MASOMO MSINGI PUBLISHERS

DEBT RECOVERY

KASNEB STUDY TEXT

CCP SECTION 6

22/2/2020

JULY 2018 SYLLABUS

This paper is intended to equip the candidate with the knowledge, skills and attitudes that will enable him/her to undertake debt recovery procedures in accordance with the law.

16.0 LEARNING OUTCOMES

A candidate who passes this paper should be able to:

- Evaluate the viability of recovering debts through legal proceedings
- Comply with the procedures for recovery of debts through legal proceeding
- Analyze the alternative models of debt recovery
- Apply knowledge of insolvency law in an international perspective.

CONTENT

16.1 Debt and borrowing

- Meaning of debt
- Types of debt
- Importance of borrowing
- Debt instruments
- Creditors and debtors rights
- Debt collection options

16.2 Debt protection

- Meaning of debt protection
- Alternatives to debt protection
- Debt protection insurance
- Distinction between debt protection insurance and credit insurance

16.3 Debt management

- Meaning of debt management
- Types of debt management
- Rescheduling debt
- Extension of time
- Foreclosure
- Conversion of debt to equity
- Payment of interest first
- Suspended payments
- Surrender of securities
- Receivership

16.4 Preliminary considerations before initiating or defending debt

- Recovery suits
- Letters of demand
- Capacity to sue

- Mediation
- Acknowledgement of debt
- Evidence of indebtness
- Statute barred debts
- Viability of debt recovery
- Availability of the debtor
- Enforcement and execution

16.5 **Debt recovery through legal suits**

16.5.1 **Institution of suit**

- Locus standi
- Jurisdiction
- Pleadings
- Service of summons

16.5.2 **Hearings**

- Summary judgment
- Attachment before judgment
- Presentation of evidence

16.5.3 **Judgement and decree**

- Extraction of decree
- Execution of decree
- Attachment and sale of property
- Attachment of debts
- Garnishee orders
- Committal to civil jail

16.6 **Alternative dispute resolution mechanisms**

- Negotiation
- Conciliation
- Meditation
- Arbitration

16.7 **Bankruptcy**

- Meaning
- Nature of bankruptcy
- Alternatives to bankruptcy
- Bankruptcy proceedings
- Rights of creditors

- Consequences of bankruptcy
- Discharge of a bankrupt

16.8 **Dissolution of partnership**

- Break-up of a partnership
- Effects of break-up
- Restriction of ceasing to be a partner on or after break-up
- Protection of property acquired after break-up
- Winding up by partners
- Distribution of partners assets on winding up
- Dissolution of a partnership which has broken up
- Power of court to appoint administrator
- Order appointing provisional liquidator
- Power of court to fix remuneration of receivers and managers
- Appointment of a receiver as liquidator
- Provisions relating to receiver or manager appointed

16.9 **Insolvency law**

- Meaning of insolvency
- Receivership
- Types of liquidation
- Official receiver/liquidator
- Committee inspection
- Distribution of assets
- United Nations Commission on International Trade Law (UNCITRAL) legislative guide on insolvency law
- United Nations Commission on International Trade Law (UNCITRAL) model law on cross border insolvency
- World Bank principles and guidelines for effective insolvency and creditors rights system.

16.10 **Emerging issues and trends**

TOPIC **PAGE NO.**

1. DEBT AND BORROWING ………………………………………………………….6
2. DEBT PROTECTION ……………………………………………………………23
3. DEBT MANAGEMENT…………………………………………………………..27
4. RELIMINARY CONSIDERATIONS BEFORE INITIATING OR DEFENDING DEBT………………………………………………………………44
5. DEBT RECOVERY THROUGH LEGAL SUITS…………………………………..53
6. ALTERNATIVE DISPUTE RESOLUTION MACHANISMS…………………….124
7. BANKRUPTCY…………………………………………………………………130
8. DISSOLUTION OF PARTNERSHIP………………………………………………144
9. INSOLVENCY LAW……………………………………………………………162
10. EMERGING ISSUES AND TRENDS……………………………………………..171

CHAPTER ONE

DEBT AND BORROWING

Meaning of debt

Debt is an amount of money borrowed by one party from another. Debt is used by many corporations and individuals as a method of making large purchases that they could not afford under normal circumstances. A debt arrangement gives the borrowing party permission to borrow money under the condition that it is to be paid back at a later date, usually with interest

How Debt Works

The most common forms of debt are loans, including mortgages and auto loans, and credit card debt. Under the terms of a loan, the borrower is required to repay the balance of the loan by a certain date, typically several years in the future. The terms of the loan also stipulate the amount of interest that the borrower is required to pay annually, expressed as a percentage of the loan amount. Interest is used as a way to ensure that the lender is compensated for taking on the risk of the loan while also encouraging the borrower to repay the loan quickly in order to limit his total interest expense.

