REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA

MILIMANI COURT

COMMERCIAL & ADMIRALTY DIVISION

INSOLVENCY CAUSE NO. 2 OF 2016

IN THE MATTER OF THE INSOLVENCY ACT, 2015

AND

IN RE AN APPLICATION BY

PETER MUNGA.....DEBTOR

VERSUS

AFRICAN SEED INVESTMENT FUND LLC.....CREDITOR

RULING

Introduction

1. This is an opposed application by the Debtor to set aside a statutory demand issued on 19 September 2016 under section 17(3)(a) of the Insolvency Act No 18 of 2015 and Regulation 15(3) of the Insolvency Regulations 2016. The anticipated consequential effect is the vacation of the creditor's petition filed on 2 December 2016.

2. The application was filed on 14 November 2016 and is supported by the Debtor's affidavits sworn of 14 November 2016 and 12 February 2017.

Background facts

3. The cursory resume of the pleadings filed herein reveals a brief factual background as follows.

4. The Debtor is a director and member of Frescho Limited (" the Borrower"). The Creditor, a company incorporated in accordance with the laws of Mauritius, in or about December 2012 loaned to the Borrower an amount of US$ 590,000=. Repayment of the loan amount together with interest and other charges was secured by an all-asset debenture issued in favour of the Creditor by the Borrower for the same amount. Additionally, the Debtor together with his co-directors also guaranteed the repayment in writing. The Borrower however defaulted and in June 2016 the Creditor issued a statutory demand to the Borrower, to no avail. Then, on 9 September 2016, the Creditor in the genuine belief that the Debtor was truly and justly indebted to it forwarded to the Deputy Registrar a statutory demand for sealing.

5. The statutory demand was signed and sealed by the court's deputy registrar on the 19 September 2016 and subsequently collected for service on 21 September 2016. Service of the statutory demand upon the Debtor was however not effected until the 21 October 2016. The demand urged the Debtor to pay the amount of US$ 664,569= within 21 days of the date of service or face the consequence of a bankruptcy petition. The demand was not heeded.

The Debtor's case

6. The Debtor challenges the statutory demand on three main grounds.

7. Firstly, it is the Debtor's contention that the Creditor took no step to recover the debt due from the Borrower through the exercise of a debenture-holder's rights. The Debtor contended that the law provides so, while also claiming that the value of the assets of the Borrower which constitute the assets pledged under the debenture is above the debt.

8. Secondly, it is the Debtor's case that the amount stated in and claimed by the Creditor through the statutory demand has been grossly overstated. In particular, the Debtor pointed to the fact that an amount of US$ 103,672= paid on 28 September 2016 had not been factored. The Debtor also pointed to the discrepancy on the amounts demanded by the Creditor on diverse dates. In June 2016, it was stated that the Creditor demanded US$ 290,465= from the Borrower. Then on 7 July 2016 a demand for US$ 590,000= was made by the Creditor of one of the guarantors, yet the statements revealed that only an amount of US$ 314,577= appeared to be due.

9. The Debtor, thirdly, contended that the Creditor was merely intent in embarrassing the Debtor through the statutory demand and ultimate bankruptcy petition.

The Creditor's case

10. As may be gleaned from the grounds filed on 2 December 2016 in opposition to the application, the Creditor's contention is that the statutory demand was validly issued on the basis of a genuinely outstanding debt. The Creditor asserted that the application is bad in law as it had been filed outside the time prescribed by the insolvency regulations for challenging statutory demands. The Creditor stated that the debt was not disputed but only stated to have been allegedly overstated yet even the admitted amount had not been paid.

11. According to the Creditor, the law allowed the creditor to choose its own way of recovering a debt without being dictated to by the debtors or any person obligated to it.

Arguments in court

The Debtor submits

12. Ms. Maureen Maitai urged the Debtor's case.

13. Ms. Maitai, firstly, submitted that the Debtor was rightly before the court as the regulations expressly allowed statutory demands to be challenged. According to Ms. Maitai, who conceded that the statutory demand had been served on 21 October 2016, a brief calculation of the time up till the filing of the motion challenging the statutory demand revealed that the application had been filed within twenty one days. Counsel stated that the court needed to be conscious of all the excluded days under section 57 of the Interpretations and General Provisions Act (Cap 2) Laws of Kenya.

