



FALQs

PART VI OF A VI PART SERIES
OF THE CORPORATE AND COMMERCIAL LAW
FREQUENTLY ASKED LEGAL QUESTIONS.

BANKRUPTCY & CORPORATE INSOLVENCY

1. What is Bankruptcy?

- It is the compulsory administration of a person's estate by the Court for the benefit of his creditors.
- It occurs when persons fail to pay their debts as and when they fall due – where the persons' liabilities exceed their assets.
- It is a legal way of managing debts.
- It is governed by the Insolvency Act No 18. of 2015 ("the Act") – particularly Part III of the Act and the Insolvency Regulations, 2016 ("the Regulations").

2. When does bankruptcy occur?

- It occurs when a person is adjudged bankrupt by the Court either on the application of the creditor or the debtor.

3. What is a statutory demand?

- It is a demand by the creditor to the debtor to pay the debt owed to the creditor.
- It precedes the bankruptcy application such that the creditor's application is not allowed without having served the debtor with a statutory demand.

4. How can the debtor set aside a statutory demand?

- A debtor can make an application to set aside the statutory demand to the court before the lapse of 21 days of service to the debtor, or after the date of advertisement in the newspaper, whichever is earlier.
- The application is made by filing Form 7 and a Supporting Affidavit in Form 8 under the First Schedule of the Regulations.
- An application to set aside a statutory demand acts as a stay on the period of compliance with the demand.
- If the application is dismissed, the court may order the creditor to file a bankruptcy order immediately.

5. When can a creditor make an application for bankruptcy?

- Section 17 of the Act provides that a creditor may make an application for bankruptcy when:
 - o The amount of debt or aggregate amount of debt is equal to or exceeds the prescribed bankruptcy level. Currently, the prescribed bankruptcy level as set in Section 3 of the Regulations, 2016 is Two Hundred and Fifty Thousand Kenyan Shillings (KES 250,000);
 - o The debt or part of the debt is for a liquidated amount payable to the applicant creditor either immediately or at some certain future time, and is unsecured;
 - o The debt is a debt that the debtor appears either to be unable to pay or to have no reasonable prospect of paying; and
 - o There is no outstanding application to set aside a statutory demand in respect of the debt.

6. Can a secured creditor make an application for bankruptcy?

- Yes, although an application for bankruptcy by creditors is mostly made by unsecured creditors, a secured creditor may make an application for bankruptcy.
- Section 18 of the Act provides that for secured creditors to make an application for bankruptcy, they must make a statement giving up the security in the event that the bankruptcy order is given.
- Also, a secured creditor may make an application for bankruptcy where the application is made with regard to the unsecured part of the debt, and not the secured part of the debt. Here, the secured and unsecured parts of the debt are treated separately.

7. How will the creditor prove that the debtor appears to have no prospects of paying the debt due and owing?

- The creditor must prove that:
 - o He served the debtor with the statutory demand;
 - o At least 21 days have lapsed since the service; and
 - o The demand has neither been complied with nor set aside.

8. What documents does the creditor need to make an application for bankruptcy?

- A Petition in Form 3 under the First Schedule of the Regulations to be accompanied by:
 - o A Verifying Affidavit in Form 4;
 - o Proof of debt set out in Form 5; and
 - o An application for appointment of a trustee in Form 9.

9. What are the conditions to be met before a debtor makes an application for bankruptcy?

A debtor can make an application for bankruptcy when:

- The debtor is unable to pay his debts;
- The bankruptcy level for debtors is Five Hundred Thousand Kenya Shillings (KES 500,000) and One Hundred Thousand Kenya Shillings (KES 100,000) for small bankruptcies;
- The debtor must not have been adjudged bankrupt or made a composition with his creditors in the presiding 5 years – this is established by an insolvency practitioner, appointed by the Court, who investigates the financial affairs of the debtor and makes a report on the same; and
- The debtor who makes such an application shall publish the notice of his application in a newspaper in addition to one in the Kenya Gazette.



10. What are the documents that accompany the debtor's application for bankruptcy?

- Petition in Form 10 under the First Schedule of the Regulations accompanied by:
 - o An Affidavit in Form 8;
 - o Statement of debtor's financial position as in Form 11;
 - o Application for appointment of trustees in Form 9;
 - o Requirements of a statement of debtor's financial position as set out in Regulation 18 (3).

