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**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 7B**

**KENYA**

This is the **summative (formal) assessment** for **Module 7B** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

**The mark awarded for this assessment will determine your final mark for Module 7B**. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

**INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT**

**Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.**

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.

2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way**. **DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.

3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).

4. You must save this document using the following format: **[studentnumber.assessment7B]**. An example would be something along the following lines: 202021IFU-314.assessment7B. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked**.

5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6.The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

7. Prior to being populated with your answers, this assessment consists of **7 pages**.

**ANSWER ALL THE QUESTIONS**

**QUESTION 1 (multiple-choice questions) [10 marks in total]**

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph **in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

**Question 1.1**

Which one of the following **may not** make an application for bankruptcy on an individual?

1. A creditor.
2. A combination of creditors.
3. A supervisor of an individual voluntary arrangement.
4. The debtor.
5. The official receiver.

**Question 1.2**

Which of the following is **not correct**?

A bankruptcy trustee may not cancel a charge created by a bankrupt if:

1. money was actually advanced or paid in good faith.
2. the actual price or value of property sold or transferred was paid.
3. there was any other valuable consideration given for the charge.
4. the official receiver deems it fit to cancel the charge.

**Question 1.3**

**When** should the liquidator of a company convene a creditors’ meeting after appointment?

1. Within 30 days.
2. Within 28 days.
3. Within 21 days.
4. Within 14 days.

**Question 1.4**

Which of the following officeholders **has no power** to challenge a transaction at an undervalue under section 682 of the Insolvency Act?

1. An administrator.
2. A liquidator in a creditors’ voluntary liquidation.
3. A liquidator in a compulsory liquidation.
4. An administrative receiver.

**Question 1.5**

Which one of the following **may not** appoint or make an application for the appointment of an administrator?

1. A creditor.
2. The Official Receiver.
3. Directors.
4. A qualifying floating charge holder.

**Question 1.6**

Which one of the following powers / functions **are not** bestowed on an administrator?

1. Power to sell charged assets.
2. Power to borrow money.
3. Power to hire or fire directors.
4. Power to disclaim onerous contracts.

**Question 1.7**

**Within how many days** of the company entering into administration must the administrator hold an initial meeting of the company’s creditors?

1. Within 14 days.
2. Within 30 days.
3. Within 60 days.
4. Within 67 days.

**Question 1.8**

**Within how many days** is a supervisor of an individual voluntary arrangement (IVA) required to file his report on the IVA?

1. Within 7 days.
2. Within 14 days.
3. Within 21 days.
4. Within 28 days.

**Question 1.9**

Which of the following **may not** make a proposal for a company voluntary arrangement (CVA)?

1. Creditors.
2. Directors.
3. Liquidator (where the company is in liquidation).
4. Administrator (where the company is in administration).

**Question 1.10**

Which of the following **oversees** a company voluntary arrangement:

1. A director.
2. Official Receiver.
3. Receiver.
4. Liquidator.
5. Supervisor.

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 [maximum 2 marks]**

What are the options available to a secured creditor in the event of bankruptcy under the Insolvency Act?

[There are three options available to the secured creditor (section 226(2)):

1. To realise by selling the charged asset and to use the proceeds of such sale to settle the debt owed by the bankrupt (only if the creditor is entitled so under the terms of the charge);
2. To have the charged asset valued and prove in the bankruptcy as an unsecured creditor for the balance (if any) after deducting the amount of the valuation; or
3. To surrender the charged assets to the bankruptcy trustee for the benefit of all creditors and prove in the bankruptcy as an unsecured creditor for the whole debt.

The Insolvency Act provides that the bankruptcy trustee may, at any time by notice, require the secured creditor who holds a charge over a bankrupt’s property to choose any of the options within 30 days of receipt of the notice (section 262(3)).]

**Question 2.2 [maximum 4 marks]**

What are the grounds for the automatic discharge of a bankrupt? Does the automatic discharge have exceptions? If so, what are these exceptions?

[Section 254 of the Insolvency Act provides for the automatic discharge of a bankrupt after the three years, after the bankrupt lodges a statement of financial position in accordance with Section 50, except under the circumstances set out under subsection 2, namely:

1. the bankruptcy trustee or a creditor has objected and the objection has not been withdrawn by the end of the three years;
2. the bankrupt has to be publicly examined, on request by a creditor or bankruptcy trustee, and has not completed that examination; or
3. an objection by a creditor or the bankruptcy trustee to the discharge has been raised; or
4. the bankrupt has not been discharged from an earlier bankruptcy.

