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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 or Avenir Next 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: **[studentID.assessment7B]**. An example would be something along the following lines: 202223-336.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 “studentID” 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 2023**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2023**. 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 **9 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 parties **may not** make an application for the bankruptcy of an individual:

- (a) A creditor.
- (b) A combination of creditors.
- (c) A supervisor of an individual voluntary arrangement. ✓
- (d) The debtor.
- (e) The Official Receiver. X

0

Question 1.2

Choose the **incorrect** statement:

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

- (a) Money was actually advanced or paid in good faith.
- (b) The actual price or value of property sold or transferred was paid.
- (c) There was any other valuable consideration given for the charge.
- (d) The Official Receiver deems it fit to cancel the charge. ✓

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Question 1.3

How long after his appointment should the liquidator of a company convene a creditors' meeting?

- (a) Within 30 days. ✓
- (b) Within 28 days.
- (c) Within 21 days.
- (d) Within 14 days. X

0

Question 1.4

Which one of the following officeholders **has no power** to challenge a transaction at an undervalue in terms of section 682 of the Insolvency Act:

- (a) An administrator.
- (b) A liquidator in a creditors' voluntary liquidation.
- (c) A liquidator in a compulsory liquidation.

(d) An administrative receiver. ✓

(1)

Question 1.5

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

(a) A creditor.

(b) The Official Receiver. ✓

(c) Directors.

(d) A qualifying floating charge holder.

(1)

Question 1.6

Which one of the following powers / functions **are not** bestowed upon an administrator:

(a) Power to sell charged assets.

(b) Power to borrow money.

(c) Power to hire or fire directors.

(d) Power to disclaim onerous contracts. ✓

(1)

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?

(a) Within 14 days.

(b) Within 30 days.

(c) Within 60 days.

(d) Within 70 days. ✓

(1)

Question 1.8

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

- (a) Within 7 days.
- (b) Within 14 days.
- (c) Within 21 days.
- (d) Within 28 days.

✓ (1)

Question 1.9

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

- (a) Creditors.
- (b) Directors.
- (c) Liquidator (where the company is in liquidation).
- (d) Administrator (where the company is in administration).

✓ (1)

Question 1.10

Which one of the following oversees a company voluntary arrangement:

- (a) A director.
- (b) Official Receiver.
- (c) Receiver.
- (d) Liquidator.
- (e) Monitor.

(0)

Q1 = 7/10

✓

QUESTION 2 (direct questions) [10 marks in total]

Question 2.1 [maximum 2 marks]

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

According to s. 226 of the Insolvency Act, when faced with a bankruptcy situation a secured creditor can exercise any of the following options:

- (i) realise the charged asset by having it sold and the proceeds applied towards settlement of the secured debt;

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- (ii) ✓ have the charged asset valued and participate in the bankruptcy as an unsecured creditor for any balance due after deducting the valuation figure; or
- (iii) ✓ surrender the charged asset to the bankruptcy trustee for the benefit of the creditors as a whole and participate in the bankruptcy proceedings as an unsecured creditor claiming the entire debt owed by the bankrupt (to the previously secured creditor).

Question 2.2 [maximum 4 marks]

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

According to s.254(1) of the Insolvency Act, a bankrupt who lodged a statement (of their financial position) with the bankruptcy trustee (as stipulated by s. 50) is automatically discharged as a bankrupt after the lapse of three years from lodging the statement.

However, the automatic discharge will not take effect in certain exceptional circumstances provided for in s.254(2) which are:

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- (i) if at the end of the three year period there is still a pending objection by the bankruptcy trustee or a creditor; ✓
- (ii) if the bankrupt is required to be publicly examined under s.180 and the examination has not concluded; or ✓
- (iii) if the bankrupt remains undischarged from a preceding bankruptcy. ✓

Question 2.3 [maximum 4 marks]

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

According to s.222(1)(a) of the Insolvency Act, the objectives are:

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- (i) to maintain the subject company as a going concern; ✓
- (ii) to realise the subject company's property for purposes of a distribution to one or more secured creditors; or ✓
- (iii) to get a better outcome for the creditors collectively than that which they would likely get if liquidation had been the first resort instead of administration. ✓

or
Preferential Creditors

QUESTION 3 (essay-type question) [15 marks]

Please select only one of the following questions below. Please delete the questions you choose not to answer.