11. Who is a bankruptcy trustee?

- An administrator appointed by the Court, Official Receiver, or creditor to oversee the debtor's estate in a bankruptcy proceeding.

12. What are the powers of a bankruptcy trustee?

- Carry on business of the bankrupt;
- Bring or defend legal proceedings relating to the bankrupt's estate;
- Accept as the consideration for the sale of any property comprised in the bankrupt's estate an amount of money payable at a future time subject to stipulations as security or otherwise as the creditors' committee or Court thinks fit;
- Borrow money for the beneficial realization of the bankrupt's estate and to give security for the borrowing over the whole or any part of the property comprised in that estate;
- Make payments or incur liabilities with a view to obtaining, for the benefit of the creditors, any property that is the subject of the right, option or power; and
- Refer to arbitration or to compromise on such terms as may be agreed, any debts, claims of liabilities.

13. What are the consequences of being adjudged bankrupt?

- The property of the bankrupt person vests in the bankruptcy trustee or the Official Receiver where there is no bankruptcy trustee;
- The bankrupt is prohibited from doing any business or from being an employee of anybody without the consent of the bankruptcy trustee or the Court;
- Any concealed property of the bankrupt may be seized upon issuance of a warrant by the Court;
- The bankrupt is prohibited from doing anything that may defeat the beneficial interest of others in the bankrupt's property;
- Any bank accounts held by the bankrupt may be revealed by a bank to which the account is held upon knowledge that the account holder is an undischarged bankrupt; and
- The bankrupt is restricted from dealing with his property. The property is handled by a bankruptcy trustee or Official Receiver.

14. How is a bankrupt discharged from bankruptcy?

- A bankrupt is automatically discharged from bankruptcy three (3) years after the bankrupt lodges the statement of financial position. However, this discharge may be challenged by the bankruptcy trustee, Official Receiver, or creditors, after leave of Court to object.
- A bankrupt may apply for an early discharge. This application may either be granted or rejected by the Court. In case the application is rejected, the Court may give a date on when the debtor may make an application again.
- There may be public examination of the bankrupt where there is an objection to the debtor's automatic discharge or is due for an automatic discharge but is still undischarged from an earlier bankruptcy.

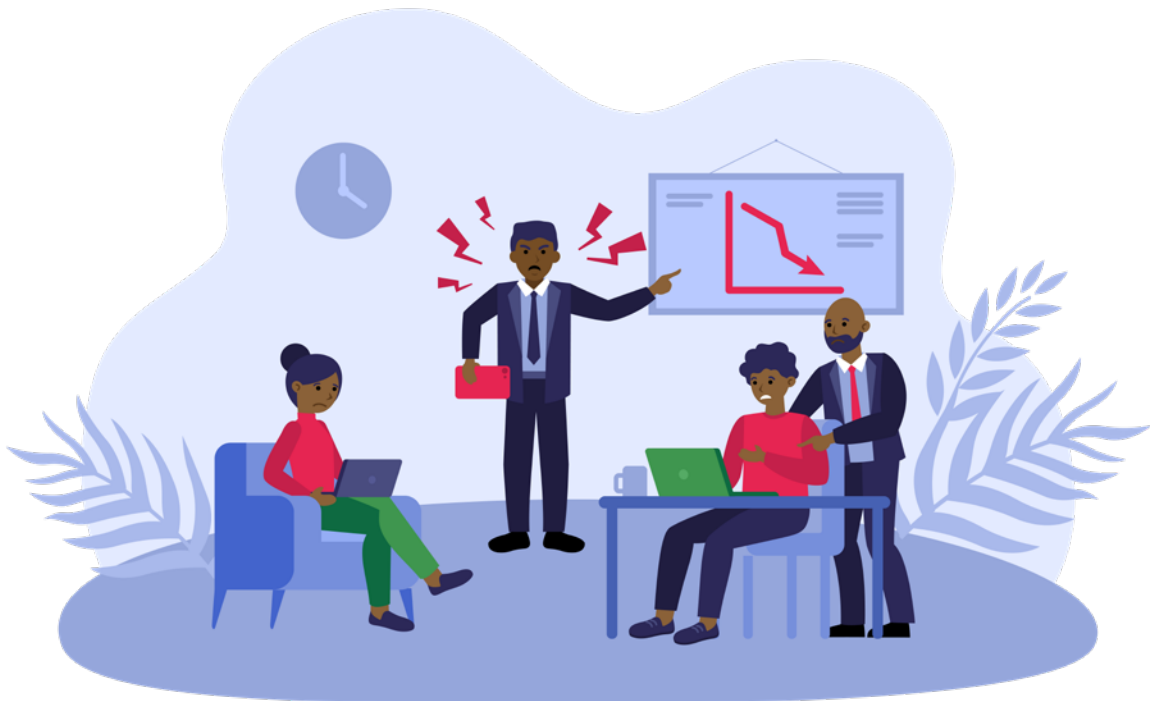
15. Are there any alternatives to bankruptcy?

