

Financing corporate rescue in Kenya: The case for a corporate rescue fund

Emily Onyango, winner of the Richard Turton Award 2024, presents a summary of her article



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This article is a summary of the full paper written by the 2024 Richard Turton Award winner, Emily Onyango from Kenya.

As part of the award, Emily was invited to attend the INSOL Europe Annual Congress in Sorrento in October 2024.

You can read the full version of the award-winning paper on our website: www.insol-europe.org/richard-turton-award

Corporate rescue in Kenya contributes to the survival of the economy as it allows for the restructuring of struggling businesses. Its success is dependent on financing to provide liquidity and stabilise operations. This paper explores the legislative framework and practice on corporate rescue financing in Kenya, the gaps, global best practices and proposes reforms to improve corporate rescue financing.

This paper answers three questions:

- (1) Are the existing modes of corporate rescue finance sufficient?
- (2) Is a corporate rescue fund necessary?; and
- (3) What lessons can be drawn from best practices?

Key recommendation in this paper are establishment of a corporate rescue fund to be utilised to adequately and efficiently finance formal corporate rescue processes once commenced in accordance with the existing legal framework.

Administrations and company voluntary arrangements are the key corporate rescue options in Kenya. To implement the objectives of these processes, financing is key. Financing is traditionally sourced through equity injections, new borrowing, additional borrowing, governments and institutional investors, venture capital and private equity firms. For corporate rescue in Kenya, the most common source of funding is additional borrowing. This paper explores these options and

provides justification why a corporate rescue fund would create efficiency in rescue financing. Additionally, this paper takes a comparative perspective which reviews the Singaporean and Ugandan jurisdictions where there is a legislative framework for rescue financing and defining what is deemed as rescue finance, which businesses qualify for it, limitations and oversight mechanisms.

The practice in corporate rescue financing in Kenya

(i) Administrations

The powers and functions of an administrator are provided under the Fourth Schedule of the Insolvency Act.² These include the power to borrow money for the beneficial realisation of the company's assets and to give security over those assets for lending.³ The Regulations also provide for post commencement credit to be paid in priority over the rights of other creditors.⁴ A major reason for the lack of success in turning around businesses in Kenya is that appointments are often made too late, and lenders typically delay funding or provide insufficient funds to mitigate their exposure.

(ii) Company Voluntary Arrangements

In Company Voluntary Arrangements (CVAs), directors make a proposal to the creditors for a voluntary arrangement under which the company enters into a composition in satisfaction of its debts or a scheme for arranging its financial affairs.⁵

Data from the regulator shows that, since the Act came into force, there have been only two CVAs in Kenya.⁶ The CVAs were mostly financed through the sale of non-core assets, as in the case of *Uchumi*,⁷ or injection of capital by shareholders, in the case of *Kaluworks*.⁸

Comparative analysis

In Singapore, corporate rescue is in the form of informal creditor workouts, schemes of arrangement⁹ and judicial management.¹⁰ Rescue financing, according to the Insolvency Restructuring and Dissolution Act, 2018 (**IRDA**) is financing necessary for the survival of the debtor and/or financing necessary to achieve a more advantageous realisation of the assets of the debtor than on winding up. In judicial management, it is financing necessary for the Court's approval of a scheme of arrangement. IRDA further provides that rescue financing is to be obtained with approval of court and is to be treated as costs and expenses of winding up and shall have priority over preferential debts if the debtor is wound up and can be secured by the debtor's unencumbered assets or subordinate to an existing security.¹¹ Notable here is the need for the debtor to prove that they are unable to secure any other source of funding without the funding being granted super-priority ranking.

In Uganda, corporate rescue can be implemented through Administrations under the Insolvency Act of Uganda¹² and a compromise or arrangement

under the Companies Act of Uganda.¹³ In 2022, the Ugandan Insolvency Act was amended to introduce post-commencement financing in administration and arrangement proceedings.¹⁴ In Uganda, to be considered as rescue financing, financing must facilitate the supervisor in implementing an arrangement or help the administrator achieve the goals of administration. To obtain rescue financing, the approval of both creditors and the court is required, and the officeholder can grant security over the debtor's property to a maximum of the value of unencumbered assets of the debtor.

