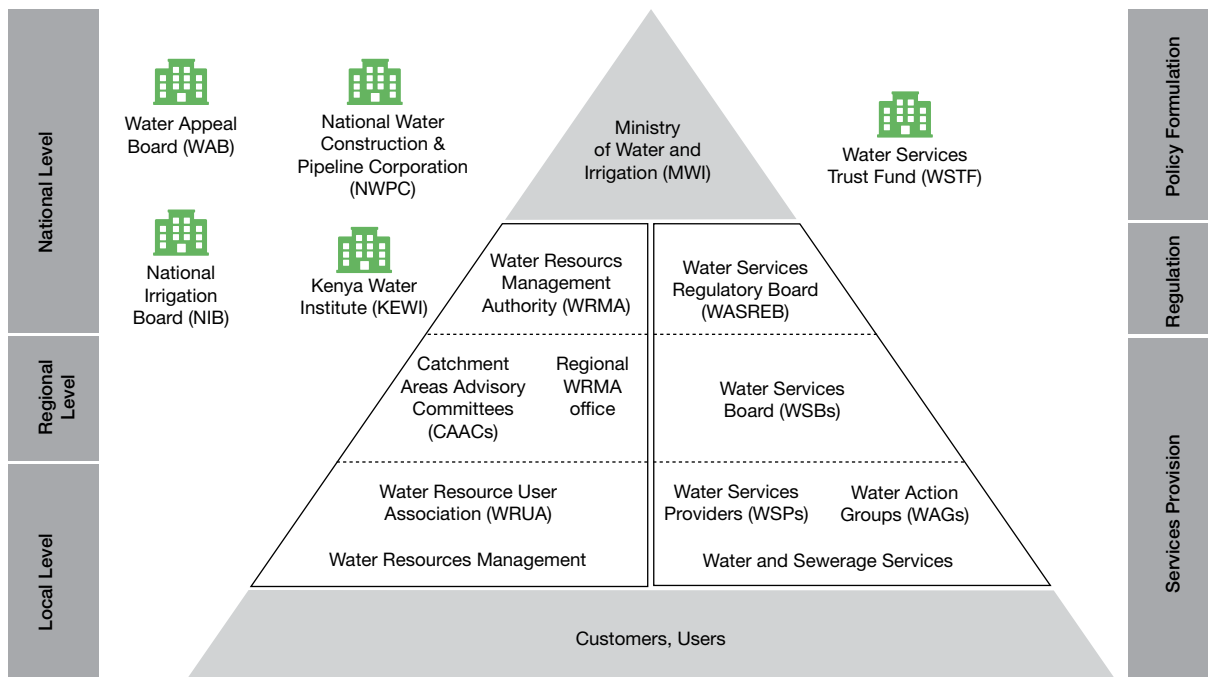
The ownership of facilities previously owned or used by the Central Government and NWCPC were transferred to the relevant Water Services Boards (WSBs) to facilitate management and operation of water services. This led to the formation of 8 regional WSBs in charge of asset management through Service Provision Agreements (SPAs).

The Water Act of 2002 also established the Water Services Regulatory Board (WASREB). WASREB's mandate is to oversee the implementation of policies and strategies relating to provision of water and sewerage services. WASREB's role is to ensure that consumers are protected and have access to efficient, adequate, affordable and sustainable water services and sanitation.

The 2002 reforms were acknowledged to have been one of most advanced and comprehensive institutional designs and intervention packages for the water sector in Africa. Most sector stakeholders in Kenya seem to agree that the 2002 reforms were a key step to improving water and sanitation services provision in the country, and that the sector has experienced significant progress since then. The reform process entailed setting up and building the capacity of the new institutions inaugurated by the Water Act 2002, and the introduction of the new service delivery framework for water and sanitation services and for water resource management. It saw the transfer of the functions previously held under various ministries, and other stakeholders to new organisations under the new institutional and service delivery framework.

The institutions set up by the Act are shown in the diagram below.

**FIGURE 3: CURRENT INSTITUTIONAL SETUP (PER 2002 ACT)**



Source: Annual Water Sector Review (2012)

As it can be seen from the diagram above, the Water Act of 2002 envisaged a number of stakeholders across the water supply and sanitation services provision chain, that can be grouped from national, regional and local levels.

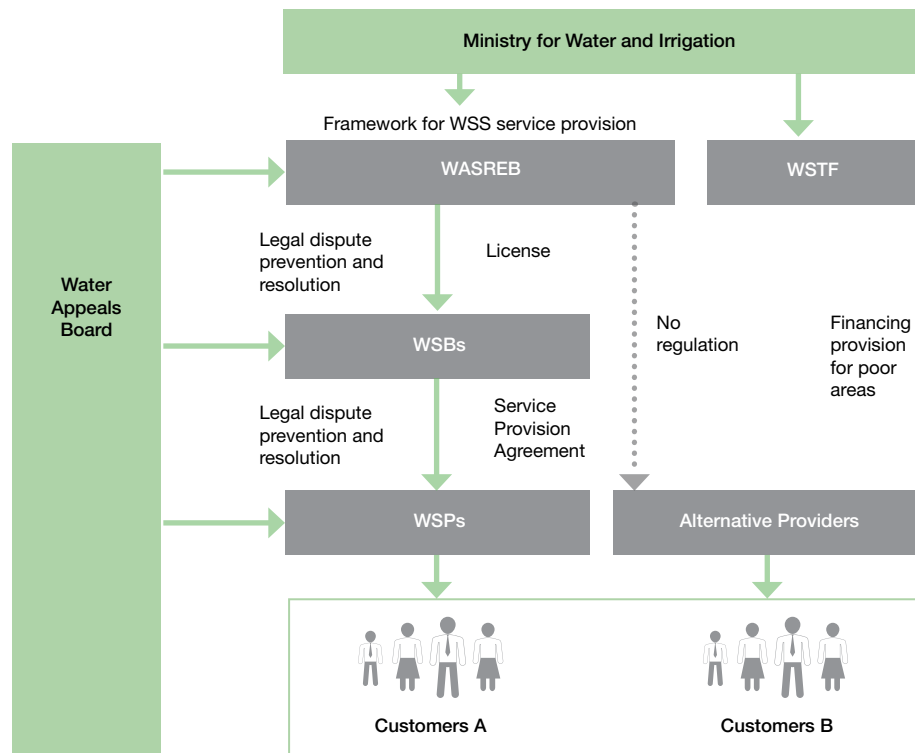
The sector devolution, discussed in the section 2.3 *Devolution in the Water and Sanitation Sector*, brings in new players such as the counties and places some of the bodies described in the 2002 Water Act existence into doubt. These would be clarified once the Water Bill 2014 has been enacted.

The current roles and responsibilities per the 2002 Act are included in Appendix 1: *Roles & Responsibilities of Water Sector Institutions*.

### 2.2.2 Regulatory Framework

The Figure below illustrates the regulatory relationship between the different players in the Water Supply and Sanitation sector as envisaged in the 2002 Water Act.

**FIGURE 4: WATER SECTOR REGULATORY FRAMEWORK**



The broad regulatory functions are summarized in Appendix 1: *Roles & Responsibilities of Water Sector Institutions*.

## 2.3 Devolution in the Water and Sanitation Sector

Following the promulgation of the new Constitution of Kenya in 2010, among other functions, the delivery of water and sanitation services function was devolved to the County Government level. This devolution is the most significant initiative in governance that Kenya has undertaken since independence. Under the Constitution of Kenya (2010), devolution has wide-ranging implications for the water sector.

The Constitution recognizes access to safe and sufficient water and reasonable standards of sanitation as a basic human right. Further constitutional provisions also firmly distribute the functions between the two levels of government with the national government being tasked with the management and protection of water resources while the county governments are tasked with the provision of water and sanitation services and the implementation of the national government policies on natural resource including soil and water conservation.

With envisaged devolution, there arose a need for legislative alignment of the Water Act of 2002 to the new constitution that led to the publishing of the Water Bill of 2014. The Bill is expected to advance the 2002 reforms with emphasis on the devolution of water services and sanitation.

### 2.3.1 Role of County Governments in the Water Sector

County Governments get their mandate to provide water and sanitation services from the Fourth Schedule of the Constitution of Kenya 2010, pursuant to article 185 (2), 186 (1) and 187 (2) and the County Governments Act 2012 (CGA). Further, article 174 (f) of the Constitution provides that one of the objects of the devolution of government is to promote social and economic development and the provision of proximate, easily accessible services throughout Kenya.

As a result, the Ministry's National Water Policy of 2012 outlines the various roles of the County Government in water supply and sanitation services provision:

- a) Ensuring access to water and sanitation according to constitutional rights.
- b) Catchment management and protection by implementing water catchment activities at county level
- c) Provide adequate consumer protection - Interests of underserved consumers should be protected by regulations ensuring progressive achievement of the right to water.
- d) Financial management through investment and finance planning through development of 5- year development plan incorporating an investment and financing plan for the provision of water services in the rural areas.
- e) Safeguarding integrity, good governance and performance in water supply service delivery.
- f) Ring-fencing of income in the water sector and autonomy of management of WSPs. Increasing mobilization and efficient use of funds.

WSS functions devolved to the counties

- Ownership of Water Service Providers
- Budgeting for the recurrent and development costs of water service provision
- Ensuring adequate resources for personnel and O&M costs to maintain services

- g) Ensuring and coordinating the participation of communities in governance
- h) Cooperate and coordinate with other counties to ensure limited water resources make inter-county sharing of resources inevitable.
- i) Contribute to research and development in the water sector

However, there are a number of roles at the County level that are yet to be operationalized as the counties seek financial and other resources to deliver this mandate. As a result and before the enactment of the Water Bill, the WSBs continue to play a significant role in the investment and management of the WSS services across their jurisdictions.

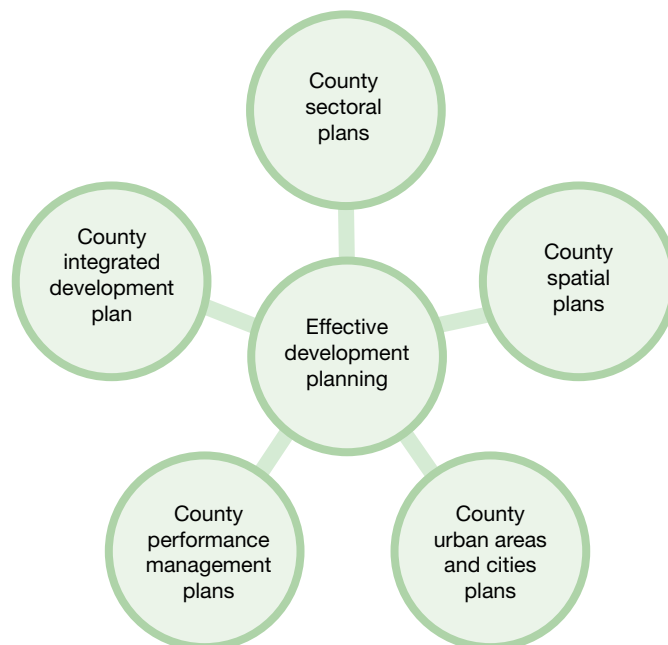
### 2.3.2 WSS Planning at County Level

Since the WSPs operate within the respective counties, their WSS investment plans need to be in line with the County Government WSS investment plans. The County Government Act of 2012 requires that each county in Kenya develop five key plans namely:

- County Integrated Development Plans (CIDP);
- County Sectoral Plans;
- County Spatial Plans;
- County Urban Areas and Cities Plans; and
- County Performance Management Plans.

These plans are interrelated as they deal with different aspects of development. Elements of Water & Sanitation Planning are covered under each of the above plans with the key plan being the CIDP.

**FIGURE 5: PLANNING AT COUNTY LEVEL**





### Water Sector Planning Framework at Counties

County Governments are required to have a County Development Plan. Section 107 (2) of the CGA provides that County Plans shall be based on the functions of the county governments as specified in the Fourth Schedule to the Constitution and on relevant national policies.

Section 104 of the CGA provides that these plans shall be the basis for all budgeting and spending in the county. No public funds shall be appropriated without a planning framework developed by the county executive committee and approved by the county assembly. Additionally, County Plans are supposed to assess development programmes for their viability - section 106 (3) of the CGA.

The county executive committee member responsible for planning submits the development plan to the county assembly for its approval and sends a copy to the Commission on Revenue Allocation and the National Treasury – section 126 of the Public Finance Management Act, 2012 (PFMA).

Through the CIDDPs, counties have created a framework through which their WSS needs can be met. The planning framework for the sector covers the following key areas;

- **Objectives:** This states the county's water and sanitation goals
- **Situational Analysis:** This establishes the key water resources in the county, water supply mechanisms in the county and water & sanitation coverage. It also covers the key issues facing the sector, causes and interventions.
- **Priority Programmes & Projects:** This identifies key programmes and projects that would enable the county meet its WSS objectives. These range from the development of water resources to the provision of water & sanitation services.
- **Resource Mobilization, Implementation & Monitoring:** Counties identify the key sources of financing for both capital and operational requirements for the programmes/projects. It also looks into implementation and providing a monitoring & evaluation framework.

### County Government Budgeting Process in Relation to WSS

The Constitution under chapter 12 provides the broad principles of public finance whereas the PFMA sets out the rules of how county governments can raise and spend money. There is a County Executive Committee member for finance who manages the county budget process (s 128 (1), PFMA). At the county level, the budget-making process is as follows:

Development of an integrated development planning process, which includes both long term and medium term planning:

- Planning for and establishing financial and economic priorities for the county over the medium term;

- Making an overall estimation of the county government's revenues and expenditure;
- Adoption of the County Fiscal Strategy Paper;
- Preparing budget estimates for the county government and submitting estimates to the county assembly;
- Debate and approval of the budget estimates by the county assembly;
- Enactment of the appropriation law and any other laws required to implement the county government's budget;
- Implementation of the county government's budget;

Accounting for, and evaluating the county government's budgeted revenues and expenditure.

**TABLE 1: COUNTY GOVERNMENT BUDGETING PROCESS**

| Deadlines   | Document                     | Process   |
|---|------------------------------|---|
| 30th August   | Budget process guidelines    | The County Executive Committee member for finance issues a circular setting out guidelines to be followed by all of the county government's entities in the budget process.   |
| 1st September   | County Development Plan      | <p>The County Executive Committee member responsible for planning submits the development plan to the county assembly for its approval, and sends a copy to the Commission on Revenue Allocation and the National Treasury.</p> <p>Within seven (7) days after its submission to the county assembly; the County Executive Committee member responsible for planning publishes and publicizes the annual development plan</p> |
| <p>28th February<br/>(Approval by the County Assembly)</p> <p>21st March<br/>(Published by the County Treasury)</p> | County Strategy Fiscal Paper | <p>The county treasury prepares and submits it to the county executive committee for approval</p> <p>The county executive submits it to the county assembly for approval by 28th February by the County Assembly, which then submits it to the County Treasury within 14 days</p> <p>The County Treasury publishes it within 7 days</p>   |

| Deadlines  | Document                  | Process  |
|--|---------------------------|--|
| 30th April   | County Budget Proposals   | Submitted to County Assemblies by the County Executive member in charge of the county treasury after the County Executive Committee's approval   |
| (Upon approval of the budget estimates by the county assembly) | County Appropriation Bill | County assembly prepares and submits a County Appropriation Bill to the county assembly of the approved estimates.   |
| Passed 90 days after approval of the County Appropriation Bill | Finance Bill              | <p>The County Executive Committee member for finance, on the same date that the revenue raising measures are pronounced, submits to the county assembly the County Finance Bill, setting out the revenue raising measures for the county government, together with a policy statement expounding on those measures.</p> <p>Passed by the County Assembly 90 days after approval of the County Appropriation Bill</p> |
| 15th June  | Cash Flow Projections     | County Government prepares an annual cash flow projection for the county for the next financial year, and submits it to the Controller of Budget with copies to the Intergovernmental Budget and Economic Council and the National Treasury.   |

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# III. Role of County Governments in WSPs Management

- How Water Service Providers are managed in Kenya
  - Key Performance Indicators in Water Service Providers
  - Role of counties in Tariff Setting for WSPs in Kenya
  - Social connection policy
- 

## 3. Role of Counties in Management of WSPs in Kenya

This section discusses the operations of WSPs in Kenya including how they are organised, their responsibilities, how they are run, versus the characteristics of a well-run utility. Since WSS services have been devolved, Counties need to understand the performance of their respective WSPs and how they would rank for commercial financing evaluation.

The chapter offers guidance into the role of county governments in tariff setting and provides an introduction to Social Connection Policy.

### CORE FUNCTIONS OF THE UTILITIES

- To source, treat and manage the town's water supply & sewerage.
- Bill and collect water and sewerage revenue.
- Supply of good quality water in sufficient quantities to meet various needs while ensuring safe disposal of waste water and environmental protection.
- Allocation of water in a sustainable, rational and economic way.

### 3.1 How WSPs Operate in Kenya

The Constitution of Kenya (2010) provides for the devolution of water services to County Governments. This has provided for a direct relationship between County Governments and WSPs as their shareholders. The Water Bill of 2014 is to provide the legislative and regulatory framework that fully incorporates the role of County Governments. However, at the time of printing, the Water Bill is yet to be enacted and the WSS services continue to be delivered under the Water Act of 2002 where WSPs act as agents of WSBs. Under the 2002 Act, WSBs own and develop infrastructure used in the production and delivery of water services WSPs as agents through SPAs as earlier discussed.

WASREB, as the industry regulator, oversees the implementation of policies and strategies relating to the provision of water and sewerage services; approving tariff rates; setting rules; and monitoring the performance of WSBs and WSPs.

WASREB licenses WSBs who in turn engage and contract WSPs to operate the systems in demarcated service areas as indicated in Figure 4: *Water Sector Regulatory Framework*. WASREB licenses WSBs and WSPs based on specific technical and financial criteria, the goal which is to ensure that the WSPs are capable of meeting routine operation and maintenance costs and have in place proper management for the for the provision of water services. The criteria for the services to be provided by the WSP can be found on <http://www.wasreb.go.ke/regulatory-tools/wsp-appointment-criteria>.

As part of its regulatory role, WASREB evaluates the performance of all the WSPs against certain parameters and publishes the results in the Water Sector Impact

Report. The annual sector impact reports can be found on the WASREB website through <http://www.wasreb.go.ke/impact-reports>.

In addition WASREB monitors the corporate governance and board composition of WSPs and has in past pursued remedial actions including through the court system, where other external interference that affects corporate governance. WASREB sector regulatory tools can be found in <http://www.wasreb.go.ke/regulatory-tools> while Corporate Governance documents issued by WASREB can be found in <http://www.wasreb.go.ke/regulatory-tools>.

The WSPs are companies incorporated under the Companies Act. As such the WSPs are required to have Company Articles and Memorandum of Association. These provide the overall objects and the management of the entities and among other management structures, the Board of Directors that is responsible for the overall management of the Company.

The Articles and Memorandum of Association are generally standard across WSPs and a sample has been provided under Appendix 4: *Sample WSP Memorandum & Articles of Association*. The shareholders are generally the County Government within which the WSP operates.

WSPs are required to maintain a management structure that provides leadership in the organization. This is headed by a Board of Directors that is made up of stakeholders (see section 3.2 *How Water Service Providers are Managed in Kenya*). A support group of board committees can be established to help the WSP's management in ensuring that they adhere to the WASREB Corporate Governance Guidance structure and other regulation laws.

## 3.2 How Water Service Providers are Managed in Kenya

### 3.2.1 Corporate Governance

#### **Board Appointment and Composition<sup>3</sup>**

The management and running of WSPs is required to be supervised by a board of directors. Under WASREB corporate governance guidelines, the utilities are required to have a minimum of 7 board members and a maximum of 11 members, with representation across the relevant County Government, WSB and stakeholders.

The corporate governance guidelines require that the appointment of directors representing stakeholders' interests shall be through a competitive stakeholder participation procedure such that no individual or group of individuals or interests can dominate its decision making.

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<sup>3</sup> Corporate Governance Guidelines, WASREB

**WSPS' BOARD COMPOSITION**

- 2 directors from the county government where one shall be a professional officer from each of the local councils covered by the WSP.
- 2 members from the business and manufacturing community nominated by their bodies.
- 1 local professional from the professional bodies nominated from the bodies.
- 1 representative from resident organizations.
- 1 member from a women organization.
- Where possible at least 3 of these members shall be women, provided that the eligibility criteria below are not compromised.
- A representative of the CEO of the respective WSB shall be invited to sit in attendance at the board where deemed necessary to offer guidance to its agent or to explain contentious issues.
- Managing Director of WSP.

Source: WASREB

The code also requires that the Board be chaired by an independent director who shall be elected from among the stakeholder directors by the other directors during the first meeting.

The Role of the Board of Directors is set as follows:

- Supervise and support the management team of the WSP
- Approve key decisions in accordance with the WSPs Articles of Association
- Be aware of the laws the company is supposed to comply with and be aware of the provisions of the Service Provision Agreement
- Ensure compliance with regulatory and reporting requirements from WSBs, WASREB and other relevant bodies

The Board of Directors is an important instrument through which a County Government can provide vision and guidance to a WSP to help in meeting its WSS goals.

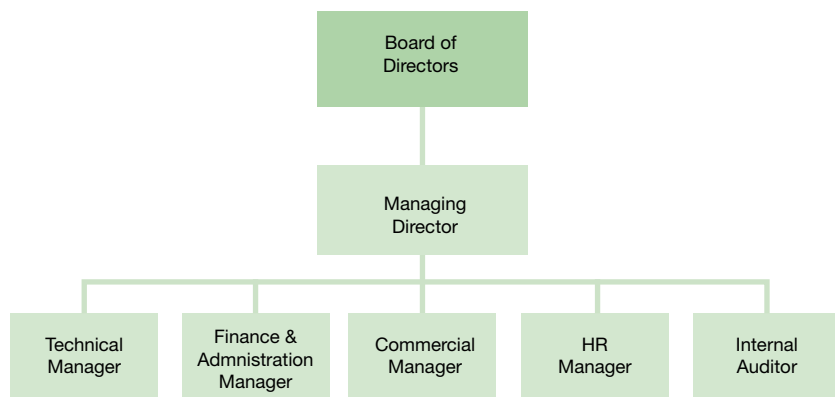
**Board Committees**

WASREB's corporate governance guidelines allow for the establishment of an Audit committee. Additional committees of the board can also be established but these additional committees shall not exceed two.

**3.2.2 Organizational & Management Structure**

The diagram below shows the recommended and typical organisation structure of WSPs in Kenya while the table that follow outlines the key responsibilities.

**FIGURE 6: ORGANIZATIONAL STRUCTURE OF A WSP**



**TABLE 2: MANAGEMENT ROLES & FUNCTIONS IN A WSP**

| Organizational Structure           | Roles & Functions   |
|------------------------------------|---|
| Management Board                   | <ul style="list-style-type: none"> <li>• Supervise and support the management team of the WSP</li> <li>• Approve key decisions in accordance with the WSP's Articles of Association</li> <li>• Be aware of the laws the company is supposed to comply with and be aware of the provisions of the Service Provision Agreement</li> <li>• Ensure compliance with regulatory and reporting requirements from WSBs, WASREB and other relevant bodies</li> </ul> |
| Managing Director/ General Manager | <ul style="list-style-type: none"> <li>• Performs the distinctive functions of a Water Utility</li> <li>• Provide strategic direction of the company under delegated authority of the Board of Directors</li> <li>• Supervises the Management team</li> </ul>   |
| Finance & Administration Manager   | <ul style="list-style-type: none"> <li>• Measuring and reporting the financial performance of the company</li> <li>• Manages the support functions such as IT and Administration</li> </ul>   |
| HR Manager                         | <ul style="list-style-type: none"> <li>• Manages the employees' development, advises and implements policies that consider immediate and long-term staff</li> </ul>   |
| Technical Manager                  | <ul style="list-style-type: none"> <li>• Manages the operations and maintenance of the water &amp; sanitation infrastructure and also manages quality standards</li> </ul>  |
| Internal Auditor                   | <ul style="list-style-type: none"> <li>• Conducts an independent assurance that an organisation's risk management, governance and internal audit control processes are operating</li> </ul>   |
| Commercial Manager                 | <ul style="list-style-type: none"> <li>• Manages the entire sales process (from water connections to cash collections) and manages customer service delivery</li> </ul>   |

### 3.3 Understanding the Key Performance Indicators for WSPs in Kenya

One of the most important criteria in any assessment of whether a WSP is a viable prospect for commercial financing will be its ability to demonstrate that it is well-run. There is no shortage of literature on identifying the characteristics of a well-run commercially viable utility and some examples are given in Table 3.

