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"We Mean Business": Issue Fifteen

Greetings!

At the core of every economy is business. From the creation of employment to the payment of taxes, it is an obvious observation that businesses are vital economic players.

In reference to the foregoing, in what is the fifteenth (15th) issue of our flagship publication, *Legal & Kenyan*, we delve into various legal matters that affect businesses. From the termination of employment contracts, discussions on start-ups and distribution of company shares upon a shareholder's death, to new tax reporting requirements for multinational enterprises, and much more…

This issue features the contribution of Maureen Shaba, Tax Manager, and Nicholas Gathecha, Tax Associate, both from Deloitte, Kenya. They cover the new requirements aimed at increasing tax transparency for multinational enterprises operating in Kenya, through what is referred to as country-by-country reporting.

From the home stable, Jacob Ochieng and Milly Mbedi offer their reflections on the new Data Protection (General) Regulations, 2021 that we all should take note of given that data processing is now so intertwined with everyday life. Pamella Ager, James Kituku and Anna Kandu then analyse the sectional properties' legal framework, highlighting recent developments in the law that have completely transformed the manner in which sectional property is owned and transferred. I come in next with an article that looks at how start-ups are poised to enhance Kenya's economic rebound, followed by Daniel Okoth and Erastus Rabut who deliver an employment law piece that examines the efficacy of discharge agreements when terminating employment. Hellen Mutua and I then discuss the rather sensitive subject of dealing with company shares upon the death of a shareholder. Daniel Okoth and Natalie Obago come next with an insightful article on the compliance and enforcement mechanisms under the Data Protection Act, 2019 while Noella Lubano follows up from where she left off in the previous issue with an article that discusses rescue options available to individuals under the Insolvency Act, 2015.

We do hope that you enjoy the read!

Sincerely,

John Mbaluto, FCIArb
Editor

Founding Partner's Note

Dedicated. Diligent. Passionate. These are just a few words I can use to describe our editorial team and the various writers who contribute to each issue of *Legal & Kenyan*.

With an acute awareness to the ever-changing tides in the Kenyan business landscape, particularly over the last couple of years, the *Legal & Kenyan* team has consistently endeavored to offer legal insights on very pertinent topics affecting the business community. This issue is no different and I am truly excited to see it *"hit the stands"*.

I do hope that as you read it, you will find it insightful.

George Oraro SC
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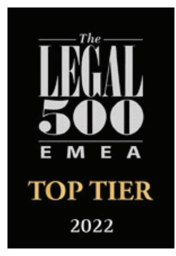

"Experienced legal experts of many years and in different legal fields of practice, with quick responses to legal needs of clients. They are willing to bend backwards for clients. They have a wide network of experienced legal firms to represent clients where the firm has no offices."

THE LEGAL 500 EMEA, 2022

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OPEN SESAME:

REFLECTIONS ON THE DATA PROTECTION (GENERAL) REGULATIONS, 2021

The substantive statute that governs data protection in Kenya is the Data Protection Act, 2019 (**the DPA**) that came into force on 8th November 2019. Pursuant to the DPA, the Cabinet Secretary for matters relating to information communication and technology (**the Cabinet Secretary**) has prescribed various regulations concerning data protection that elaborate on the provisions of the DPA in procedural terms. Key amongst these are the Data Protection (General) Regulations, 2021 (**the General Regulations**).

The General Regulations elaborate *inter alia* on the rights of data subjects, the restrictions on the commercial use of personal data, the obligations of data processors and data controllers, reporting on data breaches and stipulations for the transfer of data outside of Kenya. The General Regulations also expound on data protection impact assessments and provide for exemptions.

Rights of Data Subjects

The DPA outlines six (6) rights of data subjects. These are enumerated to include the right to be informed of the use of personal data; the right to have access to personal data; the right to object to the processing of personal data; the right to correct false or misleading data; the right to port or copy personal data; and the right to delete false or misleading data.

In relation to the right to be informed of the use of personal data, the General Regulations oblige data controllers and data processors who want to rely on consent as the legal basis for processing of personal data, to ensure that the data subject is informed of the identity of the data controller or data processor; the purpose of each of the processing operations for which consent is sought; the type of personal data that is collected and used; where applicable ,information about the use of the personal data for automated decision-making; the possible risks of data transfers due to absence of an adequacy decision or appropriate safeguards; whether the personal data processed shall be shared with third parties; the right to withdraw consent; and the implications of providing, withholding or withdrawing consent.

It is important to note that a data processor or data controller may process data without consent if the processing is necessary for any of the reasons set out under the DPA. Such reasons include where it is necessary for the performance of a contract; compliance with any legal obligations; protection of the vital interests of the data subject; performance of a task carried out in the public interest or by a public authority; and for purposes of historical, statistical, journalistic, literature, art or scientific research. A data controller or data processor is required to establish the basis before processing any personal data and should be able to demonstrate it.

The General Regulations allow for personal data to be collected indirectly from a third party, through publications, surveillance cameras, web browsing or biometric technology. Data controllers and data processors are required to notify the data subject within fourteen (14) days of such indirect collection. Where a data controller or data processor intends to use personal data for a new purpose, the data controller or data processor is required to ensure that the new purpose is compatible with the initial purpose for which the personal data was collected. In addition, where the new purpose is not compatible with the initial purpose, a data controller or data processor is required to seek fresh consent from the data subject.

Data subjects can assert their rights under the DPA by using the prescribed procedure and prescribed forms under the General Regulations to apply for restriction of processing of their personal data; object to the processing of their personal data; access their personal data; port their personal data from one data controller or data processor to another; or have their personal data erased. Any decision to decline any of these requests must be communicated with reasons for the denial to the data subject.

It is worth noting that the rights of a data subject can be exercised by other people authorised by the data subject. In cases of data collection from children, consent of the child's parent or guardian is required to be obtained. The DPA prohibits the profiling of a child for direct marketing purposes. The parent or guardian is required

to be made aware of the inherent risks of processing the data of a child and the security measures put in place to minimize the risks.

Commercial Use of Personal Data

Commercialization of personal data occurs when the personal data of a data subject is involved in the promotion of economic interests, including inducing another person to buy, rent, lease, join, subscribe, exchange products, property, information or services that enable or complete a business transaction. The General Regulations set out instances which constitute use of personal data for the purposes of direct marketing, including sending a catalogue through any medium to a data subject; displays an advertisement on an online media site a data subject is logged onto via the use of their personal data; sending an electronic message or any other advertising material to a data subject about a sale using personal data provided by the data subject.

Commercial use of personal data is authorized if the data controller or data processor has collected the personal data from the data subject; the data subject has been informed by the data controller that part of the purposes for which the data is collected is for direct marketing; the data subject has consented to the same or the data subject has not submitted an opt-out request.

Data controllers and data processors are prohibited from sending messages for purposes of direct marketing unless such messages contain an option allowing the data subjects to restrict such communication without incurring any charges. Data subjects are also allowed to request a data controller or data processor to restrict use or disclosure of their personal data to a third party for the purpose of facilitating direct marketing at no cost. The data controller or data processor is obliged to honour such a request within seven (7) days of the request. In addition, the General Regulations prohibit sending of emails for the purposes of direct marketing where the identity of the person on whose behalf the communication has been sent has been disguised or concealed; where a valid address to which the recipient of the communication may send a request that such communications should cease has not been provided; or where there is use of automated calling systems without human intervention.

