FROM DEBTOR REPRESSION TO PROTECTION: GIVING DEBTORS A FRESH START UNDER THE KENYAN INSOLVENCY REGIME

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Abstract

Anchored on the normative foundations of the fresh start policy, this article examines the treatment of bankrupts under Kenya's repealed Bankruptcy Act, Cap 53 Laws of Kenya and then traces the elements of the fresh start policy under the Insolvency Act of 2015 that repealed Cap 53. Results show that Cap 53 was repressive against the bankrupt and he was never given a second chance in his economic and social life for the benefit of his creditors. Results also show that under the Insolvency Act of 2015, the bankrupt has a second chance to run his businesses as a going concern and can therefore pay his creditors from the proceeds of those businesses. The paper concludes that the Insolvency Act of 2015 breathes fresh life to the bankrupt and inspires optimism to creditors that their debts stand a better chance to be paid than was the case under the repealed Act.

Key Words: *Bankruptcy Law; Repression; Protection; Fresh Start; rehabilitation; discharged debtor, Kenya.*

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1. INTRODUCTION

Insolvency has been historically condemned on moral, religious, social, and economic grounds.[1] In the Hammurabi Code of the Hammurabi dynasty in Babylon which may have existed in the 2250 B.C., for example, the insolvent debtor was regularly sold into slavery.[2] It also frequently happened that the debtor's kinsmen would be sold into bondage in order to pay off his obligations. The Greeks allowed the amputation of the debtor's limbs and a subsequent sale into slavery. For early Roman law, the debtor's body could be cut out and distributed to creditors, before the *Lex Poetelia* was passed in 326 BC to prohibit action on the debtor's body but instead to allow action on his property.

The Bible has varying provisions on debt. For example, people who incur debts and promise to pay their creditors should not intentionally fail to make good their promises.[3] Likewise, the Bible is categorical that taxes, revenue, respect, and honour must be paid back.[4] In addition, no debt should "remain outstanding, except the continuing debt to love one another, for he who loves his fellowman has fulfilled the law."[5] The Bible further views those who borrow and do not pay back as weak, and those with mercy and give back as righteous.[6] Chapter 5 of the Quran enjoins debtors to respect their promises in the verse "Oh, ye who believe, fulfil obligations!" Creditors are asked to be patient and generous: "if the debtor is in difficulty, grant him time till it is easy for him to repay. But if ye remit in by way of charity, that is best for you

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[1] See generally Cohen, J. "The History of Imprisonment for Debt and Its Relation to the Discharge in Bankruptcy", 3(153) *J. Legal Hist.*, 1982; Levinthal, "The Early History of English Bankruptcy", 67 (1) *U. PA. L. REV.* 1919.

[2] Ss 115 and 116 of the Hammurabi Code.

[3] Ecclesiastes 5:5.

[4] Romans 13:7.

[5] Romans 13:8.

[6] Psalms 37:21.

if ye only knew."[7] However, the Bible also requires Christians to relieve their debtors of debts at the end of every seven years.[8] Common to both Christianity and Judaism is the requirement to pardon and return every debt, and to return every slave to their families on every Jubilee year, that is, the 50th year.[9]

Mediaeval law of merchants recognised the institution of bankruptcy, borrowing from the *cessio bonorum* concept of Roman Law. *Cessio bonorum* (Latin for a surrender of goods), in Roman law, is a voluntary surrender of goods by a debtor to his creditors. It did not amount to a discharge unless the property ceded was sufficient for the purpose, but it secured the debtor from personal arrest. The creditors sold the goods as partial restoration of their claims. The procedure of *cessio bonorum* avoided infamy, and the debtor, though his after-acquired property might be proceeded against, could not be deprived of the bare necessities of life. The main features of the Roman law of *cessio bonorum* were adopted in mediaeval= law, Scots law, and in French law.

In England, the beginning of insolvency law can be traced to the 1542 Statute of Henry VIII, the Statute of Bankrupts which, after a thunderous preamble denouncing debtors acting in fraud of their creditors, directed that the bodies of the offenders and all of their assets be taken by the requisite authorities and the assets sold to pay their creditors, "a portion, rate and rate alike, according to the quantity of their debts". This is the principle of *pari passu* distribution which is still the central principle of distribution of an insolvent free estate. The statute aimed at preventing "crafty" debtors from escaping the realm, to ensure that all the debtor's assets were available for creditors and that these assets were divided equally and ratably among the debtor's creditors.

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[7] Verse 2.280.
[8] Deuteronomy 15:1-2.
[9] Leviticus 25:10.

This discussion points towards the inevitable conclusion that, historically, insolvency was viewed as either criminal or quasi-criminal. Lord Kenyon said in *Fowler v Padget*[10] that "bankruptcy is considered as a crime and a bankrupt in the old laws is called an offender". In this case, Fowler claimed that Padget had unlawfully broken into his house, trespassed and converted his goods. Padget claimed that he was justified in doing so, because under the Act,[11] Fowler had committed an act of bankruptcy. Fowler had gone from his house in Manchester, where he worked as a trader, to London because one of his creditors' business had been failing. During the ten days of his departure, Fowler's own creditors had called upon his house, and believed Fowler to have departed for fraudulent reasons under the Act of 1603.

Several other statutes followed, and the theme was the same: to criminalise bankruptcy and to penalise bankrupts. The Fraudulent Conveyances Act of 1571 for example outlawed transfers made with intent to defraud creditors. This Elizabethan statute was later held by Lord Mansfield in *Alderson v Temple*[12] to be effective to avoid not only fraudulent conveyances but also fraudulent preferences which defeated the law by usurping the function of authorities and defeated the equality intended by the law. See Lord Mansfield's dictum below:

> A general question has been asked, whether a man may or may not, on the eve of a bankruptcy, give a preference to a particular creditor? I think he may, and he may not. If one demands it first, or sues him, or threatens him, without fraud, the preference is good. But where it is manifestly to defeat the law, it is bad. In the present case there is no

10 *Fowler v Padget* (1798) 7 Term Rep 509; 101 ER 1103
11 13 Eliz. c. 7.
12 (1768) 96 E.R. 384.

> course of dealing of this kind; no demand; no threat; but it is done with a positive view of iniquity.