Recommendation: The case for a corporate rescue fund

It is clear that, for the success of any rescue efforts, the right amount of funding needs to be availed within the requisite timelines. The paper recommends that lenders should provide for an allocation of an agreed percentage of profits to be set aside for utilisation in corporate rescue financing. Alternatively, the additional interest charged, over and above the agreed interest rate, in the event of default of any client should be set aside to be utilised for financing corporate rescue efforts.

Financial institutions may also consider taking out an insurance policy, in addition to the loan insurance already in place, where the insurer supports an agreed percentage of the rescue financing in the event of a rescue plan under the existing legislative framework. The allocation of profits, additional interests and insurance pay-outs are then to be consolidated into a fund, the corporate rescue fund. To ensure compliance with the allocation of funds towards the pool of funds be known as a Corporate Rescue Fund, this paper recommends that the Central Bank of Kenya (CBK) oversees the fund's management to ensure that the funds are only



utilised where necessary approvals have been obtained and majorly only to address corporate rescue financing for formal rescue processes.

Conclusion

In conclusion, corporate rescue financing in Kenya is crucial for preserving businesses and maintaining economic stability. The current legislative framework offers a foundation for corporate rescue through administration and (CVAs). However, the effectiveness of these mechanisms is undermined by inadequate and untimely financing.

The comparative analysis of Singapore and Uganda highlights how rescue financing frameworks, with strong oversight mechanisms and eligibility criteria, can enhance the success of corporate rescues. Singapore's court sanction of super-priority ranking for rescue finance and Uganda's limit on the borrowing for post commencement finance offer useful lessons for Kenya.

To address these challenges, the paper strongly recommends the establishment of a Corporate Rescue Fund in Kenya. This fund, regulated by the CBK and sourced from allocation of profits, insurance pay-outs or default interests, would address the key

gaps of adequacy and timeliness, offering a stable and regulated source of finance. ■

Footnotes:

- 1 Parts VIII and IX, Insolvency Act, 2015 (Kenya), available at: <http://kenyalaw.org/8181/exist/kenyalex/actview.xhtml?actid=CAP%2053>
- 2 Ibid., section 576.
- 3 Ibid., Fourth Schedule, paragraph 3(1).
- 4 Regulation 131A, Insolvency Regulations 2016.
- 5 Section 625(1), Insolvency Act, 2015.
- 6 Business Registration Service, 'Office of the Official Receiver' available at: <https://brs.go.ke/office-of-the-official-receiver/>.
- 7 'Uchumi Creditors Vote to Save Retailer – Uchumi Supermarket', available at: www.uchumisupermarkets.co.ke/case-study/uchumi-creditors-vote-to-save-retailer/
- 8 'Chandaria Gets Back Seized Firm as Banks Waive Sh6 Billion Loan' (Business Daily, 31 August 2022), available at: www.businessdailyafrica.com/bd/corporate/companies/chandaria-gets-back-seized-firm-as-banks-waiver-sh6-billion-3931868.
- 9 Part 5, Insolvency, Restructuring and Dissolution Act 2018 (Singapore Statutes Online), available at: <https://sso.agc.gov.sg/5443/Acts-Supp/40-2018/?ProvIds=P15->>.
- 10 Ibid., Part 7.
- 11 Ibid., section 101.
- 12 Insolvency Act, 2011 (Uganda), available at: www.ugandalaws.com/statutes/principle-legislation/insolvency-act,-2011
- 13 Companies Act, 2012 (Uganda), available at: <https://ulii.org/akn/ug/act/2012/1/eng@2015-07-01>
- 14 Section 164A, Insolvency Act, 2011 (Uganda).

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