

REGULATORY IMPACT STATEMENT (RIS)

**CORPORATE GOVERNANCE GUIDELINES AND CODE OF CONDUCT FOR THE
SMALLHOLDER TEA FACTORIES IN KENYA, 2023**

November, 2023

LIST OF ABBREVIATIONS

CBA	Cost Benefit Analysis
RIA	Regulatory Impact Assessment
RIS	Regulatory Impact Statement
ROI	Return on Investment
KTDA	Kenya Tea Development Agency
TBK	Tea Board of Kenya

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EXECUTIVE SUMMARY

Tea is undeniably one of Kenya's vital cash crops, directly supporting over 600,000 households and exerting a significant impact on the nation's economy. Nonetheless, despite the immense contribution of smallholder tea farmers, who are responsible for over 60% of total tea production, the returns on their investment, labor, and initiative have not always matched their efforts. Smallholder tea farmers have often found themselves marginalized in decisions concerning their industry, with key determinations falling into the hands of other actors in the tea subsector, including KTDA, auctioneers, brokers, and government authorities.

Further, the tea industry has faced corporate governance issues such as unfair electoral systems, complicated marketing rules, conflict of interest, monopoly, corruption, lack of company secretary, and political interferences. In light of these issues, pursuant to Executive Order Number 3 of 2021 and in discharge of its functions, the Tea Board of Kenya conducted a consultancy bid to come up with the Tea Sub-sector (Corporate Governance) Regulations /Guidelines on Directorship. The objective of developing these regulations was to enhance accountability in the tea sub-sector and ensure its alignment with the best corporate governance practices.

The "Corporate Governance Guidelines and Code of Conduct for Smallholder Tea Factories in Kenya, 2023" therefore serves as a written testament to the unwavering commitment to fostering a culture of integrity characterized by values such as honesty, respect, responsibility, and accountability within the tea sub-sector. They act as a guiding compass, shaping the interactions, choices, and actions of directors in smallholder tea factories while upholding the highest ethical standards.

Specifically, the Corporate Governance Guidelines cover a wide range of features, including the composition of the board of directors, the role of shareholders, the management of risk, and the disclosure of information. The objective of these guidelines is to provide a framework for the smallholder tea factories to follow in order to ensure that they are meeting the highest standards of corporate governance. The comprehensive Code of Conduct on the other hand, outlines the standards that directors in smallholder tea factories must uphold, addressing various aspects including integrity, confidentiality, respect, adherence to rules and regulations, and the management of conflicts of interest. Therefore, it seeks to ensure the tea sector in Kenya operates with the highest ethical standards, promoting trust and responsibility in our interactions and decisions within smallholder tea factories.

In today's rapidly evolving society, industries are not solely judged by their financial success but also by their dedication to ethical conduct. It is imperative that different members of the tea sector acknowledge that their actions affect not only those around them but also consumers, strategic partners, and the communities they come from. Trust is the bedrock upon which these interactions are built, and this corporate governance guidelines and Code of conduct for small tea holders aims to strengthen that foundation.

1.0. Introduction

The Regulatory Impact Statement for the proposed Corporate Governance Guidelines and Code of Conduct for the Smallholder Tea Factories in Kenya, is prepared in accordance with the provisions of sections 6 and 7 (1) and (2) of the Statutory Instruments Act, 2013. Section 6 of the Statutory Instruments Act, 2013 requires the Regulation Making Authority to prepare a Regulatory Impact Statement (RIS) for the proposed regulations indicating the costs and benefits of the proposed regulations on the public and stakeholders. Section 7(1) and (2) of the Act set out the contents of a Regulatory Impact Statement for the proposed regulations as follows:

2.0. Statement of the Objectives and Reasons for the Proposed Guidelines and Code of Conduct

The overarching objectives for these Guidelines and Code of Conduct is to set out the standards of ethical behavior and conduct for smallholder tea factories to follow in order to ensure that they are meeting the highest standards of corporate governance.

The primary benefit of the proposed Guidelines and Code of Conduct would be establishment of clear standards for ethical behavior and conduct to achieve transparency, integrity, and accountability in their service delivery within the tea industry and related services.