Obligations of Data Controllers and Data Processors

The General Regulations oblige data controllers and data processors to develop, publish and update their data protection policies regularly. For instance, they are required to maintain a data retention schedule with appropriate time limits for the periodic review of the need for the continued storage of personal data that is no longer necessary or where the retention period is reached and to erase, delete, anonymise or pseudonymise personal data upon the lapse of the purpose for which the personal data was collected. The retention schedule is required to outline the purpose for retention, the retention period, provision for periodic audit of the personal data retained and actions to be taken after the audit of the personal data retained.

In relation to automated individual decision making, the General Regulations mandate data controllers or data processors to adhere to certain prescribed requirements. These include informing a data subject when engaging in processing based on automated individual decision making; providing meaningful information about the logic involved; explaining the significance and envisaged consequences of the processing; ensuring the prevention of errors; using appropriate mathematical or statistical procedures; putting appropriate technical and organisational measures in place to correct inaccuracies and minimise the risk of errors; and ensuring that a data subject can obtain human intervention and express their point of view.

The General Regulations further require that data controllers engage data processors through a contract which contains the prescribed information. Data processors are prohibited from engaging the services of a third party without prior authorisation of the data controller. If a data controller authorises the data processor to engage a third party, the data processor is required to enter into a contract with the prescribed information with the third party. However, the data processor would remain liable to the data controller for the compliance of any third party involved.

It is important to note that a data processor or data controller may process data without consent, if the processing is necessary for any of the reasons set out under the DPA.

The General Regulations also prescribe certain types of processing that is for the purpose of strategic interest of the State. These are to be processed through a server and data centre located in Kenya or stored at least one serving copy of the concerned personal data in a data centre located in Kenya. These include administering of the civil registration and legal identity management system, overseeing any system for administering public finances by any State organ etc.

Notification of Personal Data Breaches

In instances where personal data has been accessed or acquired by an unauthorised person, and there is a real risk of harm to the data subject whose personal data has been subjected to the unauthorised access, a data controller is required to notify the Data Protection Commissioner (**DPC**) within seventy-two (72) hours of becoming aware of such breach; and communicate to the data subject in writing within a reasonably practical period, unless the identity of the data subject cannot be established. The General Regulations expound on the categories of notifiable breaches to include a data breach that relates to personal identification number, account information, passwords, security codes or biometric data etc. This excludes any personal data that is publicly available. They also prescribe the details that should be included in the notification to the DPC.

Transfer of Personal Data Outside Kenya

Generally, transfer of personal data outside Kenya is allowed if it is based on appropriate data protection safeguards; an adequacy decision made by the DPC; transfer as a necessity; or with the consent of the data subject. The General Regulations outline the elements of these conditions and allow parties to enter into agreements for the transfer of personal data.

Data Protection Impact Assessment

A data protection impact assessment (**DPIA**) is defined under the DPA as an assessment of the impact of the envisaged processing operations on the protection of personal data. A DPIA is required to be undertaken where the data processing operations may result in high risks to the rights and freedoms of a data subject and a report on the same is to be submitted to the DPC at least sixty (60) days before the processing of such personal data commences. The General Regulations outline examples of such activities to include large scale processing of personal data, processing biometric or genetic data, among others.

Provisions on Exemptions under the DPA

Generally, the processing of personal data is exempt from the provisions of the DPA if it relates to processing of personal data by an individual during a purely personal or household activity; it is necessary for national security or public interest; or disclosure is required by or under any written law or by an order of the Court. The General Regulations expound on this and allow for data controllers or data processors who are national security organs and require to process personal data in furtherance of their mandate to apply for an exemption from the Cabinet Secretary. The General Regulations further categorise the ground of public interest into permitted general situation or permitted health situation.

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UNDER ONE ROOF:

ANALYSIS OF THE SECTIONAL PROPERTIES' LEGAL FRAMEWORK

The concept of sectional titles in Kenya can be traced back to the early 1960s, during the drafting of the now repealed Registered Land Act (Cap. 300) Laws of Kenya (**the RLA**). The RLA was meant to be the overarching substantive land legislation for post-independent Kenya. However, at the time, legislators were not open to the concept, hence the issue was shelved until its revival in the 1980s, following concerted efforts by the Law Society of Kenya, the Land Review Commission and the Ministry of Lands and Settlement. These efforts culminated in the enactment of the Sectional Properties Act, 1987 (**the SPA, 1987**), with the intention of introducing titled ownership for flats and apartments, which were becoming increasingly predominant in the country. In 1990, the Sectional Properties Regulations were promulgated to operationalize and facilitate implementation of the SPA, 1987.

Although these legal developments ushered in a new era of compartmentalised ownership of units, a challenge subsisted in terms of the roll out of the concept countrywide. The concept was only aligned with the RLA titles, yet there were other subsisting forms of land ownership which predated the RLA, such as the Government Lands Act (Cap. 280) Laws of Kenya, the Registration of Titles Act (Cap. 281) Laws of Kenya, the Land Titles Act (Cap. 282) Laws of Kenya, amongst others. Therefore, it was difficult for a developer who did not hold RLA head title, to implement the sectional title concept in his development. This legal incongruity led to the evolution of subleases as alternative titles, mostly in developments where the developer held a non-RLA head title.

Upon promulgation of the Constitution in 2010, the need for uniformity of property holding was appreciated. Consequently, in the spirit of Article 68 of the Constitution, several statutes were enacted to serve as a common denominator for property related transactions in the country. The Land Act and the Land Registration Act were introduced in 2012 with the Sectional Properties Act being recently enacted in 2020 (**the SPA, 2020**). Unlike its 1987 predecessor, the SPA, 2020 extends to all forms of ownership of land and head titles, with the intention to replace all subleases with sectional titles. However, the law allows a developer the latitude to retain either the sublease or sectional property ownership. In 2021, new Sectional Properties Regulations were gazetted, to facilitate implementation of the SPA, 2020 and contain the following salient features.

Transition of Subleases into Sectional Titles

Conversion of subleases into sectional titles can be initiated either by a developer, management company or the owner of an individual unit. The process entails the registration of sectional plans that have been prepared by a surveyor and approved by the county government; a sectional plan delineating the various units in any building; closure of the existing (lease) records of the units; opening of new individual (sectional) records for the respective units; transfer of information that existed in the closed records to the newly opened records e.g. ownership, charges, caveats etc; and issuance of sectional titles for the respective units.

Once a sectional title is issued, each unit becomes separate, with its corresponding distinct share in the common property. This exclusivity enables the direct levy of outgoings such as land rent or rates against each unit, as opposed to the head title.

The Registrar is empowered to register a restriction over any title, to prevent further dealings, until the concerned parties comply

with the conversion process. The SPA, 2020 has set a conversion deadline of 27th December 2022, being two (2) years from when the Act came into force on 28th December 2020. Given the current-working conditions at the Ministry of Lands it remains to be seen whether the target will be met.

Establishment of a Corporation and its Mandate

Once a sectional plan in any development is registered, the Registrar is required to constitute the respective owners of the units into a corporation. A corporation is a recognised legal entity, and has several functions under the SPA, 2020 including maintenance of the common areas; insurance of the common property; administration of the by-laws of the concerned development; enforcement of the terms and conditions relating to the land on which the development is erected; and establishment and maintenance of a fund for the corporation's expenses.

The corporation should be run by a board of management, which is required to convene annual meetings. In the corporation's meetings, members are entitled to exercise voting rights in proportion to the units which they own. Where a property is charged, the lender is entitled to exercise that right in lieu of the owner. In the discharge of its functions, a corporation is required to periodically levy each unit owner an apportioned sum, as the owner's contribution towards the corporation's fund. Where the owner fails to remit the required amount, the corporation reserves the right to register a caution against the owner's unit. The caution shall operate as a charge over the particular unit, securing the outstanding amount.