This opprobrium of insolvency can be explained. Incurring a debt creates a contractual obligation that must be honoured, and a moral obligation to pay what is owed to other people, because it is their property that was not given away for free. Failure to pay the debt can give rise to legal sanctions and, therefore, the criminal and penal sanctions imposed on debtors historically are justifiable.[13] Most bankruptcy laws were strict on the insolvent person and provided no alternatives to bankruptcy. Once the insolvent person was adjudged bankrupt by the court, the laws provided for no alternatives to bankruptcy. Under Kenya's repealed Bankruptcy Act,[14] the Official Receiver or any creditor was empowered by the Act to apply to the court to issue an adjudication order once a receiving order had been made.[15] The bankrupt person therefore continues to carry the yoke of bankruptcy unless and until he applies for discharge from bankruptcy.[16]

However, the fresh-start policy in modern insolvency law, initially championed in the United States, has created relief to overburdened debtors. At its inception, this policy was structured to reward the debtor for his efforts in maximising the returns of his creditors, as opposed to being a bankruptcy relief measure. It was argued that a motivated debtor would put greater efforts to pay his creditors, as opposed to an overburdened debtor facing

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13 See, David, G.C., "Debt Collection as Rent Seeking", 79 *Minnesota Law Review*, 199, pp. 817-42 n.57) ("It is sometimes thought that debtors are weak and creditors powerful. This may be so at the time a loan agreement is negotiated, but quite the opposite is true when the debtor is broke and has nothing to gain from prudent management of assets.").

14 Bankruptcy Act (Repealed) Cap 53 Laws of Kenya.

15 See section 20 of the Bankruptcy Act (Repealed) and Rules 180-185 of the Bankruptcy Rules.

16 S. 129 of the Bankruptcy Act and Rules 186-97 of the Bankruptcy Rules.

criminal sanctions.[17] This article examines the normative objectives of the fresh-start policy in both individual and corporate insolvency in Kenya. The article will first explore the global contemporary status of the policy and then narrow down to the Kenyan context. The aim is to demonstrate that this policy is not novel in Kenya and that it has been implemented in other jurisdictions across the globe. Finally, the article assesses whether Kenya's fresh-start policy provides a meaningful opportunity for financially challenged individuals to begin a new financial chapter in their lives.

2. THE NORMATIVE OBJECTIVES OF THE FRESH-START POLICY IN INDIVIDUAL INSOLVENCY

Most academic discussions on Insolvency Law are based on the thinking that insolvency is largely economic in nature. This is true, especially for corporate insolvency which is grafted onto a pre-existing framework of limited liability corporation law. In most jurisdictions, corporate insolvency is regulated by Company Law, and such a discussion is purely an economic one. Individual insolvency, is, however, also a social legislation, in addition to being an economic one.[18] When individuals file for bankruptcy, they seek to be relieved from their debts or to have their creditors entirely forgive them.[19] This is justified by the moral judgement that an honest but unfortunate debtor should be discharged from his debts.[20]

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17 See the arguments of Glenn, C., "Essentials of Bankruptcy: Prevention of Fraud, and Control of the Debtor", 23 *VA. L. REV.*, 1937, p. 373.

18 Todd, J.Z., "Bankruptcy Law as Social Legislation", available at <https://www.law.gmu.edu/assets/files/publications/working_papers/01-18.pdf>, (accessed on 5 December 2020).

19 See Lawrence, H.W., "Bankruptcy as an Economic Intervention", 1 *J. LIBERTARIAN STUD.* 1977, pp. 281, 283-84.

20 Peter, C.A., "With Apologies to C.S. Lewis: An Essay on Discharge and Forgiveness", 9 *J. BANKR. L. & PRAC.,* 2000., pp. 601, 601-02.

The social dimensions of insolvency are not difficult to understand. When someone incurs a debt, he assumes both contractual and moral obligations to repay that debt. The debtor is obliged to perform his obligations under contract and failure to do that may attract legal sanctions. Where the debt was secured, the creditor may seize the collateral in satisfaction of the debt.[21] In addition to the contractual obligation, debt imposes various moral obligations, whether imposed by self or by the society.[22] For example, by borrowing from the creditor, the debtor makes a promise to pay back the debt. When he fails to honour this promise, he suffers from a moral indignation which arises from a breach of trust that the creditor had on them.[23] Having a big number of debtors failing to honour their promises and filing for bankruptcy also illuminates a problem in the society: either a genuine inability to pay debts, or a conduct in which people just decide to dishonour their promises.

When debtors are economically, morally, and socially condemned this way, discharge from debt affords them an opportunity to change the relationship with their former creditors and to have a beginning with a fresh start.[24] By being discharged from debt, the debtor is freed from his past financial obligations and his future earnings can be put to other sectors of their prosperity. The moral justification of relieving debtors of the burden of debt is founded on St. Thomas Aquinas' moral reasoning. Aquinas postulated that "Man's good is to be in accord with reason, and his evil is to be against

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21 See the Movable Property Security Rights Act, 2017.

22 David, G.C., "Debt Collection as Rent Seeking", above, note 13, pp. 817-42

23 Todd, J.Z., "Rewrite the Bankruptcy Laws, Not the Scriptures: Protecting a Bankruptcy Debtor's Right to Tithe", *WIS. L. REV.*, 1998, pp. 1223, 1226.

24 See for example, *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181, 188 (1902) (stating that "[the grant to Congress [in the Constitution] involves the power to impair the obligation of contracts, and this the States were forbidden to do.") and *Wright v. Union Cent. Life Ins. Co.*, 304 U.S. 502, 517 (1938) (stating that bankruptcy proceedings constantly modify and affect property rights established by state law).

reason..."[25] Aquinas opined that natural law is a rule of reason for the common good, made by God and intrinsic in man, thereby providing a ground for decision and action.

Based on Aquinas' moral philosophy therefore, the normative objectives of the fresh start policy in Insolvency Law can be evaluated by asking the foundational questions: does the policy provide for basic human goods or values determined under requirements of practical reasonableness? Is the policy and the general Insolvency Law consistent with integral community fulfilment? Finally, is such a law morally justified, or reasonable? To answer these questions, one must satisfy himself with the human values or needs that Insolvency Law seeks to protect by making provision for debt relief. Then, he should also satisfy himself whether Insolvency Law, by making provision for debt relief and discharge of the debtor from bankruptcy, assists the nation in moving toward social justice for all members, individually, and collectively as a society.