By adhering to these standards, smallholder tea factories can enhance their corporate governance, which, in turn, fosters transparency, accountability, and trust within the sector. This improved governance is expected to lead to better financial returns, reduced conflicts of interest, increased investor and stakeholder confidence, and ultimately, the creation of a more equitable and prosperous environment for smallholder tea farmers and their communities.

The Guidelines and Code of Conduct shall be applicable to all board members, management, shareholders and stakeholders of smallholder tea factories.

The object of these Guidelines and Code of Conduct is to provide for—

- a) The establishment of a comprehensive framework for ethical behavior and governance standards for Directors in smallholder tea factories, fostering transparency, accountability, and responsible management practices.
- b) Safeguarding of interests and welfare of all parties connected to the smallholder tea factories by encompassing areas such as data protection, confidentiality, and resource management in a responsible manner.
- c) Alignment of the roles and responsibilities of Directors in the management of smallholder tea factories.
- d) Streamlining the decision-making process to enable efficient response to dynamic business environment and opportunities.
- e) Creation of a supportive organizational culture for the smallholder tea factories by encouraging people to conduct themselves with respect and professionalism.
- f) Ensuring sustainable relationships between the different stakeholders.
- g) Ensuring the long-term competitiveness of the tea industry while promoting pricing and affordability that supports source protection.
- h) Effective management of risks to safeguard the company's long-term viability and long-term competitiveness

3.0. Statement on the Effect of the Proposed Guidelines and Code of Conduct

The implementation of the proposed Guidelines and Code of Conduct for smallholder tea factories is expected to have a profound effect on the entire tea industry in Kenya. Specifically, this impact is expected to be felt on the following groups:

3.1. Effects on the Tea Industry Stakeholders

The proposed Guidelines and Code of Conduct will affect tea industry stakeholders in the following ways:

- a) Fairer prices and better returns for smallholder tea farmers for their tea.
- b) Improved access to information, which would enable tea stakeholders to make informed decision-making within smallholder tea factories.
- c) Involvement of sustainable practices in tea farming will ensure the health and productivity of tea plantations and resilient agricultural systems.

- d) Improved responsible resource management to cater for the interests and welfare of tea industry stakeholders.
- e) Effective dispute resolution of the disputes that arise in the tea industry.

3.2. Effects on the Public Sector

The proposed Guidelines and Code of Conduct will affect the public sector in the following ways:

- a) Enhanced regulatory oversight through clearer standards for oversight and enforcement.
- b) Enhanced enforcement on legal compliance within the tea industry.
- c) Enhanced consumer protection.
- d) Promotion of fair pricing and ethical practices would contribute to economic growth in the tea industry.
- e) Promotion of efficient utilization of resources and contribution to sustainable agricultural practices.
- f) Improved stakeholder trust and confidence would ensure collaboration between the public sector and industry stakeholders.

3.3. Effects on the Private Sector

The proposed Guidelines and Code of Conduct will potentially affect the private sector in the following ways:

- a) Enhanced reputation of private sectors within tea industry from adherence of guidelines on corporation guidelines.
- b) Increased investor confidence potentially lowering the cost of capital for private sector players in the tea industry.
- c) Effective risk management would help private sector entities identify and mitigate potential risks, thereby safeguarding their financial stability and operations.
- d) Gaining a competitive advantage by demonstrating reliability, transparency, and accountability, positioning themselves more favorably in the market.
- e) Practicing sustainable practices would align business operations with environmental and social responsibility, which can attract environmentally conscious consumers and investors.

4.0. Statement on Regulatory & Non-Regulatory Options

4.1. Option 1: Maintaining the Status Quo

Before considering new interventions, it is important to consider whether the problem could be resolved by making changes to practices within the existing regulatory framework, thus maintaining the status quo. Examples of this are:

- a) Making use of existing laws, regulation and/or guidelines
- b) Simplifying or clarifying existing regulation;
- c) Improving enforcement of existing regulation; or

These Guidelines and Code of Conduct represent a transformative and comprehensive approach, addressing not only the gaps in existing regulations but also providing a forward-looking blueprint for ethical conduct, governance, and sustainability within smallholder tea factories in Kenya. They therefore serve as the only necessary and unparalleled step towards fostering positive change and ensuring the long-term success and integrity of the tea industry in Kenya.