A corporation is also required to constitute a dispute resolution committee, to resolve any disputes members may have regarding the enforcement of the corporation's by-laws. The reference of a dispute to the said committee, however, does not deprive an aggrieved party of any other legally available remedies.

Lastly, it is noteworthy that the corporation is also an integral party in any tenancy arrangement involving a unit. The owner of the unit is required to notify the corporation in writing, of his or her intention to let out the unit. The owner is equally required to undertake to repair any damage the tenant may occasion to the premises. Equally, the owner should notify the corporation once a tenancy ends. In the course of the rental arrangement, the corporation has power to evict any tenant who contravenes any by-law, where the owner does not intervene despite the corporation's request to forewarn the tenant.

Inclusivity of Physically Challenged Persons

Every Kenyan has the freedom to move and reside anywhere within the country pursuant to Article 39 of the Constitution which provides for the freedom of movement. Physically challenged persons enjoy further protection under Article 54 of the Constitution, which requires that they should be treated in a dignified and respectful manner.

Flowing from these constitutional dictates, the SPA, 2020 has sought to facilitate the peaceful habitation of such persons in any development. Under the SPA, 2020, a corporation is prohibited from promulgating any by-law by which a visually challenged owner is disallowed to keep or use a guide dog within a development. This equally extends to making flats accessible by physically challenged persons.

New Transactional Requirements

Previously, there have been instances where purchasers have entered into transactions not knowing that developers had been financed to put up units. In some cases, unscrupulous developers would pocket the sale proceeds, without servicing their loans.

Having been enacted under the prism of "Ease of Doing Business", the SPA, 2020 has also curtailed the red tape that applied to sublease arrangements, such as having to defer to a management company for transactions including selling or charging a property in a development.

Upon such developers' default, the financiers would invariably move to secure their proceeds by exercising their statutory power of sale, after serving the requisite legal notices. They would then proceed to auction the units, thereby exposing the purchasers.

As a legal safeguard to prospective purchasers, the SPA, 2020 imposes a duty on any developer selling a unit to avail certain documents including the purchase agreement; the by-laws or proposed by-laws of the development; the management agreement or proposed management agreement (where applicable); the recreation agreement or proposed recreation agreement (where applicable); copy of the head title or sectional title (as applicable);copy of sectional plan or proposed sectional plan; and copy of a charge, where there is a subsisting charge affecting the particular unit.

Where a property is charged, a developer shall notify the purchaser of the charge particulars including the principal amount applicable, the repayment instalments, relevant interest rate and repayment duration. This is a significant stride towards full disclosure, which will empower purchasers to make informed decisions on whether or not to proceed with transactions.

Penal Sanctions for Non-Compliance

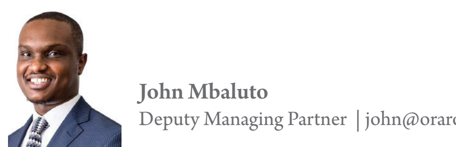
The SPA, 2020 has created some offences, for which there are prescribed punishments. For example, the failure by a proprietor to comply with the sectional plan registration requirements or the failure of a developer to avail the prescribed documents to a purchaser. The defaulter is, upon conviction, liable to pay a fine of up to KES. 20,000,000 or one (1) year imprisonment or to both. The SPA, 2020 also imposes a general fine of up to KES. 250,000 upon conviction for any other contravention of the statute.

Summation

The enactment of the SPA, 2020 is a significant leap forward in the quest to standardised and proper documentation pertaining to sectional property in the country. Having been enacted under the prism of "*Ease of Doing Business*", the SPA, 2020 has also curtailed the red tape that applied to sublease arrangements, such as having to defer to a management company for transactions including selling or charging a property in a development.

The exclusion of such intermediaries has enabled direct transactions with the government as far as their properties are concerned, thereby hastening the turn-around-time for closing transactions. Furthermore, the SPA, 2020 has entrenched the Constitutional requirement for inclusivity, by prohibiting the exclusion of assistive animals in developments, by visually impaired persons. This is a major development which ought to be applauded and commended.

Transparency has been enhanced in property transactions, as developers now have a duty of disclosure in terms of the documents and information they should avail to prospective purchasers. This will ensure that purchasers make informed decisions regarding transactions in future. To eventually realise the country's aspiration of becoming a business-friendly destination, the national government not only needs to roll out the sectional property framework, but conclusively oversee and implement the digitisation of land records, so that the records are easily available and accessible when required.



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FROM THE GROUND UP:

ENHANCING KENYA'S ECONOMIC REBOUND THROUGH START-UPS

Introduction

According to the Association of Countrywide Innovation Hubs, Kenyan tech start-ups topped the continent as they raised an impressive KES 21.4 Billion of funding in 2020. This level of funding is attributed to a socio-professional environment that is conducive to work in, even though Kenya's start-up ecosystem remains unregulated. Whereas countries like South Africa, Tunisia, Senegal, and Nigeria have pegged regulatory policies to govern start-ups, Kenya has no government policy that caters for start-ups.

Things are now, however, steered towards change. In 2021, through the Start-Up Bill, 2021 (**the Bill**), Kenya took its first steps toward regulating the start-up ecosystem.

The Bill seeks to govern the interactions and relationships between the government, incubators, start-ups, investors, and the ultimate consumers of innovative products. To do this, the Bill has been modelled to attract talent and capital which will, in turn, create innovative thinking, jobs, entrepreneurial culture, and wealth. This article seeks to analyse the possible impacts of the proposed legislation.

It has been observed that cumbersome regulations, the digital-skills gaps, limited funding, and highly fragmented markets continue to hold back African start-ups. Against this backdrop, this article postulates that the proposed legislation would be good for start-ups if the aim is to encourage their growth by providing a legally conducive and enabling environment.

Start-Ups Defined

A start-up is a business entity formed to develop a new product or service which changes the normal way of doing business and becomes ingeniously irresistible for end-users and customers. The Bill defines a start-up to include a technology-based innovative entity, that is legally recognized under the laws of Kenya with strong growth potential and a disruptive economic model.

There is a definitional difference between start-ups and micro and small enterprises (**MSEs**). MSEs are generally profit-making businesses with a small annual turnover in any sector whereas start-ups, in addition to conventional business qualities, must have a novel and innovative edge with the potential to disrupt the usual manner of doing business in that industry.

A start-up must bring a novel business idea and thus the government's efforts at regulation should focus on assisting the innovator in developing and growing the idea into a business product or service. MSEs are focused primarily on profits only whilst start-ups are focused more on the growth and development of the idea into a business product or service. These differences determine the manner of raising funds, the level of legal protection that should be afforded, the nature of government support, and the latitude to allow international investors to inject into the economy. It is therefore not at all surprising to find that the provisions of the Micro and Small Enterprises Act, 2012 are fundamentally different from those contained in the Bill.

Key Objectives

The Bill aims to foster a culture of innovative thinking and entrepreneurship; link start-ups with private investors, financial institutions, the private sector, research institutions and other institutions at the county, national and international levels; facilitate the provision of fiscal and non-fiscal support to start-ups; promote an enabling environment for the establishment, development, conduct of business, and registration of start-ups; establishment of incubation facilities at the national and county levels of government; and entrench an environment that promotes the establishment of start-ups.