Question 3.1 [maximum 15 marks]

Discuss the process of voluntary and involuntary liquidation in a winding-up.

OK 9
15

Noted entire section on
creditor v. WUP.

Voluntary liquidation is a winding up of a company by the company itself at its own instance (s.393 of the Insolvency Act). By contrast, involuntary liquidation is a compulsory winding up of a company by Court order at the instance of any of the following as eligible applicants: a creditor/(s); the company (or its directors); a shareholder/(ers); an administrator; or the Attorney General (s.424 and 425).

Accordingly, the initiation of the processes is also different. Voluntary liquidation begins with a full inquiry into the affairs of the company by the board of directors culminating into a declaration of solvency that in their opinion the company will be able to pay its debts (s.398). The declaration must be made within the 5 weeks preceding the passing of the resolution for voluntary winding up. There must also be notice (of the intended liquidation) given to the holders of a qualifying floating charge over the company's property (s.393(2) and (3)). Then comes either:

Special
Resolution
7 days

- (i) the passing of a special resolution by the members of the company to wind-up the company (s.393(1)(b)); or
- (ii) the passing of an ordinary resolution by the members of the company to wind-up the company where the company has run its course or fulfilled the purpose for which it was incorporated such that there is no further business for existence under its articles and other constitutive documents (s.393(1)(a)).

No special

The passing of the relevant resolution (whether ordinary or special) triggers the liquidation process and becomes its effective date of commencement (s.395). The relevant resolution is then published: once in the government gazette; once in at least two newspapers of circulation in the area where the company has its principal place of business; and on the company's website if it has one (s.394). It is also filed with the Registrar of Companies. The members would also have to appoint a liquidator (s.399) to take charge of the affairs of the company in place of the board of directors (and if they do not, the Court can appoint one).

Creditors voluntary liquidation?

As for involuntary liquidation, it is initiated by commencement of a case in the High Court (s.423) on any of the prescribed statutory grounds under s.424, which include:

- (i) that a special resolution has been passed by the company for its liquidation;
- (ii) that 12 months have elapsed since incorporation without the business of a company commencing or that it has suspended its business for a whole year;
- (iii) that the membership of a qualifying company falls below 2;
- (iv) that the company is unable to pay its debts within the meaning of s.384; and
- (v) that it is just and equitable to liquidate the company.

If the applicant for the winding up proves its case, the Court would make a winding up order and the Official Receiver becomes the liquidator taking charge of the affairs of the company in place of the board of directors (until someone else is appointed as liquidator). The winding up order must be filed with the Registrar of Companies within 7 days of its pronouncement and with the Official Receiver (s.432(1)). Consequences of a liquidation order include: that leave of Court is required before instituting or continuing legal proceedings against a company (s.432(2)); that any subsequent disposition of company property, transfer of shares or alteration of membership status is void if done without leave of Court (s.429); and that any subsequent attachment or other form of execution against the company's property is void (s.430).

As stated, in both forms of liquidation (voluntary and involuntary) there is a liquidator who is vested with the power and responsibility to manage the affairs of the company to point of final conclusion of the process. Only the Official Receiver or an insolvency practitioner can hold the office of liquidator.

In both forms of liquidation (voluntary and involuntary) the liquidator gathers the assets of the company, realises them and applies them to pay off the creditors equally and without preference but subject to the statutory pecking order under s.471 and the Second Schedule. If there is any surplus remaining thereafter, the liquidator makes a distribution amongst the members in accordance with their rights and interests in the company.

In terms of conclusion of the process of a voluntary liquidation, once satisfied that the winding up of the company is practically complete, the liquidator would have to prepare and present final liquidation accounts to the members at a final general meeting convened by him (and if it turned into a creditor's liquidation [s.404] then a final general meeting of the company and meeting of the creditors). The liquidator would thereafter file the liquidation accounts and a final return with the Registrar of Companies for registration (s.402 or 414)). Three months after registration of the liquidation accounts and return, the dissolution of the company takes effect and the company's name is struck off the register of companies (s.494(3)).

As for conclusion of an involuntary winding up, when satisfied that the winding up of the company is practically complete, the liquidator would have to prepare and tender a liquidation report to the members at a final general meeting of the company convened by him (s.446). Thereafter, the liquidator would be required to file a notice with the Court attesting to the holding and outcome of the final general meeting and after that, to lodge a copy of the notice with the Registrar of Companies for registration (s.468(8) and (9)). Three months after registration of the notice, the dissolution of the company takes effect and the company's name is struck off the register of companies (s.497(3)).