14. Counsel then submitted that the statutory demand did not comply with the provisions of Regulation 17(8) of the Insolvency Regulations 2016 as the Creditor had failed to indicate the security and also the value of the security it held for the debt. The security, in these respects counsel submitted was the all asset debenture which equated the value of the Borrower's assets of Kshs 115,998,746/=. Counsel then stated that since there was a security for the debt demanded the court was entitled to and could under Regulation

17(6) set aside the demand as it was evident that the security was in excess of the the debt.

15. Ms Maitai next submitted that the debt amount in the statutory demand had been overstated and this invalidated the statutory demand pursuant to section 17(6) of the Insolvency Act 2015. Counsel pointed out that the Debtor had on 10 November 2016 through its advocates pointed out and notified the creditor of the overstatement in the demand. That the statutory demand was invalidated pursuant to the provisions of section 17(6) of the Insolvency Act as the Debtor had brought to the attention of the Creditor the overstatement and also done so within 21 days of the service of the statutory demand.

16. Finally, Ms Maitai argued that the Debtor had shown that the debt was contested on a substantial ground as there was evident discrepancy on the amount demanded. The determination of the amount due was not for the insolvency court but rather for the ordinary court.

The Creditor's submissions

17. The Creditor's case was urged by Mr. Vincent Kahura.

18. Mr. Kahura submitted that it was clear that the application challenging the statutory demand had not been filed within the requisite and prescribed period under the law. It was filed three days after the time had lapsed. Accordingly, the application was fatally defective and ought to be struck out.

19. It was also the Creditor's submission that the debt was not disputed and further that the contest did not fall under Regulation 17(6) of the Insolvency Regulations to warrant the setting aside of the statutory demand. On the issue of notification of securities held by a creditor in the statutory demand, it was Mr Kahura's submission that the notification was only applicable where the insolvency debtor's debt was secured and that was not the case in the instant application. For this proposition, counsel referred the court to the case of **White *v* Davenham Trust [2010] EWHC 2748.**

20. Finally, with regard to the amounts due counsel was firm that the amount was due as stated in the statutory demand and that any credit made as alleged with regard to the payment of some odd US$ 102,000= was well after the demand had been issued. The discrepancies in the demand, according to Mr. Kahura, were inconsequential in the circumstances of the case and could well be explained at the hearing of the bankruptcy petition. Counsel also pointed out that the Debtor was obliged to pay the admitted amount but had failed to do so and that in such circumstances the statutory demand could not be set aside. For this proposition, counsel referred the court to the case of **In Re a Debtor (No 490-SD-1991)[1992]1 WLR 507.**

Debtor's rejoinder

21. In a pithy rejoinder, Ms. Maitai stated that the security which had to be disclosed was in relation to a debt and not to the person owing. Additionally, Ms. Maitai also stated the case law relied upon by the Creditor were distinguishable on fact.

Discussion and Determination

22. Having listened to counsel and perused the affidavits filed in support of and in opposition to the application, only one main issue turns for determination. It is whether the statutory demand issued on 19 September 2016 and served upon the Debtor on 21 October 2016 should be set aside.

23. A statutory demand issued under section 17 of the Insolvency Act 2015 ignites the bankruptcy process. Where a valid demand is served upon the debtor and it is not heeded within the statutory twenty one (21) days, the debtor will be deemed as unable to pay the debt demanded or having no reasonable prospect of being able to pay the debt and the creditor will be entitled to make an application to court for a bankruptcy order against the debtor, unless the statutory demand has been set aside.

24. The court's power to set aside a statutory demand issued under the Insolvency Act 2015 is founded

under the residual powers of the court and also under Regulations 16 and 17 of the Insolvency Regulations 2016. In particular paragraph 6 of Regulation 17 states as follows:

> ***The Court may grant the application if—***
>
> ***(a) the debtor appears to have a counterclaim, set-off or cross-demand which equals or exceeds the amount of the debt or debts specified in the statutory demand;***
>
> ***(b) the debt is disputed on grounds which appear to the Court to be substantial;***
>
> ***(c) it appears that the creditor holds some security in respect of the debt claimed by the demand, and either paragraph (6) is not complied with in respect of the demand, or the Court is satisfied that the value of the security equals or exceeds the full amount of the debt;or***
>
> ***(d) the <u>Court is satisfied, on other grounds</u>, that the demand ought to be set aside.***[emphasis added]

25. It is evident when one reads paragraph (d) above that the grounds for the setting aside of a statutory demand are not limited by statute. Paragraph (d) opens it up and gives the court a spacious discretion. It is certainly not possible to foresee all the instances which may properly fall under paragraph (d) of Regulation 7.