The overarching goal of the Bill is to set up an ecosystem where start-ups may be created and supported to enable them to grow and spill over into the various sectors of the economy. Noting that Kenya's national economic blueprint is heavily reliant on technology and innovation which thus far remains unregulated, the proposed law comes in handy insofar as it aims to support the digital and the knowledge-based sector of the economy.

Incubation Programmes

Incubation programmes are made up of incubators that are either companies, partnerships, non-governmental organisations, or limited liability partnerships, whose principal objective is to support the birth and development of start-ups, innovation, and activities related to the transfer of technological research, development, and innovation process, through the offer of dedicated physical spaces and services or advice. These programmes provide an enabling environment for infant technologies, ideas, and industries to grow.

As the country moves away from a resource-driven economy to a knowledge-driven economy, the government has a significant interest in setting up incubation programmes that would assist start-ups to grow, given that succesful start-ups ultimately create large-scale employment opportunities, thereby helping the government solve the unemployment problem.

Incubation is meant to support nascent ideas, innovations, and technologies ideologically. As such, incubators must be capable of giving such supportive infrastructure that can help start-ups access skillset talents, finances, and technological capacity. The Bill proposes certification of incubators as a prerequisite to ensure that incubators meet the required standards for technical capacity and technological know-how and that they possess the right conditions or environment to support start-ups.

The overarching goal of the Bill is to set up an ecosystem where start-ups may be created and supported to enable them to grow and spill over into the various sectors of the economy.

Not all start-ups necessarily have the potential or ability to disrupt any sector of the economy, as such, there must be a means of identifying qualifying start-ups that are innovative, research-based, and have technological components. This would effectively prevent the admission of non-viable start-ups into incubation programmes.

Likewise, an entity cannot remain in incubation indefinitely. There must be a means of exiting from incubation - either by attaining a certain capital threshold or by incubating for a specified number of years.

Fiscal Incentives

Innovative entrepreneurial activities do not happen randomly or in a vacuum hence, the Bill proposes to mandate the national and county governments to provide economic conditions such as incentives, opportunities, and to remove barriers to innovative businesses, thinking and ideas. This can be achieved by funding start-ups, tax exemptions, grants, and by reducing regulatory red tape in the registration processes.

As earlier indicated, unlike MSEs, start-ups are not necessarily started for profit-making, hence the mode of funding is fundamentally different from normal business associations. For instance, getting a loan to support a novel or innovative idea may prove to be challenging due to uncertainties attendant with developing new ideas. In that regard, section 31 of the Bill proposes to amend section 29(1) of the Science, Technology, and Innovation Act 2013 (**the STI Act, 2013**), to include innovative start-ups to receive financial support from the Fund created under the STI Act, 2013.

Further, the government needs to put in place measures for the granting of other fiscal incentives including tax incentives considered necessary for the development of start-ups in the country. Incentivization is crucial for start-ups since most of the time they lack capital and tax burdens make them dwindle in number instead of growing especially in the incubation stages.

Non-Fiscal Incentives

In addition to fiscal incentives, the government needs to enable access to markets, ease foreign investors' ability to get into the market, raise awareness about and encourage the use of start-up products, and encourage public procurement procedures that consider the application of start-up products and services.

Also, as noted above, start-ups are part of the migration to a knowledge-based economy that is embedded in science, technology, and innovation. As such, it is important to ensure continuous training and capacity-building to facilitate the acquisition and sustenance of skills that are innovative and novel. The government should thus support research and development activities undertaken by start-ups.

Conclusion

The uplifting of start-ups in the country enhances economic growth. Successful start-ups quickly transform the manner of doing business and the government should support innovative business culture by closing the funding gaps, building a flourishing business environment, and providing a link to institutions of growth. As observed by Dr. Jesper Vasell of KTH Royal Institute of Technology in Stockholm:

"Innovation is changing the business landscape across Africa and any entity that fails to adapt will eventually be phased out."

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GOING SEPARATE WAYS:

THE EFFICACY OF DISCHARGE AGREEMENTS WHEN TERMINATING EMPLOYMENT

Background

When an employment contract is terminated, it is common practice for employers to issue their employees with a clearance form that contains a clause which purports to discharge the employer *"from all further or future claims whatsoever"* upon payment of final terminal dues to the employee. Such clauses constitute what is referred to as a discharge agreement.

The discharge agreement is essentially a contract between an employer and an employee that crystalizes the rights of each party at the date of the termination of employment. Discharge agreements ordinarily contain an undertaking by the employer to make payment in full and final settlement of all salary and benefits payable to the disengaged employee in consideration of the employee discharging the employer from any further liability arising from the employment relationship.

The question that has innumerably arisen in ensuing litigation is whether discharge agreements are effectively binding on the parties, and whether the Courts are therefore obliged to uphold them. Put differently, whether the discharge agreements have the effect of barring further claims from being made by either of the parties.

The Employment and Labour Relations Court (**ELRC**) has laid down a general presumption that there is no equality of bargaining power in an employment relationship, with the employer holding the upper hand. Consequently, the ELRC has tended to water down the binding nature of discharge agreements. This general presumption flows from the fact that an employee, at the time of termination, would be desperate to receive payment of his terminal dues and would therefore sign the discharge forms with an element of economic duress at play, and without giving much thought to the implications of the discharge agreement.

Consequently, the ELRC's general position has been that discharge clauses contained in termination clearance forms do not discharge

the parties from further claims or statutory obligations. This article discusses and highlights the apparent paradigm shift from this erstwhile position held by the ELRC by considering emerging case law emanating from the Court of Appeal and a recent landmark decision by the ELRC that sets out the principles to consider when dealing with the legal effect of discharge agreements.

Paradigm Shift

In the case of *Thomas De La Rue (K) Ltd. v David Opondo Omutelema (2013) eKLR*, the Respondent (an employee) had signed a clearance form which was duly witnessed, in which he confirmed having received from the Appellant (the employer) *"in full and final settlement of all salary and benefits payable towards my redundancy package and all other claims arising from my employment with the company except for provident fund."* The Court of Appeal, whilst observing that the ELRC gave the discharge agreement short shrift, agreed with the ELRC that a discharge agreement cannot, in itself, absolve an employer from statutory obligations, and that it cannot preclude the ELRC from enquiring into the fairness of a termination.

However, the Court of Appeal emphasized that each case turns on its own peculiar facts and that the trial Court should make a determination whether the discharge agreement was freely and willingly executed when the employee was seized of all the relevant information and knowledge.

The Court of Appeal further found that the suggestion that the Courts should treat all cases involving discharge agreements in the same way was erroneous, and clarified that the ELRC should not adopt a general presumption and apply it rigidly in each and every case without considering whether the presumption has been rebutted or not i.e., whether evidence had been led to support or disprove the validity of a discharge agreement in the circumstances of the case.

It therefore follows that the answer to the question as to whether discharge agreements should be a bar to further claims turns on the facts of each case. In the case of *Coastal Bottlers Ltd. v Kimathi Mithika (2018) eKLR*, the Court of Appeal was once again called upon to consider the validity of a settlement agreement which read in part:

"I,...certify having received the sum of Kenya Shillings One Million Five Hundred Sixteen Thousand, Two Hundred and Eighty-One (Kshs. 1,516,281) being my full and final payment due to me from Coastal Bottlers Limited as follows...I confirm that, I have no further claim against the Company whatsoever."

The Court of Appeal held that the parties had agreed that payment of the amount stated in the settlement agreement would not only absolve the employer from any further claims under the contract of employment, but also in relation to the employee's termination. Consequently, the agreement was a binding contract between the parties as the employee neither denied signing the same nor was there any evidence of misrepresentation, duress or incapacity on the employee's part at the time of executing the settlement agreement.