The fresh start policy is anchored on the recognition of the intrinsic value of human dignity that the debtor should be given an opportunity to earn a living.[26] A debtor who has been freed from debt becomes productive again, and free from the previous burden of debt. The resulting free man has a renewed vigour, and can benefit himself, his kinsmen and the society.[27] The policy is therefore rehabilitative, salutary, and has the ability to allow the debtor to move forward with a more rational life plan. It is also within the

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25 Thomas, A., *Summa Theologia,* 1-11 q. 71, a. 2 (Benziger Brothers ed. 1947).

26 Grisez, G., "The way of the Lord Jesus, VOL. I, Christian Moral Principles", 1983, pp. 137-39 (discussing bodily life as one of basic human goods or values).

27 See RendIeman, D., "The Bankruptcy Discharge: Toward a Fresher Start", 58 *N.C.L. Rev.* 1080, pp. 723, 726. (stating that discharge has been said to "liberate the bankrupt psychologically").

humanitarian province of human nature to be compassionate with an honest but overburdened debtor.[28]

The phrase "fresh start" appears in numerous documents, some legislative and others academic, but there appears to be no consensus in its meaning.[29] Some commentators feel that the fresh start policy involves the debtor "beginning again on the economic treadmill."[30] Others opine that the concept means "obtaining longer-term financial health"[31], restoring "financial well-being"[32] and "participating in the open credit economy."[33] It has been suggested that the difficulty in reaching consensus arises from the

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28 See Resnick, AN., "Prudent Planning or Fraudulent Transfer? The Use of Non-exempt Assets to Purchase or Improve Exempt Property on the Eve of Bankruptcy", 31 *RUTGERs L. REV.,* 1978, pp. 615, 621(asserting that exemptions should further one of five social policies). These five social policies are: (1) To provide the debtor with property necessary for his physical survival; (2) To protect the dignity and the cultural and religious identity of the debtor; (3) To enable the debtor to rehabilitate himself financially and earn income in the future; (4) To protect the debtor's family from the adverse consequences of impoverishment; (5) To shift the burden of providing the debtor and his family with minimal financial support from society to the debtor's creditors.

29 Karen, G., "Demonizing Debtors: A Response to the Honsberger-Ziegel Debate", 37(1- 2) *Osgoode Hall Law Journal,* 1991, pp. 263, 263. (Karen Gross argues that instead, euphemisms are used to describe the fresh start. See P.264. The euphemisms used include: "clean sheet" and "economic rehabilitation".).

30 Lynden, G., "Bankruptcy Policy and the Decision of the High Court in Pyramid Building Society (In Liq) v Terry' 1(1) *University of Notre Dame Australia Law Review,* 1999, p. 57.

31 Jean, B., "Consumer Bankruptcy as Part of the Social Safety Net: Fresh Start or Treadmill?' 44(4) *Santa Clara Law Review*, 2004, pp. 1065 and 1070.

32 Jay, L.Z. and Lois R.L., "A Study of Consumers' Post-discharge Finances: Struggle, Stasis, or Fresh-start?",16(1) *American Bankruptcy Institute Law Review,* 2008, pp. 283-284.

33 Margaret, H., "A Theory of Discharge in Consumer Bankruptcy", 48 *Ohio State Law Journal,* 1987, pp. 1047-1048.

fact that bankruptcy is not just a legal concept, and includes money, the economy, shame, morality and social structures.[34]

However, the common denominator in all these definitions is not difficult to trace. At its simplest form, the fresh start policy is about relief for a debtor in his obligation to pay debts. Hence, the debtor is provided with a new slate or a clean slate, in the sense that he no longer has the burden of the existing debts hanging over his head.[35] Jurisdictions that allow the debtor to be discharged from debt have traces of the fresh start policy. This may suggest that the instances in which debtors have historically been discharged from their debts without being asked to provide any payment plan are also elements of the fresh start policy in bankruptcy.[36] This dimension of understanding the fresh start policy appears to suggest that discharge from debt and a fresh start are mutually interchangeable, which is not necessarily the case.[37]

Limiting the fresh start policy to its perceived "synonym", discharge from debt, "is merely a palliative solution that fails to address debtors' underlying problems in a meaningful way."[38] Hence, the fresh start could be seen in the legal and the financial sense, in which case, it should be determined whether the debtor will have prospects for an improved financial future.[39] This may

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34 E.g. Gross, note 28, at 267.

35 William, W., "Changing definitions of fresh start in U.S. bankruptcy law", 20(2) *Journal of Consumer Policy* 1997, p. 179.

36 Working Group on the Treatment of the Insolvency of Natural Persons, 'Report on the Treatment of the Insolvency of Natural Persons' (Report 77170, World Bank, 2013) 115 ('World Bank Report').

37 Jan, C.A., "The 'Fresh Start' for Individual Debtors: Social, Moral and Practical Issues" 17 *International Insolvency Review* 2008, pp. 57-59.

38 Zagorsky and Lupica, above n 32, at p. 287.

39 Karen, G. and Susan, B., "Empty Mandate or Opportunity for Innovation? Prepetition Credit Counseling and Post-Petition Financial Management Education", 13 *American Bankruptcy Institute Law Review* 2005, p. 549.

involve looking into the debtor's future prospects of employment, financial health, housing, and such other basic needs. Such a fresh start may be rehabilitative, as opposed to a mere discharge from debt. The Kenyan insolvency regime will be examined with a view to assessing its rehabilitative effect.

3. SCOPE OF THE FRESH START POLICY IN THE US AND AUSTRALIA

The United States and Australia are the two pioneer jurisdictions of the fresh start policy in individual insolvency. The two jurisdictions will be briefly discussed with a view to demonstrating that this policy is not novel in the Kenyan insolvency regime. It has been pioneered and implemented with notable success in other jurisdictions.