**TABLE 3: CHARACTERISTICS OF A WELL-RUN UTILITY**

| Characteristics of a well-run utility   |
|---|
| <p>These six characteristics of high performance organisations would be present in either public or private models and are:<sup>4</sup></p> <ol style="list-style-type: none"> <li>1. Effective staffing</li> <li>2. Consistently sufficient funding</li> <li>3. Detailed asset management systems</li> <li>4. Performance measurements and rewards aligned to organisational objectives</li> <li>5. Decision processes that are transparent and open to the public</li> <li>6. Using an effective planning process that identifies and assesses problems before arriving at solutions</li> </ol> |

<sup>4</sup> Gary Wolff and Eric Hallstein, Beyond Privatization: Restructuring Water Systems to Improve Performance, Pacific Institute, 2005

| Characteristics of a well-run utility   |
|---|
| Evidence of a high level of the following six characteristics should be identifiable in well performing public WSPs: <sup>5</sup>   |
| <ol style="list-style-type: none"> <li>1. External Autonomy</li> <li>2. External Accountability</li> <li>3. Internal Accountability for Results</li> <li>4. Market Orientation</li> <li>5. Customer Orientation</li> <li>6. Corporate Culture</li> </ol>  |
| It is widely recognised that "if you don't measure you do not manage". The following measures of 'success' should be identifiable: <sup>6</sup>   |
| <ol style="list-style-type: none"> <li>1. Effective – is it working? E.g. Quality and quantity of water supplied</li> <li>2. Equitable – can all benefit? E.g. % of population receiving the service</li> <li>3. Sustainable – will it continue? E.g. Extent of self-financing</li> <li>4. Efficient – achieved with optimum use of resources? E.g. Staffing ratios</li> <li>5. Transparent – is it apparent to all how it happens? E.g. Audited financial statements with customer audited complaints procedures</li> <li>6. Replicable – can it be repeated? E.g. Processes, procedures and quality assurance should be present.</li> </ol> |

These can be applied to the WSS sector by interested stakeholders (Lenders, WASREB & County Governments) to various degrees in judging the performance of a WSP. WASREB classifies WSS utilities to various categories in its sector Impact Report, based on performance of the following nine KPIs:

**TABLE 4: WASREB'S KEY PERFORMANCE INDICATORS<sup>7</sup>**

| Indicators                |  | Sector Benchmarks |            |                |
|---------------------------|--|-------------------|------------|----------------|
|                           |  | Good              | Acceptable | Not Acceptable |
| 1. Water Coverage         |  | > 91%             | 80-90%     | < 79%          |
| 2. Sanitation Coverage    |  | > 91%             | 80-90%     | < 79%          |
| 3. Drinking Water Quality | No. of tests – Residual Chlorine       | > 96%             | 90-95%     | < 89%          |
|                           | Compliance – Residual Chlorine         | > 96%             | 90-95%     | < 89%          |
|                           | No. of tests – Bacteriological Quality | > 96%             | 90-95%     | < 89%          |
|                           | Compliance – Bacteriological Quality   | > 96%             | 90-95%     | < 89%          |

<sup>5</sup> Aldo Baietti, William Kingdom, Meike van Ginneken, Characteristics Of Well-performing Public Water Utilities, Water Supply & Sanitation Working Notes, Note No. 9, May 2006

<sup>6</sup> Richard Franceys, Managing and Financing World Water and Wastewater, <https://www.cranfield.ac.uk/courses/training/managing-and-financing-world-water-and-wastewater.html>

<sup>7</sup> WASREB Impact Report



| Indicators  |   | Sector Benchmarks |            |                |
|---|---|-------------------|------------|----------------|
|   |   | Good              | Acceptable | Not Acceptable |
| 4. Hours of Supply                                    | Population > 100,000                      | 21-24             | 16-20      | < 15           |
|   | Population < 100,000                      | 17-24             | 12-16      | <11            |
| 5. Non – Revenue Water                                |   | <19               | 20-25%     | > 26%          |
| 6. O&M Cost Coverage                                  |   | >150              | 100-149%   | <99%           |
| 7. Collection Efficiency                              |   | >91%              | 85-90%     | <84%           |
| 8. Staff Productivity<br>(Staff per 1000 connections) | Large & Very large Companies              | < 4               | 5-8        | > 9            |
|   | Medium & Small (less than 3 towns)        | < 6               | 7-11       | > 12           |
|   | Medium & Small (more or equal to 3 towns) | < 8               | 9-14       | > 15           |
| 9. Metering Ratio                                     |   | 100%              | 95-99%     | < 94%          |

Each of the KPIs is explained in more details below.

1. **Water coverage** - assesses the utility's performance in executing its core business of supplying portable water to consumers.
2. **Sanitation coverage** – measures performance with regard to the provision of sewerage and on-site sanitation services. Improved facilities include flush or pour-flush to piped sewer systems, septic tanks, ventilated improved pit latrines (including Urine Diversion Dehydration Toilets) and traditional pit latrines (with a squatting slab).
3. **Drinking water quality (DWQ)** – DWQ measures the portability of the water supplied by a WSP. The indicator is composed of two equally weighted sub-indicators, Residual Chlorine and Bacteriological Quality.
4. **Hours of supply** – measures the continuity of services of a WSP and thus the availability of water to the customer. It has a direct bearing on the financial sustainability of the WSP: the higher the hours of supply, the higher the consumption and revenue.
5. **Non-Revenue Water (NRW)** – NRW refers to the difference between the amount of water produced for distribution and the amount of water billed to customers. It measures the efficiency of the WSP in delivering the water it produces to the customer take-off point. It captures both technical losses (leakages) and commercial losses (illegal connections/water theft, metering errors and unbilled authorised consumption).
6. **Operation and maintenance (O&M) cost coverage** – is the extent to which internally generated funds cover the cost of running a WSP. It is the first step towards full cost coverage. It ensures long term financial sustainability.

The Board of Directors is an important instrument through which a County Government can provide vision and guidance to a WSP to help in meeting its WSS goals.

7. **Revenue collection efficiency** – measures the effectiveness of the revenue management system of a WSP. Revenue collected, as opposed to amounts billed, is what impacts on a WSP’s ability to fund its operations. Collection Efficiency is a proxy indicator on the commitment of management in optimizing the WSP revenue inflow and is, indirectly, a reflection of customers’ willingness to pay and, by extension, their satisfaction with services provided
8. **Staff productivity (staff per 1000 connections)** – measures the efficiency of WSP in utilising its staff. Thus, a low figure is desirable. It should be noted that staff productivity is affected by factors such as the nature of human settlement (distances between connections), skills mix, outsourcing, the number of schemes served, and whether a utility provides water alone or water and sewerage services together.
9. **Metering ratio** – measures to what extent the WSP has implemented metering as a management tool. It provides critical information to WSPs in managing NRW and allows them to charge customers according to their consumption and thereby manage water demand.

**FIGURE 6: WASREB KEY PERFORMANCE INDICATORS FOR THE WATER SECTOR**



### 3.4 Role of Counties in Tariff Setting for WSPs in Kenya

The main source of WSP revenues is from water supply and sanitation service charges (tariffs). Other sources include connection charges, sale of bottled water, sludge (for fertilisers) and other miscellaneous revenues from disposal of old and or non-core assets etc. A WSS tariff is the price assigned to water supply and sanitation services delivered by a WSP through its WSS infrastructure to its customers.

**It is imperative that Counties support their WSPs to achieve full cost recovery whilst balancing the need to extend WSS services to all its consumers at an affordable rate.**

Being a public good, the WSS services sector is one of the regulated sectors in Kenya. As a result, both quality of service delivery and price charged for the services (tariffs) are regulated. This means that WASREB, as the sector regulator, not only provides general oversight of service provision but also approves all tariff applications from the utilities.

WASREB has developed guidelines for setting tariffs and other charges on water services in accordance with the national strategy. The guideline and various roles in tariff setting can be found WASREB's website on <http://www.wasreb.go.ke/regulatory-tools/tariff-guidelines>

#### 3.4.1 Types of Tariffs

WASREB recognizes that WSP performance is driven by several factors including whether urban or rural and whether small, medium or large. The regulator has therefore developed guidelines on what the tariffs should cover for different categories on WSPs.

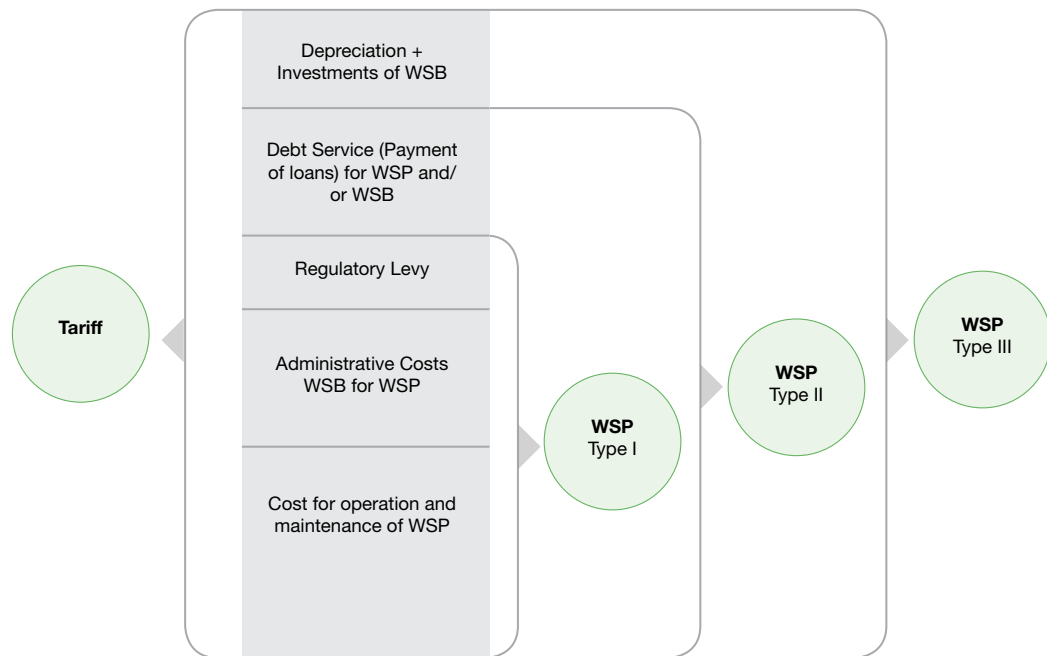
- **Type I- Full coverage of Operations and Maintenance costs is not achieved:** These are WSPs yet to achieve full O&M cost recovery. The economic viability of these WSPs is most important for WASREB hence tariff adjustments to achieve 100% O&M cost coverage will be applied. WASREB will also set targets for such WSPs to achieve a minimum acceptable service level.
- **Type II - Full coverage of Operations and Maintenance cost achieved, but repayment of debts is pending:** These are WSPs that have achieved 100% O&M coverage but cannot fully cover to debt service costs. WASREB would adjust tariffs, taking into consideration the consumers' ability to pay, the performance and cost structure of the WSPs. Tariff adjustments for these WSPs would be strongly linked to the WSP meeting acceptable standards.

Counties should ascertain the type of WSP in their jurisdiction. Counties should aim to have WSPs that are able, at the very least, to achieve full coverage of O&M costs i.e. Type II and Type III.

WASREB Guidelines allow for coverage of debt service, depreciation and investments in tariffs of Type III WSPs

- **Type III - O&M costs are covered between 100% and 150% and repayment of debts is achieved or ongoing:** WSPs in this category are viewed as being able to recover O&M cost fully including financing costs. WASREB would adjust tariffs taking into consideration the consumer's ability to pay (which is studied in detail) and ensuring the maximum number of people have access to safe drinking water. Tariff increases are strongly tied to the WSP meeting set performance standards.<sup>8</sup>

**FIGURE 8: ALLOWABLE COST COMPOSITION OF TARIFFS BY WSP TYPE**



Source: Water Services Regulatory Board – Tariff Guidelines

### 3.4.2 The Tariff Structure

The tariff structure specifies how much each category of users of water and sanitation services is charged. These categories include residential, industrial, commercial, the poor etc. The structure is useful in ensuring fair charges based on usage for more customer categories and helps institute a pro-poor policy by ensuring lower and affordable tariffs are charged to poor customers.

The Water tariff structure has the following components:

1. An average tariff or structure that would determine total O&M recovery. The pricing options include:
  - a. Variable Charges, per m<sup>3</sup> of water provided
  - b. “Block” Structures with variable charges that charge once a customer’s

<sup>8</sup> WASREB Tariff Guidelines

- c. Fixed Charge for a water service connection and some given quantity of water
  - d. Combination
2. Customer Classes that reflect different costs imposed on system due to different usage patterns, utilization rates, technical requirements and administrative requirements.
  3. A tariff structure that shows how much each user class will pay per unit consumed, for each connection type for each month of service.

The Sanitation tariff is structured as per the following pricing options;

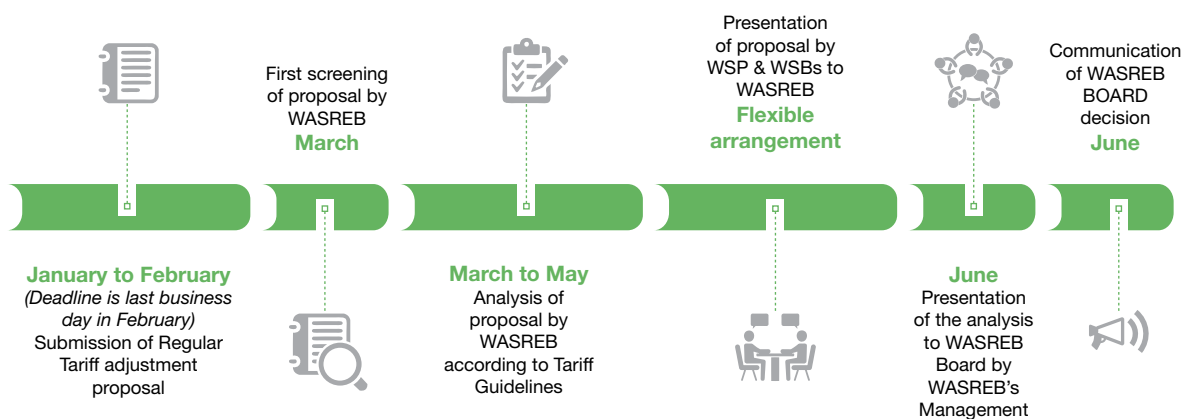
1. A fixed sewerage charge with all households with sewerage connections
2. A volumetric charge based on percentage of water usage
3. A combination of a fixed charge and a volumetric charge

### 3.4.3 Tariff Preparation and Application Process

The tariff preparation process is initiated by the WSP or WSB. The party requesting the adjustment is required to consult with other key stakeholders such as the County Government to ensure that they are aware of its intention to adjust tariffs. The WSP then develops a tariff adjustment proposal in collaboration with the WSB and submits it for approval to WASREB.

The figure below illustrates the process of tariff approval process used by WASREB. If the WSB and WSP do not agree on the Tariff Adjustment Proposal, the WSB must clearly document where there is disagreement between the WSB and the WSP when submitting the proposal, and provide a copy to the WSP. If one of the parties does not agree to the Tariff Adjustment Proposal or fails to respond to the request of the other within three (3) months, the party requesting the Tariff Adjustment may refer the matter to the WASREB for assistance or initiate a Dispute Resolution Process.

**FIGURE 9: TARIFF APPROVAL PROCESS**



In the situation where the WSP or the WSB disputes WASREB decision, the matter is referred to the Water Appeals Board for resolution within fourteen days of WASREB decision.<sup>9</sup>

WASREB may also request that the WSB prepares a Tariff Adjustment Proposal. In this case, the regulator will make its request to the WSB in writing, stating the reasons (which mainly involve increase cost of service delivery and need for higher cost recovery) for its request and the expected date of the Tariff Proposal Submission.

#### 3.4.4 How Counties can Support WSPs in Tariff Setting

##### **Policy & Legislation**

Through policy instruments such as the County Water Acts, CIDP and County water policy, County Governments can enshrine measures to ensure that their WSPs are able to run sustainably through charging cost recovery tariffs. These measures may include:

- Provision that county WSS projects have to achieve sustainable cost recovery
- Provision for Monitoring mechanisms of WSPs to ensure cost recovery tariffs are charged
- Provision for social connection policies that cover lower income groups
- Provision for supporting their WSPs through the tariff adjustment process with regulators

##### **Public Engagement**

WSPs face an uphill task in convincing members of the public to support tariff increases. As opinion leaders, County Governments can assist its WSPs creating public awareness as to the importance of utilities running sustainably.

### **3.5 Understanding Social Connections Policy Approach**

#### 3.5.1 Introduction

*Social Connections* is a term used to refer to subsidized private first-time connections of residential dwellings to public utility networks, primarily intended to benefit the low income areas. A social connection policy is an institutional policy primarily intended to benefit the poor disadvantaged or marginalized groups. The policy champions the right of access to affordable water services on a non-discriminatory basis providing for subsidizing first-time connection fees but not consumption.

There are several African countries with utilities that have developed social connection policies these countries include Uganda, Burkina Faso, Senegal, Cote d'Ivoire, Morocco and Gabon. In Kenya, water services providers began the

<sup>9</sup> Water Service Regulatory Rules, 2012

development and implementations of social connections policies in 2011 through the support of the World Bank's Water and Sanitation Program. Implementation of the social connection programs in Kenya was informed by the realization that one of the best ways to improve water services in low-income areas is often to provide them with access to a reliable supply through a piped network, either through a domestic connection (in the house or in the yard) or through a public stand-pipe connection. Thus, the adoption of this approach by the water services providers, is an attempt to address the existing inequalities and perceived barriers to WSS service provision.

The approach attempts to increase access to water by increasing affordability of connection costs while increasing the water services provider's customer and revenue bases. Other benefits derived by utilities and communities include use of quality pipes and fittings (which also contribute to the reduction in non-revenue water); increased affordability of initial connections; weakened water vendor cartels; improved environmental sanitation and hygiene; reduced time taken to fetch water from communal points; improved price of water; improved water quality; and reduced risks of waterborne illnesses.

Social connections programs can be financed either externally or internally using utility own finances and follows specific procedures for implementation. Based on the utilities financial disposition the following financing mechanisms may be considered:

- i) Creation of a social connection fund through:
  - a. Remitting of a percentage of the utility's monthly revenue collection into the social connection fund
  - b. Use of donations/grant to fund the social connection fund
- ii) Development of a credit facility funded by a financial institution
- iii) Social connection surcharge in the water tariff
- iv) Use of in-kind contributions (e.g. materials from project / labor from beneficiaries, or NGOs)

## CONSUMER FINANCING OPTIONS

- Lowering the price of a private connection.
- Subsidising the price of private connections.
- Post payment instalment plan and connecting the customer before the full fee is paid up; instalments can be incorporated in monthly bill.
- Advance payment instalment plan and connecting the customer after the full fee has been paid up.
- New connections loans through partnering with commercial banks and NGOs.

**FIGURE 10: SOCIAL CONNECTION PROGRAM IMPLEMENTATION CASE STUDY: NAIROBI**

| Case Study   |
|--|
| Nairobi Water and Sanitation Services Company  |
| <ul style="list-style-type: none"> <li>• Providing water by subsidizing first-time connections to Kayole Soweto population 89,600 (2200 plots).</li> <li>• Consumers are connected to the network for a small commitment fee of KShs. 1,648,</li> <li>• Balance of connection fees is recovered over agreed period of time (2yrs) as part of the monthly bill.</li> <li>• Financing is through a loan arrangement with local microfinance bank (K-Rep bank), working with Global Partnership on Output Based Aid (GPOBA) to provide subsidy.</li> <li>• Loan pays for connection costs to qualified individuals on credit.</li> <li>• Upon completion of the connection and evaluation of outputs, the OBA subsidy is released to reduce the loan amount.</li> </ul> |

#### PREPARATORY STEPS IN SOCIAL CONNECTION POLICY IMPLEMENTATION

- Establish a core team with the right skill mix (technical, finance and social)
- Undertake social economic assessments for the target beneficiaries that capture household incomes, expenditure, willingness and ability to pay data
- Design a scheme that suits the political economy, financial reality and expenditure patterns of low-income communities
- Prepare a project Implementation plan (may include network intensification activities in settlements where the primary and secondary network is non-existent).
- Capacity build the core team on the Implementation of the social connections
- Prepare the billing systems to allow for flexible payment arrangements
- Undertake community mobilization and sensitization activities
- Prepare an addendum detailing the consumer financing arrangement to be reviewed by the utility's Legal department and included in the customer contract document.
- Undertake registration of the customers based on the approved consumer financing options and customer's commitment.

- v) A single or a combination of any of the above funding mechanisms can be used to implement a social connection policy depending on the financial disposition of the utility.

### 3.6 Roles and Responsibilities of Counties/Water Service Boards and WSPs

#### 3.6.1 Roles and responsibilities of the County/ WSB in relation to the social connection policy

- Evaluation of budgets and reports prepared by the WSP in regard to the policy.
- Monitoring and evaluation of the implementation of projects funded under the social connection fund.
- Auditing the use of the informal settlements social connection fund.
- To provide technical and financial advice regarding the administration of the fund.
- Roles and responsibilities of WSPs
- To create the social connection fund.
- To sensitize the public on the existence and implementation of the fund.
- To implement the social connection policy.
- To utilise the social connections fund as ascribed in the policy.
- To identify beneficiary settlements.
- To develop an implementation programme.
- To periodically review the social connection policy.
- To provide update reports to the WSB/County.

#### 3.6.2 Criteria for selecting beneficiary settlements

Global experiences with subsidy programs have shown that the cost of defining and identifying individual, poor households is too expensive and an inefficient method of targeting subsidies. In the case of Kenya, the poor are geographically concentrated for the most part in the low income areas. In line with the geographic targeting approach, the utility should make a list of all eligible settlements, and prioritize project implementation based on the following criteria:

- High population density
- Presence of a high number of properties unconnected to water and sewer services.
- High levels of non-revenue water - above the 25 per cent acceptable limits of WASREB.
- Land ownership is either allotted by the county government, owner-occupied or government land
- Developed water and/or sewer reticulation systems
- Settlements that are either upgraded, in the process of upgrading or have a capital works program in progress.
- Settlements where block maps are available or mapping can be done easily.



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# IV. The Role of Counties in Commercial Financing of WSS sector

- How the Sector Has Been Financed
  - What are the Current Financing Needs
  - Why should Counties support WSPs in borrowing
  - Challenges facing WSPs in accessing Commercial Financing
  - Required County & Other Stakeholder Support and Approvals
- 

## 4. The Role of Counties in Commercial Financing of WSS Sector

This section builds a case for commercial financing of WSPs. It starts by examining the sources of sector financing, the existing funding gap and need to diversify these funding requirements by including commercial financing as source of funds. It also examines the challenges WSPs face when approaching lenders.

The section covers the required participation by County Governments and other stakeholders in supporting WSPs access commercial financing and provides a checklist of approvals and documentation required to aid this process.

### 4.1 How the Sector Has Been Financed

Traditionally, Kenya has relied on the following sources to finance the WSS services.

- Budgetary allocations
- Equalisation funds
- Decentralised funds
- Geographic earmarking (of donor funded projects)
- Water Services Trust Fund, grant funding
- Consumer tariffs/contribution

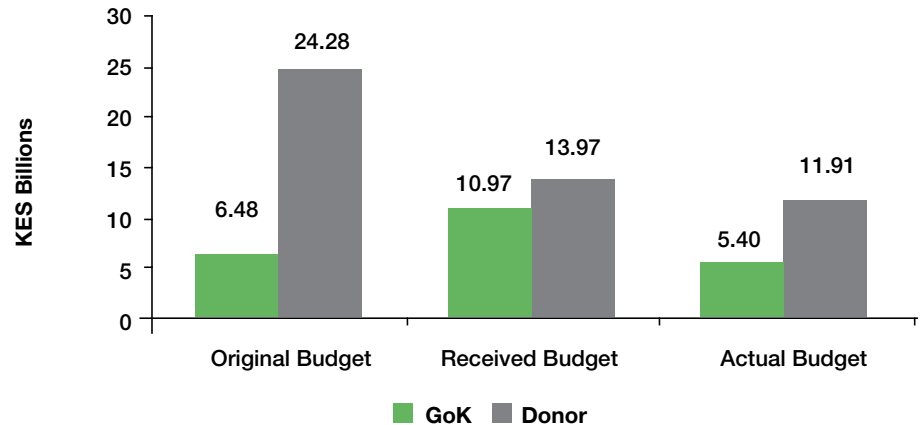
#### 4.1.1 Budgetary Allocation

The Government of Kenya allocates a portion of its annual budget towards WSS. This allocation is derived from tax revenues and/or donor financing and is crucial in meeting capital requirements of WSS projects for the country. However, the Government's annual budget also covers funding for other infrastructure projects in many different sectors and, therefore, cannot fully fund all required WSS projects. This inevitably leads to a funding gap that needs to be filled from other sources.

The Government of Kenya allocated KES. 11Bn as the gross development budget for capital investments in water services in 2014 budget. However, only KES 5.4 Bn was received, with the rest being reallocated to other sectors. This disparity in terms of the budgeted amounts and actual funds disbursed is an indicator of the inadequacy of funding from the national government to cover the financing needs for the sector.

This is discussed in further detail under section 4.2 *What are the Current Financing Needs.*

**FIGURE 11: DEVELOPMENT BUDGET BY FUNDING SOURCE 2013/14**



Source: Annual Water sector Report 2013/14

#### 4.1.2 Equalization Fund

Under the Constitution of Kenya, an Equalisation Fund has been established into which 0.5% of the annual revenue collected by the national government is paid. The national government is required to use the Equalisation Fund to provide basic services, including water, roads, health facilities and electricity, to marginalised areas so that they can benefit from the same level of service enjoyed by the rest of the nation. This funding option is therefore beneficial to the development of remote areas with poor WSS systems.

The primary source of funding for equalization fund however remains the Government. When there are competing needs, as often is the case, the fund may be underfunded.