In upholding the binding nature of the discharge agreement in the *Coastal Bottlers Ltd.* case, the Court of Appeal upheld the finding in *Trinity Prime Investment Ltd. v Lion of Kenya Insurance Company (2015) eKLR*, that the execution of a discharge voucher constituted a complete and binding contract. Accordingly, all the ELRC is required to do is to give effect to the intention of the parties as discerned from the discharge agreement, upholding the notion that the function of the Court is to enforce and give effect to the intention of the parties as expressed in their agreement as enunciated by Sir Charles Newbold P., in *Damondar Jihabhai & Co Ltd. & Anor v Eustace Sisal Estates Ltd. (1967) EA 153.*

The Employment and Labour Relations Court (ELRC) has laid down a general presumption that there is no equality of bargaining power in an employment relationship, with the employer holding the upper hand. Consequently, the ELRC has tended to water down the binding nature of discharge agreements.

Guidelines

What then should one look out for when entering into a discharge agreement upon termination of an employment relationship?

In the recently decided case of *Pauline Waigumo v Diamond Trust Bank Ltd. (2021) eKLR*, the ELRC, in declining to reopen the question of monetary compensation between parties who had signed a discharge agreement, laid out general guidelines in dealing with the effect of discharge agreements on further claims by concerned parties through future litigation, as follows:

- As a general principle, a pre-trial settlement operates as a contract between the parties
- It is to be considered as generally binding on the parties unless it is assailed on the usual grounds that will vitiate a contract
- Such settlements may, albeit not always, constitute a full settlement of the issues under consideration with the consequence that parties to them may not pursue further claims on the same subject either in Court or otherwise
- There is no general principle that such settlements will inevitably discharge an employer from his/her statutory obligations under the contract of service
- In order to determine whether the settlement operates as a bar to further claims by the parties to it, a trial Court or other arbiter must consider: the import of the settlement; whether the parties executed the agreement freely; and whether they had relevant information and knowledge regarding the settlement
- The mere existence of a pretrial settlement should not be construed as taking away the Court's jurisdiction to inquire into the lawfulness of a termination of a contract of service

Consequently, a Court faced with a question on the validity of a discharge agreement ought to address its mind firstly, to the import of such an agreement and secondly, to whether the same was freely and voluntarily executed by the parties.

Upshot

Discharge agreements are intended to determine with finality the rights of the parties at the time of termination of employment. The common grain flowing from the foregoing analysis is that discharge agreements are binding on parties if the they are entered into freely and willingly, and in the absence of any of the conditions that would warrant the setting aside of a contract such as coercion, fraud, mistake, misrepresentation, or incapacity.

It cannot be gainsaid that there is an apparent shift by the Courts in dealing with the effect of discharge agreements on further claims by the affected parties through litigation. Whereas it can be said that Courts have breathed life into discharge agreements, it must be noted that these agreements do not negate an employee's right to institute a claim for unfair or unlawful termination – with each case turning on its own facts, including the validity (or lack thereof) of the discharge agreement.

Ultimately, employers are still duty-bound to ensure strict compliance with the provisions of the Employment Act, 2007 during termination of employment.

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FAIR DISTRIBUTION:

DEALING WITH COMPANY SHARES UPON A SHAREHOLDER'S DEATH

The administration of the estate of a deceased person is an undeniably trying process. The estate is subject to several processes and procedures before it is eventually distributed to the heirs or beneficiaries, and there is no exception where the assets of the estate of the deceased include shares in a company.

During the lifetime of a shareholder, the rights, responsibilities, and other entitlements of the shareholder tend to be clear as they are provided for extensively under the Companies Act, 2015 (**the Companies Act**), the Articles of Association of the company and in some instances, a Shareholders' Agreement. However, once the shareholder dies, complexities may arise in respect of the ownership and distribution of the shares, the properties of the company and the available recourse for heirs or beneficiaries of the deceased's estate in the event of a dispute.

This article seeks to discuss the transmission of shares after the death of a shareholder; the powers of the personal representative of a deceased shareholder in respect of such shares; the process of succession, and the recourse available to the beneficiaries of the deceased's estate should there be a dispute.

Title to Shares after a Shareholder's Death

In situations where shares in a company are jointly held by two or more persons, then upon the death of one of those persons, the shares belong to the surviving joint shareholder. The jointly held shares do not form part of the free property of the deceased shareholder that would be available for distribution as their interest is effectively extinguished upon death.

Where the deceased person(s) held shares solely by themselves, then upon their death, the shares form part of the free property of the deceased's estate. Free property means property that the deceased was free to do with as they pleased during their lifetime and the deceased's interest is not extinguished upon death. In such a case, upon the death of the shareholder, the next step would be for the personal representatives of the deceased's estate i.e., either the executor or the administrator of the estate, to have the shares registered in the name of the estate of the deceased and subsequently transmitted to the ultimate beneficiary. After the grant of representation has been confirmed, the shares can then be transferred to the heirs or beneficiaries of the estate.

Powers of the Personal Representative

The Companies Act and the Articles of Association of a company are the main determinants of the powers of the personal representative of the estate of a deceased shareholder as far as shares are concerned. Section 82 of the Companies Act provides that the personal

representative of a deceased member of a company may assent on behalf of the deceased when it comes to the conversion of a company i.e., from a private limited company into an unlimited company, and public to a private limited company.

The personal representative may also transfer the shares or other interest of a deceased member of a company. Such transfer can happen even though the personal representative is not a member of a company and is effective as if the personal representative had been such a member at the time of the execution of the document. This transfer is of course to the heirs or beneficiaries of the estate of the deceased whether through administration of the estate or the execution of the will of the deceased.

The Articles of Association of a company may provide further extensive powers to a personal representative of the estate of a deceased shareholder should the members deem it necessary to do so. For companies registered under the now repealed Companies Act (Cap. 486) Laws of Kenya, the default articles applicable are the regulations under Schedule 1 thereof, which are known as Table A. Article 29 thereof provides that the company will only recognize the survivor of the deceased where the deceased was a joint shareholder, and the personal representative of the deceased where he or she was a sole shareholder.

The default articles applied to companies registered under the current Companies Act are The Model Articles for Private Companies Limited by Shares (**the Model Articles**). Article 65 of the Model Articles provide that upon the death of a member, the company will recognise the legal representative of the estate of the deceased shareholder as having a title to the share of the deceased shareholder.

However, it should be noted that the personal representative of the estate of the deceased cannot be registered in his or her own name as the owner of the shares of the deceased. The rationale is that the personal representative is strictly a representative of the estate and has no personal interest in the shares or the company. This was enunciated by the Court in *Robert Max Mulie (Executor of the Estate of Bernhard Martens) v Ismail M.H. Mawji t/a Manohar Lall & Rai (MLR) Associates (2016) eKLR*, where Justice Ochieng held as follows:

"When the courts have said that the executor's title dates from the date of the death of the deceased, that means that even if the will was opened weeks or months after the deceased passed on, as soon as it became clear who the will had designated as the executor, the said executor's authority qua executor, was deemed to have become effective from the moment when the deceased passed on. The word "title" in that respect does not refer to right of ownership of the property constituting the estate of the deceased."

Therefore, it bares emphasis that being a personal representative of the estate of a deceased shareholder does not make one the owner of the shares.