- Yes, Section 14 of the Act provides four alternatives to bankruptcy as follows:
- **Voluntary Agreements** – this is where debtors seek to obtain creditors' approval of a debt settlement proposal. The process of voluntary agreements starts in either of two ways, that is, by an application for an interim order or an expedited procedure;
- **Make a proposal to creditors** – this is where the debtor intends to make a proposal to the debtor's creditors for a voluntary arrangement. The debtor may submit to the Official Receiver a document setting out the terms of the debtor's proposal and a statement of the debtor's financial affairs.

- **Payment in Instalments** – A summary instalment order is made by the Official Receiver directing the debtor(s) to pay their debts in instalments or in some other way, and in full or to the extent that the Official Receiver thinks fit in the circumstances; and
- **No asset procedure** – this applies to a debtor where:
 - o The debtor has no realizable assets;
 - o The debtor has not previously been admitted to the no asset procedure;
 - o The debtor has not been previously adjudged bankrupt;
 - o The debtor has total assets that are not less than One Hundred Thousand Kenya Shillings (KES 100,000) and do not exceed Four Million Kenya Shillings (KES 4,000,000); and
 - o The debtor does not have the means to repay any amount towards those debts.

16. What is Corporate Insolvency?

- This is where companies are unable to pay their debts when they fall due. It is where the companies' liabilities exceed their assets.



17. What is Winding up/Liquidation?

- This is the dissolution of a company

18. What are the types of Liquidation?

- There are two types of liquidation as follows:
 - o Voluntary Liquidation: could be by members or creditors of the company; and
 - o Compulsory Liquidation.

19. What are the reasons for voluntary liquidation?

- Lapse of time;
- Occurrence of an event; or
- Special resolution.

20. What is the process/procedure for members' winding up?

- This is outlined under section 382 and 398 (1) of the Act, which procedure is as follows:
 - o Directors make and deliver to the Registrar a statutory declaration of solvency;
 - o Notice of the resolution to wind up is issued and served on members and floating charge holders;
 - o A members' special general meeting is held seven days from the date of issuing the notice, and upon consent of all floating charge holders;
 - o Members in the general meeting pass the resolution for voluntary winding up, after which liquidation commences;
 - o The company must publish the resolution within 14 days of passage in the Kenya Gazette, in at least two newspapers and on their website, if any – failure to make such publication is an offence punishable by law;
 - o A liquidator is then appointed in the general meeting to wind up the affairs and distribute the assets of the company; and
 - o Upon appointment of the Liquidator, the powers of the directors cease to be in force.

21. What are the functions of the liquidator once appointed?

- Publish a notice of his appointment within seven days of appointment in the Kenya Gazette, two newspapers of daily circulation, and on the company's website, if any -failure to which constitutes an offence and attracts a fine of Five Hundred Thousand Kenya Shillings (KES 500,000) and a daily fine of Fifty Thousand Kenya Shillings (KES 50,000);
- Lodge a copy of the Notice to the Registrar for registration – failure to which attracts a penalty of Two Hundred Thousand Kenya Shillings (KES 200,000);
- Take office and assume the liquidation process;
- Where the liquidator is of the opinion that the company cannot pay its debts in full within the stipulated time, the Liquidator should:
 - o Notify the Registrar of Companies;
 - o Convene a meeting with creditors and lay before it a statement of the assets and liabilities of the company, failure to which attracts a fine of Five Hundred Thousand Kenya Shillings (KES 500,000);
 - o Upon the meeting, the winding up is converted into creditors voluntary winding up;
 - o Actions of the Liquidator requiring approval are approved by members in a general meeting;
 - o If winding up continues for more than 1 year, the Liquidator must convene a general meeting of the members within 3 months from the end of the year and must do so after every other year and lay before it an account of his acts and dealings and of the conduct of the winding up during the preceding year;
 - o When the affairs of the company are fully wound up, the Liquidator must prepare a winding up account showing how it has been conducted and the property of the company disposed of;
 - o He must then, by a 30-day notice in the Kenya Gazette and in at least two newspapers circulating in Kenya, summon a general meeting of the members and lay before it account giving any explanations necessary. If the Liquidator fails to convene the last general meeting of the company, he is liable to a fine not exceeding Five Hundred Thousand Kenya Shillings (KES. 500,000); and