#### 4.1.3 County Allocation

The constitution of Kenya outlines that County Governments are responsible for water and sanitation services in their respective jurisdictions. Since the promulgation of the Constitution, there has been little WSS investment funded by the counties. In financial year 2012/2013, the National Government disbursed KES 0.03Bn to the County Governments for development of water services.

Although this is supposed to come from the equitable share, most counties have received what they consider to be inadequate allocation of funds to invest in their WSS services.

#### 4.1.4 Donor Funding

Donors have been active in the development of the Kenyan WSS sector. In the 2013/2014 budget, the gross budget for capital investments in water services was KES25Bn, of which KES13.9 Bn is donor funded.

However, donor terms and conditions of lending are strict and don't always allow funds to be directed towards priority projects. Furthermore, there is a gap in coordination of donor activity at both the National and grass-root level that further exacerbates the lack of prioritization of projects.

With devolution, mechanisms of getting funding to counties are yet to be determined and operationalised.

#### 4.1.5 Water Services Trust Fund

The WSTF was established under the Water Act of 2002. This body is funded by the Government of Kenya and development finance institutions to finance the implementation of water sector projects, and is specifically focused on the poor areas. It is a vehicle that is used by the government and donors to manage grant funding to the WSS sector.

In relation to the financing needs, the fund is relatively small with a capped investment fund ceiling often insufficient to meet all the requirements of larger capital investments. Since the funding is mostly in the form of grants, there is uncertainty on availability and processes that are helpful in sieving the potential poor beneficiaries makes the fund slow in responding to urgent/emergent funding needs.

#### 4.1.6 Consumer Contribution (WSS system generated revenue)

The WSPs internal revenue generation from billings is explained earlier under section 3.4. This is imperative to the operations of the WSP and provides a key source of loan repayment from the WSPs. As explained earlier, this is a function of the water consumption (from water meters) and the respective tariffs.

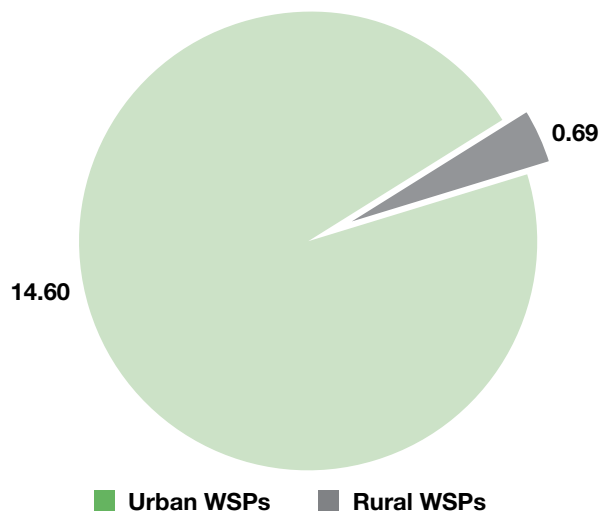
The revenue generated from the tariffs by WSPs has increased since the introduction of the water sector reforms through the enactment of the Water Act of 2002. The increase has mainly been driven by two factors: increased network expansion and billings & increases in water tariffs. Reforms have also seen the introduction of the ring-fencing of revenues collected by WSPs to remain and be reinvested back to the water sector. This resulted into more accountability.

In 2013/14, WSPs made KES. 15.31Bn in revenues. This is in contrast with KES. 7.2 Bn collected in 2009/2010 representing a compound annual growth rate of 21% per annum over the 5 year period. Most of the collections have ben from urban WSPs.

As discussed earlier, the tariffs in the water sector are set on the principle of cost-recovery. This means that tariff setting in its current form is focused on the WSP meeting its operations and maintenance cost. This provides minimal allowance for the WSP to make surpluses that could be used in reinvesting in infrastructure or servicing project financing debt.

However, WSPs can apply to WASREB for tariff increments to cater for the cost of servicing debt. Due to the public nature of water services, this process is inelastic and adjustments are tightly controlled. It is particularly important for WSPs that are keen on accessing commercial financing to demonstrate that they have excess cash flow to cover debt service.

**FIGURE 12: CONSUMER TARIFFS COLLECTED IN 2013/14 (KES BILLIONS)**



Source: WASREB Impact Report 2013/14

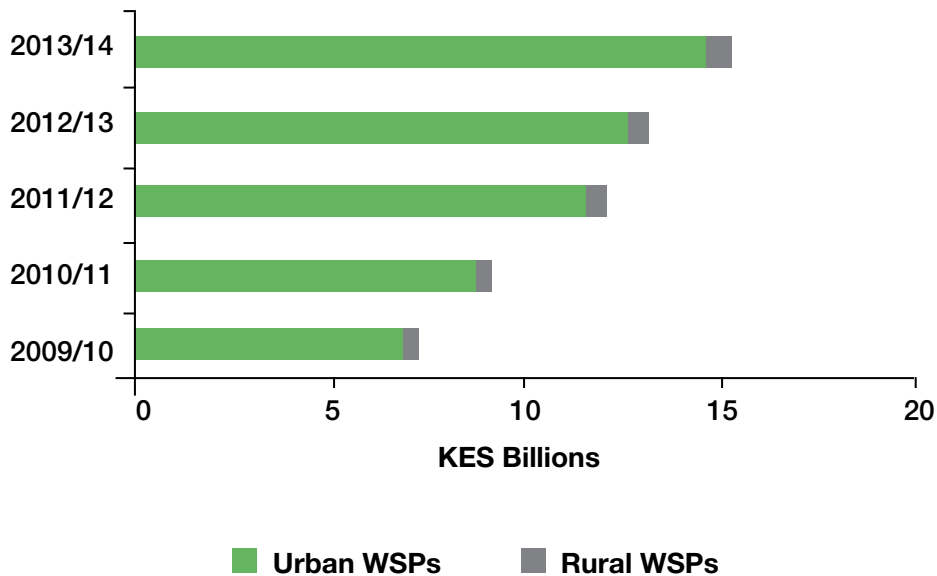
## 4.2 What are the Current Financing Needs

### 4.2.1 Available Sector Funding and Deficit

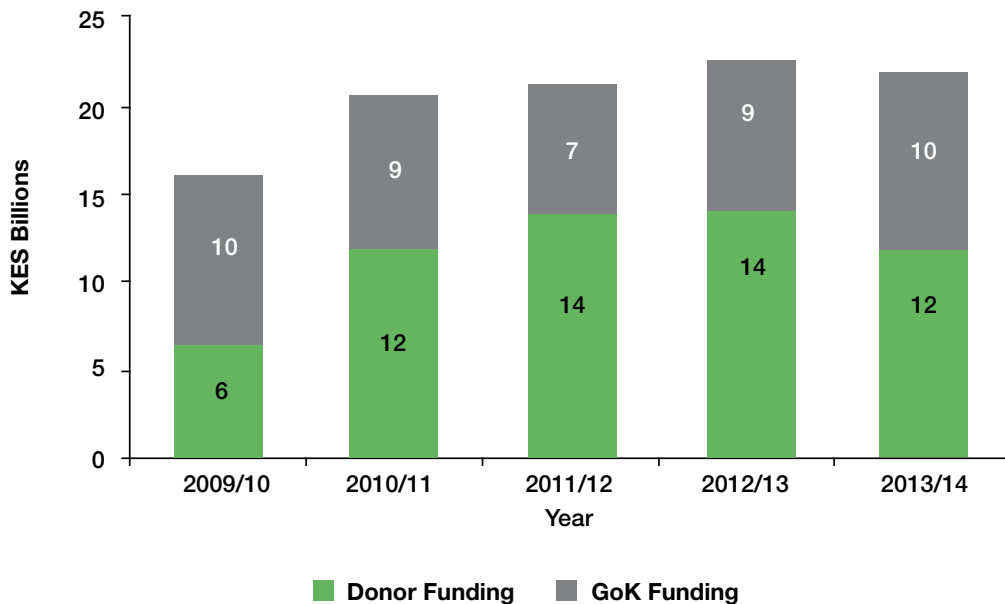
As discussed earlier the financing for WSS infrastructure has traditionally been drawn from two main sources: government budgetary support and financing from development partners. The sector’s overall financing has steadily been growing over the last 5 years from KES 16 Bn in 2009/10 to KES 22 Bn in 2013/14 as indicated in Figure 14.

The day to day running of the operations and maintenance cost for the infrastructure is usually financing by the WSP revenues about KES. 15.31 Bn in 2013/14.

**FIGURE 13: URBAN AND RURAL WSPS REVENUE COLLECTIONS**



**FIGURE 14: DONOR & GOVERNMENT OF KENYA CONTRIBUTION TO WATER SECTOR BUDGET**



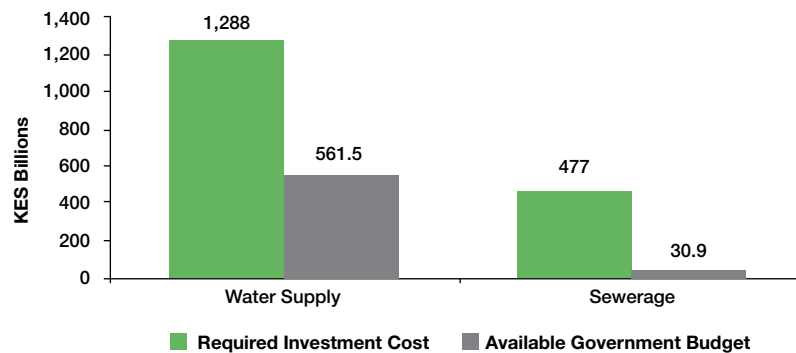
Source: Annual Water Sector Report 2013/14/ WASREB 2013/14

For the country to reach the 100% coverage, substantial investment in WSS infrastructure is required for both rehabilitation of existing infrastructure, as well as for expanding water supply and sewer connections to unserved areas. For example, over the last three years, investment in the sector has averaged about KES 20 billion against a requirement of KES 300bn required annually as discussed in the Sector Investment Plan.

Separately, to meet the country's water and sanitation financing gap, the NWMP 2030 projects an investment of KES 1,764bn (equivalent to KES 110 billion per annum) for the sector as indicated in Figure 15.

The available government budget for the water sector up to 2030 is projected at KES 1, 246 billion (or KES 80 billion per annum). This does not include financing from development partners. This analysis implies a financing gap of KES 1,172 billion for the sector. This sets the funding shortfall at 56% of the planned expenditure.

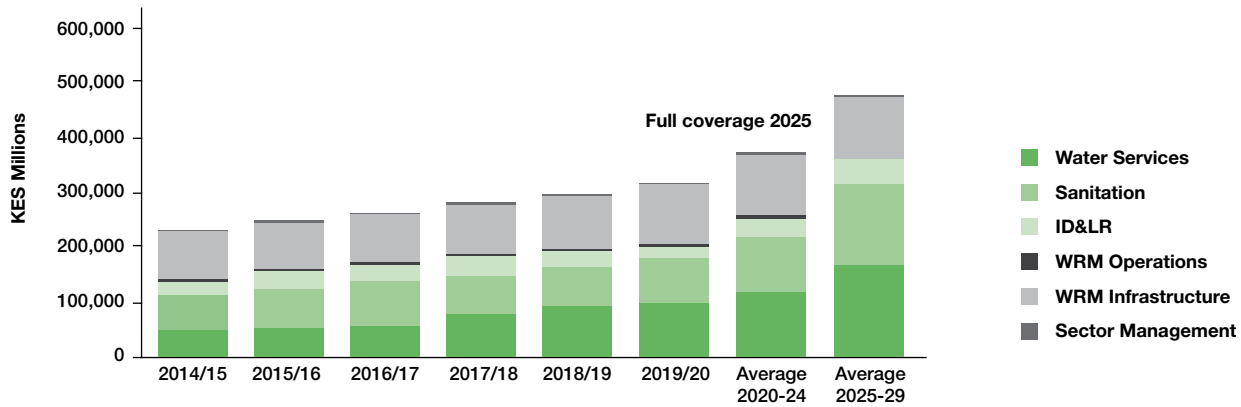
**FIGURE 15: PROJECTED INVESTMENT REQUIREMENT & AVAILABLE FINANCING**



Source: NWMP 2030

In addition, the Sector Investment Plan (SIP) projects that the total projected annual water sector expenditure will rise every year as population, coverage and service standards rise. The SIP water sector expenditure is composed of 6 areas of expenditure (see Figure 16). The project expenditure is driven by the current level of facilities, the policy targets on future coverage and level of services and the current and future water sector efficiency improvements.

**FIGURE 16: WATER SECTOR FINANCING NEEDS 2014-2025**

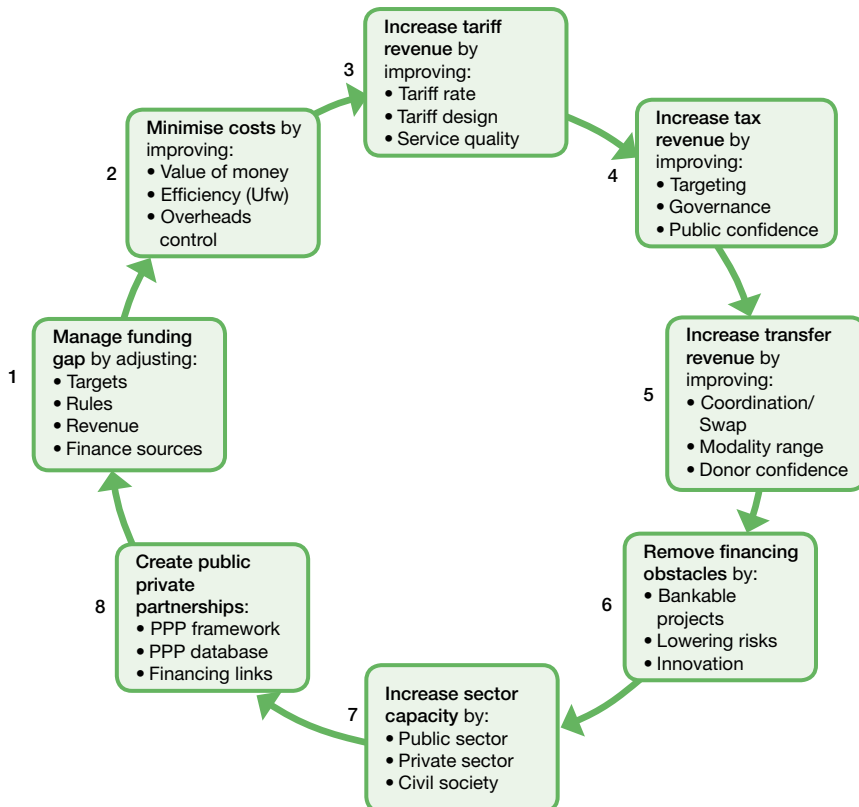


Source: MWI Sector Investment Plan

4.2.2 Bridging the Funding Deficit

The ministry has developed strategies on how to bridge the financing gap as shown in the diagram below.

**FIGURE 17: CLOSING WATER SECTOR FINANCING GAP**



The Ministry has formulated three broad strategies to meet the funding gap:

- reducing costs
- increasing revenues
- improving the enabling environment to attract new financing sources

### **Reducing Costs - Efficiency Improvements and Savings**

In meeting the financing gap, there is need to consider operational improvements in WSPs. This could be through improving Operational & Maintenance Cost Coverage, Billing and Collection Efficiency and Staff Efficiency.

### **Increasing revenues**

The Ministry's objective is to progressively increase the sector revenue in the medium to long term by raising tariffs so that they reflect the real cost of supply whilst being socially and economically affordable. The tariff reviews would include considering the affordability & willingness to pay. It is therefore important to consider social protection measures for the poor householders in addition to undertaking constant operational performance monitoring and implementing performance improvement measures so that costs for the service provision are minimized.

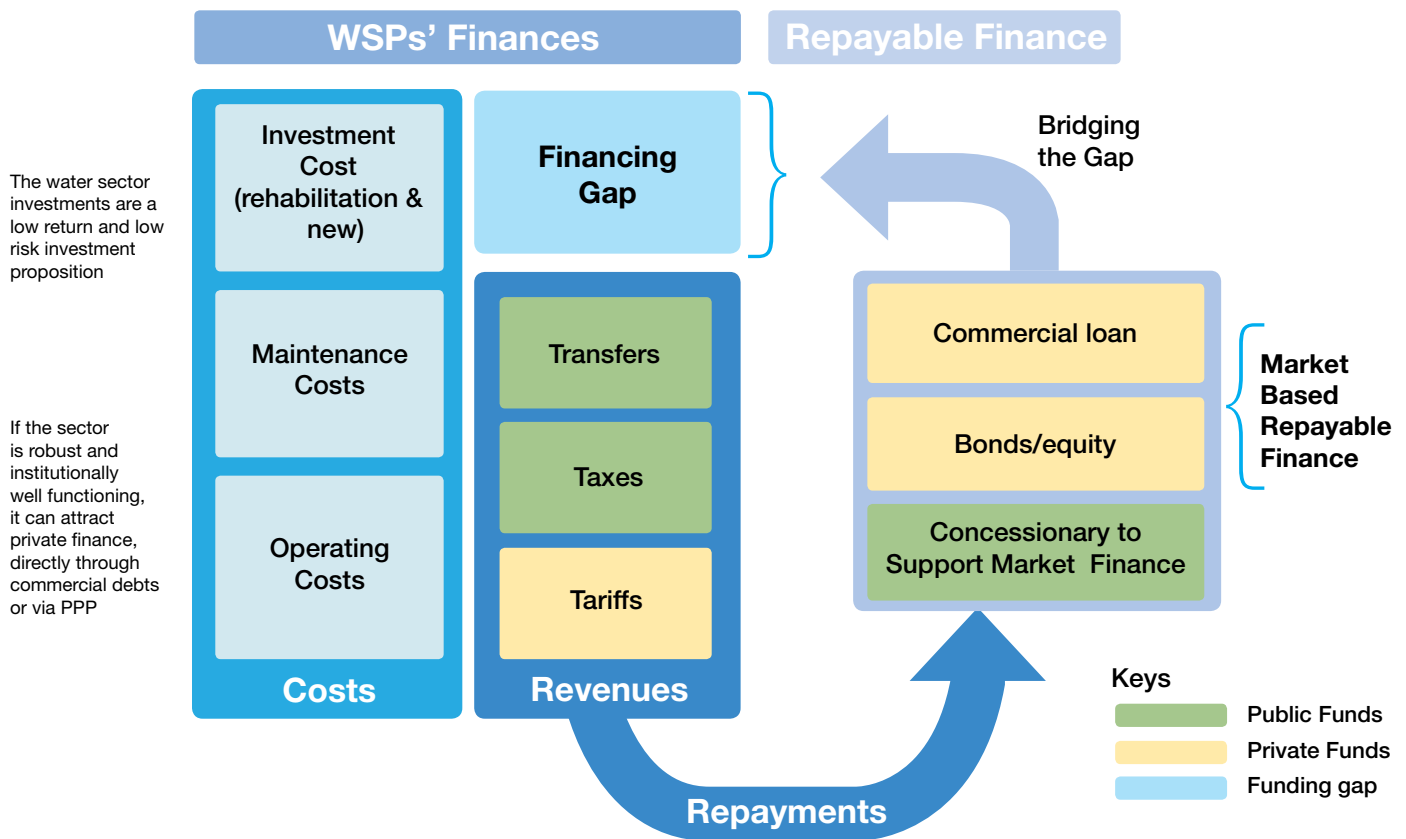
### **Improving the enabling environment to attract new sources including Private Sector Participation & Commercial Financing**

There is increasing private sector interest for financing of public infrastructure through commercial lending and other private sector participation (PSP) arrangements. This would include commercial financing for both the private and public sectors and as well as PPP structures where relevant.

This provides an opportunity for commercial banks, as shown below and as discussed overleaf, to provide commercial financing to the sector.



**FIGURE 18: NEW SOURCES OF FINANCE**



Source: Adapted from OECD (2010b)

The opportunity for commercial financing will occur as part of the repayment based finance where WSPs can directly source funds from lending institutions, which are repaid through revenues from the WSS operations

### 4.3 Why Counties should Support WSPs in Borrowing

As discussed in the sections above, lack of access to adequate financing is a challenge in the WSS sector. There is therefore an opportunity for commercial financing – a largely untapped financing source in the sector. This section covers some of the rationale for these opportunities.

#### WSPs management and enabling environment is changing to encourage commercial funding

Traditionally, the water sector has had low lender interest due to lack of sector understanding, low risk appetite and complex financing environment. There are current initiatives under way to improve the utilities performance and accountability. Year on year, the WASREB Impact Report has shown steady improvement in utilities management and financial standing. In addition, a creditworthiness analysis carried out for the 2013/14 financial year indicated

**WHY WSPs SHOULD BORROW**

- WSPs management and enabling environment is changing to encourage commercial funding
- Growing demand for WSS services show a continued business case for WSPs
- Well Regulated Sector
- WSPs are well structured
- Availability of Risk Mitigation Tools

that thirteen WSPs could be considered creditworthy with seventeen other WSPs classified as not yet creditworthy but having the potential of being creditworthy. (See separate title Creditworthiness Index Report for in-depth analysis)

In addition, the Government is promoting Public Private Partnership arrangements for WSS and a number of WSS projects are already included in the initial PPP programme. Whereas these are largely Bulk Supply schemes that are expected to be designed, financed, developed or operated by the private under a PPP programme, it is expected that project developers will raise commercial debt financing to finance part of the capital expenditure requirements. As part of this initiative, the Government is developing PPP Guidelines for the water and sanitation sector that will make it clearer and easier for the private sector to bid for and operate these programmes.

Growing demand for WSS services shows a continued business case for WSPs. With the increasing population coupled with the drive to meet the sector goals for water for all by 2030, the demand for services is expected to grow. There is therefore not only demand for new investments as discussed earlier, but also more revenues from the services delivered. The management reforms instituted through the WSS reforms of 2002 coupled with the availability of technical assistance from development partners further increases the sector's potential to generate more revenue.

**A Well-Regulated Sector**

WASREB has enforced industry-wide best practice standards in corporate governance and reporting and has made the sector more transparent and accountable. WASREB is currently incorporating creditworthiness to its annual sector capacity report.

**The WSPs are structured as companies that can borrow**

Most WSPs are registered as companies under the Companies' Act of Kenya. This requires them to operate in a semi-autonomous way with their board of directors being responsible for overseeing a management team. Under the Water Act of 2002, revenues collected by the WSPs are legally ring-fenced ensuring sustainable service provision and re-investment into the sector. This ring-fencing is likely to be continued or even enhanced in the 2014 Water Bill once enacted.

**Availability of Risk Mitigation Tool for Lenders**

In order to catalyse commercial financing for the sector, the government and development partners have developed a number of tools to help mitigate some of the risks associated with commercial lending to the sector. These tools are as follows.

- **Partial Credit Guarantees:** A government or development partner provides a partial guarantee, to the lender, should the WSP default on its obligations. In Kenya, the USAID- DCA programme is available for some lenders for water sector lending.
- **Subsidies:** A government or development partner provides a subsidy payment to the WSP if a project achieves a pre-specified level of output (e.g. connections made, water supplied, reduction in non-revenue water). Subsidies gives lenders confidence in the cash flow of WSPs, enabling reductions in collateral and shortening the average life of loans. In Kenya, the GPOBA programme by the World Bank and the Aid on Delivery (AOD) of KFW programmes are available to subsidise lending by WSPs for water projects.
- **Credit ratings:** If WSPs establish strong credit histories, they will improve their visibility and bankability with development institutions and private lenders. A current Creditworthiness Index review and shadow credit rating reports for selected utilities shows that over 30% of the WSPs surveyed were found to be credit worthy.
- **Availability of technical assistance both to the lenders and the utilities:** A World Bank-established OBA facility that allows WSPs to access technical assistance in developing projects for financing specifically for the is for pro poor WSS projects, These technical advisers are available to the banks and the utilities designing projects that would be financed through commercial lending.

### Demystifying the risks in the WSS sector

For commercial financing to take root, it requires the commercial banks to structure commercial loan products that mitigate these risks. Commercial banks are often reluctant to lend to WSPs for a number of reasons, including:

- Water is often viewed as a social good with little ability to generate financial return;
- Banks in Kenya do not lend for periods beyond seven years, whereas the useful life of water assets is often much longer;
- Water assets provide limited collateral to lenders due to low liquidation value;
- Utilities, due to limited commercial borrowing occurring in the sector, are often not conversant with the lending criteria of banks

There have been successful Commercial Bank Lending Experiences that can be replicated.

With the reforms discussed above, commercial banks have started lending to the sector. Some examples of commercial financing products in Kenya are listed in Figure 19: Example of Water Sector Commercial Financing in Kenya.