3.1 United States

Throughout the history of American bankruptcy law, bankruptcy was exclusively a creditor's remedy, in the sense that once the debtor was adjudged as bankrupt, his/her assets would be distributed to all creditors.[40] Even when the fresh start policy was incorporated into the Bankruptcy Code, it was initially intended to reward the debtors for their efforts in attempting to pay their creditors despite the hardship they experienced.[41] During the nineteenth century, State legislatures started enacting insolvency laws aimed at affording debtors some relief from the enforcement of creditors' claims.[42]

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40 See generally Cohen, J., "The History of Imprisonment for Debt and Its Relation to the Discharge in Bankruptcy", 3 *J. LEGAL HIST.* 1982, p. 153.

41 See Cohen, above, at 156-57. See also Glenn, "Essentials of Bankruptcy: Prevention of Fraud, and Control of the Debtor", 23 *VA. L. REV.* 1937, p. 373 and Radin, M., "The Nature of Bankruptcy", 89 *U. PA. L. REV.* 1940, p. 1, 6, and 8-9, arguing that paying back the creditors was the only route to legal relief from the harshness of bankruptcy.

42 See Coleman, P., "Debtors and Creditors in America", *Passim,* 1974; and Noel, F., "A History of the Bankruptcy Clause of the Constitution, 1918, p. 55-65, who have rendered useful accounts on these early bankruptcy laws in the US.

The laws sought to abolish the requirement for civil imprisonment as a way of enforcing bankruptcy law. These laws therefore introduced provisions that allowed debtors to execute an oath of impoverishment or to surrender their unencumbered assets to their creditors in exchange for relief of debt.[43] The laws also protected the debtors from future imprisonment for debts owed at the time of release.[44] These early enactments were accompanied by other legislative frameworks aimed at reducing the harshness of creditor remedies against the debtor.[45]

The recognition of debtor protection in American law in the 19th century was largely informed by the continued recognition of the importance of credit in the national economy during that time.[46] Entrepreneurs played a key role in the economic development of the country and therefore there was a need to protect them against the harshness of bankruptcy especially where they were willing to pay but genuinely unable to do so. Indebtedness, previously understood as a result of poor financial management and extravagance, came to be recognised as an indispensable aspect of commercial activity. In addition, the financial crises of the time showed that indebtedness was not just a result of dishonesty and poor financial management, but a by-product of other underlying financial decisions some of which were beyond the scope of the debtor's ability.[47]

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43 See Coleman, above, at p. 256.

44 See, e.g., Act of Feb. 23, 1824, 22 Ohio Laws 326 (establishing public commissioner of insolvents to administer property assigned to obtain release from imprisonment).

45 See Coleman, P., above, note 41, passim (exemptions and moratory or stay laws); Feller, A.H., "Moratory Legislation", 46 *HARV. L. REV.* 1933, p. 1061; Priest, "Law and Economic Distress: Sagamon County, Illinois", 2 *J. LEGAL STUD.* 1973, pp. 1837-44 (moratory and valuation laws).

46 Horwitz, M., "The Transformation of American Law 1780-1860, 1977, pp. 228-29.

47 Kent, J., "Commentaries on American Law", 1827, p. 321 (availability of relief from consequences of "inevitable misfortune" particularly appropriate for merchants, given the "enterprising nature of trade" and its "extraordinary

Two approaches in such early bankruptcy laws in the US, that have been argued as the early antecedents of the fresh start policy, were evident. The first was the view that debtors are potentially valuable contributors to the national economy, and that such contribution is simply hampered by unfortunate financial conditions. According to them, debt relief would, therefore, set them free from the debt burden and release their useful entrepreneurial skills which would in effect allow them to present a more realistic promise of repaying their creditors.[48] The second view was that the debtor's default was a matter of misfortune, and that, rather than exercising forceful collection of debt, the creditor should exercise mercy on the suffering debtor as a matter of moral uprightness. Hence, debt relief legislation was aimed at reducing the role of the state in assisting the creditor to collect his debt from a suffering and genuine debtor.[49]

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hazards"); On A National Bankrupt Law, 1 *Am. JURIST & L. MAG.* 35, 39, 51 (1829).

48 See, e.g., CONG. GLOBE, 27th Cong., 1st Sess. 134 (1841) (message of President Tyler transmitting petitions for a bankruptcy act: "The distress incident to the derangements of some years past has visited large numbers of our fellow citizens with hopeless insolvency, whose energies, both mental and physical, by reason of the load of debt pressing upon them, are lost to the country.") and 2 Blackstone, W. *Commentaries on the Law of England* *482-83. ("the bankrupt becomes a clear man again: and . . . may become a useful member of the commonwealth").

49 See, e.g., CONG. GLOBE, 26th Cong., 1st Sess. 814 app. (1840) (remarks of Daniel Webster attributing failure to "selfish, unjust, or indifferent creditors"); id., 27th Cong., 1st Sess. 318 (1841) (remarks of Representative Roosevelt describing effects of insolvency as a "moral calamity": "Talk of slavery and abolition! What slavery was to compare with the bondage of the mind and heart? Men talked of physical chains and shackles, but these were nothing to the chains of the soul."); and Tiffany, J., "A Treatise on Government and Constitutional Law, 1867, p. 215 ("One of the first duties of legislation, while providing for the obligation of contracts, is, to relieve the unfortunate and meritorious debtor from a slavery of mind and body, which deprives him in great measure of the enjoyment of the comforts of life and the common benefits of society.").

These concerns found their way into the US Constitution and, among the federal powers granted by the Constitution, the federal government was given the authority "[t]o establish uniform Laws on the subject of Bankruptcies throughout the United States."[50] By the time the first permanent American legislation, the Bankruptcy Act of 1898 was enacted,[51] the modern concept of bankruptcy law of debtor protection was already well established. Discharge from bankruptcy under the Act was available to any debtor who made a timely application, unless he had concealed property after filing the petition, given false testimony in the proceeding, or failed to keep adequate records prior to bankruptcy "with fraudulent intent and in contemplation of bankruptcy."[52] The Act further provided only that the discharge "shall release" a bankrupt from all his dischargeable debts.[53] Prior common law doctrines did not have this provision as discharge from bankruptcy under common law simply interposed a bar against the judicial enforcement of debts.[54] The 1898 Act reinforced the idea that debtor relief measures served the public welfare by restoring the overburdened debtor to economic productivity. The discharge was available to the "honest but unfortunate" debtor due to the "public interest" in affording him "a fresh start in life," a "new opportunity," and "a clear field for future effort."[55] This view was supported by the fact that debt and insolvency were largely products of business activities and therefore not easy to avoid.