26. My view is that, when asked to set aside a demand on any other ground other than the grounds stated under paragraphs (a),(b) and (c), the question then becomes whether the applicant-debtor can show a substantial reason akin to the reasons under the preceding three paragraphs. The court must also consider the consequences of setting aside the demand and whether the creditor ought to pursue the bankruptcy proceedings rather than engage in a litigation that is obviously bound to succeed in his favour. The test, which is not necessarily conclusive, is whether it would be unjust for the statutory demand to give rise to insolvency proceedings in the particular case.

27. It brings me to the instant case.

28. There is first the issue of time bar. The regulations stipulate that the challenge be mounted at least within twenty one days of service of the statutory demand.

29. It is common cause that the statutory demand was served on 21 October 2016. The application to set aside was filed on 14 November 2016. Simple arithmetic would lead one to an aggregate of twenty three (23) days, excluding the day of service of the demand and also the day of filing of the application to set aside: see section 57 (a) of the Interpretation and General Provisions Act (cap 2) Laws of Kenya. The application was filed late, some two days late.

30. Ms Maitai urged that the court should not reckon the last day as it fell on a Sunday and also the first two days of the time-bar period as they fell on a weekend. Counsel invoked section 57 (b) of the Interpretation and General Provisions Act (Cap 2) which reads thus:

> ***"(b) if the last day of the period is a Sunday or a public holiday or an official non-working day (which are in this section referred to as excluded days), the period shall include the next following day not being an excluded day"***

31. True, the first two days in the computation of time fell on a Saturday and a Sunday. Saturdays are official non–working days within our civil service. The last day also fell on a Sunday. It must however be noted that section 57(b) of the Interpretation and General Provisions Act (Cap 2) stipulates that excluded days (being Sunday, public holidays and official non-working days) are not to be reckoned in the computation of time where the act or proceeding is directed or allowed to be done or taken within any time not exceeding six days. Where the period exceeds six days then the excluded days are to be reckoned in. They count. I am satisfied that the application was filed outside the prescribed time line.

32. The question then is whether such non-compliance would dictate that I strike out the application without considering its merits.

33. My reading of Regulation 16(1) which sets the period, within which time an application to set aside a statutory demand ought to be made, does not reveal that the time limit is a mandatory requirement. Compulsive and mandatory words have not been used. The Regulation likewise does not state the consequences of non-compliance.

34. I take the view that strict compliance with Regulation 16(1) is not necessary and non-compliance should not be fatal *per se*. The draconian and crippling consequences of insolvency orders would not allow a contrary interpretation as it would mean that a delay, no matter how trivial, would invalidate and make fatal even merited applications seeking to challenge statutory demands. In my view, that could not have been the intention of the legislature. Each case must be viewed on its own unique circumstances.

35. Additionally, legislative intent must also accord precedence to substance rather than technicalities. That is the pragmatism by which courts must be guided in the consideration of any legislation.

36. Unless, substantial injustice or prejudice is to be occasioned by some technical defect or irregularity and which injustice or prejudice cannot be remedied by a court order, technical defects and irregularities should not stand in the way of adjudicating disputes. Compliance with time lines, in my respectful view falls in the realm of technical requirements unless the consequences of non compliance are expressly stated.

37. I therefore disagree with Mr. Kahura's submission that since the application was filed late, the delay was fatal. There was delay yes, but not such as would warrant a striking out in the circumstances of the case. I have also not witnessed any prejudice on the part of the Creditor which may not be remedied even with an order for costs.

38. I now consider the grounds put across for the setting aside of the statutory demand.

39. Firstly, the Debtor has complained that the statutory demand did not indicate that the debt is secured, the nature of the security and also the value of the security. Additionally, the Debtor stated that no attempt had been made by the Creditor to recover the debt by realizing the security.

40. It is true that the loan amount advanced to the Borrower was secured by an all asset debenture issued in favour of the Creditor by the Borrower in the principal sum of US$ 590,000=. It is also true that the same loan was also secured by a guarantee issued by the Debtor for the same principal amount. Finally, there is no controversy that the impugned statutory demand made no mention of either the debenture or the value of the security.