**FIGURE 19: EXAMPLE OF WATER SECTOR COMMERCIAL FINANCING IN KENYA**

| Embu Water and Sanitation Company (EWASCO)  | Nakuru Water and Sanitation Services Company (NAWASSCO)   | Kisumu Water and Sewerage Company Limited (KIWASCO)  |
|---|---|--|
| <p><b>Objective</b></p> <ul style="list-style-type: none"> <li>To install 23 kilometres of pipeline in Embu, Kenya</li> </ul> <p><b>Approach</b></p> <ul style="list-style-type: none"> <li>Commercial financing backed by a guarantee from the</li> <li>The WSP also received AoD subsidies on delivery of pre-determined indicators</li> </ul> <p><b>Result</b></p> <ul style="list-style-type: none"> <li>The utility secured KES 81.5 Million in commercial financing from a commercial bank</li> </ul> | <p><b>Objective</b></p> <ul style="list-style-type: none"> <li>To develop public, prepaid meters strategically-placed in 10 low-income settlements of Nakuru.</li> </ul> <p><b>Approach</b></p> <ul style="list-style-type: none"> <li>Combined investment of KES 23 Million from a commercial bank and WSTF. Bank provided financing for the construction of the water point bases.</li> <li>WSTF financed 15 meters, the software program and staff training.</li> </ul> <p><b>Result</b></p> <ul style="list-style-type: none"> <li>Using the standard tariff structure, NAWASSCO will recover the cost of the investment in 26 months and achieve a net present value (NPV) profitability of 72% over five years. Other benefits to NAWASSCO include: no loss of water, pre-payment, 100% collection rate, and no paper billing.</li> </ul> | <p><b>Objective</b></p> <ul style="list-style-type: none"> <li>KIWASCO completed a water treatment plant in 2011 and intended to increase water distribution. The WSP required finance for the construction of 35 Km of pipe infrastructure and the installation of 1,500 metered connections in Nyamasira.</li> </ul> <p><b>Approach</b></p> <ul style="list-style-type: none"> <li>KIWASCO received technical assistance in developing a feasibility plan and financing proposal to the bank.</li> <li>KIWASCO received for achieving the connection target, whereby the OBA pays 50% of the interest accumulated.</li> </ul> <p><b>Result</b></p> <ul style="list-style-type: none"> <li>A loan of USD 245,122 from a commercial bank with an eight month grace period and five-year repayment term.</li> </ul> |

**Focus on Public Private Partnerships (PPP)**

With the enactment of the PPP act in 2013, the national government has provided a policy framework for the private participation in the development and operation of infrastructure.

This has led to the development of a national priority list of PPP projects as indicated in Table 5. This has provided an opportunity for lenders to finance the implementation of these projects by the private sector.

A number of PPP projects that have been approved for rollout under the PPP programme.

**TABLE 5: NATIONAL PRIORITY LIST OF WATER SECTOR PPP PROJECTS**

| Project Name                                      | Contracting Authority                          | Project Description   | Cost          |
|---|--|---|---------------|
| Nairobi Bulk Water Supply                         | Athi Water Services Board (AWSB)               | Construction of Maragua and Ndaragu Dams and the supply of bulk water to Nairobi County on a PPP basis  | KES 6.8 Bn    |
| Mwache Multipurpose Dam                           | Coast Development Authority                    | Construction of a Dam with capacity of 209million m <sup>3</sup> , supply of 190,000 of m <sup>3</sup> of domestic water/ day and irrigation of 5,050Ha.  | USD 290 Mn    |
| Turkwel Downstream Irrigation                     | Kerio Valley Development Authority (KVDA)      | Development of 3,215Ha of land for irrigation   | USD 7.65 Mn   |
| Arror Multipurpose Dam                            | Kerio Valley Development Authority (KVDA)      | Construction of a Dam, generation of 80MW hydro power, irrigation of 5,000 Acres  | USD 302 Mn    |
| Munyu Multipurpose and Greater Kibwezi irrigation | Tana & Athi Water Rivers Development Authority | Construction of a Dam with 625 mil cm <sup>3</sup> , 40MW hydro power generation, 13,000Ha irrigation and water supply  | USD 1.6 Bn    |
| Tana Delta Irrigation                             | Tana & Athi Water Rivers Development Authority | Expansion of irrigation scheme from 1,763Ha to 5,000Ha to produce 24,000Metric tons of rice/annum   | Not available |
| Tana Delta Irrigation sugar project               | Tana & Athi Water Rivers Development Authority | Development of 20,000Ha of sugar fields and construction of 10,000 capacity sugar processing plant and installation of a 34MW cogeneration power plant and installation of ethanol plant with capacity of 75,000ltrs/ day | USD 120 Mn    |
| Nandi Forest Multipurpose Dam                     | Lake Basin Development Authority               | Construction of a Dam, generation of 50MW hydro power, irrigation of 7,000Ha  | USD 4.09 Mn   |
| Magwagwa Multipurpose dam                         | Lake Basin Development Authority               | Construction of dam, installation of 120MW hydro-plant, and development of 15,000Ha of irrigated land   | USD 979 Mn    |
| Murang'a Mukuyu Water Supply                      | Murang'a County                                | Expansion, Upgrading and rehabilitation of distribution networks  | Not Available |

## CHALLENGES FACING WSPs IN ACCESSING COMMERCIAL FINANCE

- Affordability Constraints
- Risk profile and difficulties in managing certain risks
- Lack of funds at decentralised level
- Short tenor of available financing
- Lack of understanding by lenders
- Lack of bankable projects

### 4.4 Challenges facing WSPs in accessing Commercial Finance Affordability Constraints

In Kenya, it may be difficult to increase tariffs to cover costs beyond a certain point for the poor. This is a particular constraint for setting connection charges, which are used usually to cover part of the costs of network expansion. If set too high, connection charges can be a significant hurdle preventing access by poor customers to the network.

Social Connections Policies covered in section 3.9 address this issue.

#### **Risk profile and Difficulties in Managing Certain Risks**

The water sector combines a number of risks which characterise infrastructure sectors. Investments in poor areas are considered particularly risky, because of assumed low collection rates and limited revenues.

Subsidies are available via the WSTF for commercially financed water projects in poor areas. Lack Will to Raise Tariffs.

Political unwillingness to raise tariffs can also be an important risk in the sector. In addition, other stakeholders, such as civil society and the business community, can block tariff increases.

Strong education campaigns and stakeholder networks, like the Kenya 2030 Water Resources Group partnership can help increase understanding and support.

#### **Lack of funds at Decentralised level**

In Kenya, the devolution of WSS services has created large investment needs among County Governments and WSPs, whereas they have limited access to financing.

Being newly set up entities, financial management systems are yet to be fully entrenched at the County level. Also, many WSPs are small and lack the creditworthiness to access commercial finance.

Technical assistance is available in some areas to creating water sector financing plans for County governments.

#### **Short Tenor of Available Financing**

Water investments are often long-term investments, whilst most commercial lenders in Kenya would mostly offer short-term borrowing horizons. Their willingness to offer longer tenors would depend on the perceived risk of the investment and the existence of investors willing to invest over the long term (such as pension funds, for example).

Subsidies and credit guarantees currently available in Kenya help banks extend loan tenors.

**Lack of understanding by Lenders**

Financiers are not familiar with the water sector, as it is often seen as very political and “difficult” due to the political nature of tariff setting and in some cases, vocal resistance to charging for water services.

A Lender’s Manual for Commercial Financing of the Water and Sanitation Sector of Kenya is available for and trainings have been delivered to many interested banks. The manual is available on WASREB’s website.

**Lack of Bankable Projects**

“Bankable” projects are few and far in between in the water sector. This may be due to lack of skill in developing commercially viable projects at WSP level, low tariffs, reliance on poor customers, etc.

The WSTF subsidy program has a technical assistance program to cover 90% of assistance needed in project design and financial structuring.

**4.5 Required County and Other Stakeholders Support & Approvals for Commercial Financing****4.5.1 Overview**

This section covers the applicable laws in determining the roles and relevant approvals required from key stakeholders, particularly how borrowing by WSPs may remain within the restrictions posed by article 212 of the Constitution.

**4.5.2 The Applicable Legal Framework**

Currently the Water Sector in Kenya is governed by the Water Act of 2002. This law underpins the legal and regulatory framework the water sector operates under.

With the promulgation of the constitution of Kenya in 2010, water service provision was devolved to the county governments. This has led to the drafting of the Water Bill of 2014 to harmonize the sector’s legal framework with the constitution. County legislatures are also required to enact County Water Acts to govern water service provision at county Level.

The adoption of the Constitution of Kenya also led to the enactment of the following laws to govern various aspects that affect the Water Sector.

- i. The County Governments Act, 2012
- ii. The Public Finance Management Act ( PFMA), 2012
- iii. Transition to Devolved Government, 2012

**4.5.3 The Borrowing Restriction**

Article 212 of the Constitution of Kenya, 2010 provides that borrowing by county governments may only be carried out with a national government guarantee as well as the county assembly’s approval. Article 260 of the Constitution further

defines borrowing as repayment of a debt using public funds. Therefore, where a debt will be repaid using public funds (whether by the county government itself or a county corporation), the restriction at article 212 aforementioned applies.

WSPs, being separate legal entities may escape the restrictions faced by county governments in borrowing directly. They however face an important restriction in that any debt they take on cannot be repaid using public funds. 'Public money' as defined at section 2 of the PFMA includes:

- All money that comes into possession of, or is distributed by, a national government;
- Money raised by a private body where it is doing so under statutory authority;
- Money held in trust for third parties by national government entities; and
- Money capable of generating liability for the Government

In order to avoid falling afoul of the borrowing restriction, the WSP has to adhere to the general conditions outlined below:

- The WSP must have its own legal personality and be capable of borrowing in its own right (such a limited liability company or a county corporation)
- The WSP must be capable of repaying any borrowing without using public funds. The company must therefore be able to generate its own revenue;
- The WSP should NOT be designated a county entity under s 5 PFMA (as such an entity is subject to further restrictions on its borrowing under s 142, PFMA);
- The WSP must be contracted, as opposed to being authorized by statute, to carry out this service and collect payment for the provision of such services.

Where the WSP meets and continues to meet conditions stipulated above, borrowing should remain within the prescriptions of the law.

#### 4.5.4 The Role of Key Stakeholders in borrowing by WSPs

The following are the key stakeholders involved in borrowing by WSPs

- Water Service Provider
- Water Services Regulatory Board
- Commercial Lenders
- The Water Services Board
- County Government
- National Government

#### **Water Service Provider**

The Constitution of Kenya (2010) provides for the devolution of water services to County Governments. This has provided for a direct relationship between County Governments and WSPs as their shareholders. The Water Bill of 2014 is to provide the legislative and regulatory framework that fully incorporates the



role of County Governments. However, the Water Bill is yet to be enacted and the WSS services continue to be delivered under the Water Act of 2002 where WSPs act as agents of WSBs. By virtue of section 53 (1) of the Water Act, the WSPs are agents of the WSB to provide water and sanitation services.

The WSPs have various obligations with regard to commercial financing which include:

- To avoid liability for national government; this means that the WSPs assets, which are held on behalf of the public, cannot be charged;
- To apply for financing and adhere to the terms of the lender, using the funds for the purposes of developing and implementing water supply projects;
- To repay the loan without resorting to public funds, and ring-fence its revenue account in order to achieve this purpose;
- As the agent of the WSB, to obtain the approval of the WSB in order to apply for funds;
- To follow all relevant provisions of the law in sourcing and applying the funds (e.g. public procurement law).

### **Water Services Regulatory Board**

WASREB is established under section 46 of the Water Act.

- Section 47 (a) of the Water Act provides that WASREB shall issue licences for the provision of water services.
- WASREB is also obliged to approve the agreement between the WSB and the WSP for the provision of water and sanitation services.
- Another function of WASREB is to issue guidelines on tariff setting and determine fees, charges, levies, premiums and other charges to be imposed for water services; as provided for under section 47 (g) and (o) of the Water Act.

### **Commercial Lender**

The Lender's interest in safeguarding the borrowing restriction is to ensure that its loan agreement is not tainted with illegality. The principle of illegality operates to render a contract so tainted unenforceable. A lender has to ensure the WSP approaching them for financing satisfies the conditions set out earlier in Section 4.5.3.

### **Water Services Boards**

Section 51 of the Water Act establishes Water Service Boards, which are responsible for the provision of water and sewerage services within their areas of coverage and are licensed by WASREB. Whilst the Constitution of Kenya 2010 now assigns this to County Governments, the legal framework regulating water service provision has not been amended accordingly. The role of the WSBs therefore overlaps with that of the County Governments. Our advice here is therefore provided in light of the existing legislative and institutional framework.

Section 55 (1) of the Water Act provides that a WSB may arrange for the exercise and performance of all or any of its powers and functions under its licence to

provide water and sanitation services by one or more agents, to be known as water service providers. The WSBs being principals of WSPs with regard to provision of water and sanitation services, the WSBs role is to approve/authorize the borrowing by WSP to access additional funds.

WSBs are also permitted under section 55 (5) of the Water Act to contract other WSPs to service the same area of supply; the WSB should not contract other WSPs in regards to the same area for the life of any loan taken by the WSP. This will facilitate the generation of more revenue by the WSP thereby enabling it to repay the loan on time.

WSBs are also obliged to enter into service provision agreements with WSPs that include but not limited to the supply area, development, rehabilitation and maintenance of water and sewerage facilities of the WSBs.

According to section 73 of the Water Act, the WSBs are responsible for the review of the water services tariffs proposals from WSP before submission to WASREB for consideration.

### **County Government**

County Governments get their mandate to provide water and sanitation services from the Fourth Schedule of the Constitution of Kenya 2010, pursuant to article 185 (2), 186 (1) and 187 (2) and the County Governments Act 2012.

County Governments contract WSPs to provide water and sanitation services under section 6 (2) of County Government Act which provides that a County Government has all the powers necessary including entering into contracts for the discharge of its functions. The PMFA establishes county corporations under section 182 as read together with section 2 for the purpose of carrying out the County Government's mandate.

As the successor to municipalities (shareholders of WSPs), County Governments should respect ring-fencing arrangements.

County Governments should ensure that county corporations are NOT declared as county entities so that additional borrowing restrictions under section 142 of the PFMA restrictions do not apply.

### **National Government**

The National Government plays no role in the commercial financing process. For the remainder of the stakeholders, their interest is in ensuring that commercial financing does not incur any liability for the National Government in order not to breach the borrowing restriction.

#### 4.5.5 Checklist of Required Approvals & Documentation

In performing its due diligence, County Governments will be concerned with whether the WSP is operating legally and whether it has sufficient authority to borrow. County governments should review the following:

##### Operational

- **Memorandum and Articles of Association for the WSP concerned** – In this document the county government would look at whether the WSP board is empowered to borrow and the modalities in place for approval of borrowing.
- **The license granted to the WSP by WASREB for the provision of water services:** This will determine whether the WSP is duly licensed as a WSP
- **The Service Provision Agreement (SPA) between the WSB and the WSP in relation to the provision of water services:** The agreement will be useful in determining the length of time the WSP can provide services prior to application of renewal and the service area within which the WSP can operate.
- **WASREB approval of Tariff increment:** This is if the WSP has applied for a tariff increment to enable it meet the financing costs.
- Any agreement between the County Government and the WSP concerned to ensure that no conflict arise due to preceding agreements.

##### Authority to borrow

- **The WSP's Board of Directors authority to borrow:** A template for this board resolution has been provided in Appendix 7: *Water Service Provider Approval Template for Borrowing by Board of Directors*.
- **Approval from the WSB for the WSP's borrowing:** This approval will include the WSB acknowledgement that the WSP is borrowing and will also provide assurance that the WSB will renew the SPA over the life of the loan. A template for this approval has been provided in Appendix 8: *Water Service Board Approval Template for Borrowing by WSB*.
- **Approval from the County Government for the WSP's borrowing:** A template for this approval is provided in Appendix 6: *County Government Approval Template for Borrowing*.
- County Water Act (if one exists) or Water Bill if legislation is pending.

##### Comfort

- WASREB guidelines/directives on tariffs for the area concerned;
- WSB/County Government agreement on ring-fencing, service exclusivity for life of loan (Draft Memorandum of Understanding in Appendix 5);
- If the WSP has applied for subsidy under the World Bank's OBA programme or KFW's Aid- On delivery (AOD) programme, Letter of Approval of subsidy from WSTF would be required.

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# V.

## The Borrowing Process

- Project Appraisal: Understanding how WSPs develop financeable projects
  - Borrowing Process for WSPs
- 

### 5. Introduction to Commercial Borrowing for WSPs

This section provides a discussion on the key aspects counties needs to consider internally in appraising a project's viability prior to going to the market.

It also covers the typical procedures a WSP can follow to borrow from the lender.

#### 5.1 Project Appraisal: Understanding how WSPs develop financeable projects

##### 5.1.1 Overview

A project appraisal entails a validation of the project feasibility study. Following project appraisal and loan approval, the WSP carries out the final detailed designs and costing of the project prior to implementation. The following section covers the analysis of a project's bankability.

This section of the toolkit will provide a Project Appraisal - Due Diligence Checklist: This will give an overview of the important aspects of the project that require an appraisal with an accompanying set of key considerations.

The project due diligence checklist can be used by counties to determine if the project meets key eligibility criteria for commercial financing

##### 5.1.2 Project Appraisal - Due Diligence Checklist

###### **Institutional Analysis**

Institutional analysis helps in assessment of the strengths and weaknesses of the WSP, and determines whether the strengths offset any weaknesses, and if not, if there are specific measures that should be implemented prior to loan approval. Key indicators are:

- Vision - Does the WSP have a clearly stated vision that is widely known to its staff? The vision should provide a futuristic picture of what the utility wants to attain and the staff should be able to state it.

- Goals - Does the WSP's business plan or other planning documents describe short to medium term goals? Ideally, goals should be specific, measurable and time-bound.
- Cultural values - Interview staff on the presence of employee unions or employee associations and determine whether their objectives are aligned with that of the WSP
- Structures, systems and processes – Compare the actual organizational structure to the recent structure approved by the WSP's board and get reasons for any deviation.
- Resources - Check management and other level of staff qualifications vis-à-vis their position.
- External relations - Check with various stakeholders outside the WSP to determine the goodwill (or lack of it) that the WSP has built over the years. These will include WASREB, WSTF, depository banks, WSB officials, media, suppliers/contractors and customers.

### Technical and Operational Soundness

The project should be able to address the problems identified in the feasibility study. Technical appraisal of WSS projects may require the lender to hire a consulting engineer to review the technical aspects of feasibility study.

The appraisal team needs to answer the following questions;

- Is there a balance between water source capacity and facilities, and the average day or peak hour demand regardless of the level of water losses?
- Is the pipe network appropriately sized to maintain minimum and maximum pressures?
- Is there a study on identifying and segregating the causes of non-revenue water? Are the recommended corrective measures relevant to the identified causes of NRW?
- Is the project technically feasible in the proposed project site?
- Is the technology appropriate for the present level of expertise of the WSP? Will it require capacity building and staff training?

### Financial Sustainability & Project Cost Analysis

The project should be able to generate sufficient income to cater for the capital outlay and operational & maintenance costs of running the project.

In reviewing project costs, the following are key areas of emphasis:

- Quantities reflected in cost estimates should be reflected in the preliminary design of works and facilities presented in the feasibility study.
- Level of detail of estimation should be checked. Basis of cost estimation for single items costing more than 10% should be evaluated further.
- Lump sum items should be scrutinized. Review the breakdown of these costs if they are a significant component of the total project cost.
- Check assumptions/references for unit costs.

### DUE DILIGENCE CHECK LIST FOR PROJECT APPRAISAL

- Institutional Analysis
- Technical and Operational soundness
- Financial Sustainability & Project Cost Analysis
- Social and political soundness
- Environmental factors
- Proposed Implementation plan
- Legal & Regulatory Approval

Source: USAID Water Supply Appraisal Guide Book

In reviewing Financial Sustainability, key areas of appraisal include:

- Is the projected number of connections consistent with the market survey and population growth of the locality?
- Is the projected increase in consumption consistent with the existing consumption pattern of the locality and/or similar communities?
- Does the tariff structure provide enough revenue for O&M, debt service, reserves and taxes? If not, are future tariff increases (size and timing) identified.
- Has the WSP presented the project and planned tariff structure to its customers through a public hearing? Has WASREB approved the proposed tariff structure? Is there a clear strategy on how to obtain approvals for the tariff increase?
- In the case of default or events leading to default, are there available interventions to correct or avert the situation?

### **Social and Political Soundness**

The community and its opinion leaders must support the project prior to its implementation. The following will form part of the key appraisal queries that will help determine stakeholder support for the project:

- Does the project address the priority needs of the locality?
- What is the perception of customers as to the present quality of service delivered to them?
- Are there programs by the WSP to promote “project ownership” by the community through involving local labour during project construction?
- Does the WSP have an advocacy program to win the support of local leadership for the program?

### **Environmental**

In carrying out the environmental impact due diligence, the lender must ensure that the WSP has commissioned a formal environmental impact assessment of the project and has submitted this study to the National Environmental Authority (NEMA) for approval. Banks must understand if:

- The project will require an environmental impact assessment and environmental clearance?
- The implementation of the project will produce environmental damage? What measures can be taken to mitigate the effects? Would the mitigation measures be sufficient?

### **Project Implementation**

- Can the project be implemented any time during the year, regardless of the season?
- Will the project be implemented by the WSP or by a contractor?
- Is the project size attractive to contractors? How will the required equipment and expertise be made available?

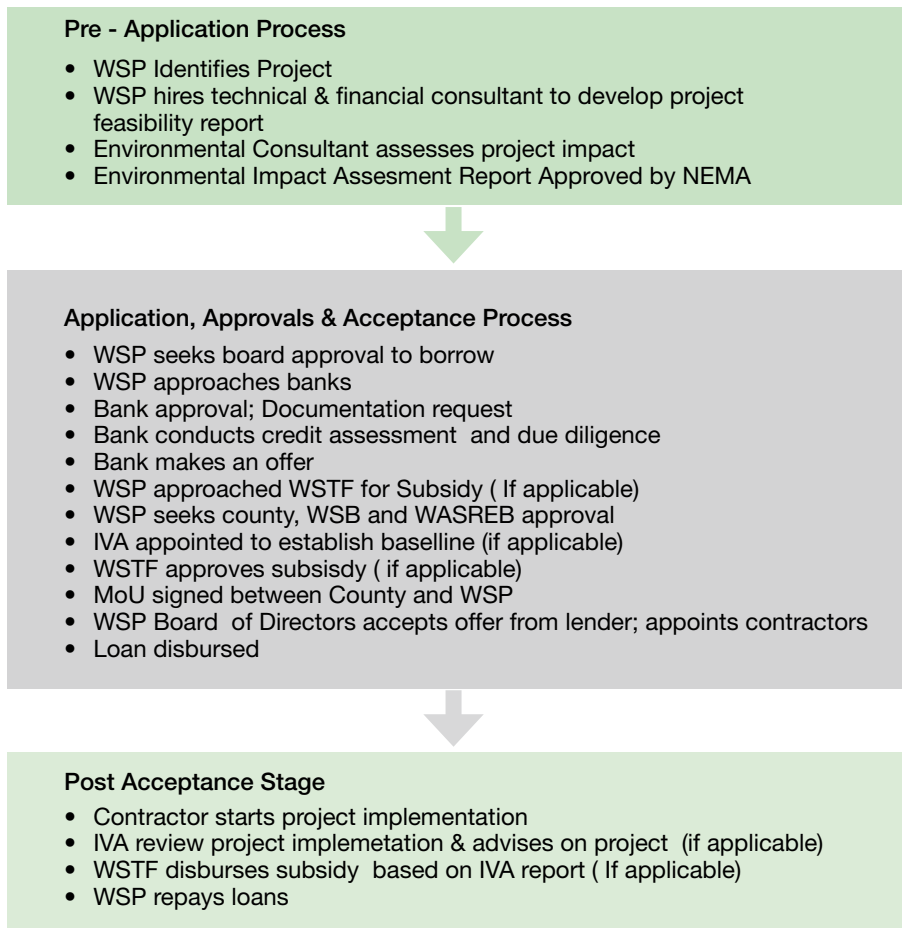
- Does the WSP have the technical expertise to supervise the project's implementation or will it hire services for project supervision?
- How will outside services be procured? Is there an existing procurement procedure? Does the WSP adhere to the procurement regulations for public entities as stipulated by law?
- Does the project estimate provide for price and quantity contingencies?
- Is there an officer or project management unit to provide progress reports and feedback on the project's progress?

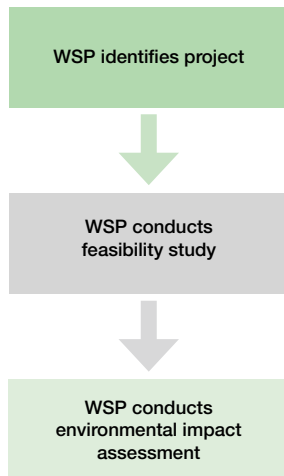
## 5.2 Borrowing Process for WSPs

### 5.2.1 Borrowing cycle

Introduction of private financing into the current system dominated by government financing will depend on the implementation of a sound borrowing cycle which determines the future flow of earnings and their stability. The envisaged commercial financing borrowing cycle to WSPs is shown in Figure 20.

**FIGURE 20: THE BORROWING CYCLE**



**FIGURE 21: PRE-APPLICATION PROCESS**

### 5.2.2 Pre-Application Process

#### Project Identification

The process of commercial lending starts with the WSP identifying a WSS project to be developed based on their prevailing service needs. To do this, the WSPs often conduct a user survey to identify what gaps there are in their performance and capacity provision.

The WSP needs to consider whether the project will address the current needs of the population. Careful consideration of different alternatives is therefore important to find the best fit and enable the WSP to save on expenditure.

#### Feasibility Study

In this phase the WSP prepares a project feasibility report that includes an updated business plan covering how the project fits within the business plan of the utility.

In assessing the viability of a project, the WSP would often hire a Financial & Technical consultant to assist in conducting a feasibility study and developing a business plan that may be used in the loan application process with the lender.