Apart from the honest but unfortunate class of debtors, there was the "improvident" or "extravagant" consumers who required protection. These

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50 U.S. CONST. art. I, & 8, cl. 4.

51 Bankruptcy Act of 1898, ch. 541, 30 Stat. 544.

52 Above. Section 14(b), 29, 30 Stat. at 550, 554.

53 Bankruptcy Act of 1898, section 17, at 550-51.

54 See *Jersey City Ins. Co. v. Archer*, 122 N.Y. 376, 25 N.E. 338 (1890); *Hill v. Trainer*, 49 Wis. 537, 5 N.W. 926 (1880); Another Question under the Bankrupt Act of 1867, 4 ALB. L.J. 294 (1871).

55 *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934); *Stellwagen v. Clum*, 245 U.S. 605, 617 (1918); *Wetmore v. Markoe*, 196 U.S. 68, 77 (1904).

were the class of consumers who were neither entirely dishonest, nor entirely victims of misfortune.[56] Yet, between 1926 to 1960, there were no significant legislative activities to take care of these emerging classes of debtors requiring protection.

However, these judicial pronouncements and a posture of openness to the phenomenon of consumer bankruptcy were not enough to accord debtors a fresh start. Hence, the Bankruptcy Code was enacted in 1978. Even after the enactment of the Bankruptcy Code, the phrase "fresh start" was not as conspicuous as one would have expected. The phrase appears in Chapter 15 of the Code and is worded as follows:

> In determining whether to provide additional assistance under this title or under other laws of the United States, the court shall consider whether such additional assistance, consistent with the principles of comity, will reasonably assure —
> . . . .
> (5) if appropriate, the provision of an opportunity for a *fresh start* for the individual that such foreign proceedings concern.[57]

However, despite appearing only once in the text of the Bankruptcy Code, the importance of the principle is rarely questioned as the Supreme Court

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[56] See, e.g., Douglas, W.O., "Wage Earner Bankruptcies-State vs. Federal Control, 42 *YALE L.J.* 1933, pp. 591, 598-601; see also Sturges, A., and Cooper, D.E., "Credit Administration and Wage Earner Bankruptcies", 42 *YALE L.J.* 1933, pp. 487, 514-16., at 514 (noting that any effort to distinguish between "honest" and "reprehensible" debtors requires moral judgments, "because the classes do not otherwise exist").

[57] Bankruptcy Act. Section 1507(b) (emphasis added).

started recognising it as early as in 1885.[58] Various provisions of this Code indirectly grant the insolvent debtor opportunities for a fresh start. For example, the automatic stay in section 362(a) provides an immediate reprieve from efforts of creditors to collect debt.[59] In addition, section 322 allows debtors to retain and use various types of their property during and after their bankruptcy.[60] Further, through a judicially confirmed plan of reorganisation, debtors can readjust their outstanding debt and payment schedules.[61] Most importantly, courts grant debtors a discharge of debt and enjoin creditor efforts to collect discharged debt.[62] The Code also has prohibitions against discrimination on people who have been adjudged as bankrupt.[63] Hence, the US, being one of the earliest pioneers of the fresh start policy in bankruptcy law, has made both legislative and judicial milestones in cementing the policy in its bankruptcy law.

3.2 Australia

The preamble and the object clauses of the Australian Bankruptcy Act of 1966 do not suggest the existence of a fresh start policy in the legislation.[64] However, the text of the Act has several provisions that can be construed to refer to the policy. For instance, section 153 of the Bankruptcy Act provides that from the date of the conclusion of (or discharge from) his bankruptcy, the debtor is 'discharged' or released from his contractual obligations to pay

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58 *Traer v. Clews*, 115 U.S. 528, 541 (1885) ("The policy of the bankruptcy act was, after taking from the bankrupt all his property not exempt by law, to discharge him from his debts and liabilities, and enable him to take a fresh start.").

59 See 11 U.S.C. s. 362(a) (providing that a petition filed operates as a stay of various enumerated acts)

60 See s. 522.

61 See ss. 1322, 1325.

62 See ss. 524, 727, 944, 1141, 1228, 1328

63 See s. 525; see also Douglass G. Boshkoff, Fresh Start, False Start, or Head Start?, 70 *IND. L.J.* 549, 549 (1995) (describing bankruptcy law's tripartite protection for individual debtors).

64 Bankruptcy Act 1966 (Cth).

the debts proved in the bankruptcy.[65] Whether construed in the wider or the narrow sense, discharge from bankruptcy connotes the release of the bankrupt from his debt obligations and allows him/her to have a fresh start in his economic and social life. Related to this is the fact that once the bankrupt is discharged from bankruptcy, he has no obligation to continue making contributions to the creditors in payment of the debt.[66] This relief from the debt burden and the freedom to start earning afresh from the debtor's assets is what gives the debtor a fresh start in his social and economic life.[67]

In addition, the discharged bankrupt can also acquire assets without running the risk of such assets being recovered to settle the creditors' debts.[68] The conditions imposed by the law during bankruptcy also have elements of the fresh start policy. For example, during bankruptcy, creditors are not allowed by the Act to continue pursuing the debtor for the repayment of the debt.[69] This makes it possible for the court to make the correct determination of the bankrupt's case and make an order for equal treatment and payment of creditors from the debtor's realisable assets.[70]

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65 Bankruptcy Act s. 153.

66 During bankruptcy, income contributions are required once the debtor's income exceeds the relevant income threshold: Bankruptcy Act s. 139P.

67 Margaret, H., "A Theory of Discharge in Consumer Bankruptcy", 48 *Ohio State Law Journal*, 1987, p. 1085.

68 See Bankruptcy Act s. 116(1), which provides that the bankrupt's divisible property includes property belonging to or vesting in a bankrupt at the commencement of the bankruptcy, and property acquired by the bankrupt after the commencement of bankruptcy and before discharge.