Credit card debt operates in the same way as a loan, except that the borrowed amount changes over time according to the borrower's need, up to a predetermined limit, and has a rolling, or open-ended, repayment date. Certain types of loans, like student loans, can be consolidated.

Corporate Debt

In addition to loans and credit card debt, companies that need to borrow funds have other debt options. Bonds and commercial paper are common types of corporate debt that are not available to individuals.

Bonds are a type of debt instrument that allows a company to generate funds by selling the promise of repayment to investors. Both individuals and institutional investment firms can purchase bonds, which typically carry a set interest, or coupon, rate. If a company needs to raise $1 million to fund the purchase of new equipment, for example, it can issue 1,000 bonds with a face value of $1,000 each. Bondholders are promised repayment of the face value of the bond at a certain date in the future, called the maturity date, in addition to the promise of regular interest payments throughout the intervening years. Bonds work just like loans, except the company is the borrower, and the investors are the lenders, or creditors. Commercial paper is simply short-term corporate debt with a maturity of 270 days or less.

Good Debt Vs. Bad Debt

In corporate finance, there is a lot of attention paid to the amount of debt a company has. A company that has a large amount of debt may not be able to make its interest payments if sales drop, putting the business in danger of bankruptcy. Conversely, a company that uses no debt may be missing out on important expansion opportunities.

Different industries use debt differently, so the "right" amount of debt varies from business to business. When assessing the financial standing of a given company, therefore, various metrics are used to determine if the level of debt, or leverage, the company uses to fund operations is within a healthy range.

Types of debt

There are lots of types of debt, and if you’re trying to pay different creditors it’s important to understand the priority of each. This can make it complicated to work out what’s the best method of dealing with your situation.

In this section we talk through the debts we hear about from our clients every day.

There are some bills and debts that should be dealt with as a priority. This is because the consequences of not paying them can leave you at risk of losing your home or other assets.

1. **Business debts**

   Advice and support if you're self-employed or run a small business
2. **Consumer credit**

   The most common debts are covered by the Consumer Credit Act
3. **Contract debt**

   Help and advice if you've entered into a fixed contract
4. **Court debts and fines**

   Court fines for criminal offences are some of the most important debts to pay
5. **Debts to other people**

   Advice if you've borrowed from family, friends or a loan shark
6. **Government debts**

   How to deal with council tax debts and licenses

7. **Housing debts**
   Practical advice on dealing with rent or mortgage arrears and avoiding repossession
8. **Joint debts**
   Taking out debts in joint name will usually affect both of you
9. **Payday loan debt**
   These short-term loans are expensive and can quickly spiral out of control e.g Tala and Branch mobile loans
10. **Student loan debt**
    Repaying your student finance can be a financial burden
11. **Utility bill debt**
    How to deal with gas, electricity and water arrears

Categories of debts

Most Kenyans encounter some form of debt at one point in their lives. Debt comes in several forms, but all debt can be categorized within a few main types including secured debt, unsecured debt, revolving debt and mortgages. Not all debts are created equally; therefore, some are considered better than others.

1. **Secured Debt**

Secured debt is any debt backed by an asset for collateral purposes. A credit check is necessary for the lender to judge how responsibly you handle debt, but the asset is pledged to the lender in case you do not repay the loan. For example, if you require a loan to purchase a car, the lender supplies you with the cash necessary to purchase it but also places a lien, or claim of ownership, on the vehicle's title. In the event you fail to make payments to the lender, it can repossess the car and sell it to recoup the funds. Secured loans like this have a fairly reasonable interest rate, which is based on your creditworthiness and the value of the collateral.

2. **Unsecured Debt**

Unsecured debt lacks any collateral. When a lender makes a loan with no asset held as collateral, it does so only on the faith in your ability and promise to repay the loan. Granted, you are still bound by a contractual agreement to repay the funds, so if you default, the lender can sue to reclaim the money owed. Doing so comes at a great cost to the lender, however, so unsecured debt generally comes with a higher interest rate. Some examples of unsecured debt include credit cards, signature loans, gym membership contracts and medical bills.