In appraising the project, the lender should ensure that it covers the following areas comprehensively:

- Institutional Analysis
- Technical and Operational Soundness
- Financial Sustainability & Project Cost Analysis
- Social and political soundness
- Environmental factors
- Proposed Implementation plan
- Legal & Regulatory Approval

The lender then focuses on the financial viability judging this on the following parameters:

- Total estimated cost of the project
- Financing of the project in terms of its capital structure, debt equity ratio and the WSP's share of total cost
- Projected cash flow and profitability
- Sensitivity in the repayments capability to the following factors
- Time delay
- Acute reduction/slowing of sales
- Sensitivity to cost overruns (small or large)
- Impact on the overall tariffs
- Financiability including debt service



## Environmental Impact Assessment (EIA)

The WSP often requires the hiring of a consultant to conduct an Environmental Impact Assessment of the project. The EIA report will then be submitted to National Environmental Management Authority (NEMA) for approval.

**FIGURE 22: DOCUMENTATION REQUIRED PRE-APPLICATION STAGE**



### Tapping Technical Assistance to Develop the Project Feasibility

As part of the loan application process, WSPs can commission external technical advisers assist them in developing a feasibility study and business plan. The scope for the technical advisers would include reviewing various aspects of the project including:

- Technical project justification and operational soundness. This includes reviewing the demand gap to be met from the project execution
- Cost analysis
- Social and political soundness
- Environmental factors
- Proposed Implementation plan
- Recommendations an project monitoring e.t.c

This tool kit includes a list of technical consultants from whom the WSPs can select appropriate advisers.

WSPs can also access subsidies that cater for up to 90% of the costs of hiring consultants through the WSTF.

### 5.2.3 Application, Approvals & Acceptance Process

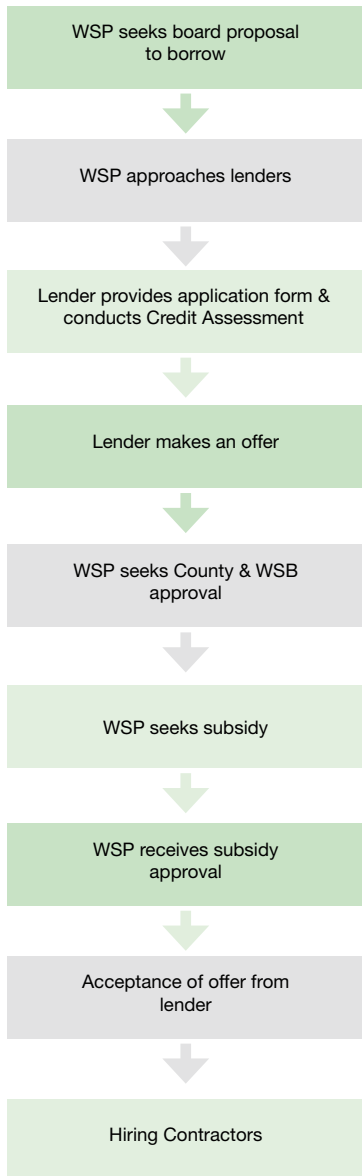
#### 1. WSP seeks board approval to borrow

- The management of the WSP would seek approval for commercial borrowing from its board of directors.

#### 2. WSP approaches lenders

- The WSP conducts a market sounding by sending the project to different lenders to gauge their appetite to lend. Utilities then formally approach banks through the floatation of a tender. A direct request can be done if preferable candidates have been identified for the award.
- The floatation of a tender from the WSP inviting expressions of interest and sending a request for proposal (RFP) to shortlisted lenders along with an information memorandum covering a high level overview of the project.

**FIGURE 23: LOAN APPLICATION, APPROVALS AND ACCEPTANCE PROCESS**



- Lenders respond to the RFP by providing a draft term sheet covering key variables such as the term, interest rate, switching costs, hedging options etc
  - A draft RFP can be found in Appendix 3: *Request for Funding Proposal Template*.

**3. Lender provides application form & conducts Credit Assessment**

- The Lender would provide the application forms and documentation requests to the WSPs.
- Lender analyzes WSPs feasibility study and financials to determine the ability to repay debt.
- Apart from the information provided by the WSP, the lender can access key operational and financial indicators in WASREB’s annual Impact Report. This report will also include a creditworthiness index that will rank WSPs based on the performance on a basket of indicators that will be used to determine the WSP’s creditworthiness.

**4. Lender makes an offer**

- On strength of its credit analysis, the lender makes a loan offer. In determining the spread over the base lending rate, the lender should also review the effect of the following risk mitigation tools employed:
  - The subsidy offered to the WSP in repayment of the debt. In Kenya, the World Bank and KFW have the OBA and AOD programmes respectively
  - Guarantee facilities that the lender may have that will seek to have the debt underwritten by a guarantor. In Kenya the DCA guarantee is offered by USAID.

The subsidy and guarantee programmes are covered in section 4.3 *Why Counties should Support WSPs in Borrowing*.

**5. WSP seeks County and WSB approval**

- County and WSB approval looks at whether all requirements have been met and that all regulations have been adhered to in order to facilitate the funding.
- The Approvals will indicate the awareness of the WSB and the County of the borrowing process the WSP and its approval of the process.

**6. WSP seeks subsidy facility**

- This process is only necessary where the WSP is seeking subsidy support from WSTF under the OBA programme or from KFW under the AOD programme.
- Baselines are determined by.
- If needed, WSP can request financial, technical or environmental technical assistance from WSTR.

**7. WSP receives subsidy approval (if applicable)**

- The WSP (if applicable) will receive an approval for the subsidy from the WSTF.
- Subsidy approval will entail the verification of the project crossing pre-set milestones will have prior to disbursements. The verification will take the form of physical inspection in the field by qualified technicians or engineers and can take up to 30-60 days.

**8. WSP Board accepts offer from lender**

- WSP Board in conjunction with the lender must agree on terms of association. This occurs after the lenders have provided the requested amount and further agreements have been made on how the loan is going to be drawn-down.

**9. WSP appoints contractors**

- WSPs are required to appoint independent contractors from a transparent and fair vetting process. This will not be necessary if the WSP is using its own manpower and resources for the project.
- WSPs owned by County Governments must follow the procurement rules described in the Public Procurement and Disposal Act of 2005 and associated rules and regulations. They must also adhere to World Bank procurement rules if they have applied for OBA subsidy or technical assistance.

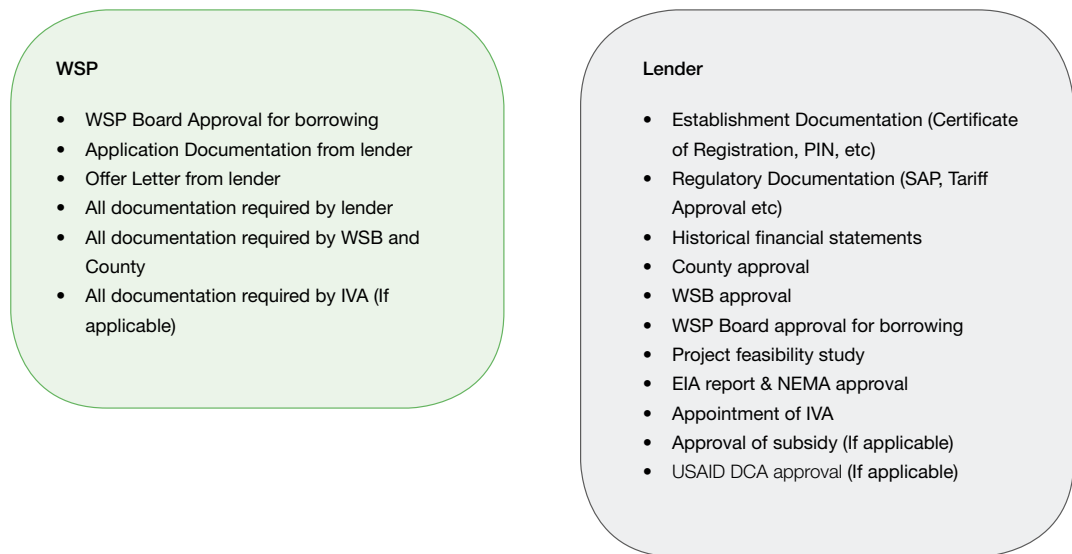
Key guiding principles for procurements managed by WSPs are:

- o Transparency in the procurement process and in the implementation of procurement contracts.
- o Competitiveness by extending equal opportunity to eligible and qualified companies.
- o Streamlined procurement process.
- o Accountability of public officials directly or indirectly involved in the procurement process and implementation of procurement contracts and the private parties awarded contracts.
- Public monitoring of the procurement process and the implementation of awarded contracts.
- If the WSP had previously acquired contractors, they are required to produce a statement of works from previous assignments and any other documentation from previous works.

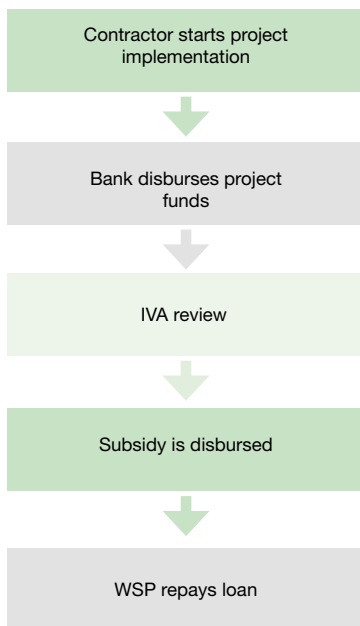
**Loan Disbursement**

- After the required conditions have been met and document submissions finalized, the loan shall be disbursed.

**FIGURE 24: DOCUMENTATION REQUIRED: APPLICATION, APPROVALS & ACCEPTANCE PROCESS**



**FIGURE 25: POST- ACCEPTANCE**



5.2.4 Post-Acceptance

**1. Contractor starts project implementation**

- The appointed contractor begins the job once the loan facility has been fully approved.
- A Project Implementation Plan will be drawn up before any finances are transferred. The implementation plan is used a yardstick of to measure the progress in implementing the project by the lender.

**2. Bank disburses based project funds**

- Project funds will not be paid directly to the WSPs. They will be domiciled in an account where outflows are made based on approvals from both the WSP and the lender. The project disbursements should be made directly to the contractor on the basis of issuance of certificates of competition.

**3. IVA reviews project implementation & advises on project milestones being met and subsidy target being met**

- IVA reviews the project based on the baseline survey carried out to ensure that it meets the output targets set to qualify for the subsidy.

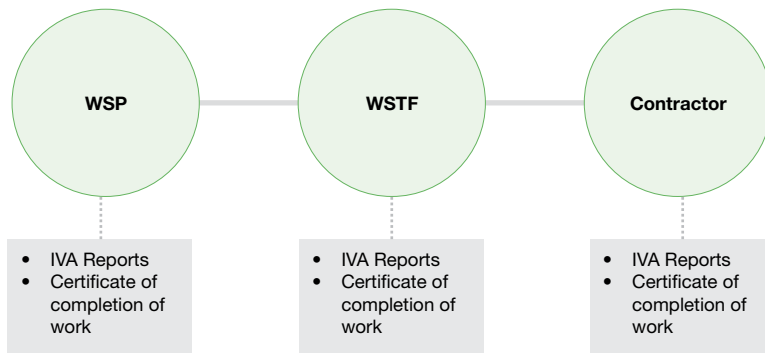
**4. Subsidy disbursed based on IVA report**

- The subsidy will be disbursed based on pro-poor targets set when the baseline was determined.

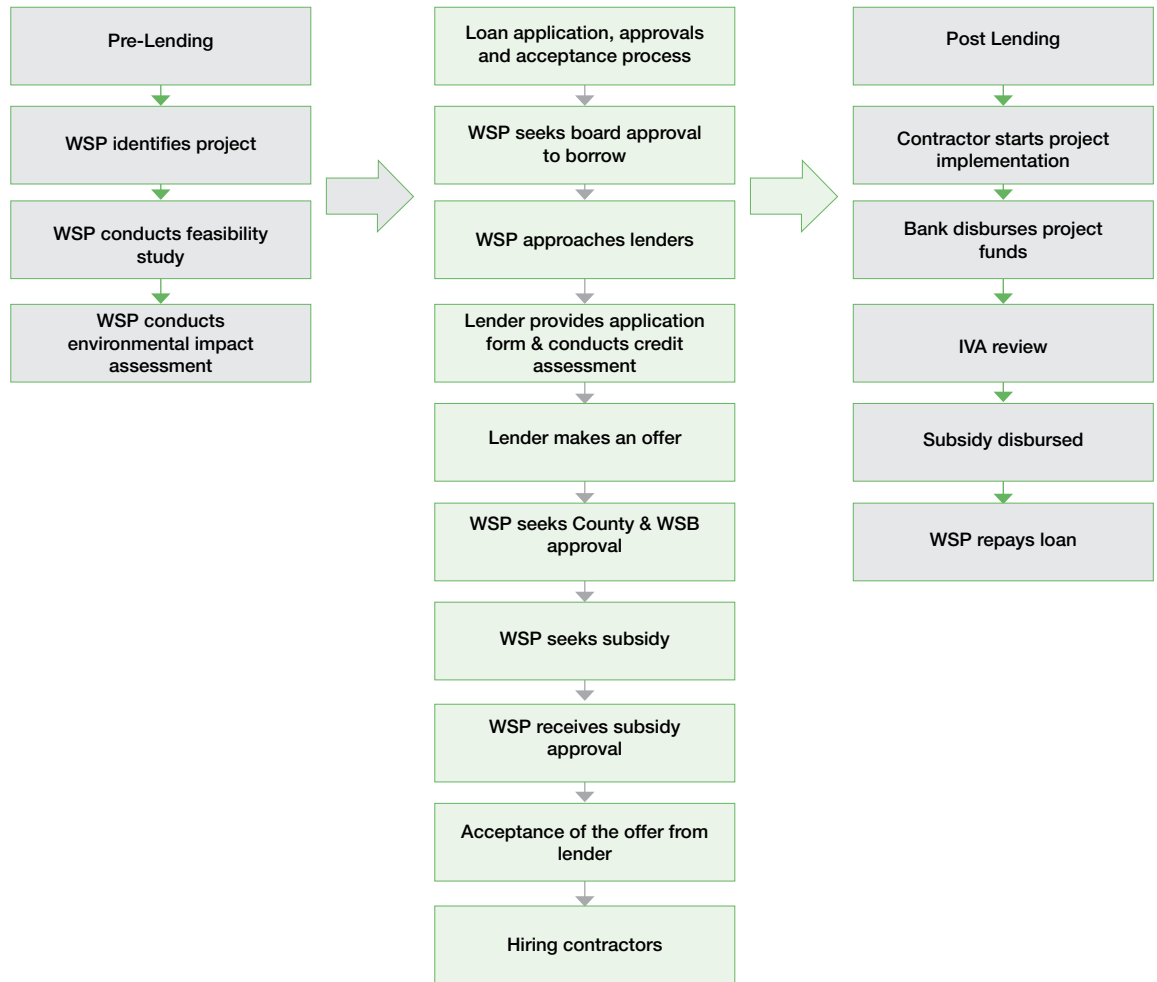
### 5. WSP repays loans

- WSP repays the loan upon the expiry of the moratorium period agreed with the lender.
- Payments could be monthly, quarterly, semi-annually or annually depending with the lenders agreement. Non-payment of these debts might ultimately call for a bankruptcy petition filed by either financier.

**FIGURE 26: DOCUMENTATION REQUIRED: POST-ACCEPTANCE**



**FIGURE 27: SUMMARY OF BORROWING PROCESS**



# VI. Appendices

- Appendix 1: Roles and Responsibilities per the 2002 Water Act
- Appendix 2: List of Water Service Providers
- Appendix 3: Request for Funding Proposal Template
- Appendix 4: Sample WSP Memorandum & Articles of Association
- Appendix 5: Sample Memorandum of Understanding between County Government, WSB, WSP & WSTF
- Appendix 6: County Government Approval Template for Borrowing
- Appendix 7: Water Service Provider Approval Template for Borrowing by Board of Directors
- Appendix 8: Water Service Board Approval Template for Borrowing by WSB
- Appendix 9: WSP Capacity Diagnostic Assessment Tool

All document templates in this section can be downloaded from the regulator's website [www.wasreb.go.ke/publications](http://www.wasreb.go.ke/publications)

## 6. Appendices

### 6.1 Appendix 1: Roles & Responsibilities of Water Sector Institutions

The table below shows the functions as envisaged per the 2002 Water Act.

**TABLE 6: WATER SECTOR INSTITUTIONS**

| Institution                                | Roles & Responsibilities  |
|--|---|
| Ministry of Water and Irrigation           | <ul style="list-style-type: none"> <li>• Development of legislation and policy</li> <li>• Strategy formulation</li> <li>• Sector coordination and guidance</li> <li>• Financing, monitoring and evaluation.</li> </ul>  |
| Water Resource Management Authority (WRMA) | <ul style="list-style-type: none"> <li>• Implementation of policies and strategies relating to management of water resources</li> <li>• Development of catchment level management strategies, including appointment of catchment area advisory committees and their facilitation.</li> </ul>  |
| Water Services Regulatory Board (WASREB)   | <ul style="list-style-type: none"> <li>• Overseeing the implementation of policies and strategies relating to provision of water and sanitation services</li> <li>• Regulating the provision of water supply and sewerage services</li> <li>• Licensing water services boards and approving their appointed water services providers.</li> <li>• Monitoring the performance of WSBs and WSPs</li> </ul>                                   |
| Water Services Boards (WSBs)               | <ul style="list-style-type: none"> <li>• Responsible for contracting WSPs to provide water services within their jurisdiction.</li> <li>• Responsible for the development of WSS assets, investment planning and implementation within their area of jurisdiction</li> <li>• Responsible for Rehabilitation and replacement of infrastructure</li> <li>• Responsible for procurement and leasing water and sewerage facilities</li> </ul> |
| Water Service Providers (WSPs)             | <ul style="list-style-type: none"> <li>• Provision of water and sanitation services, ensuring good customer relations and sensitization, adequate maintenance of assets and reaching a performance level set by regulation</li> </ul>   |
| Water Services Trust Fund (WSTF)           | <ul style="list-style-type: none"> <li>• Assisting in the financing of provision of water services in areas that are inadequately provided for.</li> </ul>  |
| Water Appeals Board (WAB)                  | <ul style="list-style-type: none"> <li>• Arbitration of water related disputes and conflicts between institutions and organization</li> </ul>   |

| Institution   | Roles & Responsibilities   |
|---|--|
| National Water Conservation & Pipeline Corporation (NWCP) | <ul style="list-style-type: none"> <li>Mandated to develop state schemes i.e. construction of dams and water pans; development of canals; flood control works and drilling of boreholes</li> </ul> |
| Kenya Water Institute (KEWI)                              | <ul style="list-style-type: none"> <li>To provide the sector with Training for water professionals and research</li> </ul>   |
| Catchment Area Advisory Committees (CAAC)                 | <ul style="list-style-type: none"> <li>Advises on water allocation at water catchment level and resolves disputes over water</li> </ul>  |
| Water Resource User Associations (WRUA)                   | <ul style="list-style-type: none"> <li>Provides a Forum for conflict resolution and cooperative management of water resources in designated catchment areas</li> </ul>                             |

## 6.2 Appendix 2: Water Service Providers in Kenya

| WSPs in Kenya (100) |                 |                |                  |                  |               |                    |
|---------------------|-----------------|----------------|------------------|------------------|---------------|--------------------|
| Urban (65)          |                 |                |                  | Rural (35)       |               |                    |
| Very Large (5)      | Large (19)      | Medium (13)    | Small (25)       | Large (9)        | Medium (6)    | Small (10)         |
| 1. Nairobi          | 1. Nzoia        | 1. Ruiru Juja  | 1. Naivasha      | 1. Othaya        | 1. Gatanga    | 1. Nyandarua       |
| 2. Mombasa          | 2. Nyeri        | 2. Machakos    | 2. Kapsabet      | Mukuruweni       | 2. Ngagaka    | 2. Murugi          |
| 3. Eldoret          | 3. Kakamega     | 3. Kiambu      | Nandi            | 2. Murang'a      | 3. Nithi      | Mugumango          |
| 4. Nakuru           | 4. Kirinyaga    | 4. Isiolo      | 3. Kibwezi       | South            | 4. Githunguri | 3. Embe            |
| 5. Thika            | 5. Malindi      | 5. Limuru      | Makindu          | 3. Gatundu South | 5. Kyeni      | 4. Muthambi 4K     |
| 6. Limited          | 6. Mathira      | 6. Nol Turesh  | 4. Gulf          | 4. Kahuti        | 6. Tuuru      | 5. Rukanga         |
|                     | 7. Nakuru Rural | Loitoktok      | 5. Karuri        | 5. Imetha        |               | 6. Ndaragwa        |
|                     | 8. Kilifi       | 7. South       | 6. Nyanas        | 6. Tetu Abadare  |               | 7. Kikanamuka      |
|                     | 9. Tilibei      | Nyanza         | 7. Lamu          | 7. Karimenu      |               | 8. Mawingo         |
|                     | 10. Kisumu      | 8. Mavoko      | 8. Kiambere      | 8. Gatamathi     |               | 9. Nyasare         |
|                     | 11. Embu        | 9. Kitui       | Mwingi           | 9. Ngandori      |               | 10. Kathiani       |
|                     | 12. Kericho     | 10. Oloolaiser | 9. Eldama Ravine | Nginda           |               | 11. Tachasis       |
|                     | 13. Gusii       | 11. Amatsi     | 10. Narok        | 10. UBA Kenya    |               | 12. Engineer       |
|                     | 14. Nanyuki     | 12. Lodwar     | 11. Mandera      | Bank Limited     |               | 13. Nyakanja       |
|                     | 15. Nyahururu   | 13. Mikutra    | 12. Kapenguria   |                  |               | 14. Mbooni         |
|                     | 16. Murang'a    |                | 13. Mwala        |                  |               | 15. Kinja          |
|                     | 17. Garissa     |                | 14. Maralal      |                  |               | 16. Tia Wira       |
|                     | 18. Meru        |                | 15. Yatta        |                  |               | 17. Upper Chania   |
|                     | 19. Kwale       |                | 16. Iten Tambach |                  |               | 18. Ruiru Thau     |
|                     | 20. Sibo        |                | 17. Olkalau      |                  |               | 19. Gitei          |
|                     | 21. Tavevo      |                | 18. Namanga      |                  |               | 20. Kathita Kiirua |
|                     | 22. Kikuyu      |                | 19. Runda        |                  |               |                    |
|                     |                 |                | 20. Kiamumbi     |                  |               |                    |
|                     |                 |                | 21. Rumuruti     |                  |               |                    |
|                     |                 |                | 22. Matungulu    |                  |               |                    |
|                     |                 |                | Kangundo         |                  |               |                    |
|                     |                 |                | 23. Wote         |                  |               |                    |
|                     |                 |                | 24. Moyale       |                  |               |                    |
|                     |                 |                | 25. Olkejuado    |                  |               |                    |



### 6.3 Appendix 3: Request for Funding Proposal Template

#### Request for Proposals

#### Long Term Funding of

[Amount in KES]

For

[Name of Water Service Provider]

Closing date and time [Insert Date & Time of Closure of RFP]

#### 1 Introduction

The [Name of WSP] at its meeting held in [Insert Date] duly approved, in principle, a [Insert project(s) duration]-year capital investment program of [Insert project Investment amount] in support of [Insert short description of projects].

The overall financial implications of the capital investment program are set out in the table below:

| FY                      | Total (KES)                          |
|-------------------------|--------------------------------------|
| [Insert Financial Year] | [Insert Planned Project Expenditure] |
|                         |                                      |
| TOTAL                   | [Insert Total Expenditure]           |

In addition [Insert additional loan details].

An Information Memorandum accompanying this Request for Proposals provides further information on [Insert Name of WSP].

#### 2 Requests for proposals

##### 2.1 General information

- Proposals from qualifying Kenyan and international financial institutions are invited in terms of the above resolution.
- Proposals will be accepted until on [Insert time day month year] and no late submissions will be accepted.
- Proposals must be in sealed envelopes and deposited in the tender box at [Insert address of opening venue] that are clearly marked [Insert title of RFP]
- Proposals will be opened in public in the [ Insert address of opening venue] at [Insert time day month year]
- The [Board of WSP] may at its discretion reinvest any unused portion of the amount drawn down with the financial institution until progress with the capital expenditure program justifies the withdrawal. The Board will consider alternatives for phased draw-downs from the successful tenderers provided that commitment fees are clearly articulated.
- The [Board of WSP] is not obliged to accept any tender and may accept different tenders for the deposit and the loan

but is prepared to offer the deposit as ceded security for the loan.

- g. The [Board of WSP] records its intention to fund [Insert % of Project to be finance through debt] of the capital programme with loans from financial institutions
- h. The [Board of WSP] undertakes to annually provide the financial institution(s) with both its interim financial statements and its annual audited financial statements. These statements will be provided within [Insert number of months] of close of the financial year and within [Insert number of months] of the half-year closure.

## 2.2 Specific information

Clauses to be incorporated into the loan agreement are attached in the Annexure.