69 Bankruptcy Act s 58(3).

70 For example, see *Re McMaster ex parte McMaster* (1991) 33 FCR 70, 72-73, as per Hill, J.

The Act also makes it difficult for creditors to access certain properties from the debtor for realisation and distribution.[71] This includes superannuation interests, tools of trade, means of private transport, and household items. This enables the bankrupt to maintain the basic standards of living and social contact both during bankruptcy and after discharge from bankruptcy. For this reason, therefore, although the Australian Bankruptcy Act of 1966 does not have an express clause mentioning the fresh start policy of bankruptcy law, the text of the Act can be construed to make provision for such a policy. This discussion on the manifestations of the fresh start policy in both the US and Australian legislation forms the foundation to discuss this policy in Kenyan bankruptcy legislation.

4. ELEMENTS OF DEBTOR REPRESSION IN KENYA'S REPEALED BANKRUPTCY ACT

Like most other laws, Kenya adopted the Bankruptcy Act from the United Kingdom. The repealed Bankruptcy Act, Cap 53 Laws of Kenya, is a replica of the English Bankruptcy Act of 1940 and the Bankruptcy Amendment Act of 1926. The accompanying Bankruptcy Rules, adopted in 1948, are similar to the English Bankruptcy Rules of 1952 which do not differ significantly from the English Bankruptcy Rules of 1915. This Act does not have an "object" clause or a detailed preamble that shows the objectives and purposes that the Act seeks to meet. In the absence of such a clause, the text of the Act itself will be examined to trace the elements of debtor repression as opposed to protection.

Under section 10 of the Bankruptcy Act and Rules 119 to 124 of the Bankruptcy Rules of 1948, the court presiding over the bankruptcy proceedings may appoint an official receiver to be the interim receiver of the property of the debtor, for purposes of 'protecting' that property. This would

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[71] Bankruptcy Act s 116(2); Bankruptcy Regulations 1996 (Cth) ('Bankruptcy Regulations') reg 6.03.

mean that the debtor cannot use that property for any productive purposes as it would be placed under an interim receiver. The property would, in effect, remain in an unproductive status pending the final determination of the bankruptcy proceedings. Once the court has made a receiving order, the official receiver becomes receiver of the debtor's property and any transactions subsequently entered by the debtor are prima facie invalid whether or not the other party to the transaction has notice of the receiving order. This, in effect, means that the debtor has no right over his own property.[72] These are elements of debtor repression.

Under the Act, the debtor is required to appear for a public examination, immediately after submitting his statement of affairs.[73] If the debtor does not appear for the examination without sufficient explanation, the court may issue a warrant for his arrest. The court will then adjudge him as bankrupt and will not be discharged from bankruptcy without obtaining an order from the court for the examination to continue. The debtor is examined on oath and must answer all questions which the court may put or allow to be put to him. Notes of the examination are taken down in writing and after being read over to or by the debtor and signed by him may be used in evidence against him in other proceedings. These notes are open to the examination by the creditors at all reasonable times.

Under certain circumstances, the court can order the arrest of the debtor and the seizure of any books, papers or goods in his possession.[74] One of these circumstances is when there is evidence to believe that the debtor has absconded or will abscond payment of the debt, after the bankruptcy notice has been issued to him. The second circumstance is when there is reason to believe that he is about to remove his goods from the jurisdiction of the court with a view to protecting them from the control of the official receiver or

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72 Section 9 of the Bankruptcy Act and Rules 138-148 of the Bankruptcy Rules.
73 See section 17 of the Act and Rules 151-159 of the Bankruptcy Rules.
74 S 26 of the Bankruptcy Act.

trustee. Thirdly, the court may order arrest when he fails to attend his public examination without a sufficient reason.

Once the debtor is adjudged bankrupt by the court, he is disabled from doing certain things with his property. First, all property belonging to him vests in the trustee in bankruptcy for distribution to his creditors. His hands on the property are tied. He cannot appropriate it in any way. Second, whether alone or with other people, he cannot obtain credit to the extent of 10 pounds or upwards from any person without informing that person that he is an undischarged bankrupt.[75] 10 pounds is approximately Kshs 1,500/-! Third, if he is to engage in business with other people in a different name other than the name with which he was adjudged bankrupt, he must inform those people about the name he was adjudged as bankrupt with.[76] In addition, if he is to be appointed the director of a company, he must seek the leave of the court that adjudged him as bankrupt.[77] He cannot even be elected a Member of Parliament.[78]

This discussion points to the inevitable conclusion that the repealed Bankruptcy Act, Cap 53, was laden with debtor-repressive provisions that made it impossible for the debtor to be socially or economically productive, either during the bankruptcy proceedings or after being adjudged bankrupt by the court. Even for a debtor who lacks sufficient assets to settle the debts they owe the creditors; it would be difficult for such debtors to continue carrying out reproductive activities with a view to raising additional property to settle part of the remaining debt. The debtor is therefore completely rendered helpless and unproductive. This position is now history, as the new insolvency regime has aspects of the fresh start policy which will be examined in the section that follows.

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75 S 139(a) of the Bankruptcy Act.
76 S 139(b) of the Act.
77 S 188 of the Companies Act.
78 Article 99(2)(f) of the Constitution of Kenya, 2010.

5. ELEMENTS OF THE FRESH START POLICY FOR INDIVIDUAL INSOLVENTS UNDER THE INSOLVENCY ACT OF 2015

The period 2008-2014 was characterised by renewed clamour for reform of business laws in Kenya, including the Bankruptcy Act, with a view to modernising and simplifying the insolvency process which has been characterised by heavily technical and bulky procedures.[79] Kenya's Vision 2030,[80] for example, it comprises three pillars: economic, social and political pillars. The economic pillar aims at maintaining a sustained economic growth of 10% p.a. over the next 25 years. One of the enabling blocks of this pillar is the development of a vibrant and globally competitive financial services sector in Kenya that will create jobs and promote high levels of savings to finance Kenya's overall investment needs. To do this, the government required a robust legal and institutional framework.[81]

Kenya's Economic Recovery Strategy for Wealth and Employment Creation (2003-2007)[82] also played a key role in the development of the new legal and institutional frameworks in business. The Strategy noted that one of the biggest hurdles that businesses faced was lack of access to affordable credit. The Strategy also noted that the ability of Kenya's financial sector to contribute to the development process has been undermined by a non-performing loans portfolio which stood at nearly 30 percent of the total loans

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79 Muriuki, M., "Reforming Insolvency Law in Kenya", 2014, Available at <https://www.academia.edu/10462649/Reforming_Insolvency_Law_in_Kenya>, (accessed on 19 December 2020).