Under section 258(1) a bankrupt may at any time apply to Court for an order for early discharge from bankruptcy.]

**Question 2.3 [maximum 4 marks]**

What are the **objectives** of the administration procedure under the Insolvency Act?

[Under section 522(1), the objectives of administration are:

1. To maintain the company as a going concern;
2. To achieve a better outcome for the creditors as a whole than would likely be the case if the company were liquidated (without first being under administration); and
3. To realise the property of the company in order to make a distribution to one or more secured or preferential creditors.

The administrator is enjoined to perform his or her functions with the above objectives in mind (section 522(3)).]

**QUESTION 3 (essay-type questions) [15 marks in total]**

**PLEASE SELECT ONLY ONE OF THE FOLLOWING QUESTIONS BELOW. PLEASE DELETE THE QUESTIONS YOU CHOOSE NOT TO ANSWER.**

**Question 3.2 [maximum 15 marks]**

Discuss the process of administration under section 534 of the Insolvency Act.

[During administration, the company is protected from any adverse action by creditors seeking to liquidate the company. The Insolvency Act gives the company an opportunity to operate as a going concern and not necessarily engage in the sale and realization of its assets as a primary option.

1. Administration may be initiated:
2. By an administration order from the High Court

Through an application to the court and may only be done if the company is or is likely to become unable to pay its debts and the administration has real prospects of achieving its objectives.

1. By the holder of a floating charge

Holders of floating charges may appoint an administrator if such a charge empowers them to appoint an administrator of the company. To do so, they must first notify the High Court (by a notice of appointment, a statutory declaration and an affidavit of statement of facts), the Official Receiver, the company’s directors, contributories and creditors. Section 534 of the Act provides that the holder must be a holder of a qualifying floating charge in respect of a company’s property. A qualifying floating charge is one which is created by a document that states that this section of the Act applies to the floating charge or purports to empower the holder of the floating charge to appoint an administrator of the company.

The holder of a qualifying floating charge may also apply to Court for an administration order. The Court has the power to make an administration order in respect of a company even if a company may be able to pay its debts.

1. By the company or its directors

A company or its directors may initiate administration of a company out of court, through lodging with the High Court a notice of its intention to appoint an administrator, a statutory declaration and evidence of the administrator’s consent to act. The company or its directors must also notify the Official Receiver, any holder of a floating charge and the company’s directors, contributories and creditors.

Upon appointment, the administrator is deemed an officer of the Court, whether appointed by the Court or not. With respect to a holder of a floating charge.

1. Position of Creditors once a Company is under Administration

Once appointed, the administrator shall assume control of all the property to which the administrator believes the company is entitled to and has to manage the affairs and property of the company. While a company is under administration, a creditor may take steps to enforce a security over the company’s property only with the consent of the administrator or with the approval of the Court. The administrator may also make a distribution to creditors of the company and where a creditor is neither a secured nor a preferential creditor, a payment may be made to the creditor as part of a distribution only with the approval of the Court.

1. Administrator’s powers over charge property

The administrator of a company may dispose of, or take action relating to, property that is subject to a floating charge as if it were not subject to the charge. If this is done, the holder of the floating charge has the same priority in respect of acquired property as that holder had in respect of the property disposed of. However where a company’s property is subject to a non-floating charge, an administrator, should they intend on disposing the property, must make an application under section 588 of the Act to dispose property secured by charge if the Court believes that disposal of the property would be likely to promote the purpose of the administration of the company. Even so, the Act still provides protection to secured creditors where it expressly provides that an administrator’s statement of proposals may not include action that affects the right of a secured creditor of the company to enforce the creditor’s security (section 590).]