41. I am unable to agree with or find any reason in the submission by the Debtor that the Creditor was legally bound to first proceed and realize the security under the debenture before proceeding under the Insolvency Act or even to enforce the guarantee executed by the Debtor. Even though Ms. Maitai strongly submitted that the law so provided, her submissions lost their vigor when no reference was made to a single legal provision or authority. Rather, it was counsel for the Creditor who correctly submitted and availed case law that a creditor who holds an array of security is not duty bound to take one particular line first. As was stated by the Court of Appeal in **Barclays Bank of Kenya Ltd *v* Kepha Nyabera & 191 others [2013]eKLR**

> ***"The general rule is that a secured creditor is not obliged to resort to his security. He can claim repayment by the debtor personally and leave the security alone. He can sell the charged securities or set off or combine accounts. All these remedies could be exercised at any time or times, simultaneously or contemporaneously or successively or not at all. "*** [emphasis added]

42. I agree with this general rule that a secured creditor is not obliged to resort to his security for recovery of the debt. Indeed, the above broad proposition in law is sound and makes commercial sense. No creditor

would otherwise carry the business of secured lending if he was to be liable to the borrower or any sureties on the order of security to resort to. The creditor ought to have a free hand, when to act and on which security, without any direction by the debtor, sureties or the court.

43. I would perhaps add that an exception to the general principle would be allowed where the parties have expressly agreed to the contrary and the security documents themselves stipulate the agreement. The parties must then be held to their bargain.

44. In the instant case, no such agreement exists. Instead, Clause 10 of the Guarantee Deed dated 17 December 2012 and executed by the Debtor stipulated as follows:

> **"10. Effect of other guarantees etc**
>
> ***This guarantee is in addition to and shall not merge with or otherwise prejudice or affect any other right, remedy, guarantee, indemnity, security or judgment and may be enforced notwithstanding the same or any other bill, note, mortgage, charge, pledge or lien now or hereafter held by or available to the Creditor"***

45. The clause is relatively clear. The guarantee and any liabilities there under were independent of any securities held by the Creditor. This should adequately reinforce the position that the Creditor did not need to chose at the behest of the Debtor or even the Borrower which security to resort to first. Further, the Guarantee Deed also contained an appropriate notification demanding that the guarantors, including the Debtor, obtain independent legal advice prior to signing the document. There was no suggestion that this was not done and likewise there has been no suggestion that the Debtor did not understand the contents of the guarantee.

46. I find the Debtor's contention that the Creditor needed to first exhaust all other remedies and securities it held to be misconceived.

47. I move to the question of the statutory demand not having stated the existence of a security and also revealed the value or estimated value of the security. According to the Debtor such omission is enough to cause the setting aside of any statutory demand.

48. The existence of the debenture is not in doubt. The value of the debenture, in my view, is apparently also not in controversy. Under the debenture the Borrower pledged all its movable and immovable assets both present and future as security for the US$ 590,000= debt. The Debtor submitted and indeed availed evidence to the effect that as at 31 December 2015 the Borrower's assets aggregated Kshs 115,998,746/= in value. This ought to be the value of the security. Neither the security debenture nor the value of the assets or security for that matter was specified in the statutory demand.

49. According to the Debtor, there was non-compliance with clear statutory provisions in re the statutory demand and the non-compliance invalidated the demand.

50. It is not in doubt that one of the reasons the court may oblige an applicant with an application to set aside a statutory demand is, as stated under Regulation 17(6), when

> ***"it appears that the creditor holds some security in respect of the debt claimed by the demand, and either paragraph (6) is not complied with in respect of the demand, or the Court is satisfied that the value of the security equals or exceeds the full amount of the debt*** ."

51. Regulation 17(7) of the Insolvency Regulations on the other hand provides as follows:

> ***"Where the creditor holds some security in respect of his debt and has complied with paragraph (6) in respect of it, but the security is undervalued in the demand, the court may require the creditor to amend the demand accordingly, without affecting the creditor's right to present a bankruptcy application in respect of the original demand"***

52. Under the same Regulation, compliance is deemed where the full amount of the debt is specified in the demand besides also stating the nature of the security, its value as at the date of the demand and the net amount claimed by the demand: see **Regulation 17(8).**

53. It is clear that the statutory demand ought to contain details of any security held by the creditor, particularly the nature and value thereof. I must also point out that the security is with regard to the debt and not the debtor. It is not the assets of the debtor to be declared and stated in the statutory demand but the nature and value of any security pledged by any person to secure the debt. It must be the value of any property that is to be available for the satisfaction of the debt.

