



East African Tea Trade Association
Tea Trade Centre, Nyerere Avenue, Mombasa

EATTA POSITION ON THE REVIEW OF DRAFT TEA REGULATIONS, 2020

The performance of the tea industry is vital to the Kenyan economy. Tea accounts for approximately 26% of Kenya's export earnings and is one of the leading foreign exchange earners contributing over Kshs 117 billion in 2019. The tea industry contributes about 4% to the GDP. More than 750,000 farmers directly earn a living from tea and more than 6 million Kenyans directly or indirectly depend on tea.

Tea is also the only cash crop grown widely in geographically dispersed areas in Kenya. The small-scale tea farmers' account for over 60% of Kenya's production through 69 KTDA managed tea factories with the rest being produced by the independent tea companies and plantations.

Tea is grown in 21 counties and is therefore an effective catalyst for development. Tea has assisted to fund maintenance of rural roads through tea cess and voluntarily provides health and education facilities to rural populations. Kenyan tea is of such a high premium in some consuming markets that the importers keep track of the auction trends on a weekly basis and will make purchase orders for a specific plantations or garden marks.

During the media briefing held on Thursday, 16th April, 2020, the Cabinet Secretary Agriculture, Hon. Peter Munya, presented the draft Tea Regulations for review by the public. The target of the regulations appears to be on the tea auction system and the smallholder tea sub-sector in Kenya. This sub-sector accounts for over 60% of the tea production in Kenya while plantations and independent tea factories account for 40% of the tea production.

It is the general view of EATTA that some of the proposed Regulations will have some positive impact on the tea industry and should be maintained. However, most of the regulations have far-reaching ramifications on the tea sector if allowed to be enacted in the current form; they should, therefore, be amended or deleted, or some exemption provisions inserted to the regulations before they are enacted. The absence of a National Tea Policy and sound Tea legislation and Regulations is a key contributor to the myriad challenges facing the tea sector.

Positively impacting Regulations: The following sections of the proposed regulations will be advantageous to the tea producers: Regulation 10 (7) and (17) which provide for mechanisms to ensure adequate leaf supply before granting a license to set up a factory; Regulations 10 (19) and 18(2) which provides for a clear mechanism for licensing and renewal of licenses and ensuring ethical management or governance of tea-producing companies; Regulation 23 (4) which provides for recognition and adoption of technology and promotion of electronic trading of tea and the general collation of data that will be useful for future planning purposes.

Faults in Regulations: There are inadequacies in the proposed Regulations and it is suggested that these either be deleted, amended or some exemption provisions inserted before the regulations are enacted into law:

Definitions and interpretations– There are need to make amendments to some of the terms and definitions in clause 2 of the proposed tea regulations to bring clarity and uniformity in the meanings of the terms used. The

affected definitions are; tea leaf, cottage, tea factory limited company, green leaf agreement, licensee, plantation tea grower and smallholder tea grower.

Registration and Licensing provisions - Regulations 10, 16, 18, 22, 24, 25, 29, 32, 34 and 35 need to be reviewed. The same applies to Regulations 16 and 24 on monthly return provisions for a tea packer and the provisions for registration of a marketing agent.

Value addition of 40% in two years is unrealistic – Reg. 16 (2) that requires all tea buyers /exporters to value add at least 40% of annual tea exports is unrealistic. Implementation of this Regulation will require huge capital investments and serious government support hence cannot be left to buyers to achieve on their own within two years. Sri Lanka has a robust value-added industry but it was built over 20 years and their government provided the necessary infrastructure and incentives. Also, the value addition for export is done with specific market requirements determined from comprehensive market intelligence and segmentation and this too requires a lot of government support.

The entire clause should be deleted and the government needs to conduct an initial in-depth study to evaluate the impact of the 40% value addition regulation prior to its being legislated. Even the measures on value addition and branding may not work as there are no incentives in the Regulations, which only have penalties. Further, value addition should be demand-driven based on the market and therefore the targets of 40% for buyers and exporters in Regulation 16 (2) and 20% for importers in Regulation 32 (12) is arbitrary. The value addition definition should be widened to include blended and bespoke made tea products.