- o Within 7 days of the meeting, the Liquidator must deliver a copy of his account to the Registrar for registration together with a return giving details of the holding of the meeting, minutes and its date. Failure to file returns is an offence attracting a fine not exceeding Five Hundred Thousand Kenya Shillings (KES. 500,000) and further daily fine of Fifty Thousand Kenya Shillings (KES. 50,000).
- As soon as practicable after receiving the accounts and return, the Registrar shall register them and on expiration of 3 months, from the date of registration, the company is deemed dissolved.
- However, the dissolution of a company may be deferred by the Court on the application of the Liquidator or other interested party. The Court order must be delivered to the Registrar within 7 days of its making. Failure to serve the order is an offence and on conviction, one is liable to a fine not exceeding Two Hundred Thousand Kenya Shillings (KES. 200,000) and a further daily fine of Twenty Thousand Kenya Shillings (KES. 20,000) until compliance.
- In such a case, the company shall be dissolved at the direction of the Court.

22. What informs a creditors' voluntary winding up?

- Directors are unable to make a formal declaration that the company can pay all its liabilities in full within 12 months.
- A company uses this method of liquidation when it is insolvent.

23. What is the procedure for a creditors' voluntary winding up?

- Directors are unable to make a solvency declaration;
- Notice of the resolution to wind up is issued and served on members and floating charge holders;
- The directors convene a general meeting of members to pass a special resolution;
- The members' general meeting is held first and its business is:
 - o to resolve to wind up;
 - o to nominate a liquidator;
 - o to nominate five representatives to be members of the liquidation committee (such members can be removed by creditors).
- The creditors' meeting is convened within 14 days from member's meeting, with a 7-day notice period. They must also convene a meeting of creditors, sending notices to creditors individually and advertising the meeting once in the Kenya Gazette and once at least in two newspapers circulating in Kenya;
- One of the directors presides at the creditors' meeting and lays before it a full statement of the company's affairs and a list of creditors with the amounts owing to them.
- The creditors' meeting;
 - o nominates a liquidator; and
 - o appoints five representatives of creditors to be members of the committee of inspection.
- The Liquidator appointed by the creditors takes office in case of conflict of choice. Only if creditors nominate the same person as members or, they fail to do so, can the members' Liquidator be final. Courts can be called upon to arbitrate in case of application by any party.
- On appointment of a Liquidator, Directors' powers cease.

24. What are the functions of the Liquidator once appointed?

- Within seven days after being appointed as liquidator of a company, the Liquidator shall:
 - o Publish a notice of the liquidator's appointment once in the Kenya Gazette and once in at least two newspapers circulating in the area in which the company has its principal place of business in Kenya; and on the company's website (if any). Failure to do so, will attract a fine of Five Hundred Thousand Kenya Shillings (KES. 500,000) and a further daily fine of Fifty Thousand Kenya Shillings (KES 50,000);
 - o Within fourteen days after publishing the notice of the Liquidator's appointment, the Liquidator shall lodge a copy of the notice with the Registrar for registration. Failure to do so, is an offence, attracting a fine of Two Hundred Thousand Kenya Shillings (KES 200,000);
 - o Actions of the Liquidator requiring approval are approved by the liquidation committee;
 - o If winding up continues for more than 1 year, the Liquidator must convene a general meeting of the members within 3 months from the year end and must do so after every other year and lay before it an account of his acts and dealings and of the conduct of the winding up during the preceding year. Failure to do so may lead to fine not exceeding One Million Kenya Shillings (KES. 1,000,000);
 - o When the affairs of the company are fully wound up, the Liquidator must prepare a winding up account showing how it has been conducted and the property of the company disposed of;
 - o He must then, by a 30-day notice in the Kenya Gazette and in some newspaper circulating in Kenya, summon a general meeting of creditors and table his liquidation accounts, and summon a general meeting of the members and lay before it an account giving any explanations necessary. If the Liquidator fails to convene the last general meeting of the company, he is liable to a fine not exceeding One Million Kenya Shillings (KES.1,000,000);
 - o Within 7 days of the last meeting, the Liquidator must deliver a copy of the account to the Registrar together with a return giving details of the holding of the meetings and the dates on which they were held. Failure to do so is an offence attracting a fine of Two Hundred Thousand Kenya Shillings (KES. 200,000) and further daily fine of Twenty Thousand Kenya Shillings (KES. 20,000);
- As soon as practicable after receiving the account and return, the Registrar shall register them and on expiration of 3 months, from the date of registration, the company is deemed dissolved.
- However, the dissolution of a company may be deferred by the Court on the application of the Liquidator or other interested party. The Court order must be delivered to the Registrar within 7 days of its making. Failure to serve the order is an offence and on conviction, one is liable to a fine not exceeding Two Hundred Thousand Kenya Shillings (KES. 200,000) and a further daily fine of Twenty Thousand Kenya Shillings (KES. 20,000) until compliance; and
- In such a case, the company shall be dissolved at the direction of the Court.