Further specific conditions are stated below:

- a. No conditional proposals shall be considered and all proposals must indicate that the relevant credit approval has been pre-obtained from a duly authorized body;
- b. All tenderers shall submit their standard loan agreement together with their completed term sheets and repayment schedules, adjusted with the conditions contained and stipulated in this invitation. Each party shall carry its own costs in the finalization of the loan agreement;
- c. The Board shall not be responsible for any costs incurred in the preparation of the proposals;
- d. The Board reserves the right to not to accept any proposals or accept part of a proposal or to combine proposals;
- e. The Board reserves the right to negotiate with the successful tenderer(s);
- f. Funds shall be deposited in the Board's bank account free of bank charges or commissions or any other costs;
- g. Price variations due to statutory changes in the [Insert relevant acts e.g. Banks Act, Companies Act] and other related legislation that can be proven to directly increase the costs of the loan shall be for the account of the Board. No other variations shall be entertained;
- h. Failure to comply with the required term sheets shall lead to disqualification of the tender;
- i. Unsolicited variations and proposals shall only be considered from the successful tenderer(s);
- j. Tenderers may tender for the whole or part of the amount requested. The RfP allows for tenderers to submit both variable-rate and fixed-rate tenders;
- k. Repayment shall be on half yearly basis on an amortizing profile;
- l. Interest rates quoted shall be in [ Insert how interest rates should be quoted];
- m. The interest rate of fixed-rate tenders shall be fixed on the day of drawdown and be based on [Insert reference rate and spread ];
- n. The interest rate on variable-rate tenders shall be expressed as a margin above the [Insert reference rate ];
- o. Tenders for the deposit shall mirror the conditions of the loan i.e. be expressed as a fixed- or variable-rate above the [Insert reference rate ] and in the case of a fixed rate shall be fixed on the day of deposit and in the case of a variable rate shall be reset at quarterly intervals.

## 2.3 Basis of award of loan component

Adjudication of the loan will take place on the following basis:

- a. Interest rate: weight 80 points, with the lowest tenderer being awarded 90 points and one point being deducted for every one basis point increase in the price offered;
- b. Reinvestment rate: weight 10 points with the highest tenderer being awarded 10 points and 1 point being deducted for every basis point decrease in interest rate offered;
- c. Switching cost: weight 10 points with lowest offer being awarded 10 points and every sequential offer reducing by one point.

The tender shall be awarded to the qualifying bid with the highest score

## 2.4 Basis of award of Deposit Component

The deposit will be awarded to the Bidder offering the highest rate without any further considerations being taken into account.

## 2.5 Term sheets

The term sheets and information about the tenderer shall be substantially in the following format and shall be duly signed by an authorized representative.

| Term Sheet for Loan  |           |  |
|--|-----------|--|
| Amount (KES)   |           |  |
| Profile ( amortized with X installments per annum)                       |           |  |
| Term (Months)  |           |  |
| Fixed Rate Margin (in basis points above reference rate)                 |           |  |
| Floating Rate Margin (in basis points above reference rate)              |           |  |
| Security Required except Deposits (If applicable)                        |           |  |
| Disbursement   |           |  |
| Reinvestment Rate (in basis points above reference rate)                 |           |  |
| Cost of Switching Option (as one-off basis points of outstanding amount) |           |  |
| Authorized Representative  | Name      |  |
|  | Position  |  |
|  | Date      |  |
|  | Signature |  |
| Witness  | Name      |  |
|  | Position  |  |
|  | Date      |  |
|  | Signature |  |

| Term Sheet for Deposits   |  |
|---|--|
| Fixed Rate Offered (in basis points)  |  |
| Floating Rate Spread (in basis points as reset quarterly above the 91 day T-bill) |  |

| Information of Tenderer       |                    |  |
|-------------------------------|--------------------|--|
| Name of financial institution |                    |  |
| Physical Address              |                    |  |
| Postal Address                |                    |  |
| Company Registration Number   |                    |  |
| PIN number                    |                    |  |
| Authorized Representative     | Name               |  |
|                               | Telephone Contacts |  |
|                               | Email Address      |  |
| Proof of Authority Attached   |                    |  |

## ANNEXURE: Clauses to be incorporated into the loan agreement

### 1 Definitions

- 1.1. “Audited annual financial statements “Means the audited annual financial statements of the [ Insert name of WSP]
- 1.2. Bid” means a written offer in a prescribed or stipulated form in response to this invitation
- 1.3. “Closing time” shall be the date and time specified above.
- 1.4. “Credit approval” shall mean an irrevocable commitment to extend the loan to the [Insert name of WSP]]. Should there be disagreement on the conditions the conditions contained in this invitation will prevail.
- 1.5. “Interim financial statements” shall mean the unaudited 6 monthly management accounts of the [Insert name of WSP] ]
- 1.6. “Loan agreement” means the written agreement entered into between the [Insert name of WSP] and the financial institution including all documents by reference and appendixes and attachments.
- 1.7. “Corrupt practice” means the use of offering of items of value to influence the decisions of the [Insert name of WSP]] in the procurement process.
- 1.8. “Day” means calendar day.
- 1.9. “Draw down” Drawdown shall mean the transfer of funds from the financial institution to the [Insert name of WSP]].
- 1.10. “Default “shall be defined as the failure of the board to make a due payment on the scheduled repayment date .Should such a default exceed two weeks it shall be regarded as a permanent default and the financial institution shall be entitled to call the entire loan including in the case of fixed interest loans any breakage costs and to take such further actions as required to recover the outstanding amount.
- 1.11. “Fixed Interest rate”: Fixed interest rate shall mean interest rate set on award and remaining constant for the entire duration of the loan.
- 1.12. “Force Majeure” means an event beyond the control of the financial institution and the [ ]. Such events include acts also described as “Acts of God”, and may include but are not limited to wars, revolution, civil unrest, fires, floods and epidemics.
- 1.13. “Fraudulent Practice” means a misrepresentation of the facts to influence the procurement process and includes collusion among tenderers any other action denying free and fair competition.
- 1.14. “Repayment” shall mean the scheduled amount due by the [WSP] on a scheduled repayment date and the schedule shall be attached to the term sheet. The schedule shall in the case of a floating interest rate loan be updated every time an interest rate variation occurs.
- 1.15. “Scheduled repayment date” shall be the date on which payments to the financial institutions are due as per the term sheets
- 1.16. “Switching costs” shall mean the cost of changing from a variable interest rate to a fixed interest rate.
- 1.17. “Tenderer” shall mean the financial institution responding to this invitation by submitting a proposal.
- 1.18. “Penalty Amount” shall be the additional amount payable per calendar day for failure of the [ ] to make scheduled repayments.
- 1.19. “Public holiday” shall be any day recognized in the Republic of Kenya as a public holiday. Should a scheduled repayment fall on a Sunday or a public holiday repayment shall move to the next working day without any penalty being incurred.
- 1.20. “Variable or floating interest rate” Floating interest rate shall mean an interest rate reset every three months as a fixed margin above the agreed benchmark rate.

1.21. "Written" means handwritten in ink or any form of electronic or mechanical writing.

## **2 Settlement of disputes**

- 2.1 If any dispute or difference of opinion of any kind arises between the parties in connection with issues arising out of the contract, the parties shall for [ ] days make every effort to resolve the dispute amicably.
- 2.2 If after the period the dispute has not been resolved either party can refer the matter for mediation.
- 2.3 Should it not be possible to resolve the differences the matter shall be settled by a Kenyan court of law. During the duration of the legal proceedings both parties shall continue to perform their obligations unless mutually agreed. This shall specifically apply to repayments due by the [Insert name of WSP]

## 6.4 Appendix 4: Sample WSP Memorandum & Articles of Association

### THE COMPANIES ACT (CHAPTER 486)

#### COMPANY LIMITED BY SHARES

#### MEMORANDUM OF ASSOCIATION

of

#### WATER UTILITY COMPANY LIMITED

---

1. The name of the Company is “WATER UTILITY COMPANY Limited”
2. The registered office of the Company will be situated in the Republic of Kenya.
3. The objects for which the Company is established are:
  - (a) To carry on the business of water and sewerage services within the area under the jurisdiction of (Insert County) and its environs in accordance with the terms and requirement of water services provider as provided by license and the Water Act, 2002 and any subsequent amendments thereto or enactments thereof.
  - (b) To manage and maintain assets and facilities of water and sanitation services provision in accordance with the license granted and the provisions of the laws aforesaid.
  - (c) To provide and distribute a constant supply of potable water for commercial, industrial and domestic purposes within the area of operation.
  - (d) To design and construct dams reservoirs and weirs, to dig wells and drill or sink boreholes and carry on any other water conservation and reticulation works for the provision of water for domestic, industrial and agricultural purposes.
  - (e) To acquire for its own use and distribution by sale to the public water pumps, engines, tanks, pipes and any other equipment and chemicals that may be deemed necessary for and connected to the carrying out of the said business of the Company.
  - (f) To be responsible for the treatment and disposal of sewage in its area of operation by such means and at such times and locations as are appropriate.
  - (g) To obtain water for the purposes of distribution and supply from all appropriate sources in accordance with water resource regulations.
  - (h) To enter into agreement with the consumers on water and sewerage tariffs and collection of revenues and design tariff structures as may be required in accordance with the laws and regulations governing water service provision.
  - (i) To undertake laboratory facilities and analysis to ensure that acceptable water and effluent quality standards are maintained.
  - (j) To enter into investment of land such as to acquire, lease, own or utilize for the purposes of water undertakings.

- (k) To purchase, or otherwise acquire or lease facilities assets, warehouse, building or machinery and equipment for the purposes of water undertaker ship and to establish workshops for the repair and fitting of metering equipment, electric motors, pumps and other associated equipment common and incidental to the provision of water and sanitary services.
- (l) To construct stand pipes and water kiosks in area as may be conducive to local conditions and delineate water supply zones and sewerages zones within the area of operation.
- (m) To acquire, establish, construct and provide workshops, waterworks, offices and other premises and facilities necessary or convenient for the performance of the objects of the company, and for that purpose, buy, take on lease or in exchange, hire or otherwise, acquire immovable property and interests therein, and rights over the same and concessions, grants, rights, powers and privileges in respect thereof.
- (n) To maintain a data base, registers, books and records in quality and quantity for technological, financial, commercial property and facilities information to facilitate efficient management audit and supervision and to keep the license, regulators, consumers informed about quality service and performance.
- (o) To insure and keep insured all buildings, assets and facilities, equipment that is in the possession and control of company against all losses, risks and damage.
- (p) To keep and maintain fire-fighting equipment such as hydrants and pumps and portable fire extinguishers at the premises and to protect them from loss and damage and to train and mobilize staff and consumers for the aforesaid purposes.
- (q) To carry on any other business which may seem to the Company necessary to, or capable of, being conveniently carried on in connection with the objects of the Company or calculated directly or indirectly to enhance the value of, or render profitable, any of the property or rights of the Company, or to improve the quality, efficiency, effectiveness or extent of the services provided to the customers of the Company.
- (r) To apply for, buy or otherwise acquire patents, patent rights, trade marks, designs licenses, concessions or the like conferring an exclusive or non-exclusive or limited right to their use, or any confidential or other information or a process which may seem to the Company capable of being used for the purpose of the company or the acquisition of which may seem to the company calculated, directly or indirectly, to benefit the company, and to use exercise, develop and grant licenses in respect of, or otherwise turn to account, rights, information and processes so acquired, and to expend money in experimenting upon testing, or improving any such patents, inventions or rights.
- (s) To acquire and undertake the whole or any part of the business, property, and liabilities of any person or company carrying on or proposing to carry on, any business which the Company is authorized to carry on, or possessed of property suitable for the purposes of the Company, which can be carried on in conjunction there with or which is capable of being conducted so as directly or indirectly to benefit the Company.
- (t) To amalgamate, enter into partnerships or into any arrangement for sharing profits, union of interest, cooperation, joint venture, reciprocal concession, or for limiting competition with any person or company carrying on in conjunction therewith or which is capable of being conducted so as directly or indirectly to benefit the Company or to improve the quality, efficiency, effectiveness or extent of the services provided to the customers of the Company.
- (u) To apply for, promote and obtain any legislation, charter, privilege, concession, license or authorization of any government, state municipality or authority or other authority for enabling the company to carry out any of its objects into effect or for extending any of the powers of the company or for extending any modification of the constitution of the company or for any other purpose any proceedings or application which may seem calculated directly or indirectly to prejudice the interests of the Company.
- (v) To apply for, purchase, take on lease or in exchange, hire or otherwise acquire any real and personal property and

any rights or privileges which the company may think necessary or convenient for the purpose of its business or businesses, and in particular any land, buildings, plant, and stock in trade.

- (w) To sell, improve, manage, exchange, let, develop, grant, dispose or, turn to account or otherwise deal, with all or any part of the property, rights, interest or privileges of the company.
- (x) To invest any real or personal property, rights, or interest acquired by or belonging to the Company in any person or company on behalf of or for the benefit of the company and with or without any declared trust in favour of the company.
- (y) To pay for any business, property, or rights acquired or agreed to be acquired by the Company by the issue or transfer of shares of this or any other company credited as fully or partly paid up, or debentures or other securities of this or any other company.
- (z) To lend and advance money or give credit to such persons or companies and on such terms as may seem expedient, and in particular to customers and persons having dealings with the company, and to guarantee the performance of any contract or obligations and the payment of money of or by any such persons or companies and generally to give guarantees and indemnities.
- (aa) To receive money on deposit or loan and borrow or raise money in such manner as the Company shall think fit (but always in accordance with the laws of Kenya) and in particular by the issue of debentures or debentures stock, perpetual or otherwise, and to secure, charge or lien upon all or any of the property or assets of the Capital, and also by a similar mortgage, charge, or lien to secure and guarantee the performance by the company or any person or company of any obligation undertaken by the company or any other person or company as the case may be.
- (bb) To make, draw, accept, endorse, negotiate, discount, buy, sell, execute, issue and deal in bills of exchange, promissory notes, bills of lading, warrants, debentures and other negotiable or transferable instruments.
- (cc) To sell, improve, manage, exchange, let, develop, grant, dispose or, turn to account or otherwise deal, with all or any part of the property, rights, interest or privileges of the company.
- (dd) To apply for, promote and obtain any legislation, charter, privilege, concession, license or authorization of any government, state municipality or authority or other authority for enabling the company to carry out any of its objects into effect or for extending any of the powers of the company or for extending any modification of the constitution of the company or for any other purpose any proceedings or application which may seem calculated directly or indirectly to prejudice the interests of the company.
- (ee) To enter into any arrangements with any government or authorities (international, regional, national, local or otherwise) or any person or company that may seem conducive to the objects of the company and to obtain from any such governments authority, person or company any rights, privileges, charters, contracts licenses and concessions which the company may think it desirable to obtain, and to carry out, exercise and comply with any such arrangements, rights privileges and concessions.
- (ff) To establish and maintain or procure the establishment and maintenance of any contributory or non-contributory pension or superannuation funds for the benefit of, and to give or procure the giving of donations, gratuities, pension, allowances or emoluments, to any persons who are or were at any time in the employment or service of the company or is allied to or associated with the company or with any such subsidiary company or who are or were at any time Directors or Officers of the Company or of any dependants of any such persons and also establish and subsidize and subscribe to any institutions. Associations, Clubs or funds calculated to be for the benefit of or to advance the interests and well-being of the company or any such other company as aforesaid and make payments of the matters aforesaid either alone or in conjunction with any such other company as aforesaid.
- (gg) To establish, promote, or assist in or enter into contracts with any person or company for the promotion of any



company or companies, for the purpose of acquiring all or any of the other purpose which may seem directly calculated to benefit the company and to place or guarantee the placing of, underwrite, subscribe for or otherwise acquire all or any part of the shares, debentures or other securities of any such other company.

- (hh) To remunerate or make donations to any person or persons whether Directors, Officers or Agents of the company for services rendered or to be rendered in or about the conduct of the company's business.
  - (ii) To invest and deal with the monies of the company not immediately required upon such securities or in the purchase of shares on other companies and in such manner as may from time be determined by the Directors.
  - (jj) To insure against losses, damages risks and liabilities, which the company may incur.
  - (kk) To deal with the company's employees in all matters including:
    - i. To appoint and employ such persons on such terms and conditions as the company thinks fit, and to terminate their appointments accordingly.
    - ii. To purchase, rent, take on lease or in exchange or otherwise acquire dwelling houses of occupation by employees of the company.
    - iii. To purchase land and construct thereon dwelling house for occupation by employees of the company.
    - iv. To sell, rent or lease dwelling houses and land for residential purposes to employees of the company.
  - (ll) To carry out all acts necessary for the purpose of improving:
    - i. The skill, knowledge or usefulness of persons employed in connection with the provision of water and sewerage services.
    - ii. The efficiency of equipment of the company or the manner in which the company is operated, and that connection to provide or assist other persons in providing facilities for training, education and research.
  - (mm) To protect from alienation all water services assets under its area of jurisdiction.
  - (nn) To plough back all surplus income for the purposes of development and renewal of water assets until such a time that optimal coverage of water services in the area of jurisdiction is achieved.
4. It is hereby declared that:
- a) The Company shall not support or participate in any activity of a political nature but the Members may freely exercise their constitutional rights to comment on political and other matters in their personal capacity and the Company may comment publicly or privately on any matter of a political nature which affects the activities of the Company.
  - b) The income and property of the Company howsoever derived shall be applied solely towards the promotion of its objects as set forth in this Memorandum of Association. No portion of such income and property shall be paid or transferred, directly or indirectly, by way of dividend, gift, division, bonus or otherwise howsoever by way of profit, to the Members; provided that nothing herein shall prevent any payment in good faith by the Company:
    - (i) of reasonable and proper remuneration to any officer or servant, or to any Member in return for any service actually rendered to the Company including re-imbusement of reasonable travel and accommodation expenses for attendances at meetings, nor
    - (ii) of interest on money lent by any Member or other person or company to the Company at such reasonable rate of interest as the directors of the Company shall deem fit; nor
    - (iii) of reasonable and proper rent for premises demised or let by any Member.
5. Members may not secure loans for commercial or personal enterprises using any assets owned and/or managed by the Company as security, save for cash.

6. The word “company” in these objects, except where used in reference to the Company, shall be deemed to include any partnership or other body of persons whether incorporated or not incorporated and whether domiciled in the Republic of Kenya or elsewhere.
7. The meaning of any general word or words in any paragraph of these objects shall not be restricted by being construed ejusdem generis with any particular word or words in the same paragraph.
8. No addition, alteration or amendment shall be made to or in the provisions of the Memorandum of the Company for the time being in force unless the same shall have been previously submitted to and approved by the Registrar of Companies and provided further that any such addition, alteration or amendment shall have been approved by a special resolution passed at a General Meeting of the Company. No such additional amendment may be made which would have the effect of changing the objects of the Company to objects which are inconsistent with clause 2 of this Memorandum of Association.
9. If upon the winding up or dissolution of the Company there remains after the satisfaction of all its debts and liabilities, any property whatsoever, the same shall not be paid to or distributed amongst the Members, but shall be given or transferred to some other institution or institutions having objects similar to the objects of the Company, and which, in addition shall prohibit the distribution of its or their income and property among its or their members to an extent at least as great as is imposed on the Company, such institution or institutions to be determined by the Members at or before the time of dissolution, and in default thereof by a Judge of the High Court of Kenya.
10. The liability of the Members is limited.
11. The share capital of the Company is Kenya Shillings two thousand (KES 2,000) divided into one hundred (100) redeemable preference shares of Kenya Shillings twenty (KES 20) each.
12. The Company shall have the power to increase or reduce such capital and to attach thereto respectively any preferential, deferred, qualified or other rights, privileges, restrictions or conditions and to issue all or any part of such original, increased or reduced capital with or subject to such preferential, deferred, qualified or other rights, privileges, restrictions or conditions provided that in all cases upon the redemption of such shares in the Company the applicable Members shall hereby be deemed to have irrevocably waived any right to receive back any moneys paid by them to the Company on the issue of such shares, provided that no such change shall offend the principle enshrined in this Memorandum of Association that the Company shall not distribute to its Members any part of any profits generated other than in the circumstances expressly authorised by the Memorandum of Association.
13. Any alteration to the conditions set out in paragraphs 11, 12 and this paragraph 13 of the Memorandum is hereby prohibited for the purposes of section 25 (2) of the Companies Act (Chapter 486, Laws of Kenya), provided that this paragraph shall not prevent the Company from increasing or reducing its share capital in accordance with the Companies Act (Chapter 486, Laws of Kenya).

We, the several persons whose names, addresses and occupations are subscribed, are desirous of being formed into a company in pursuance of this Memorandum of Association and we respectively agree to take the number of shares in the capital of the Company set opposite our respective names.

| Names, Postal Addresses and Occupation of Subscribers | Number of shares taken by each Subscriber | Signatures of Subscribers |
|---|---|---------------------------|
|   |   |                           |
|   |   |                           |
|   |   |                           |

Dated this            day of                            2015.

WITNESS to the above Signatures:-

**CERTIFICATE UNDER THE COMPANIES REGULATIONS**

It is hereby certified that the above Memorandum of Association of “WATER UTILITY COMPANY LIMITED” were produced by the method of Xerography.

DRAWN BY:  
MOHAMMED MUIGAI ADVOCATES  
MM CHAMBERS, 4TH FLOOR, K-REP CENTRE,  
WOOD AVENUE, KILIMANI  
P.O. BOX 61323-00200  
NAIROBI

## THE COMPANIES ACT (CHAPTER 486)

### COMPANY LIMITED BY SHARES

#### ARTICLES OF ASSOCIATION

of

#### WATER UTILITY COMPANY LTD

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1. The regulations contained in Table A in the First Schedule to the Act shall not apply to the Company.
2. In these Articles, if not inconsistent with the subject or context:
  - (a) “Act” shall mean the Companies Act (chapter 486);
  - (b) “Articles” shall mean these Articles of Association as now framed or as from time to time altered by Special Resolution;
  - (c) “Board” shall mean the Board of Directors of the Company or the Directors present at a duly convened meeting of the Directors at which a quorum is present;
  - (d) “Company” shall mean Water Utility Company Limited;
  - (e) “debenture” shall include debenture stock;
  - (f) “Director” shall include an alternate director;
  - (g) “dividend” shall include bonus;
  - (h) “Kenya” shall mean the Republic of Kenya;
  - (i) “Member” shall mean a shareholder in the Company;
  - (j) “month” shall mean a calendar month;
  - (k) “paid up” shall mean paid up or credited as paid up;
  - (l) “Seal” shall mean the common seal of the Company;
  - (m) “Secretary” shall include a temporary or assistant secretary and any person appointed by the Board to perform any of the duties of the Secretary;
  - (n) “Shillings” and “KES” shall mean Kenya shillings;
  - (o) the expression “in writing” or “written” shall include words written, printed, lithographed or represented or reproduced in any other mode in visible form;
  - (p) words signifying the singular number only shall include the plural number and vice versa;
  - (q) words signifying the masculine gender only shall include the feminine gender;
  - (r) words importing persons shall include corporations;
  - (s) reference to any provision of the Act shall be construed as a reference to such provision as modified or re-enacted by any act for the time being in force.
3. Subject to the last preceding Article, any words or expressions defined in the Act shall, if not inconsistent with the subject or context, bear the same meaning in these Articles.

## OBJECTS

4. The Company is established for the objects expressed in the Memorandum of Association as amended from time to time.

## PRIVATE COMPANY

5. The Company is a private company and accordingly:
  - a) the number of Members of the Company (exclusive of persons who are in the employment of the Company and of persons who, having been formerly in the employment of the Company, were while in such employment and have continued after the determination of such employment to be Members of the Company) is limited to fifty; provided that where two or more persons hold one or more shares in the Company jointly, they shall, for the purpose of this Article, be treated as a single Member;
  - b) any invitation to the public to subscribe for any shares or debentures of the Company is prohibited;
  - c) the Company shall not have power to issue share warrants to bearers;
  - d) the right to transfer shares is restricted in the manner hereinafter provided.

## ACTIVITIES OF THE COMPANY

2. Any branch or kind of activities which the Company is either expressly or by implication authorised to undertake may be undertaken by the Board at such time or times as it shall deem fit and, further, may be permitted by it to be in abeyance, whether such branch or kind or activity may have been actually commenced or not so long as the Board may deem it expedient not to commence or proceed with the same.
3. The registered office of the Company shall be at such place in Kenya as the Board shall from time to time appoint.
4. No part of the funds of the Company shall be employed in the subscription or purchase of or in loans upon the security of the Company's shares or those of its holding company (if any) and the Company shall not give, whether directly or indirectly and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of or in connection with any purchase or subscription by any person of or for shares in the Company or in its holding company (if any) and the transactions mentioned in the proviso to Section 56 (1) of the Act are prohibited to the extent that they conflict with the objects of the Company.
5. No part of the funds of the Company shall be employed to lend money or give credit to any person (whether a member of the Company or not) or company with or without security; nor to give guarantees or indemnities for the payment of money nor the performance of contracts or obligations by any such person or company; nor to secure or undertake in any way the repayment of money lent or advanced to or liabilities incurred by any person or company and otherwise to assist any such person or company.

## SHARE CAPITAL

6. The share capital of the Company is Kenya Shillings two thousand (KES 2,000) divided into one hundred (100) redeemable preference shares of Kenya Shillings twenty (KES 20) each.
7. Subject to Article 12 below and without prejudice to any special rights previously conferred on the holders of any Shares, any Share in the Company may be issued with or have attached thereto any preferential, deferred, qualified or other rights, privileges, restrictions or conditions, whether in regard to voting or otherwise, as the Company may from time to time by Special Resolution determine, provided that no such change shall offend the principle enshrined in the Memorandum of Association that the Company shall not distribute to its Members any part of any profits generated other than in the circumstances expressly authorised by the Memorandum of Association.