80 Kenya's economic blueprint, launched by President Mwai Kibaki on June 11, 2000.

81 See page 15 of Vision 2030, available here at <http://vision2030.go.ke/wp-content/uploads/2018/05/Vision-2030-Popular-Version.pdf>, (accessed on 19 December 2020).

82 Government of Kenya., *Economic Recovery Strategy for Wealth and Employment Creation* 2003-2007. Ministry of Planning and National Development.

and advances from commercial banks by the end of 2002. It further noted that a vibrant and integrated financial sector that ensures mobilisation of adequate financial resources to finance the required investment was required. The government would carry out a comprehensive study of the financial sector to identify weaknesses that have impeded growth of the sector and reforms that are needed to strengthen its intermediation role.[83]

The reform of Insolvency Law in Kenya, however, has a long history. In 1992, a Task Force charged with reviewing laws relating to insolvency of companies and partnerships made recommendations targeted at modernising and simplifying insolvency laws.[84] The then serving Attorney General Amos Wako, tasked the Kenya Law Reform Commission to review this taskforce report and draft an insolvency law that addressed the concerns raised. Stakeholders like lawyers, bankers, accountants, and other public sector agencies such as the Official Receiver were consulted with a view to gathering as much information as possible on the correct approach that the insolvency framework should take.

The Commission also considered the best practices as evidenced by legislative initiatives in jurisdictions such as the United Kingdom, New Zealand, Australia, and Canada besides making study tours in these countries to study the practices and policies of their insolvency legal regimes. The first Insolvency Bill was concluded in the year 2008 and tabled in Parliament. Subsequent Bills were drafted in the years 2010, 2012, and 2014. Most of the innovations and reforms were introduced in the 2008 Bill and subsequently cascaded in the other Bills with minor changes therein. The Insolvency Act of 2015 ("The Act") was assented to by the President on September 11, 2015.[85]

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83 Economic Recovery Strategy, above, p. 41.
84 Muriuki, note 78 at page 2.
85 The Insolvency Act, 2015 Act No. 18 of 2015.

The Act has a heavily worded Preamble, and the most relevant part to the fresh start policy is "…to provide alternative procedures to bankruptcy that will enable the affairs of insolvent natural persons to be managed for the benefit of their creditors…"[86] The objects of the Act are listed in section 3(1) and include to establish and provide for the operation of a framework for the efficient and equitable administration of the estate of the insolvent natural persons and unincorporated entities…that maintains a fair balance between the interests of those persons …and those of their creditors,[87] to enable those persons and entities to continue to operate as going concerns so that ultimately they may be able to meet their financial obligations to their creditors in full or at least to the satisfaction of those creditors,[88] to achieve a better outcome for the creditors as a whole than would likely be the case if those persons and entities were adjudged bankrupt,[89] to provide an orderly system for adjudging irredeemable persons bankrupt and for the efficient and optimal administration and distribution of their estates for the benefit of their creditors.[90] These objectives are designed in a manner that reflects the fresh start policy as outlined in previous sections as they all appear to give the distressed debtor a second chance. When the distressed debtor has a second chance and his estate is managed in a proper and efficient manner, his creditors benefit more than they would have benefitted had the debtor been declared bankrupt as was the case under the repealed bankruptcy regime.

Section 14 of the Act lists the alternatives to bankruptcy that an insolvent natural person may be subjected to. The debtor can enter a voluntary arrangement, make a proposal to pay his creditors, pay creditors in instalments under a summary instalment order, and enter a no-asset

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86 See Preamble, Insolvency Act, 2015.
87 S 3(1)(a).
88 S 3(1)(b)(i).
89 S 3(1)(b)(ii).
90 S 3(1)(d).

procedure. The High Court in *Rajendra Ratilal Sanghani v Schoon Ahmed Noorani*[91] opined that;

> The overall design of The Insolvency Act is to give a distressed Debtor a second chance. Where the Debtor is a natural person, Part 11 of The Insolvency Act provides for Alternatives to Bankruptcy. One such alternative is for a Debtor to seek an Interim Order so as to make a proposal to his/her Creditors for a Composition in satisfaction of the debts or a Scheme of Arrangement of its financial affairs[92]

The creditor had opposed the debtor's application for an interim order and the court proceeded to note that;

> the objective of the relief is to grant the Debtor some brief breathing space to present a viable proposal to his/her Creditors

and that

> The presentation of the Application for and the making of the Interim Order guarantees a measure of protection to the debtor and will necessarily impede a creditor from taking adverse steps against him/her[93]

Expectedly, such a protection is likely to be abused by a malignant debtor, and the court in *Rajendra* noted that;

> because of the immunity that the Debtor will enjoy upon presentation of the Application and the grant of the Interim

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91 [2018] eKLR.
92 Ibid, at paragraph 1.
93 At paragraph 11.

> Orders, there may be real temptation by a debtor, acting in bad faith, to abuse the process[94]

However, this can only happen in rare cases and it does not discount the importance of the fresh start policy.

A creditor or more than one creditor can apply to the court for a bankruptcy order in respect of a debt owed to them.[95] However, the court can only issue the bankruptcy order if it is satisfied that the debt has already fallen due and has indeed not been paid, and that the debtor has no reasonable prospect of paying the debt once it has fallen due.[96] The court will dismiss the application where there is reason to believe that the debtor has made an offer to secure off compound interest for the debt, if the offer was accepted the application would be dismissed, and that the offer was unreasonably refused by the creditor.[97] These provisions are made available to ensure that creditors do not file frivolous applications made to injure the reputation of a debtor who has not completely shown that he is unable to pay the debt and who has already made a reasonable offer to settle the debt he owes the creditors.

In *In re Samwel Kazungu Kambi*,[98] the petitioner, the creditor, averred that the debtor had a debt totalling to Kshs.809,595/= which, despite several requests to pay, had refused to pay. The petitioner had represented the debtor in an election petition and an amount of Kshs. 1,404,595/= was agreed. The debtor was only able to pay Kshs.300,000/= through a cheque. The debtor,

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94 See Rajendra, note 90, at paragraph 11. See also remarks by Scott VC in *Hook v Jewson Ltd* [1997] 1 BCLC 664, where he stated that "*Judges must, I think, be careful not to allow applications for interim orders simply to become a means of postponing the making of bankruptcy orders in circumstances where there is no apparent likelihood of benefit to the creditors from such postponement*"

95 S 17 of the Act.

96 S 20(1).

97 S 20(3).

98 [2020] eKLR.