4.2. Option 2: Passing the Guidelines and Code of Conduct

The object of these Guidelines and Code of Conduct is to provide for—

- a) A comprehensive framework that actively promotes ethical behavior, transparent governance, and responsible conduct within smallholder tea factories.
- b) Safeguarding of interests and welfare of all parties connected to the smallholder tea factories by encompassing areas such as data protection, confidentiality, and resource management in a responsible manner.
- c) Alignment of the roles and responsibilities of Directors in the management of smallholder tea factories.
- d) Streamlining the decision-making process to enable efficient response to dynamic business environment and opportunities.
- e) Creation of a supportive organizational culture for the smallholder tea factories by encouraging people to conduct themselves with respect and professionalism.
- f) Ensuring sustainable relationships between the different stakeholders.
- g) Ensuring the long-term competitiveness of the tea industry while promoting pricing and affordability that supports source protection.
- h) Effective management of risks to safeguard the company's long-term viability and long-term competitiveness

4.3. Option 3: Other Practical Options

Alternatives to the Guidelines include information and education, market-based structures, self-regulation and co-regulation.

4.3.1. *Information and education;*

Information and education can be used to providing information and education to stakeholders within the smallholder tea industry. This information and education can be aimed at various tea stakeholders which include farmers, directors, and other actors in the tea value chain.

Educational programs, workshops, and awareness campaigns can be conducted to inform stakeholders about ethical practices, governance principles, and industry standards. This would empower them to make informed decisions and adopt best practices voluntarily.

While information and education encourage voluntary compliance, builds awareness, and fosters a culture of responsibility, it fully depends on the willingness of individuals to engage with educational initiatives. This may make enforceability process difficult prompting the guidelines and code of conduct to remain unappalled.

4.3.2. *Incentive/ market-based structures*

Incentive/ market-based structures involves shaping ethical behavior through market forces and consumer preferences. Consumers, recognizing and valuing ethically produced tea, may influence market demand. Private sector entities may adopt ethical practices to align with consumer expectations and gain a competitive edge. Driven by consumer demand, it effectively rewards ethical practices, however, this approach relies on market forces, may not address systemic issues without clear standards.

4.3.3. *Self-regulation*

Self-regulation entails industry players developing a framework to self-regulate a sector without external mandates. Organizations within the tea sector would ordinarily collaborate to create and enforce their own ethical guidelines and governance standards. This can include developing codes of conduct and mechanisms for self-monitoring. This in turn can promote the tea industry autonomy, flexibility in adopting standards and potential for faster adaptation to changing circumstances. However, this approach may lack uniformity and external oversight forming a potential for non-compliance without regulatory enforcement.

4.3.4. Co-regulation

Co-regulation involves a collaborative effort between industry players and regulatory bodies to establish and enforce ethical standards. In this approach, regulatory bodies work alongside industry stakeholders to create and enforce standards. This collaboration allows for a balance between industry autonomy and external oversight. The effect of this approach is that it may combine industry expertise with regulatory oversight, promoting a more comprehensive and balanced approach. However, it would still require mechanisms that provide for effective collaboration and coordination and safeguards against potential for conflicts of interest.

5.0. Costs-Benefit Analysis (CBA)

This section analyses the CBA of the proposed Guidelines and Code of Conduct in various dimensions including the Economic, Environmental and social impact.

5.1. Economic, Environmental and Social Impact

The proposed Guidelines and Code of Conduct, if passed, will be instrumental in fostering positive changes across economic, environmental, and social dimensions within the smallholder tea industry in Kenya.

5.1.1. The Economic Impact of the Guidelines and Code of Conduct

The economic benefits of proposed Guidelines and Code of Conduct are:

- a) Enhanced profitability through promotion of fair returns to smallholder tea factories.
- b) Clear governance standards attract investments, boosting the financial stability of smallholder tea factories and fostering economic growth.
- c) Implementation of sustainable practices ensures the judicious use of resources, contributing to cost-effectiveness and long-term economic viability.
- d) Increased efficiency and productivity through streamlined governance structures, promoting efficient decision-making.
- e) Adhering to governance guidelines can help mitigate legal and reputational risks, which could otherwise result in significant economic losses.

The economic costs of the proposed Guidelines and Code of Conduct include:

- a) Implementation costs to cater for expenses related to legal consultation, policy drafting, training programs, and communication strategies.