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

**PLEASE SELECT ONLY ONE OF THE FOLLOWING QUESTIONS BELOW. PLEASE DELETE THE QUESTIONS YOU CHOOSE NOT TO ANSWER.**

**Question 4.1 [maximum 15 marks]**

You have been approached by the directors of Eat it All Limited (EAL) to advise on their options in light of the company’s recent financial problems. The directors disclose the following to you:

* The company has not been doing well for the past three (3) years and the directors knew the company was insolvent;
* The company has outstanding loans owed to certain creditors. 20% of these loans are secured while 80% are unsecured;
* The company recently dismissed three of its directors for the misappropriation of funds;
* One of the company’s assets was sold to one of the main shareholder’s spouse at a value lower than market price;
* During the last nine months the company sold some assets to pay certain creditors who had threatened to sue them;
* As a result of its insolvency, the company was in the process of transferring (but this has not yet been completed) one of its most valuable assets to an SPV owned by its parent company;
* The directors have provided you with an independent business review report by a top audit firm that shows the company is viable and can return to profitability if certain structural changes are adopted. The directors inform you that they have shared this report with the company’s main creditors who are owed 80% of its total debts and who have shown their willingness to discuss any proposals from the company. The remaining creditors were unwilling to engage the directors.

The directors have asked you to **advise them** on the best course of action for the company and the various options available to them.

[To: The Directors of Eat it All Limited (EAL)

From: Insolvency Practitioner

Date: 24 July 2021

Subject: The Best Course of Action for EAL and Options Available

I have been approached to provide advice on the options available to EAL in light of its recent financial difficulties. I would advise as follows:

1. **Wrongful Trading**

Under Section 506(3) and (5) of the Insolvency Act, a liquidator may make an application to court and court may find directors liable if they conducted the business of the company knowing that there was no reasonable prospect of EAL being placed in insolvent liquidation.

From the facts the directors knew that the company had not been doing well for three years and that EAL had become insolvent. Section 506(6), however, provides a defence to the directors that they took all steps to avoid potential loss to company’s creditors, as directors of a company could have reasonably taken.

1. **Scheme of Arrangement**

The directors of EAL may by board resolution propose a compromise with the unsecured creditors who comprise 80% in value of the company’s outstanding loans. EAL would thus make an application to court for preliminary orders requiring a meeting of the creditors. Once such meeting is convened then the required threshold for approval of such scheme is 75% in value of the creditors or a class of creditors. Once the voting threshold is reached EAL would apply to court for sanctioning of the scheme to become binding on all creditors, even the ones who may have not consented.

1. **Fraudulent Trading**

The Court may order the three directors who were dismissed for misappropriation of funds to make such contributions to the company’s assets as the court considers fair and reasonable (Section 505(2)). This is because the Insolvency Act makes any person who carries on the business of a company with the intent to defraud creditors (or other fraudulent purpose) liable for fraudulent trading.

In addition, fraudulent trading is a criminal offence under section 1002 of the Companies Act, 2015. The offence is applicable whether or not EAL has been liquidated or is in the process of being liquidated.

1. **Impeachable Transactions**

Under the Section 682(5) of the Insolvency Act, a transaction is deemed to be undervalue if the company receives value considerably lower than the consideration the company is providing for the transaction. On application by the directors, the Court may find that the transaction with the shareholders spouse was undervalue and make an order setting aside the sale of the asset and restoring the position to that which existed before the transaction was made.

1. **Preference Transactions**

Where a company enters into a transaction that prefers certain creditors over others, a preference is deemed to arise. On application by the directors, the Court may find that the company gave a preference to some creditors, who had threatened to sue, by selling company assets and paying them off. The Court may make an order voiding the act constituted by the preference and restoring the position to that which existed before the transaction was made.

1. **Onerous Contracts**

The Insolvency Act provides for liquidator’s right to disclaim onerous contracts. Although this right is not explicitly provided to an administrator, it is arguable that the administrator has a power to disclaim an onerous contract such as the sale of the EAL’s most valuable assets to an SPV owned by the parent company. This is because this would defeat the objectives of the administration.

1. **Company Voluntary Arrangement (CVA)**

A CVA means a composition or arrangement proposed by the directors of a company setting out the solutions that the directors propose to be adopted to change the fortunes of a financially distressed company. If approved by the creditors and the court, then a supervisor is appointed to oversee the implementation of the arrangements under the proposals.

Therefore, the independent business review report can be provided by the directors to the supervisor so appointed to make a proposal for a CVA for approval by the shareholders and creditors.

Since the main creditors (80% in value) has expressed willingness to discuss the proposals, the CVA may be approved even if the remaining creditors do not consent. ]

**\* End of Assessment \***