Mr. Kazungu Kambi, however opposed the petition and averred that at no time has he neglected to pay the outstanding bill of costs arising out of retainer on legal professional services offered by the petitioner. He further averred that the outstanding amount stood at Kshs.509,595/= which he was ready and willing to settle by equal monthly instalments. The court noted that the debtor was then Commissioner with the National Land Commission and that he could pay the amount owed to him by the creditor. In addition, the only evidence the creditor furnished the court with to show that the debtor was incapable of paying his debt was one cheque of Kshs. 300,000/= returned unpaid. The court noted that:

> It is my view that the Court in giving effect to a petition for bankruptcy order and appointment of a receiver ought to take into account the business realities of the situation and should avoid taking a narrow legalistic view that because a debtor is faced with a bounced cheque, he or she should be declared bankrupt

This is perfectly in line with the fresh start policy which focuses on the business realities of the time and continuity of the debtor's economic activities.

A bankruptcy trustee is empowered to appoint, with the approval of the creditors' committee, the bankrupt to perform several tasks regarding the bankrupt's assets and business. He can, for example, appoint the bankrupt to superintend the management of the bankrupt's estate or part of it.[99] This is a departure from the repealed regime where the bankrupt had no chance to control his estate once he was adjudged bankrupt. The trustee may also appoint the bankrupt to carry on with the bankrupt's business for the benefit

[99] S 63(2)(a) of the Act.

of his creditors.[100] This is in line with the object of insolvency law under the fresh start policy which is to maintain the bankrupt's business as a going concern for the benefit of the creditors.

During bankruptcy, the bankrupt is allowed to retain some items as his own property when the rest of the property is vesting on the bankruptcy trustee. The items include necessary tools of trade, household furniture and personal effects, and a motor vehicle.[101] The motor vehicle must be worth one million shillings, unless a different amount is prescribed by insolvency regulations.[102] Other than assets that the bankrupt is permitted to retain by the Act and the bankruptcy trustee, the bankrupt may retain additional assets if his creditors pass such a resolution in their creditors' meeting.[103] The bankruptcy trustee is also permitted by the Act to allow the bankrupt to retain some amount of money that is necessary for the upkeep of the bankrupt and his family members.[104] This is in line with the fresh start policy that focuses on continuity and protection of the bankrupt to be in a better position to maximise creditor returns that they would have been if they were not protected by the law.

When the bankrupt is being publicly examined by the court, he is entitled to be paid expenses he has incurred while attending the examination. If the expenses have not been paid, the Act allows the bankrupt not to attend the examination as he is not obliged to do so.[105] This is meant to ensure that the bankrupt is not overburdened with unnecessary expenses.

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[100] S 63(2)(b) of the Act.
[101] S 161(2) of the Act.
[102] S 161(3)(c) of the Act.
[103] S 162 of the Act.
[104] S 167(1) of the Act.
[105] S 184 of the Act.

If the bankrupt was a party to ongoing contracts before being adjudged bankrupt, he is permitted to continue performing the contract and to disclaim the contract if it is onerous property.[106] The bankruptcy trustee has power to recover remedies from the other party to the contract if the other party terminates it. If the bankrupt is jointly liable with another party to the contract, that other party may sue and be sued without having to enjoin the bankrupt in the suit.[107] This provision is meant to ensure continuity of contracts entered by the bankrupt before being adjudged as bankrupt and is in line with the fresh start policy.

The bankrupt is automatically discharged from bankruptcy three years after lodging a statement of the bankrupt's financial position but may also apply to be discharged earlier than that.[108] Upon discharge, the bankrupt is released from all debts proved during the bankruptcy, except debts arising from fraud and breach of trust and amounts payable under the Matrimonial Causes Act and the Children Act.[109] This analysis points to the conclusion that the Insolvency Act of 2015 is a departure from the repealed Bankruptcy Act, Cap 53, in that it introduces elements of the fresh start policy in insolvency law.

6. CONCLUSION

The fresh start policy is anchored on the recognition of the intrinsic value of human dignity that the debtor should be given an opportunity to earn a living. The debtor is relieved from his debt burden and is given a second chance to be productive. Such productivity is beneficial to his creditors as they stand a better chance to be paid the debts owed to them by the debtor. The repealed

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106 S 190 of the Act.

107 S 192 of the Act.

108 S 254 of the Act. Though he may not be so discharged if the bankruptcy trustee objects to the automatic discharge, if the bankrupt is required to be publicly examined but has not yet been discharged and if the bankrupt has not yet been discharged from an earlier bankruptcy.

109 S 267 of the Act.

Bankruptcy Act, Cap 53 Laws of Kenya, did not have an object clause setting out the policy of the Act towards both the debtor and his creditors. The provisions of the Act were repressive to the debtor and denied his creditors a good opportunity at repayment of the debts owed to them by the debtor. Under the Act, the debtor had no permission to use his estate in any productive manner as the estate was placed under the official receiver or a bankruptcy trustee appointed by the court presiding over the bankruptcy proceedings. His hands on the property are tied. He cannot appropriate it in any way. Second, whether alone or with other people, he cannot obtain credit to the extent of 10 pounds or upwards from any person without informing that person that he is an undischarged bankrupt. Such a law was repressive and inimical to progressive economic and social relationships.

The Insolvency Act of 2015 has inspired optimism to creditors that their debts stand a better chance to be paid and has allowed the debtor a second chance at both economic and social lives as the debtor can remain productive as he continues to pay the debt owed to him by his creditors. As stated in the preamble, the Act provides alternative procedures to bankruptcy that will enable the affairs of insolvent natural persons to be managed for the benefit of their creditors. In addition, the objects clause states that the law seeks to enable those persons and entities to continue to operate as going concerns so that ultimately they may be able to meet their financial obligations to their creditors in full or at least to the satisfaction of those creditors and to achieve a better outcome for the creditors as a whole than would likely be the case if those persons and entities were adjudged bankrupt. The Act has therefore cemented the fresh start policy and has created a conducive environment for creditors to recover their debts from honest but unfortunate debtors.