- b) Compliance Costs that may involve adjustments to existing practices, monitoring mechanisms, and reporting systems.
- c) Investments in technology and infrastructure to facilitate better data management, transparency, and accountability.
- d) Training and Capacity Building programmes may require resources and time, affecting the daily operations of the tea factories.

5.1.2. The Social Impact of the Guidelines and Code of Conduct

The social benefits of proposed Guidelines and Code of Conduct are:

- a) Empowerment of smallholder tea farmers by providing them with a voice in decision-making processes, and contributing to their socio-economic upliftment.
- b) Improved working conditions within smallholder tea factories, promoting a positive and respectful work environment.
- c) Community development through improved infrastructure, access to education, and healthcare facilities, positively affecting the social fabric of tea-growing communities.
- d) Social harmony and inclusivity within the tea industry that fosters a sense of community and shared responsibility.

The social costs of proposed Guidelines and Code of Conduct are:

- a) Implementation Costs for smallholder participation in decision-making may include resources for training, awareness programs, and creating platforms for their engagement.
- b) Compliance Costs, which may involve expenses, related to facility upgrades, safety measures, and employee training, affecting the operational budget of smallholder tea factories.
- c) Infrastructure Investment to cater for the initial costs of improving infrastructure, education, and healthcare facilities.
- d) Sensitization and Training may require investments in sensitization programs and diversity training to foster a culture of respect and understanding among the tea valuers chain.

5.1.3. The Environmental Impacts of the Guidelines

The environmental benefits of proposed Guidelines and Code of Conduct are :

- a) Promotion of sustainable practices can lead to reduced environmental impact, preservation of ecosystems, and long-term health of tea farms.

- b) Adherence to global environmental standards can enhance the environmental reputation of the tea industry thereby attracting environmentally conscious consumers and positively impact market positioning.
- c) By promoting responsible resource utilization, the guidelines contribute to the preservation of biodiversity within tea plantations and their surrounding ecosystems.
- d) Emphasis on sustainable practices prepares the tea industry to adapt to climate change, ensuring resilience and environmental sustainability.

The environmental costs of the proposed Guidelines and Code of Conduct are:

- a) Allocating resources for biodiversity preservation within and around tea plantations might influence the availability of land for tea cultivation.
- b) Adaptation to climate change might involve investments in climate-resilient technologies, which could have environmental implications in terms of their production and use.
- c) Adapting to climate change may also require modifications in production processes, potentially influencing resource use and emissions.
- d) Adhering to global environmental standards may involve compliance costs related to monitoring, reporting, and implementing necessary changes.
- e) Implementing sustainable practices may involve the use of new technologies or equipment, which could have environmental impacts associated with their production and disposal.

6.0. Conclusion

The proposed Guidelines and Code of Conduct if effectively implemented holds the promise of transformative impacts on smallholder tea factories in Kenya. By embracing and embodying the principles outlined in these guidelines, these factories can expect a multifaceted array of benefits that extend beyond mere compliance.

Firstly, a robust adherence to governance practices is anticipated to enhance the financial landscape of smallholder tea factories. Improved decision-making, risk management, and operational efficiency are poised to contribute to increased revenues and cost savings. This financial resilience will not only fortify the factories against economic uncertainties but also position them for sustainable growth and competitiveness in the market.

Furthermore, the implementation of the guidelines is envisaged to foster a culture of transparency and accountability within the smallholder tea factories. Stakeholders, including investors, customers, and

employees, are likely to place greater trust in entities that demonstrate a commitment to ethical and responsible business practices. This trust, in turn, can translate into strengthened relationships, enhanced market reputation, and increased stakeholder confidence towards the smallholder tea factories.

Beyond the financial realm, these guidelines aim to positively affect the smallholder tea industry's social and environmental dimensions, promoting sustainability and social responsibility. They align with global trends and position the industry as a responsible resource steward. Implementing these guidelines will thus improve employee satisfaction and productivity within smallholder tea factories.

Therefore, the Corporate Governance Guidelines and Code of Conduct for Kenyan smallholder tea factories could lead to responsible, sustainable, and prosperous business practices. Implementing these guidelines can help tea industry players navigate challenges, capitalize on opportunities, and contribute to Kenya's socio-economic and environmental fabric.

7.0. Recommendation

The approval and operationalization of the proposed Guidelines and Code of Conduct is recommended based on the Regulatory Impact Assessment.