Registration of a tea buyers or exporter- Reg.16 (4) (a-c) should be deleted as this is commercially sensitive information which if shared will undermine the competitiveness of the tea sector while interfering with proprietary rights of businesses and investors.

Conflict with Law of Contract– Reg. 22 (3) on Management Agent Agreement is restrictive to a maximum of 5 years which is against the Law of Contracts Act and the principle of privity of contract; the words “*not exceeding five (5) years*” in the clause should be deleted. This should be considered as a private contract between two willing parties and may be punitive if there is no room for renewal upon good performance. The same applies to company secretarial services. In both respects, there should be a provision enabling renewal. For the Government to dictate terms of remuneration in and life of a private contract is illegal for a number of reasons. It is anticompetitive as it is setting prices contrary to the Competition Act on price fixing. The remuneration should be dictated by the economy. Privity of contract, Government is not a party to the contract between the Agent and the factory which are both privately owned entities.

Tea relisted for sale (Reg. 24 (2))- The provision is that any teas that are not sold during a particular auction shall be re-listed for sale during the subsequent auction. In order to avoid loss by producers, the process of cataloguing has to be taken into account. There is need for such sale to be allowed to happen at any subsequent auction and not the immediate subsequent auction as this may cause logistical hurdles.

Electronic trading system – Reg. 23 (3) is applauded by stakeholders as a great proposal but the stipulated period of two months for setting up a robust system is not realistic. The EATTA auction automation process was signed between EATTA and TMEA in December, 2016 with a completion date of December, 2019 in order to cater for the development of a home-grown software, acquisition of hardware and need for training and change management. The project is at the final stages with ongoing user training, deployment of infrastructure

(data Centre) and piloting. The process of automation is currently in the final stages with members being sensitized to log in and purchase tea using the platform.

Conflict with Competition Act – Reg. 24(1) that provides for all teas processed and manufactured in Kenya for the export market except for orthodox and purple teas, within two (2) months from the commencement date of these regulations, being offered for sale exclusively at the tea auction floor among other challenges contradict the Competition Act. Direct sales are commercial decisions made by tea producers and to restrict them from offloading their products through their channels of the choice is anti-competition and therefore the entire sub-Regulation should be deleted or reviewed. Dependence on one selling channel only can lead to lowering of prices. It is clear that the auction and private channel complement each other in obtaining the best possible average price.

Tea Buyers Performance Bond (Reg. 24 (3))- The requirement is that all tea buyers shall henceforth submit to the Regulatory Authority (AFA) a performance bond in the form of a bank guarantee equivalent to 10% of the estimated value of the tea they intend to buy to underwrite commercial risks associated with buyers who fail and/or refuse to pay in full for the tea bids they win at the auction. This requirement is not necessary as tea is only collected from warehouses upon payment by buyers. The consequence of such a move would be to increase costs to the buyers that shall consequently be passed on to the farmers and investors. The most affected shall be the SMEs who constitute the majority of the tea buyers. There has never been a problem of payment by buyers since they are properly vetted by EATTA upon admission into membership.

Payment for all teas (Reg. 24(7))- The requirement is that all buyers pay in full for all teas they win at the auction before they take custody of the and lift the tea for export is not necessary. This is already provided for in the internal regulations of the auction organizer. As it stands no buyers take custody of the tea before it is paid for. In addition, it confirms that there is no necessity for a buyer's deposit.

Direct participation in the tea auction (Reg. 24(8))- This requires tea factory limited companies to register and participate at the Auction directly. Brokers and other service providers are expressly stopped from dealing at the auction on behalf of Tea factories. This fails to take cognizance that the Auction centre does not only deal with Kenyan Teas and that it may be impractical for the factories to directly deal at the Auction. Tea Factories dealing directly may not appreciate the sensitive dynamics of the trade and there are also more services offered by the Broker's other than at the Auction. This is over legislation by Government.

Brokerage services (Reg. 24 (9 and 10))-The provisions state that a registered tea broker shall offer brokerage services to a maximum of fifteen (15) factory limited companies. The provision does not take provide the criteria for allocating each broker 15 factories and that the brokers provide services to producers' tea factories in ten countries. The capping the number of tea clients, a broker can engage with is in itself a restrictive trade practice and therefore unlawful and against the CAK Act, as it infers that tea factory companies are not free to choose the broker whose quality services they prefer.

