



## INSOLVENCY LAW 2015 APPLICATION IN COVID - 19 PERIOD

Following the declaration of Covid-19 as a Global pandemic and the Governments' directive undertaken to contain the spread of the infection, the adverse impact on the economy is already being felt.

For many, the pandemic has been especially arduous financially, and will continue to be so in the near future. Individuals, small businesses and companies in Kenya are anxious of the short- and long-term ramifications of the pandemic will be on their livelihoods. Given the local and global effects of this pandemic, it is more likely that many people and businesses will face some insolvency related problems.

### **Conditions for insolvency**

#### **What is the test to determine insolvency?**

A debtor is deemed to be insolvent when they are unable to pay their debts, meaning: (i) If a creditor to whom the debtor is indebted in the sum of 100,000 Kenya shillings or more issues a written demand (statutory demand) requiring payment within 21 days and the company has not complied; (ii) If execution or other process issued on a judgment decree or order is returned unsatisfied as against the debtor; or (iii) If proved to the court that the debtor is unable to pay its debts as and when they fall due.

The Insolvency Act, 2015 provides for a number of options available to natural persons and incorporated bodies when they are faced with insolvency. These options vary depending on the amount of debt owed and the nature of the debtor, i.e. whether it's a natural person or an incorporated body.

#### **Options available under the Insolvency Act 2015:**

## Natural persons

### 1) Summary Installment Order (SIO) (Division 2 Insolvency Act)

A summary installment order is an order made by the Official Receiver under **Section 326** of the Insolvency Act directing the debtor to pay the debtor's debts- (a) in installments; and (b) in full or to the extent that the Official Receiver considers practicable in the particular circumstances of the case. In determining whether to issue the SIO, the Official Receiver will give an opportunity to both the debtor and the creditors to make representations as regards the matter. A Summary Installment Order may only be issued with regards to debt not exceeding Kshs.500, 000/-.

This procedure is especially helpful during this period as the debtor is able to obtain reprieve for up to 3 years by paying installments that he/she is able to pay during the said period. A debtor facing liquidity issues during this period may apply to the Official Receiver for this Order to be issued in order for them to focus on rebuilding their business.

### 2) No asset Procedure

This is a procedure under Section 344 of the Insolvency Act where the debtor has no realizable assets and owes debts between Kshs.100,000/- to Kshs.4,000,000/- . Under this procedure, the Official Receiver upon being satisfied that the debtor falls within the criteria set out under Section 345 admits the debtor to the No Asset Procedure (NAP).

In order to be admitted by the Official Receiver to the No Asset Procedure, a debtor is required to fall within the following criteria:

- a) the debtor should have no realisable assets;
- b) the debtor should not have previously been admitted to the no-asset procedure;
- c) the debtor should not have previously been adjudged bankrupt
- d) the debtor should have total debts that are not less than one hundred thousand shillings and not more than four million shillings; and
- e) the debtor does not have the means to repay any amount towards those debts.

Once a debtor is admitted, most debts are not enforceable and upon discharge after 1 year, the debtor is released from the outstanding amounts owed.

This procedure is especially helpful to a person who is operating a small scale business. The procedure is not as adverse and as long term as a bankruptcy order, but it has the same effects as one.

### **3) Individual Voluntary Arrangement**

This is a procedure under the Insolvency Act where the debtor makes a proposal to creditors on how he would intend to offset his debt. The proposal is deliberated on in creditors' meetings. Once agreed amongst the debtors' creditors, the said proposal becomes binding on the debtor. The viability of the proposal is determined by voting by the creditors. When approved by majority of the creditors, it is presented to court for adoption and is binding to all parties.

During the period of the proposal, the debtor may obtain interim orders of stay on all action by creditors.

This procedure is vital during this pandemic period as the debtor is able to negotiate with his/her creditors in a less acrimonious setting and come up with a proposal that is acceptable to all. This procedure ensures continuation of business when a person is facing liquidity problems and also ensures that no adverse action is taken against the debtor especially if the liquidity problem is temporary.

### **4) Bankruptcy**

Bankruptcy is a process where a debtor is declared unable to pay his/her debts and a bankruptcy trustee takes over the estate of the bankrupt for purposes of collecting and paying creditors. The Bankruptcy period automatically lapses after three (3) years and upon the lapse, the debtor is absolved of any personal liability for the debts specified in the order; if the discharge from bankruptcy is not opposed.

Bankruptcy allows the debtor to have a fresh start in business without debt. This is especially helpful to persons with larger debts which might be excluded under the other alternatives to bankruptcy.

## **Incorporated entities:**

### **a) Company Voluntary Arrangements**

This is an arrangement where the company makes a proposal to its creditors on how to offset its debts. This option involves the restructuring of debts over terms agreeable to both the company and its creditors. The proposal becomes binding if it is approved by creditors and adopted in Court.

This procedure is helpful during this period when corporate entities are facing temporary financial difficulty due to the pandemic. Under the procedure, the company will, based on its books, structure a repayment plan that will allow it to continue operating without creditors taking adverse action against them. During the period of the proposal, there is a moratorium/stay on all execution or recovery actions against the company thereby allowing the Company to negotiate with its creditors on how to offset or restructure its debt.

This procedure is vital during this period as it allows the company to continue trading while it offsets its debt in a manner that is favorable to both the company and its creditors.

### **b) Administration**

This is a procedure where an Administrator is appointed to run the company. The company would be maintained (for a period of one (1) year with a possibility of extension by Court) or sold as a going concern so as to enhance value for the benefit of its creditors.

An administrator is appointed either by the court, directors/members of the company or creditors and by a holder of a qualifying floating charge. During the period of administration, there is a moratorium on all proceedings against the company.

This procedure ensures the company continues to trade and possibly revert back to its Directors and shareholders once debts are paid. If debts are insurmountable, then the company continues to trade and is sold as a going concern thereby helping creditors get the best value under the difficult circumstances.

### **c) Administrative Receivership**

This is where an Administrative Receiver is appointed by a lender (debenture holder), with a security created before the commencement of the Insolvency Act in 2015, to sell off or manage that security. The Administrative Receiver is tasked with the duty to realize enough of the company's assets to pay the debenture holder. This procedure ensures that the debenture holder protects its interests when the company is facing financial difficulty. In some instances, upon recovery of the debenture holder's debt, the Administrative receiver is able to handover the company back to its directors.

This procedure ensures that there is accountability by the practitioner (Administrative Receiver) to the company and the debenture holder thereby protecting their interest.

### **d) Liquidation**

Liquidation is the process by which the management of the company's affairs and control of its assets are taken out of its directors' hands and vest in a liquidator. The assets are then realized by the liquidator and debts are paid out of the proceeds of sale in order of priority. Once the assets are sold and creditors paid, the Liquidator closes the company.

This is a drastic measure as the company will cease to exist after liquidation. However, liquidation is usually meant to protect the creditor and debtor as the company's assets are vested in the liquidator.

If a company is faced with debt and there is no possibility for its rescue, liquidation would be the best way forward in that the creditors interests would be protected and they would be paid out of the company's assets in a procedural manner with no undue preference to anyone. The Directors of the Company on the other hand will be able to start afresh as the company is a separate legal entity from its Directors and Shareholders.