8. The special rights conferred upon the holders of any shares or class of shares shall not, unless otherwise expressly provided by the conditions of issue of such shares, be deemed to be altered by the creation or issue of further shares ranking *pari passu* therewith.
9. The shares in the capital of the Company consist only of redeemable preference shares. The Shares shall be at the disposal of the Members which may by a unanimous decisions of all the Members from time to time allot and issue them to such persons on such terms and conditions (including the number of shares to be issued or allotted) and at such times as it may determine provided that no shares shall be issued at a discount except in accordance with section 59 of the Act provided that provided that no such terms shall offend the principle enshrined in the Memorandum of Association that the Company shall not distribute to its Members any part of any profits generated other than in the circumstances expressly authorised by the Memorandum of Association.

### **REDEMPTION OF SHARES**

10. The Shares shall be liable to be redeemed in accordance with section 60 of the Act and such redemption shall be at the sole option of the Members provided that the Board shall at all times be entitled to require the Members to redeem any Shares which have been issued and allotted by the Company, by giving written notice of such requirement to the Members.
11. Without prejudice to the waiver by Members contained in regulation 13 of the Company's Memorandum of Association, no redeemable preference shares shall be redeemed otherwise than out of those profits that would have been distributable to the Members as dividends if the Company had been authorised to pay such dividends or the proceeds of a fresh issue of Shares made for the purposes of the redemption and all provisions of statute relating to the redemption of shares and the creation and increase where requisite of a capital redemption reserve shall be duly observed.
12. Any provision in the Articles which states that the Board shall have the power to redeem Shares on behalf of a Member shall be deemed to include a further statement under which the Member in question irrevocably appoints the Board to act as its attorney in relation to the effecting of any such redemption.

### **CERTIFICATES**

13. Every person whose name is entered as a Member in the Register of Members shall be entitled, without payment, to one certificate for all its Shares. Every certificate shall be issued within sixty days after allotment or issue, shall be under the Seal and shall specify the share or shares to which it relates and the amount paid up thereon. In the case of shares held jointly by several persons, the Company shall not be bound to issue more than one certificate therefor and delivery of a certificate to one of the several joint holders shall be sufficient delivery to all.
14. If a share certificate is defaced, lost or destroyed, it may be replaced on payment of such fee, if any, not exceeding Kenya Shillings two hundred (KES 200.00) and, in the case of loss or destruction, on such terms, if any, as to evidence and indemnity and payment of the out-of-pocket expenses of the Company of investigating such evidence, as the Board may think fit and, in case of defacement, on delivery of the old certificate to the Company.

### **TRANSFER OF SHARES**

15. The transfer of any share in the Company shall not be permitted, save as provided in Article 16.

### **TRANSMISSION OF SHARES**

16. The transmission of any share in the Company, whether in consequence of the death or bankruptcy of a Member or for any other reason whatsoever shall not be permitted, save with the prior written approval of the Members.

## **INCREASE OF CAPITAL**

17. The Company may from time to time, by Ordinary Resolution, increase its capital by such sum to be divided into Shares of such amounts as the resolution shall prescribe provided that no such alteration shall be offend the principle enshrined in the Memorandum of Association that the Company shall not distribute to its Members any part of any profits generated other than in the circumstances as expressly authorised by the Memorandum of Association.

## **GENERAL MEETINGS**

18. The Company shall, in each year, hold a General Meeting as its Annual General Meeting in addition to any other Meetings in that year and shall specify the meeting as such in the notices calling it. Not more than fifteen months shall elapse between the date of one Annual General Meeting of the Company and that of the next. So long as the Company holds its first Annual General Meeting within eighteen months of its incorporation, it need not hold it in the year of its incorporation or in the following year. Annual and other General Meetings shall be held at such times and places as the Board shall appoint. All General Meetings, other than Annual General Meetings, shall be called Extraordinary General Meetings.
19. The Board may, whenever it thinks fit, convene an Extraordinary General Meeting. Extraordinary General Meetings may also be convened in default of such requisition on the requisition of not less than 10% in number of the total Membership. If, at any time, there are not within Kenya sufficient Directors capable of acting to form a quorum, any Director or any two Members of the Company may convene an Extraordinary General Meeting in the same manner, as nearly as possible, as that in which Meetings may be convened by the Board.

## **NOTICE OF GENERAL MEETINGS**

20. Every General Meeting shall be called by at least twenty-one days' notice in writing (exclusive of the day on which it is served or deemed to be served and of the day for which it is given). The notice shall specify the place, the date and the time of such General Meeting and, in case of special business, the nature of that business and shall be given, in manner hereinafter mentioned or any such other manner, if any, as may be prescribed by the Company in General Meeting, to such persons as are, under these Articles, entitled to receive such notices from the Company; provided that a Meeting may be called by shorter notice than that specified in this Article if so agreed by the Members referred to in and otherwise in accordance with the provisions of Section 133 (3) of the Act.
21. In every notice calling a Meeting there shall appear, with reasonable prominence, a statement that a Member entitled to attend and vote thereat is entitled to appoint one or more proxies to attend and vote in its stead and that a proxy need not be a Member.
22. The accidental omission to give notice of a Meeting to, or the non-receipt of notice of a Meeting by, any person entitled to receive such notice shall not invalidate the proceedings at that Meeting.

## **PROCEEDINGS AT GENERAL MEETINGS**

23. All business shall be deemed special that is transacted at an Extraordinary General Meeting and also all business that is transacted at an Annual General Meeting with the exception of consideration of the accounts and balance sheets, and any other documents accompanying or annexed thereto, the reports of the Directors and Auditors, the election of Directors, the appointment of Auditors and the fixing of the remuneration of any officer of the Company or servant of the Company.
24. No business shall be transacted at any General Meeting unless a quorum is present when the Meeting proceeds to

business. The Members in General Meeting may by ordinary resolution vary the quorum for such Meetings and unless decided otherwise by the Members in General Meeting and save as otherwise provided by these Articles, two (2) Members, present in person or, in the case of a corporation, represented in accordance with Article 42, shall be a quorum.

25. If, within thirty minutes after the time appointed for the Meeting, a quorum is not present, the Meeting, if convened on the requisition of Members, shall be dissolved. In any other case, it shall stand adjourned to the same day in the next week at the same time and place and if, at such adjourned Meeting, a quorum is not present within thirty minutes after the time appointed for the Meeting, the Meeting shall be dissolved.
26. The chairman of the Board shall preside at every General Meeting as chairman of that meeting. If there is no such chairman present within fifteen minutes after the time appointed for the same the person elected as deputy -chairman of the Board shall act as chairman of the General Meeting. If neither is able nor willing to act as Chairman, the Members present shall choose some Member to be chairman of the Meeting.
27. The Chairman of any Meeting at which a quorum is present may, with the consent of the Meeting and shall, if so directed by the Meeting, adjourn the Meeting from time to time and from place to place as the Meeting determines but no business shall be transacted at any adjourned Meeting other than the business which might have been transacted at the Meeting from which the adjournment took place. Whenever a Meeting is adjourned for thirty days or more, notice of the adjourned Meeting shall be given in the same manner as in the case of an original Meeting. Save as aforesaid, it shall not be necessary to give any notice of an adjournment or of the business to be transacted at an adjourned Meeting.
28. At any General Meeting, a resolution put to the vote of the Meeting shall be decided on a show of hands unless (before or on the declaration of the result of the show of hands) a poll is demanded by the Chairman of the Meeting or by any Member present in person or, in the case of a corporation, represented in accordance with Article 42. Unless a poll is so demanded, a declaration by the Chairman of the Meeting that a resolution has, on a show of hands, been carried or carried unanimously or by a particular majority or lost or not carried by a particular majority and an entry to that effect in the book containing the minutes of the proceedings of the Company shall be conclusive evidence of the fact without proof of the number or proportion of the votes recorded in favour of or against such resolution. A demand for a poll may be withdrawn.
29. A poll demanded on the election of a Chairman or on a question of adjournment shall be taken forthwith. A poll demanded on any other question shall be taken at such time and place and in such manner as the Chairman of the Meeting shall direct.
30. If a poll has been duly demanded, the result of the poll shall be deemed to be a resolution of the Meeting at which the poll was demanded.
31. The demand for a poll shall not prevent the continuance of a Meeting for the transaction of any business other than the question on which a poll has been demanded and such demand may be withdrawn at any time.
32. On a poll votes may be given personally or by a representative of a corporation appointed in accordance with Article 42.
33. In the case of an equality of votes, either on a show of hands or on a poll, the Chairman of the Meeting shall be entitled to a second or casting vote.
34. If any vote shall be counted which ought not to have been counted or might have been rejected, the error shall not vitiate the resolution unless it is pointed out at the same Meeting and not, in that case, unless it shall, in the opinion of the Chairman of the Meeting, be of sufficient magnitude to vitiate the resolution.
35. Subject to the provisions of the Act, a resolution in writing signed by all the Members for the time being entitled to receive notice of and to attend and vote at General Meetings or, being corporations, by their representatives appointed in accordance with Article 42, shall be as valid and effective as if the same had been passed at a General Meeting of the Company duly convened and held. Such resolution may be contained in one document or in several documents in like



form each signed by one or more of the Members or by their representatives as aforesaid.

36. The Members may participate in any meeting of the Members by means of conference telephone or other communication facilities as permit all persons participating in the meeting to hear each other simultaneously and such participation shall constitute a presence at a meeting of the Members as if those participating were present in person.

**VOTES OF MEMBERS**

37. On a show of hands every Member who is present in person or, being a corporation, is present by a representative appointed in accordance with Article 42 shall have one vote. On a poll every Member shall have one vote for each share for which it is the holder.
38. No Member shall be entitled to be present at any General Meeting or to vote on any question, personally, at any General Meeting or on a poll or to be reckoned in a quorum whilst any sum shall be due and payable to the Company in respect of any of the Shares held by it, whether alone or jointly with any other person, or whilst any other sum payable by it to the Company under these Articles shall remain due and payable.
39. In the case of joint holders of a share, the vote of the senior who tenders a vote in person, shall be accepted to the exclusion of the votes of the other joint holders and, for this purpose, seniority shall be determined by the order in which the names stand in the Register of Members.
40. A Member of unsound mind in respect of whose estate a manager has been appointed under section 26 of the Mental Health Act (Chapter 248, Laws of Kenya) may vote, whether on a show of hands or on a poll, by such manager who may vote on the depositing to the Secretary not less than forty eight hours before the time for holding of the Meeting, of proof of its appointment under such legislation.
41. No objection shall be raised to the qualification of any voter except at the Meeting or adjourned Meeting at which the vote objected to is given or tendered and every vote not disallowed at such Meeting shall be valid for all purposes. Any such objection made in due time shall be referred to the Chairman of the Meeting whose decision shall be final and conclusive.
42. Any corporation which is a Member or Director of the Company may, by resolution of its Directors or other governing body or by notification in writing under the hand of some officer of such corporation duly authorised in that behalf, authorise such person as it thinks fit to act as its representative at any Meeting of the Company or the Board and the person so authorised shall be entitled to exercise the same powers on behalf of the corporation which he represents as that corporation could exercise if it were an individual Member of the Company or member of the Board.
43. An instrument appointing a proxy shall be in the following form or a form as near thereto as circumstances admit:

**“WATER UTILITY COMPANY LIMITED”**

1) I/We ....., of ....., being a Shareholder/Shareholders of the above-named Company, hereby appoint ..... of ..... or failing it ..... of ..... as my/our proxy to vote for me/us on my/our behalf at the Annual/ Extraordinary General Meeting of the Company to be held on the ..... day of ..... 20.. and at any adjournment thereof.

Signed this ..... day of ..... 20..

This form is to be used \*in favour of/against the resolution. Unless otherwise instructed, the proxy will vote as he thinks fit.

\*Strike out whichever is not desired”.

**DIRECTORS**

44. The number of Directors shall be not less than two and not more than nine in number. The first Directors shall be appointed, in writing, by the Members.
45. A Director need not be a member but shall be entitled to receive notice of and to attend and speak at all General Meetings of the Company.
46. Any Director may appoint another Director or any other person who is approved by the Directors to be his alternative (an "Alternative") to act in his place at any meetings of the Board at which he is able to present. The Alternative shall be entitled in the absence of his appointer to exercise all rights and powers of a Director and to attend and vote at the meetings of the Board at which his appointer is not personally present and, where he is a Director, to have a separate vote on behalf of his appointer in addition to his own vote. A Director may, at any time, revoke the appointment of an Alternate appointed by him. The appointment of Alternate shall be revoked, ipso facto, if his appointer for any reason ceases to be a Director. Every appointment and revocation under this Article shall be effected by notice in writing under the hand of the appointer served on the Company and on such Alternate.
47. The Directors, other than those whose remuneration is determined by agreement between them and the Board, shall be entitled to such remuneration for their services as the Board may, from time to time, in general meetings determine and such remuneration shall be divided among the Directors in such proportion and manner as they may determine or, failing such determination, equally, except that in such event any Director holding office for less than a year shall only rank in such division in proportion to the period during which he has held office during such year.
48. An Alternate whose Appointer is a Member shall, in the absence of a direction to the contrary in the instrument appointing him, be entitled to receive notice of and to vote at General Meetings as if he had been appointed a proxy of his appointer under the provisions of these Articles.
49. A Director shall vacate office as such if :
  - i) he is removed from office pursuant to Section 185 of the Act or by a Special Resolution of the Company in General Meeting;
  - ii) he becomes prohibited from being a Director by reason of any order made under Section 189 of the Act;
  - iii) he becomes of unsound mind;
  - iv) he fails, without reasonable cause and without consent of the Board, to attend three consecutive meetings of the Board and the Board resolves that, by reason of such failure, he shall cease to be a Director; or
  - v) he resigns his office by giving notice in writing to the Board.
50. The Board may, at any time and from time to time, appoint a person to be a Director to fill a casual vacancy or as an addition to the Board but so that the total number of Directors shall not at any time exceed the maximum number (if any) fixed by or in accordance with these Articles from time to time. A Director so appointed shall retire at the next General Meeting and shall be eligible for re-election.
51. The Company may, by Ordinary Resolution, appoint another person in place of a Director who has vacated office as such under Article 49 and, without prejudice to the powers of the Directors under Article 50, the Company may, by Ordinary Resolution appoint any person to be a Director either to fill a casual vacancy or as an additional Director.

**DIRECTORS' CONTRACTS**

52. A Director or Member may contract with and be interested in any way, whether directly or indirectly, in any actual or proposed contract or arrangement with the Company, either as vendor, purchaser or otherwise, and shall not be liable to account for any profit made by it by reason of any such contract or arrangement, provided that the nature of the interest of the Director or the Member in such contract or arrangement is declared at the meeting of the Board at which the

question is first taken into consideration if its interest then exists or, in any other case, at the next meeting of the Board held after he or it became interested and it shall be the duty of the Director or the Member so to declare its interest. No Director shall vote as a Director in respect of any contract or arrangement in which he or the Member appointing him is interested and, if he does vote, his vote shall not be counted but he shall, nevertheless, be counted in the quorum present at the meeting. These prohibitions may, at any time, be suspended or relaxed, to any extent, by a Special Resolution of the Company in General Meeting and they shall not apply to any arrangement for giving a Director an indemnity.

53. For the purpose of Article 52, a general notice given to the Board by a Director at any meeting of the Board to the effect that he or the member appointing him as a Director is a member of a specified corporation, company or firm and is to be regarded as interested in any contract which may, after the date of the notice, be made with that corporation, company or firm, shall be deemed to be a sufficient declaration of interest in relation to any contract so made.
54. A Director may act by himself or its firm in a professional capacity for the Company, except as Auditor of the Company, and he or its firm shall be entitled to receive remuneration for professional services rendered as if he were not a Director.

### **POWERS AND DUTIES OF THE BOARD**

55. The Board may exercise all the powers of the Company to borrow or raise money and to mortgage or charge its undertaking, property or any part thereof and to issue income notes, bonds, debentures and other securities.
56. The business of the Company shall be managed by the Board which may pay all such expenses of and preliminary and incidental to the promotion, formation, establishment and registration of the Company as it thinks fit and may exercise all such powers of the Company as are not by the Act or by these Articles required to be exercised by the Company in General Meeting (subject nevertheless to the provisions of these Articles and of the Act) and to such regulations, being not inconsistent with such provisions, as may be prescribed by the Company in General Meeting but no regulation made by the Company in General Meeting shall invalidate any prior act of the Board which would have been valid if such regulation had not been made. The general powers given by this Article shall not be limited or restricted by any special authority or power given to the Board by any other Article.
57. The Board may establish any local boards or agencies for managing any of the affairs of the Company, either in Kenya or elsewhere, and may appoint any persons to be members of such local boards or managers or agents and may fix their remuneration and may delegate to any local board, manager or agent any of the powers, authorities and discretions vested in the Board, with power to sub-delegate, and may authorise the members of any local board or any of them to fill any vacancies therein and to act notwithstanding vacancies. Any such appointment or delegation may be made upon such terms and subject to such conditions as the Board may think fit and the Board may remove any person so appointed and may annul or vary any such delegation but no person dealing in good faith and without notice of any such annulment or variation shall be affected thereby.
58. The Board may, by power of attorney, appoint any person or any fluctuating body of persons, whether nominated directly or indirectly by the Board, to be the attorney of the Company for such purposes and with such powers, authorities and discretions, not exceeding those vested in or exercisable by the Board under these Articles, and for such period and subject to such conditions as it may think fit. Any such power of attorney may contain such provisions for the protection and convenience of persons dealing with any such attorney as the Board may think fit and may also authorise any such attorney to sub-delegate all or any of the powers authorities and discretions vested in him.
59. The Company may exercise the powers conferred by section 37 of the Act with regard to having an official Seal for use outside Kenya and such powers shall be vested in the Board.
60. The Company may exercise the power conferred by section 121 of the Act with regard to the keeping of a branch register and the Board may, subject to the provisions of section 122 of the Act, make and vary such regulations as it may think

fit regarding the keeping of any such branch register.

61. All cheques, promissory notes, drafts, bills of exchange and other negotiable and transferable instruments and all receipts for moneys paid to the Company shall be signed, drawn, accepted, endorsed or otherwise executed as the case may be in such manner as the Board shall from time to time determine.
62. The Board shall cause Minutes to be made, in books provided for the purpose, recording, in respect of every Meeting of the Company, of the Board and of committees or sectoral boards formed by the Board, the names of all persons present and all resolutions and proceedings at such Meetings. The Minutes of every such Meeting shall be read at the next Meeting of the Company, of the Board or of the committee or sectoral boards, as the case may be, and, after being amended or corrected, if necessary, and approved by the Meeting, shall be signed by the Chairman of the Meeting and, once so signed, shall be prima facie evidence of the matters stated therein.
63. The Board may grant pensions, annuities, gratuities or other allowances on death, sickness, disability or retirement to any person who is or has been employed by or in the service of the Company or of its holding company or any subsidiary company of the Company or to any person who is or has been a Director or other officer of the Company or of its holding company or any such subsidiary company and to the widow, family or dependants of any such person. The Board may establish and maintain or concur with such holding or subsidiary company (if any) as aforesaid in establishing and maintaining any schemes or funds for providing such benefits as aforesaid and may pay out of the funds of the Company any premiums, contributions or sums payable by the Company under the provisions of any such scheme or fund.

#### **PROCEEDINGS OF THE BOARD**

64. The Board may meet together for the despatch of business, adjourn and otherwise regulate its Meetings as it thinks fit. Unless stated otherwise in the Articles questions arising at any meeting shall be determined by a simple majority of votes cast. In case of an equality of votes, the chairman of the meeting shall have a second or casting vote. The Secretary, on the instructions of the Chairman or on the requisition of a Director, shall at any time summon a Board meeting. At least seven days' notice (inclusive of the date of service and the date of meeting) of all Board meetings shall, unless waived by all Directors, be given in manner hereinafter mentioned to all Directors and Alternates.
65. The quorum necessary for the transaction of the business of the Board shall be one third in total of the Directors from time to time, provided that one person whether a Director or not, although a duly appointed Alternate for any number of Directors, shall not constitute a quorum.
66. The continuing Directors may act notwithstanding any vacancy in their body but, if and so long as their number is reduced below the minimum number fixed by these Articles as the necessary quorum for Board Meetings, the continuing Directors may act for the purposes of increasing the number of Directors to that number or of summoning a General Meeting of the Company but not for any other purpose.
67. The Board may elect a Chairman and Deputy-Chairman of its meetings and determine the periods for which they, respectively, are to hold office and the Board may remove any person from office as Chairman or Deputy Chairman at any time. If no such Chairman or Deputy-Chairman is elected or if at any meeting neither the Chairman nor the Deputy-Chairman is present within fifteen minutes after the time appointed for holding the same, the Directors present may choose one of their number to be chairman of the meeting.
68. A meeting of the Board at which a quorum is present shall be competent to exercise all powers and discretions for the time being exercisable by the Board.
69. The Board may form committees and sectoral boards of its members or consisting of one or more of its members and others and may delegate any of its powers to any such committee. Any committee or sectoral board so formed shall, in the exercise of the powers so delegated, conform to any regulations that may be imposed on it by the Board.

70. The meetings and proceedings of any committee or sectoral board consisting of two or more persons shall be governed by the provisions herein contained for regulating the meetings and proceedings of the Board so far as the same are applicable and are not superseded by any regulations imposed by the Board under the last preceding Article.
71. A resolution in writing signed or approved by letter, telegram, telex or fax by all the Directors or by all the members of a committee or sectoral board shall be as valid and effectual as a resolution passed at a meeting of the Board or, as the case may be, of such committee duly called and constituted. Such resolution may be contained in one document or in several documents in like form each signed by one or more of the Directors or members of the committee concerned.
72. The Board or a committee of the Board may participate in any meeting of the Board by means of conference telephone or other communication facilities as permit all persons participating in the meeting to hear each other simultaneously and such participation shall constitute a presence at a meeting of the Board as if those participating were present in person.
73. All acts done by the Board or any committee or by any person acting as a Director shall, notwithstanding that it is afterwards discovered that there was some defect in the appointment of any Director or person acting as aforesaid or that he or any Director or member of such committee had vacated office or was not entitled to vote, shall be as valid as if every such person had been duly appointed and had continued to be a Director or member of such committee and to be entitled to vote.

#### **CHIEF EXECUTIVE OFFICER**

74. The Board may from time to time appoint a person as chief executive officer (“CEO”) for such period and upon such terms as it thinks fit and, subject to the provisions of any agreement entered into in any particular case, may revoke such appointment.
75. A CEO shall receive such remuneration in the form of salary as the Board may determine.
76. The Board may entrust to and confer upon a CEO any of the powers exercisable by it, other than the powers to borrow money and charge the property and assets of the Company, upon such terms and conditions and with such restrictions as it thinks fit and either collaterally with or to the exclusion of its own powers and may from time to time, subject to the terms of any agreement entered into in any particular case, revoke, withdraw, alter or vary all or any such powers.

#### **SECRETARY**

77. The Secretary to the Company shall be appointed by the Board for such term, at such remuneration and upon such conditions as it may think fit and the appointment of any such Secretary may be terminated by the Board. The provisions of sections 178 to 180 inclusive of the Act shall be observed.

#### **THE SEAL**

78. The Board shall provide for the safe custody of the Seal which shall only be used by the authority of the Board or a committee authorised by the Board in that behalf and every instrument to which the Seal shall be affixed shall be signed by a Director and by the Secretary or by a second Director or by some other person appointed by the Board for that purpose.

#### **ACCOUNTS**

79. The Board shall cause proper books of account to be kept with respect to:
  - a) all sums of money received and expended by the Company and the matters in respect of which such receipt and expenditure takes place;

- b) all sales and purchases of goods by the Company; and
  - c) the assets and liabilities of the Company.
80. The books of account shall be kept at the registered office of the Company or at such other place or places in Kenya as the Board deems fit and shall always be open to the inspection of the Directors.
81. The Board may, from time to time, determine whether and to what extent and at what times and places and under what conditions or regulations the accounts and books of the Company or any of them shall be open to the inspection of Members not being Directors and no Member, not being a Director, shall have any right of inspecting any account or book or document of the Company except as conferred by statute or authorised by the Directors or by the Company in General Meeting.
82. The Directors shall from time to time, in accordance with sections 148 to 152 inclusive, and 154, 155 and 157 of the Act, cause to be prepared and to be laid before the Company in General Meeting such profit and loss accounts, balance sheets and reports as are referred to in those Sections.
83. A copy of every balance sheet, including every document required by law to be annexed thereto, which is to be laid before the Company in General Meeting, together with a copy of the Auditor's report, shall, not less than twenty-one days before the date of the Meeting, be sent to every Member and every holder of income notes or debentures of the Company.