Direct Remittance to Factory accounts (Reg. 24 (11))- Remittance to Producers is currently within 14 days from the date of the Main Grade auction as stipulated in the existing EATTA Rules & Regulations, which also impose penalties on defaulters to discourage such practices. The proposal does not take into consideration weekends and public holidays. Some Producers opt to have their funds channeled through their respective broker who provides other services and advances which may require deduction from their proceeds of sale. This provision has not factored other service providers such as warehousemen.

Auction operations –Reg. 24 (15 & 16) -Many of the tea trade's unequivocal successes over the past 50 years derive from the effective self-governance, based on sound rules and regulations that have been proposed, discussed and adopted, some of which have later been appropriately amended to meet with the changing circumstances. The regulations are also ambiguous on further powers yielded by the Cabinet Secretary which gives the office holder discretion on the action that can be taken.

Approval of trading rules and regulations (Reg. 25)- The Regulation provides for submission of auction trading rules to the C.S for approval. This is an illegal provision since regulations 25(4) has already set out what should be contained in auction rules. The auction rules are made in accordance with the law and approval of members of the association and requirement for approval by Government renders such action illegal. This is also another case of over regulation by the Government.

Registration of tea importer- Reg. 32 provides for importation of tea into Kenya. Though regulation 32(11) provides that teas imported for blending or export shall be so exported within six (6) months of import, a distinction has to be made for auction teas brought in by other EATTA Member Countries. If the regulations are too rigid, other regional countries will set up their own auction centre and Kenya will lose largely the advantages that come with EATTA/Kenya having the regional auction centre.

Audited financial statements are private – Forms AFA/TD/E1 and Form AFA/TD/E2 require presentation of audited financial statements which are private and confidential business information. This provision should be deleted and replaced with “audit certificate”

Blending declaration– Reg. 38 (1) which requires that a person who blends any or various grades of tea produced in Kenya with any other tea produced outside Kenya to declare the percentage of Kenyan tea on the packaging and on the blend sheet needs to emphasize on the mark of origin as opposed to requirements on percentage.

Draconian measure on private business - Form AFA/TD/E1 provides power to AFA to seize and remove or order the removal of any manufactured tea or processing capacity if installed contrary to conditions of the licence. It should be amended to propose AFA serves notice to the offending party to remedy the situation within a reasonable timeline. If production is more than the licensed capacity due to favorable weather, the factory should not be penalized.

Conclusion

Generally, the proposed Regulation don't properly implement the objectives of the Crops Act as set out in section 3, that include development and growth in tea industry, enhancement of productivity and incomes of farmers and the rural population, improvement in investment climate and efficiency of agribusiness, reduction in unnecessary levies, taxes or other barriers to free movement of tea products with provision of a rationalized taxation system, reduction of unnecessary regulation or over-regulation of the tea industry and promotion of competitiveness of Kenyan tea. The Regulations concentrate only on registration, taxation and licensing matters for the tea subsector are also not rationalized. Also, scrutiny of the Regulations reveals that some sections of the Crops Act that pertains to tea were not operationalized in the Regulations. There is need for a thorough review of the Regulations.

With a view to streamlining the challenges facing the tea sector the Government is requested to create an enabling environment and address concerns on the lack of a comprehensive National Tea policy, legal and

regulatory framework; over-production of tea versus tea quality, zero rating VAT on tea in order to encourage local consumption and enhance exports and need to create an autonomous Tea Board and removal of Tea research from KARLO. There is also need to address issues on the unfavourable land tenure and rates and increased high cost of inputs, cost effective Standard Gauge Railway, low levels of value addition at less than 10% and market access constraints.

About the East Africa Tea Trade Association

The East Africa Tea Trade Association (EATTA) is a voluntary, non-profit umbrella body representing the interests of the tea industry in Africa. EATTA was registered in 1956 and has 220 members drawn from ten countries (Kenya, Uganda, Tanzania, Rwanda, Burundi, Ethiopia, DRC, Malawi, Madagascar and Mozambique) all actively engaged in growing, buying, broking and warehousing of tea. 67% of the volume of tea is traded through the Tea Auction Centre.

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