The Process of Succession and Dispute Resolution

When it comes to shares in a company, the Courts have held time and time again that the shares are to be transferred to the heirs or beneficiaries of the deceased shareholder at the end of the succession process, that is, after the grant of representation is confirmed, and the mode of distribution determined either by the Court, the heirs or beneficiaries of the estate of the deceased or as set out in the will of the deceased as is applicable. However, this can only happen where there is no dispute as to the ownership of the shares by the deceased nor the identity or entitlement of the heirs or beneficiaries of the deceased's estate.

Disputes can and do arise when it comes to succession processes in companies. One of the issues that oftentimes arises is where the ownership of the shares by the deceased is disputed. In the case of *Patrick Kibathi Kigwe & 2 others v Charles Kigwe Gathecha (2015) eKLR*, the Court held as follows on this issue:

Where the deceased person(s) held shares solely by themselves, then upon their death, the shares form part of the free property of the deceased's estate. Free property means property that the deceased was free to do with as they pleased during their lifetime and the deceased's interest is not extinguished upon death.

"The reality is, this Court can only adjudicate on transfer of shares to the extent the process involves the deceased's property and estate. However, the valuation of shares of a company, valuation and apportionment of the company's property is subject to the Companies Act, the Memorandum and Articles of Association of the company. This Court's jurisdiction begins and ends with the transfer of shares in accordance with the will of the deceased and preservation of the estate until distribution. Thereafter, the beneficiary is at liberty to pursue his rightful role and shares from the company.

In case of any dispute, then the matter should be adjudicated by the Commercial Division of the High Court and such an issue ought to be raised in the Commercial & Tax Division of the High Court, as the Family Division of the High Court lacks the jurisdiction to handle such disputes. Should the Commercial & Tax Division of the High Court decide that the deceased owned shares in a company prior to her death, then the shares would form part of the deceased's estate and can be distributed by the Family Division of the High Court."

As indicated above, the distribution of shares, once the issue of ownership has been settled, would be overseen by the Family Division of the High Court in a succession cause. If the deceased died intestate, that is, without having left a will, the Court may render a decision on distribution, or the beneficiaries of the estate may come to an agreement on this issue. Where the deceased died testate, the will would determine the mode of distribution of the shares. In some instances, Articles of Association of the Company may provide for who the heirs are to be or that the directors would have the first right of refusal when the heirs of the deceased inherit the shares.

The Family Division of the High Court has also clarified that any issues arising with respect to the property of a company in which the deceased was a shareholder are for the Commercial & Tax Division of the High Court to decide. In such cases, the Family Division only comes in once it is clear that the deceased has shares in the company for purposes of distribution, but not for purposes of determining a dispute among the shareholders of the company. Accordingly, any assets of the company subject to dispute will be dealt with in accordance with the Companies Act and respective company law provisions and will not be brought before the Family Court in the distribution process as company assets are separate from the assets of the estate of the deceased. The same principle applies to the liabilities of a company in which the deceased was a shareholder.

Administering the estate of a deceased which is comprised of shares can be viewed as an inherently complex process. However, the ambit of both succession and company law has provided an adequate framework which guides both companies and heirs or beneficiaries on how shares of a deceased person are to be dealt with in various circumstances. The role of a personal representative is particularly important in the distribution of the shares, as they have a legal responsibility to ensure that the estate of the deceased is not wasted and is distributed among the heirs or beneficiaries of the same as per the will or stipulated by the laws of succession in case of intestacy.

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ACCEPT ALL COOKIES?:

COMPLIANCE AND ENFORCEMENT MECHANISMS UNDER THE DATA PROTECTION ACT, 2019

Background

Bruce Schneir, an American privacy specialist and computer security professional, famously stated that *"data is the pollution problem of the information age and protecting privacy is the environmental challenge"*. In Kenya, the Data Protection Act, 2019 (**the Act**) provides an elaborate regime for dealing with the *"environmental challenge"* that is protection of data through inter alia the establishment of the Office of the Data Protection Commissioner (**ODPC**), which is primarily tasked with overseeing implementation of the Act and comprises of the Data Protection Commissioner (**DPC**) and other staff appointed by the DPC.

To this end, the ODPC has, in conjunction with the Cabinet Secretary for matters relating to information communications and technology, promulgated the Data Protection (Compliance and Enforcement) Regulations, 2021 (**the Regulations**), which will come into effect on 14th July 2022.

In this article, we set out an overview of the compliance and complaint handling mechanisms under the Act and the Regulations, and we also highlight the consequences of non-compliance.

Functions of the ODPC

The functions of the ODPC are contained in section 8 of the Act and include receiving and investigating any complaint by any person on the infringement of rights and obligations set out under the Act. Section 9 (1) of the Act gives the DPC wide powers to superintend compliance with the Act, including powers to conduct investigations; facilitate conciliation, mediation and negotiation on disputes; issue summons to witnesses for purposes of investigation; and to impose administrative fines for failure to comply with the Act.

Lodging Complaints

Pursuant to section 56 (1) of the Act, a data subject who is aggrieved by the decision of any person pertaining to the Act, can make a complaint to the DPC. Subsection 2 as augmented by Rule 4 (1) of the Regulations permits lodging of complaints either orally or in writing through electronic means, including by email, web posting, complaint management information systems, or by other appropriate means. The DPC is required to reduce a complaint made orally to writing.

Pursuant to Rule 4(3) of the Regulations, a complaint can be lodged in person, by a person acting on behalf of the complainant, or by any other person authorized by law to act on behalf of a data subject (such as an Advocate, an agent or anonymously). Once a complaint is received, the DPC is required to conduct a preliminary review upon which the ODPC may either admit the complaint, advise that the matter is not within its mandate, advise that the matter lies for determination by another body or institution and refer the complainant to that body or institution, or alternatively decline to admit the complaint altogether where the same does not raise any issue under the Act.

The various avenues through which a complaint may be lodged, coupled with the fact that there is no cost implication for lodging a complaint, conforms the process to the dictates of the right of access to justice as enshrined under Article 48 of the Constitution of Kenya, 2010. This is further buttressed by section 56 (5) of the Act which provides for an expeditious ninety (90) day period within which the DPC must investigate and make a determination on complaints made to it.

Admission and Investigation of Complaints

Rule 6 (4) of the Regulations provides that where a complaint is admitted, the DPC may either conduct an inquiry into the complaint; conduct investigations; facilitate mediation, conciliation, or negotiation; or use any other mechanism to resolve the complaint. In this regard, the ODPC has recently published a draft Alternative Dispute Resolution (**ADR**) Framework which is currently at the public participation stage, and which are ultimately aimed at codifying the ADR processes contemplated under the Act.

Rule 11 of the Regulations requires the DPC to, upon admission of a complaint, notify the respondent of the same within fourteen (14) days so as to give the respondent a chance to either respond to the allegations against them; resolve the complaint made in a manner that is satisfactory to the complainant; or make representations and submit evidence relevant to support their representations. Where a respondent fails to act on the complaint against them, the DPC will proceed to determine the complaint without any responses thereto. However, the DPC reserves the right to discontinue a complaint where the same does not merit further consideration or where a complainant refuses, fails or neglects to communicate further without justifiable cause. A complainant is also at liberty to withdraw the complaint before its determination.

Section 57 of the Act, taken in conjunction with Rule 13 (1) of the Regulations, gives the DPC discretion to conduct investigations, issue summons requiring attendance of any person at a specified time and place for examination, administer an oath or affirmation on any person during proceedings, require any person to produce any document or information and upon obtaining warrants from the Court, enter into any establishment or premises to conduct a search and may seize any material relevant to the investigation.