#### **AUDIT**

84. Auditors shall be appointed and their duties regulated in accordance with sections 159 to 162 of the Act.

#### **NOTICES**

85. Any notice or other document may be served by the Company on any Member or Director either personally or by sending it through the post (by airmail where such service is available) in a prepaid letter or by telegram, telex or fax addressed to such Member or Director at its registered address as appearing in the Register of Members or the Company's other records, whether such address shall be within or outside Kenya, or by telex or by telegram addressed as aforesaid. In the case of joint holders of a share, all notices shall be given to that one of the joint holders whose name stands first in the register of Members and notice so given shall be sufficient notice to all the joint holders.
86. Where a notice or other document is sent by post it shall be deemed to have been served on the third day after the day on which it was posted, if addressed within Kenya, and on the seventh day after the day on which it was posted if addressed outside Kenya. In proving such service or sending, it shall be sufficient to prove that the cover containing the notice or document was properly addressed and put into the post office as a prepaid letter or prepaid airmail letter. Where a notice is sent by telegram, telex or fax it shall be deemed to have been served at the expiration of twenty-four hours after the time at which it was sent.
87. A notice may be given by the Company to the person entitled to any share in consequence of the death or bankruptcy of a Member by sending it through the post in a prepaid cover or by telegram, telex or facsimile transmission addressed to it by name or by the title of representative or trustee of such deceased or bankrupt member or any like description at the address supplied for the purpose by the person claiming to be so entitled or by giving the notice in the manner in which the same would have been given if the death or bankruptcy had not occurred.
88. Notice of every General Meeting shall be given in some manner hereinbefore authorised to every Member, to every person upon whom the ownership of a share devolves by reason of its being a personal representative or trustee in bankruptcy of a Member where the Member, but for its death or bankruptcy, would have been entitled to receive notice of the Meeting, to the Directors of the Company and also to the Auditors for the time being of the Company.



## 6.5 Appendix 5: Sample Memorandum of Understanding between County Government, WSB, WSP & WSTF

**Memorandum of Understanding**  
**Between**  
**The County Government of**  
**[insert]**  
**And**  
**[INSERT The Water Service Provider]**  
**And**  
**The Water Services Trust Fund**  
**And**  
**[INSERT The Water Services Board]**

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### 1. Purpose

This purpose of this Memorandum of Understanding (MOU) is to set out the terms and understanding between:

- i. The County Government of ..... (The “County Government”); and,
- ii. (Water Service Provider) (the “Water Service Provider”) and
- iii. The Water Services Trust Fund (WTSF); and
- iv. The relevant Water Services Board (WSB) in the transitory period pending any review of the legal and institutional framework concerning water service provision.

### 2. Background

[To add specific background of project]

### 3. Water Service Provider Obligations

In accessing commercial financing, the Water Service Provider shall be required to:

- a. Generate its own revenue by carrying out its services and collect payment for provision of such services and therefore not borrow or repay using public funds
- b. Use funds obtained via commercial financing to develop and implement water supply and sanitation projects within their service areas in accordance with the project rules
- c. Access loans from commercial lenders, provided that neither the National government nor the County Government guarantees the loan taken by the WSP.
- d. Be in compliance with WASREB, parent WSB and Water Resources Management Authority regulations and any other statutory requirements governing the operation of a WSP
- e. Charge connection fees and consumers’ tariffs as mutually agreed by the County Government and the WSP; and as approved by WASREB
- f. Have in place concrete measures to ensure that residents of low income areas will benefit from the investment and



service.

- g. Provide a copy of this MoU to intended financiers as well as the WSTF.

#### 4. Guarantees

It is understood by all parties that neither the County nor National Government shall guarantee any borrowing by the WSP. Neither the County nor National Government has any obligation to cover any liabilities service any debts incurred by the WSP.

#### 5. Reporting Obligations

The WSP will report to the WSTF as follows:-

- a. Pre-loan phase and Technical Assistance Phase
  - i. The WSP shall fill an Expression of Demand form (Annex 1 to this Memorandum of Understanding);
  - ii. The WSP shall provide its Technical Assistance Requirements (being the technical, financial and economic viability of the proposed project);
- b. Finance Progress Reports
  - i. The WSP shall provide reports on progress made towards meeting financiers' lending conditions.
- c. Implementation
  - i. The WSP will provide Construction Progress Reports which will include financial, technical and administrative aspects of the project including compliance to the World Bank fiduciary guidelines;
  - ii. Reporting on social and environmental impacts as detailed on the Environmental and Social Management Framework (ESMF) and Resettlement Policy Framework (RPF).
- d. Changes in management/ownership of the WSP
  - i. During the life of any loan taken by the WSP, the WSP shall be under a continuous obligation to inform the financier as well as the WTSF of any changes in its management or ownership.
- e. Inspection

The WTSF shall be entitled to carry out inspections on the projects for which finance is obtained.

#### 6. WSP & County obligations in relation to WSP funds

- a. All funds collected for water services by the WSP through water bills, commercial financing and other sources shall be used entirely for the purpose of covering costs for the provision of water services and asset development in accordance with regulations made by the Regulatory Authority.
- b. For the duration of the loan, dividends or other payments shall not be paid to the owners of public water service providers.
- c. During the duration of any loan taken by the WSP, the County shall remain entitled to collect licensing fees from the WSP in accordance with the terms of its license, but shall not increase any such fees for the duration of the loan.
- d. The loan shall as far as possible, conform to the loan structure set out in Annex 2 to this Memorandum of Understanding. At all times during the duration of any loan taken by the WSP, that WSP will maintain a debt service account with the financier.
- e. For the duration of any loan taken by the WSP, the County agrees not to license any other public water service provider to provide water services in the area served by the WSP.

**7. The Subsidy application process**

In the provision of the Subsidy, the following activities/processes will be undertaken by the relevant parties:

- a. Promotional activities and Calls for Proposals by the WSTF via broadly accessible media
- b. Submission of the Expression of Demand form by the WSP
- c. Application for Technical Assistance to prepare project proposals by the WSP
- d. Preparation of project proposal, loan application and request for subsidy by the WSP
- e. Submission of project proposal, loan application and request for subsidy to the WSTF and Commercial Lender
- f. Appraisal of project proposal and request for subsidy by the WSTF and Issuance of Certificate of Eligibility for Subsidy
- g. WSP presents the project proposal, loan application and Certificate of Eligibility for Subsidy Funding to the Commercial Lender for appraisal and due diligence exercise.
- h. WSP signs loan agreement with Commercial Lender.
- i. WSTF and WSP sign the subsidiary agreement and the 1st tranche of subsidy to the WSP is made.
- j. WSP procures works, materials, hires contractor and supervises works during project implementation
- k. IVA verifies the project's physical outputs and reports to WSTF.
- l. WSTF pays 2nd tranche of subsidy and the WSP pays back the loan.
- m. WSP commissions the project and provides service delivery to the beneficiaries.
- n. IVA verifies three months' of continuous billing operation and reports to WSTF.
- o. WSTF pays 3rd tranche of subsidy and WSP pays back the loan.
- p. WSP continues to operate the project and uses project collections to repay the remainder of the loan.

**8. General**

This MOU in no way restricts either of the parties from participating in any activity with other public or private agencies, organizations, or individuals.

**9. Contact Information**

**The County Government of:**

Party's representative.....  
 Position.....  
 Postal Address.....  
 Telephone.....  
 E-mail.....

**Water Service Provider**

Party's name.....  
 Party's representative.....  
 Position.....  
 Postal Address.....  
 Telephone.....  
 E-mail.....

**The Water Services Trust Fund:**

Party's name.....  
Party's representative.....  
Position.....  
Postal Address.....  
Telephone.....  
E-mail.....

**The Water Services Board**

Party's name.....  
Party's representative.....  
Position.....  
Postal Address.....  
Telephone.....  
E-mail.....

**10. Duration**

This MOU is effective on the date of the final signature by the authorized officials from the County Government and Water Service Provider and shall remain in force for the duration of the loan (s) to which it applies. This MOU may be modified at any time by written agreement of the parties.

Nothing in this MOU shall be interpreted to limit or otherwise affect any authorities, powers, rights, or privileged accorded to the County Government or Water Service Provider or any of the officers, employees, or organizational units under any statute, rule, regulation, contract or agreement.

**11. Execution**

IN WITNESS to this Memorandum of Understanding, the authorized officials of the parties concerned have signed this contract in their respective names on the dates shown below:

**For the County Government**

Signature.....  
Name.....  
Position.....  
County Government of .....  
Date:.....

**For the Water Services Trust Fund:**

Signature.....  
Name.....  
Position.....  
Date:.....

**For the Water Service Provider:**

Signature.....  
Name.....  
Position.....  
Company .....  
Date:.....

**For the Water Services Board:**

Signature.....  
Name.....  
Position.....  
Board .....  
Date:.....

**6.6 Appendix 6: County Government Approval Template for Borrowing**

COUNTY GOVERNMENT APPROVAL OF BORROWING BY THE WATER SERVICES PROVIDER RESOLUTION (TEMPLATE)

EXTRACTS OF THE MINUTES OF THE MEETING OF THE COUNTY EXECUTIVE COMMITTEE OF COUNTY OF THE COUNTY GOVERNMENT OF \_\_\_\_\_ HELD AT \_\_\_\_\_ ON THE \_\_\_\_\_ DAY OF \_\_\_\_\_ 20\_\_\_\_

PRESENT:

- 1.
- 2.
- 3.
- 4.
- 5.
- 6.
- 7.

THE MEETING BEING QUORATE:

(Insert a summary of the minutes of the meeting)

.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....

WHEREAS, the (INSERT WATER SERVICE PROVIDER) intends to borrow the sum of [KES.....] from \_\_\_\_\_ (the "Loan") on the terms that the annual interest rate of the Loan shall be ..... [Rate %]; that the Loan shall mature on \_\_\_\_\_; that the Loan shall be due and payable in full at the end of such period; and that the Loan shall be evidenced by a Loan Agreement (the "Loan Agreement").

WHEREAS, the WATER SERVICE PROVIDER has requested the approval of the County Government to take the Loan; RESOLVED, that the County Government of \_\_\_\_\_ hereby approves the Loan; RESOLVED, that the County Government of \_\_\_\_\_ will not declare the company a county entity for the duration of the loan agreement.

We, the undersigned, being the County Executive Committee members present at the meeting of the County Government of ..... consent and agree that the above resolution was made at a County Executive meeting held on the .....day of ..... 20... at ..... O'clock at ..... location.

.....  
Name Signature

.....  
Name Signature

.....  
Name Signature

.....  
Name Signature

.....  
Name Signature

.....  
Name Signature

IN WITNESS WHEREOF, I ..... being the County Secretary of the County Government of..... certify that the above named County Executive Members on the ..... day of ..... 20.... acknowledged the above signatures or marks to be theirs; and having understood the contents of this corporate resolution, freely and voluntarily executed it.

**6.7 Appendix 7: Water Service Provider Approval Template for Borrowing by Board of Directors**

WATER SERVICES PROVIDER BORROWING RESOLUTION (TEMPLATE)

\_\_\_\_\_ LIMITED

EXTRACTS OF THE MINUTES OF THE MEETING OF THE BOARD OF DIRECTORS OF  
\_\_\_\_\_ LIMITED HELD AT \_\_\_\_\_ ON THE \_\_\_\_\_ DAY OF \_\_\_\_\_  
20\_\_

PRESENT:

- 1.
- 2.
- 3.
- 4.
- 5.
- 6.
- 7.

THE MEETING BEING QUORATE:

(Insert a summary of the minutes of the meeting)

.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....  
.....

WHEREAS, this Board of Directors deems it desirable and in the best interests of .....  
Water Services Providers (the “Company”) to borrow [KShs.....] from \_\_\_\_\_ (the “Loan”).  
NOW, THEREFORE, BE IT RESOLVED, that this Company will borrow [KShs.....] from  
\_\_\_\_\_ ; on the terms that the annual interest rate of the Loan shall be ..... [Rate %]; that the  
Loan shall mature on \_\_\_\_\_ ; that the Loan shall be due and payable in full at the end of such period; and  
that the Loan shall be evidenced by a Loan Agreement (the “Loan Agreement”).  
RESOLVED FURTHER, that the ..... and ..... of this  
company hereby authorized, directed and empowered to execute, for and on behalf of this company and in its name, any and

all documents required in connection with the Loan, including but not limited to the Loan Agreement, substantially in the form attached hereto as Exhibit A, with such changes thereto as the person executing same shall approve, such approval to be conclusively evidenced by the execution and delivery thereof.

RESOLVED, that the officers of this company are, and each acting alone is, hereby authorized to do and perform any and all such acts, including execution of any and all documents and certificates, as such officers shall deem necessary or advisable, to carry out the purposes and intent of the foregoing resolutions.

RESOLVED FURTHER, that this Company shall open and keep a "Water Revenue Collection Account" with the bank issuing the loan, for the duration of the loan.

RESOLVED FURTHER, that any actions taken by such officers prior to the date of the foregoing resolutions adopted hereby that are within the authority conferred thereby are hereby ratified, confirmed and approved as the acts and deeds of this Company.

We, the undersigned, being the directors present at the meeting of this Company consent and agree that the above corporate resolution was made at a board of directors meeting held on the .....day of ..... 20... at ..... O'clock at ..... location.

.....  
Name Director's signature

.....  
Name Director's signature

.....  
Name Director's signature

.....  
Name Director's signature

.....  
Name Director's signature

IN WITNESS WHEREOF, we ..... and ..... being the Chairman and Secretary certify that the above named directors on the ..... day of ..... 20.... acknowledged the above signatures or marks to be theirs; and having understood the contents of this corporate resolution, freely and voluntarily executed it.

### 6.8 Appendix 8: Water Service Board Approval Template for Borrowing by WSB

WATER SERVICES BOARD RESOLUTION APPROVING BORROWING BY THE WATER SERVICE PROVIDER  
TEMPLATE (TEMPLATE)

WHEREAS, this Board of Directors deems it desirable and in the best interests of .....  
Water Services Providers (the "Company") to borrow [KES.....] from \_\_\_\_\_ (the "Loan").

NOW, THEREFORE, BE IT RESOLVED, that this Company may borrow [KES.....] from  
\_\_\_\_\_; on the terms that the annual interest rate of the Loan shall be ..... [Rate %]; that the  
Loan shall mature on \_\_\_\_\_; that the Loan shall be due and payable in full at the end of such period; and  
that the Loan shall be evidenced by a Loan Agreement (the "Loan Agreement").

RESOLVED FURTHER, that the Managing Director of this company hereby authorized, directed and empowered to execute,  
for and on behalf of this company and in its name, any and all documents required in connection with the Loan, including  
but not limited to the Loan Agreement, substantially in the form attached hereto as Exhibit A, with such changes thereto as the  
person executing same shall approve, such approval to be conclusively evidenced by the execution and delivery thereof.

RESOLVED, that the officers of this company are, and each acting alone is, hereby authorized to do and perform any and  
all such acts, including execution of any and all documents and certificates, as such officers shall deem necessary or advisable,  
to carry out the purposes and intent of the foregoing resolutions.

RESOLVED FURTHER, that any actions taken by such officers prior to the date of the foregoing resolutions adopted  
hereby that are within the authority conferred thereby are hereby ratified, confirmed and approved as the acts and deeds of  
this corporation.

We, the undersigned, being all the directors of this Corporation consent and agree that the above corporate resolution was  
made at a board of directors meeting held on the .....day of ..... 20... at ..... O'clock  
at ..... location.

.....  
Name Director's signature

.....  
Name Director's signature

.....  
Name Director's signature

.....  
Name Director's signature

.....  
Name Director's signature



## 6.9 Appendix 9: WSP Capacity Diagnostic Assessment Tool

### Overview of Approach

As part of the credit appraisal, commercial banks or their advisers may visit the utilities to assess their management capacity. They can use the following tool to test Knowledge, Skills, Attitudes and Practices. This tool is sufficiently robust to meet the objective to assess the current capability of WSPs in relation to accessing and managing commercial financing and inform the next steps of the assignment.

### Management Quality Attitudes and Practices

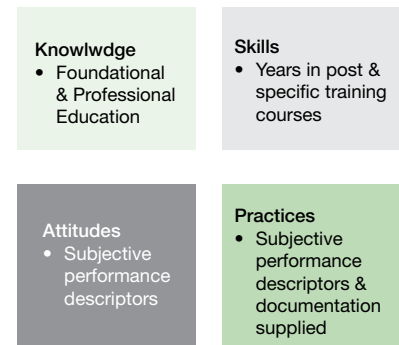
Objective performance indicators provide good measure regarding the output of an institution; they cannot describe why there may be particular strengths and weaknesses. Some studies have shown that ‘Qualitative measures or targets give a better indication of performance than Quantitative’ (Peters and Waterman 1982:284). In order to evaluate the qualitative component, we adapted a methodology derived from earlier utility studies by USAID through the Camp Dresser McKee WASH programme to assess attitudes and practices as being critical for successful water and sanitation utilities.<sup>10</sup>

This methodology has been in existence since 1998. We have adapted it to take account of the operating environment in Kenya as well as breakthroughs in technology (such as mobile telephones and associated technology) and other industry or management good practice. These developments and advances could not have been foreseen in the original design of the diagnostic tool.

The approach focuses on problem definition and identification in institutional areas. It is interdisciplinary and seeks to identify crosscutting issues. It is also designed to avoid the temptation to jump to ‘quick-fix’ solutions while ignoring the more difficult and basic issues. The methodology is based upon team field investigation procedures which identify, define, and verify institutional performance using indicators which have been pre-identified. It also acts as a form of validation of the Skills and Knowledge data also collected.

The WASH approach perceives the main categories or performance indicators of a WSP to be as indicated in Figure 29.

**FIGURE 28: CAPABILITY ASSESSMENT METHODOLOGY**



<sup>10</sup> WASH Technical Report No 37, Guidelines For Institutional Assessment - Water And Wastewater Institutions,1986 [http://pdf.dec.org/pdf\\_docs/pnaaz336.pdf](http://pdf.dec.org/pdf_docs/pnaaz336.pdf)

**FIGURE 29: WASREB KEY PERFORMANCE INDICATORS FOR THE WATER SECTOR**

The indicators and their sub components are set out in detail in the toolkit. The tool employs three data-gathering techniques in order to measure effectiveness in each of these performance categories:

- interviewing (this technique should account for two thirds of the usable information collected)
- reviewing institutional documentation such as business & Strategic plans, customer charter, KPI reporting
- observation

### Interviews

To ensure consistency in the structure of the interview, the interview team should focus on particular practices and target interviewees:

- a) 'Leadership', 'Management' and 'Autonomy' through interviews with the Managing Director;
- b) 'Consumer and Commercial orientation' through interviews with the Commercial Manager and Customer Care team;
- c) 'Maintaining and Developing Staff with the Human Resources Manager and;
- d) 'Technical capability' with the Technical Manager.

### Scoring

'Attitudes and Practices' can be determined from the interviewers' reflective scoring process based on approximately ten self-administered reflection questions

on each of eight main attitude areas. These areas coincided with the practice areas that toolkit focuses upon in interviews with senior managers and visits where possible to treatment works and water kiosks as a means of broadening our understanding of capability.

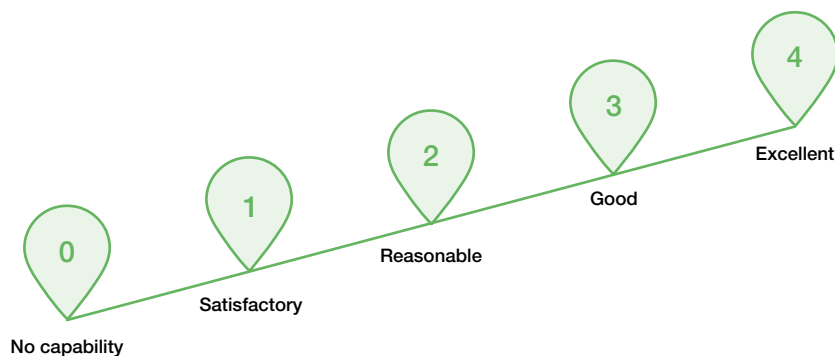
In order to make subjective judgments on capability and management quality, the particular practices focused on in the assessment need to be linked to:

- The risks and resilience of the utilities' business model with a focus on water resources management (product availability risks);
- Water supply management (product retailing risks: physical losses);
- Sewage collection;
- Treatment and waste disposal risks (product recycling risk);
- Project planning and delivery risk (commercial finance absorption capacity);
- Consumer billing (commercial losses and also issues of bill concentration)
- Bill collection and customer care risks (cash flow risks)

These topics are seen to embody the risks related to commercial lending to WSPs and therefore also form part of the toolkits that is designed to enhance utility and lenders awareness of each other's concerns regarding borrowing and lending.

A five-point scale is utilized in scoring. In the course of the evaluation, some areas can be left blank if the scorer did not believe they had adequate knowledge or expertise to make a judgment.

**FIGURE 30: FIVE POINT SCORING SCALE FOR KSA ASSESSMENT**



There is deliberately no ‘mid-point’ on the ‘unsatisfactory’ to ‘excellent’ part of the scale to limit a scorer’s tendency to mark as ‘average’ at a mid-point.

All scoring need to be undertaken independently. This is a subjective process because different scorers having different opinions and experiences which affect the awarding of outcome they give. The tool kit also recognize ‘primacy’ (different scoring levels for initial visits) and ‘recency’ effects (scoring most strongly the most recently visited service provider when scoring in a batch). These cognitive biases mirror a lender’s likely subjective determination of ‘quality of management’, often influenced by ‘first impressions’ (in the premises or the people met) and/or confidence in ‘ability to do business with that person’ which is known can outweigh the more objective financial indicators with respect to a lender’s perception of borrowing and loan servicing capacity.

**Analysis & Reporting**

The analysis and reporting is in two parts. There is a cross-utility analysis, which identifies trends and outliers in Sections under Findings- Management Quality Attitudes and Practices and Risk and Resilience, and an analysis and report on each individual utility set out in Figure 31: Sample Spider Diagram.

Results are reported using spider diagrams which identify strengths and gaps as well as some associated commentary on an exception basis.

**FIGURE 31: SAMPLE SPIDER DIAGRAM**



### Knowledge and Skills

‘Knowledge’ and ‘Skills’ can be determined by collecting information on formal professional and educational qualifications of staff and the number of years in the position to act as another proxy for skills.

Data requirements which are related to Knowledge and Skills are set out in the data diagnostic toolkit attached

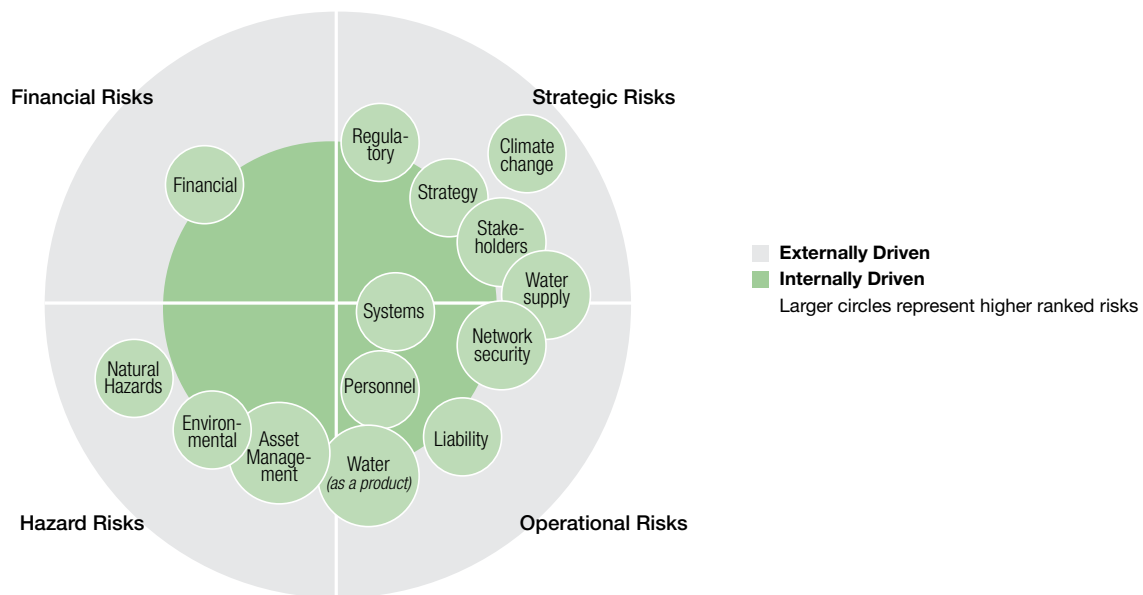
### Risk and Resilience

There are specific issues of risk and resilience that a commercial lender would want to understand in order to ensure that appropriate mitigation measures are put in place.

The approach should be tailored to match the Capability Assessment against the likely risks related to water and wastewater management. This is both to determine if and where capacity building is likely to be required and to guide potential borrowers on the likely issues to consider with respect to lending to water and sanitation service providers.

This approach was adapted from the Marsh 2013 Water Industry Insurance and Risk Benchmarking Report which identifies four key risk areas: financial, strategic, operational and hazards.<sup>11</sup>

**FIGURE 33: WATER INDUSTRY RISKS RADAR**



Source: Marsh & McLennan – 2013 Water Industry Insurance & Risk Benchmarking Report

<sup>11</sup> <http://uk.marsh.com/Portals/18/Documents/2013%20Water%20Industry%20Insurance%20and%20Risk%20Benchmarking%20Report%20Aust-UK%20Electronic%20-%20may13.pdf>

The toolkit adapts the Operational and Hazard risks approach to explain capacity issues with respect to the most significant risks regarding water and sanitation management.

Financial risks approach has been omitted as these are comprehensively catered for through the shadow credit rating assessment. Also omitted were two 'strategic risks', as defined by Marsh, with respect to 'regulatory' and 'stakeholder' issues as these are already captured in the 'Organizational Autonomy' scoring and commentary for each WSP.

The objective was to make these risks more explicit from a technical perspective.



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