25. What is compulsory liquidation?

- A compulsory liquidation is a liquidation imposed by the Court through a Court order, upon hearing and deciding on a petition presented to it.
- Only the High Court has jurisdiction to supervise the liquidation of companies registered in Kenya.

26. What are the distinguishing features of a compulsory liquidation?

- Both solvent and insolvent compulsory liquidations are possible.

27. Who can petition for a compulsory liquidation?

- A compulsory winding-up petition may also be presented by any of the following parties:
 - o The company or its directors;
 - o Creditors;
 - o Contributor;
 - o Attorney General;
 - o Provisional Liquidator /Administrator;
 - o Liquidator; or
 - o Official Receiver.

28. What are the grounds for the petition for a compulsory acquisition?

- Members have by special resolution resolved that the company be wound up by the Court;
- A public company has failed to acquire trading certificate for more than 12 months;
- The company has failed to commence business within a year of incorporation;
- The company has suspended its business for a whole year;
- The number of members has fallen below the statutory minimum;
- The company is unable to pay its debts i.e., insolvent;
- The Court is of the opinion that it is just and equitable that the company be wound up;
- If, in the opinion of Attorney General, it is in the public interest for the company to be liquidated after receiving investigation reports from an investigator, Capital Markets Authority or Registrar;
- If the company or its directors have been convicted of an offence involving fraudulent conduct;
- If in the opinion of the Official Receiver, a voluntary liquidation cannot be continued with due regard to the interests of the creditors or contributories; and
- Winding up proceedings have been commenced outside Kenya in respect of a company incorporated outside Kenya but carrying on business in Kenya.



29. Where can I get further information on bankruptcy and insolvency?

- You can obtain further information from the Business Registration Service website, under the tab for the Office of the Official Receiver in Insolvency under this link: <https://brs.go.ke/official-receiver.php>. You can find useful information such as all the relevant forms and laws relating to this topic.

30. Which matters are classified as commercial disputes?

- According to Chief Justice A.M Cockar's listing of 18th November 1997 on Classification of Commercial Matters (available at <http://kenyalaw.org/kl/index.php?id=829>), the following matters can be classified as commercial matters:
 - o All proceedings in which an injunction is sought to restrain the realization of securities whether debentures or charges;
 - o All company matters and applications including winding up excluding cases in which a company is suing or being sued as an entity;
 - o All bankruptcy matters;
 - o All matters relating to arbitration other than enforcement of awards, excluding matters relating to land affected by the Land Control Board;
 - o All intellectual property matters;
 - o All claims for the recovery of unsecured debts (but including claims against guarantors) due to a bank or other financial institution in which a defence is filed. On the filing of the defence, the matter is automatically transferred to the commercial court; and
 - o Such matters as are certified by a judge of the commercial court as being suitable for determination in the commercial court having regard to the amount involved, the need for a speedy hearing and the nature of the case.
- In considering the nature of the case, the judge could be guided by the wording similar to the definition of a commercial action in the English Order 72 Rule 1 (1), that is:
 - o Arising out of the ordinary transactions of merchants and traders and without prejudice to the generality of the foregoing, any cause relating to the construction of a mercantile document, the export and import of merchandise, affreightment, insurance, banking, mercantile agency and mercantile usage.

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