Upon the conclusion of the investigations, the DPC is then required to make a determination based on findings thereof. Under Rule 14 (2) of the Regulations, the said determination should be in writing and should state, among others, the remedy to which the complainant is entitled. The remedies contemplated include issuance of an enforcement notice to the respondent, issuance of a penalty notice imposing an administrative fine in case of non-compliance, dismissal of the complaint where it lacks merit, recommendation for prosecution, or an order for compensation to the complainant by the respondent.

Enforcement Notices

In case of failure to comply with the Act, section 58 empowers the DPC to serve an enforcement notice requiring the recipient to take certain defined steps within a period of time specified within the notice itself. The enforcement notice must clearly indicate what provision of the Act has been or is likely to be contravened; what steps the recipient can take to address the actual or potential contravention of the Act; the timeframe within which the recipient is to implement the remedial steps; and any right of appeal available to the recipient. An appeal against a decision arising out of the enforcement notice may be made to the High Court within thirty (30) days from service of the notice.

Section 9 (1) of the Act gives the DPC wide powers to superintend compliance with the Act, including powers to conduct investigations; facilitate conciliation, mediation and negotiation on disputes; issue summons to witnesses for purposes of investigation; and to impose administrative fines for failure to comply with the Act.

Failure to comply with an enforcement notice constitutes an offence and upon conviction one is liable to a fine not exceeding KES. 5,000,000, or to imprisonment for a term not exceeding two (2) years, or to both. Further, the obstruction of the DPC in relation to the exercise of her functions under the Act attracts criminal liability and sanctions.

Penalty Notices, Administrative Fines and Compensation

In case of failure or likelihood of failure to comply with an enforcement notice, the DPC may issue a penalty notice requiring the person in default to pay the ODPC an amount specified under the penalty notice. A penalty notice is to be issued for each breach identified in the enforcement notice and shall contain, among others, an administrative fine imposed as contemplated under section 63 of the Act.

Section 63 of the Act prescribes the administrative fine payable under a penalty notice as not more than KES. 5,000,000 or in the case of an enterprise, up to one percent (1%) of its annual turnover for the preceding financial year, whichever is lower. Rule 20 (4) of the Regulations provides that a penalty notice may impose a daily fine of not more than KES. 10,000 for each breach identified until the breach is rectified. It is important to note that the right of appeal to the High Court has been preserved, as against any administrative action taken by the DPC, including as against the issuance of penalty notices.

The seemingly steep administrative fine is intended to deter non-compliance with the provisions of the Act. Indeed, data protection enforcement authorities in other jurisdictions such as the Information Commissioner's Office (**ICO**) in the United Kingdom, have not shied away from imposing hefty fines against persons found to be in violation of data protection laws. For instance, the United Kingdom's ICO fined American Express Services Europe (a credit card company) a sum of nine thousand euros (€ 9,000) for sending marketing emails to various customers who had not given their consent for the same.

Should Kenya's DPC follow the precedents set by other jurisdictions' data protection enforcement authorities, then the importance of compliance with the Act will not need to be gainsaid. The DPC would however do well to temper the need for compliance and enforcement of the Act with proportionality and reasonableness, in line with the principle that the punishment should fit the crime.

In addition to administrative fines, section 65 of the Act provides that a data subject who suffers damage by reason of contravention of a requirement of the Act is entitled to compensation for that damage from the data controller or data processor, save where the data controller or data processor can establish that the damage occasioned on the data subject is not attributable to any fault on their part.

Conclusion

The Regulations offer comprehensive enforcement mechanisms coupled with penal sanctions for non-compliance. It is worth noting that the DPC is taking proactive steps to operationalize the Act and, in addition to the Regulations, has also embarked on a recruitment drive aimed at bolstering the human resource of the ODPC. It is yet to be seen how strict the DPC will be in dealing with complaints arising from breaches of the Act and imposing penalties where applicable. It is only a matter of time before occasion for the DPC's intervention arises, more so once the Regulations take full effect. It is therefore advisable for all data processors and data controllers to err on the side of caution by ensuring full compliance with the Act and the Regulations rather than being *"caught off-side"* by the imminent compliance and enforcement phase of the nascent data protection laws.

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SAVE ME TOO!:

RESCUE OPTIONS AVAILABLE FOR INDIVIDUALS UNDER THE INSOLVENCY ACT, 2015

In the previous edition of this publication under the article entitled *Save Me!*, we looked at rescue options under the Insolvency Act, 2015 (**the Act**) for companies under financial distress. In this article, aptly entitled *Save Me Too!*, we turn to look at rescue options available under the Act for individuals under financial strain.

Prior to 2015, the bankruptcy of a natural person was a matter regulated by the Bankruptcy Act (Cap. 53) Laws of Kenya (**the Bankruptcy Act**) which is now repealed. Having been enacted during colonial days, the Bankruptcy Act was one of the many statutes that Kenya inherited from the British, and as such, reflected the British legislative process alongside the way of living, far put out from the realities of post-independence Kenya. Moreover, the Bankruptcy Act was an archaic law, having been enacted in 1930 and was thus out of step with current times and arguably did little to resolve the insolvency situation of natural persons, with there being no rescue measures available to reduce the obligations of the insolvent person.

Then came 2015 and the coming into force of the Act, an instrument intended to resolve this lacuna. The Act provides elaborate provisions as to who may apply for bankruptcy, the various rescue measures available and the protections available to both debtors and creditors alike. This article thus lends itself to discuss the nuances and salient features of the Act, particularly as applicable to debtors.

Who may apply for Bankruptcy?

The Act at Part III provides the details of how bankruptcy of natural persons is to take place. Part III of the Act focuses on the procedure of bankruptcy, and it begins by setting out the various classes of people entitled to make an application for bankruptcy and the prerequisites to making the application. An application for bankruptcy can be a product of the creditors, the debtor, or a supervisor to a voluntary arrangement approved by the Court.

Creditor's Application

A creditor may only make an application if the amount owed by the debtor has reached the prescribed bankruptcy level, which currently stands at KES. 250,000. Before making this application, the creditor

must show that the debtor has consistently defaulted in making payments. Essentially, the yardstick is to show that the debtor is experiencing a cashflow/technical insolvency, that is, he or she is unable to pay their debts as and when the same fall due. One way of proving inability to pay is the debtor's failure to make good the statutory demand and twenty-one (21) days have lapsed since the notice was last issued. Equally, a person may prove inability to repay the debt where the debtor is unable to satisfy a Court decree.

In dealing with a creditor's application, the Court will not grant the Orders for bankruptcy unless it can be shown that the debt is due and owing and the debtor has not taken any steps to remedy the default, or that the debtor has no reasonable prospects of paying the amount when it becomes due. Further, the Court will dismiss an application if it can be shown that the debtor has made an offer to secure or compound a debt, that the acceptance of the offer would have warranted the dismissal of the application or that the offer has been unreasonably rejected.

Alternatives to Bankruptcy

The Act has signalled a transformative shift from the previously draconian procedure of bankruptcy to a more versatile system of protection, otherwise referred to as rescue measures. The Act provides alternatives to bankruptcy that a debtor may opt to invoke to protect his interests. These options are discussed in detail below.

Voluntary Arrangement

The voluntary arrangement takes the form of a scheme where the debtor makes a proposal to the creditors to settle the debt within a set period under specific terms. The debtor may prepare the proposal based on the performance of his business, or any such contingent funds that he may be hopeful of. Thus, if the debtor makes a quarterly income, he may propose to pay the creditors a percentage of the income at every interval when the income is realised. In the proposal, the debtor must identify a supervisor, who should be a qualified insolvency practitioner.