54. Regulation 17(6)(c) however appears to make it optional, that even where there is no compliance but the court is satisfied that the value of the security equals or exceeds the full amount of the debt, then the court may still set aside a statutory demand. Effectively, it would mean that even where the nature and value of the security is not stated in the statutory demand, the demand may not be fatally defective. The court is still at liberty to set it aside on the equitable ground that there is adequate security for the debt. The rationale appears simple. The debtor may be in a better position to show the value of the security than the creditor who may only be holding a non-possessory security whose value may not be clear at the time of issuing the demand.

55. I view it that it is not mandatory that the nature and value of any security held be stated and where there is an omission, it is incumbent upon the debtor to satisfy the court under Regulation 17(6)(c). Such satisfaction may be achieved at the hearing of the bankruptcy application.

56. In the instant case as well, I hold the view that the outstanding amount was a debt that the Debtor was liable for as a guarantor and not as a principal debtor. The provision of the insolvency regulations which dictate disclosure of security held had no relevance at all.

57. It was finally the Debtor's substantive argument that the statutory debt ought to be set aside as the amount claimed had been overstated, a claim denied by the Creditor.

58. I must first point out that overstatement or an exaggeration of the amount claimed is not stipulated as one of the grounds for setting aside a statutory demand. It would however fall under the general residual and discretionary grounds. Besides, section 17(6) of the Insolvency Act also decrees that a statutory demand will be invalidated where the debtor disputes the amount demanded and notifies the creditor of his contest on the basis that the amount has been overstated and further the notification is communicated within the statutory period of the demand.

59. The Debtor sought to rely on this section to have the statutory demand invalidated while pointing out that the after the demand was received and prior to the expiry of 21 days the Creditor was notified of the dispute as to the amount demanded. The contest was basically and substantially that an amount of US$ 103,672= which was paid to the Creditor on 28 September 2016 had not been accounted for in the demand.

60. It is important to point out that the mere overstatement of amount claimed in a statutory demand does not per se invalidate the demand. The debtor is obligated to contest the amount and within the requisite period and additionally it must be such as to cause prejudice and injustice to the debtor if the demand was allowed to subsist.

61. There is additional support from the statute itself that the demand is not invalidated upon a dispute being raised by the debtor. To begin with, section 17 of the Insolvency Act must be read in its entirety and in a wholesome manner. Subsection 7 anticipates that even where there is an overstatement of the amount due, the debtor is still to comply with the statutory demand. He does so by

> ***"(a) Taking steps that would have complied with the demand had it stated the correct amount owing, such as by paying the creditor the correct amount owing plus cost ; and***

(b) Taking those steps within the period specified in the demand for the debtor to comply."

62. These provisions, which are found under subsection 7, are a clear indicator that the debtor is still expected to comply with the statutory demand not withstanding any overstatement of the debt

63. I hasten to add that Section (17)(5) of the Insolvency Act states that

"***This section is subject to sections 18 to 20."***

64. And the sections referred to are all for the filing and hearing or determination of the bankruptcy application, which in my view is a reflection of the view that a statutory demand which is impugned merely because of an overstatement of the amount due would not stop the filing and determination of a bankruptcy application by a creditor.

65. It would perhaps also be important to point out that the Debtor herein has not attempted to comply with the allegedly overstated demand as outlined under section 17(7) of the Insolvency Act and paid the admitted portion of the debt. I would consequently not set aside the statutory demand because of the allegedly overstated amount as it was also not shown to my satisfaction that there was an overstatement or that the amount was disputed on substantial grounds.

Conclusion

66. The Debtor disputed the demand on various grounds. The debt was also disputed but I have not found that it was disputed on substantial grounds.

67. It was clear that the demand served upon the Debtor was based upon a guarantee executed and binding on the Debtor. The Creditor was entitled to demand the amount once the Borrower defaulted. The Debtor has not shown any substantial grounds for disputing the debt. By contrast, the Creditor has shown that the debt was clearly owed. As a secured creditor with multiple remedies, the Creditor was entitled to elect which to enforce, at what time, in what order and in the way it chose. It opted to call in the guarantee and no payment has been made. The mere existence of a secured remedy against another party is not a substantial ground for refusing to allow a creditor to pursue a remedy in bankruptcy against a guarantor. The liability of a guarantor is generally coextensive with that of the principal debtor, not contingent on the security provided by the principal debtor proving to be inadequate.

68. I am unable consequently to exercise my discretion to set aside the statutory demand dated 19 September 2016.

Disposal

69. The Debtor's application fails. I dismiss the application dated 14 November 2016 and filed on 19 November 2016 with costs to the Creditor.

Dated, signed and delivered at Nairobi this 12th day of May, 2017.

J.L.ONGUTO

JUDGE