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

Please select only one of the following questions below. Please delete the questions you choose not to answer.

Question 4.2 [maximum 15 marks]

$\frac{7}{15}$

High Def Co Limited (the company) is engaged in the manufacturing of spoons. The company has a total of 10 secured creditors with an outstanding debt of KES 5 billion in aggregate. The company also has outstanding unsecured debts of KES 100 million, including employees who are owed KES 10 million in unpaid wages. As a result of prevailing bad market conditions, the company's fortunes took a turn for the worst and the company is unable to pay its debts. One of the secured creditors, 1M Bank, approaches you to advise on the steps to be taken and, in addition, you are informed of the following:

- that one of the secured creditors has filed a liquidation petition in Court that has not yet been dispensed with and no order has yet been made;
- that 1M Bank has discovered that the directors have known for 12 months that the company is unable to pay its debts;
- the company has in the last six months paid-off some of its unsecured creditors; and
- part of the securities that 1M Bank holds relate to charges over land.

not just (and)

The company's land encumbered by the charges held by 1M Bank is classified as secured assets and does not form part of the estate of the company (as an insolvent). It would therefore be in 1M Bank's interests to swiftly explore a first resort of enforcing the charges, realising the land and applying the

proceeds to settle the company's indebtedness to 1M Bank. If there is any surplus remaining from the proceeds, 1M Bank would have to remit it to the liquidator of the company (if a liquidation order is eventually made) or to the company itself (if the liquidation application is unsuccessful).

If after enforcement of the charges there is still a balance owing from the company but the liquidation order has not been made, 1M Bank can sue the company for the balance.

*expenses
of 3rd party
goes*

However, if a winding up order has been made by the time that 1M Bank has found a balance to be owing after enforcement of the charges, then in consequence of that order, 1M Bank would not be able to sue the company without leave of Court.

1M Bank could in such event either apply to Court for leave to sue the company for the balance or it could participate in the pending liquidation proceedings as an unsecured creditor for that balance. It must be pointed out nonetheless that (in such event) the pecking order for the balance of the debt owed to 1M Bank would be fifth on the priority list for payment from the assets of the company after satisfying the following (s.471 and Second Schedule of Insolvency Act):

- (i) first priority given to settlement of the liquidator's remuneration and the costs of the liquidation process as well as the reasonable costs incurred in the liquidation court case and by the applicant to protect the assets of the company;
- (ii) second priority given: to the emoluments of the company's employees up to a cap, to the statutory deductions relating to employees (e.g income tax, mandatory pension contributions and medical insurance premiums);
- (iii) third priority given to outstanding corporate income tax, withholding tax and customs and excise duty due from the company; and
- (iv) fourth priority given to the holders of floating charges that have not yet crystallised.

If a liquidation order is made and it turns out that the assets of the company are insufficient to settle its debts (state of insolvent liquidation) then it would be useful for 1M Bank to explore some initiatives to help increase the asset pool available for debt settlement. The said initiatives include:

- (i) representations being made to the liquidator to apply to the Court to have the directors of the company declared as liable to contribute to the assets available to satisfy creditors in the winding up process on grounds that they knew or ought to have known that the company could not avoid an insolvent liquidation (since they have been aware for the past 12 months that the company was unable to pay its debts [s.506 of the Insolvency Act]); and
- (ii) representations being made to the liquidator to apply to Court to have the payments made to some unsecured creditors voided and the recipients repay the company on grounds that they were put in a better position than they would have been had they participated as unsecured creditors (given fifth priority) in the company's insolvent liquidation (s.683 and 684).

Alternatively, if the liquidator is not persuaded to take such action against the directors then (if the debt owed by the company to 1M Bank constitutes atleast half of the total indebtedness or if 1M Bank rallies such number of creditors who together with 1M Bank constitute that proportion), a request could be made to the Official Receiver to apply for a Court order for public examination of the directors with a view to gathering concrete evidence to fortify the cause for the aforesaid personal liability of the directors and voiding of the preferential transactions.

*Preference transaction ?
Fraudulent trading ?
Administration option ?*

Receivership under land laws ?

*** End of Assessment ***