During the pendency of the voluntary arrangement, the Court may stay execution, actions, or any legal proceedings against the debtor or bring to a halt any recovery proceedings, prohibit distress from being levied on the debtor's property or stop any proposed sale of the debtor's properties.

To commence a voluntary arrangement, the debtor must make an application in Court for an interim Order. To obtain an interim Order, the debtor must meet the requirements under section 306 (1) of the Act which are:

- The debtor intends to make a proposal under the relevant provisions of the Act
- On the day of the making of the application the debtor was an undischarged bankrupt or was able to make an application for the debtor's own bankruptcy
- No previous application has been made by the debtor for an interim Order during the twelve (12) months immediately preceding that day
- The supervisor designated under the debtor's proposal is willing to act in relation to the proposal

After the making of an interim Order, the supervisor is required to make a statement on the viability of the proposal, whether a meeting should be convened between the debtor and the creditors and the date and time when such a meeting should be convened. Once the meeting is convened, the creditors have three (3) options available to them - one is to adopt the proposal as it is; the other is to adopt the proposal but make modifications to it at which point the debtor has the choice to either accept or reject the modifications; and lastly lies the option to reject the proposal altogether. If the proposal has been approved, an application will then be made to Court for approval upon which the proposal takes effect officially.

The interim Order offers significant protection to the debtor as was highlighted in the case of *Rajendra Ratilal Sanghani v Schoon Ahmed Noorani (2018) eKLR* where the Court stated:

The Act has signalled a transformative shift from the previously draconian procedure of bankruptcy to a more versatile system of protection, otherwise referred to as rescue measures. The Act provides alternatives for bankruptcy that a debtor may opt to invoke to protect his interests.

"As pointed out earlier, proceedings of this nature afford the debtor a certain amount of freedom. Just by example, upon grant of an interim Order any proceedings (including execution or other legal process) may only be begun or continued against the debtor or the debtor's property with the sanction of the Court. An undeserved application should be disallowed at once if its clear motive is to attain a collateral objective of granting protection to an undeserving debtor. So, for instance, a debtor who is neither an undischarged bankrupt or is able to make an application for his own bankruptcy should not be allowed to use the process to avoid his/her obligations or as a stalling device."

Instalment Order

This is an Order made by the Official Receiver requiring the debtor to pay the amounts owing in instalments, in full, or in a manner that the Official Receiver considers satisfactory. This application may be made by the debtor or by a creditor with the debtor's consent. The application must be accompanied with a proposed appointment of a supervisor who should be a qualified insolvency practitioner.

The instalments are to be paid within a period not exceeding three (3) years, or if satisfied and with the consent of the supervisor, for an extended period not exceeding five (5) years. During the subsistence of the instalment Order, no action or proceedings may be instituted against the debtor's assets subject to the instalment Order without the approval of the Official Receiver, and the debtor defaults in the instalments.

No-Asset Procedure

A debtor may make an application to the Official Receiver for admission to a no-asset procedure by showing that he or she has no realisable assets, and that their debts are not less than KES. 100,000 and not more than KES. 4,000,000. In addition, the debtor must show that he or she has not previously been admitted to this scheme and that they have not been previously adjudged bankrupt.

As soon as practicable after receiving an application from a debtor for entry to the no-asset procedure, the Official Receiver is required to send a summary of the debtor's assets and liabilities to each known creditor of the debtor. Once a debtor has made this application, there are restrictions as to the amount of credit he or she may subsequently borrow and applications for such credit facilities must be accompanied by notifications of the debtor's status.

Upon admission to the no-asset procedure, the Official Receiver is required to notify all the creditors and to make a publication in the manner prescribed by the insolvency regulations. No creditor should take steps to recover from a debtor who has been admitted to the no-asset procedure. A debtor is discharged from the no-asset procedure after the lapse of twelve (12) months. After the expiry of the said period, all debts that were owing before the debtor was admitted to the no-asset procedure become extinguished.

Conclusion

The Act has been termed as debtor-friendly in that it aims to protect debtors before adverse steps are taken against them. In this regard, it bears to note that where a debtor can demonstrate that he has taken steps to pay the debt, or make proposals towards payment of the debt, the creditors would have an uphill task in Court in trying to prove that the person should be adjudged bankrupt.

Conversely, if it can be shown that the debtor has not taken any steps to remedy the default, and the creditors have carefully taken steps to act within the statutory parameters, then disproving the creditor's entitlement to the Orders sought becomes difficult. The Act therefore works in favour of whichever party is able to properly invoke its provisions.

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HEIGHTENED SCRUTINY:

NEW STEPS TO INCREASE TAX TRANSPARENCY FOR MULTINATIONAL ENTERPRISES IN KENYA

Base erosion and profit shifting (**BEPS**) refers to efforts by multinational entities to avoid or minimize paying income tax in jurisdictions with relatively high income tax rates by reducing their taxable income in those jurisdictions and shifting their profits to jurisdictions with lower income tax rates. According to the Organization for Economic Cooperation and Development (**OECD**), BEPS denies tax authorities globally of approximately Two Hundred and Forty Billion United States Dollars (USD 240 Billion) annually. In an effort to curb these revenue losses, the OECD has formulated various action plans to guide member states on the actions to take in order to reduce tax avoidance.

Kenya, being a member State of the OECD/Group of Twenty (**G20**) Inclusive Framework on BEPS, has progressively amended its tax laws to curb various forms of tax avoidance including BEPS. This article focuses on a proposed amendment to Kenya's tax laws to further implement BEPS Action 13.

Country-by-Country (**CbC**) Reporting is a product of Action 13 of the OECD/G20 BEPS Action Plan. In October 2015, the OECD/G20 published the Transfer Pricing Documentation and CbC Reporting Action 13 Final Report (**the BEPS Action 13 Final Report**). The BEPS Action 13 Final Report recognised that enhancing transparency for tax administrations by providing them with adequate information to conduct transfer pricing risk assessments, is an essential part of tackling the BEPS problem.

CbC Reporting requires large multinational enterprises (**MNEs**) to file a CbC Report that provides a breakdown of the amount of revenue, profits, taxes and other indicators of economic activities for each tax jurisdiction in which the MNE group conducts business. Based on the OECD, CbC Reporting only applies to MNE groups with an annual consolidated group revenue of Seven Hundred and Fifty Million Euros (€750 Million) or more in the preceding fiscal year. Tax authorities can use the CbC information to perform high-level transfer pricing risk assessments and to evaluate other BEPS related risks.

What this means for Multinationals in Kenya

The Finance Act, 2021 introduced CbC Reporting on Kenyan-headquartered MNEs, with effect from 1st January 2022. In a bid to provide clarity on the CbC Reporting requirements, the Cabinet Secretary for National Treasury and Planning (**the Cabinet Secretary**) issued the draft Income Tax (Country-By-Country Reporting Standard for Multinational Enterprises) Regulations, 2021 (**the draft Regulations**) and invited the public to submit their views on the same.

As per the draft Regulations, Kenyan-headquartered MNEs whose consolidated revenue is at least Twenty Million Euros (€20 Million) are now required to file an annual CbC Report with the Kenya Revenue Authority (**KRA**) no later than twelve (12) months after the last day of the MNEs' fiscal year. The CbC Report should contain information relating to capital, revenues, tax paid and accrued, assets and number of employees for each jurisdiction in which the MNE operates. Qualifying MNEs which do not adhere to the foregoing, shall be subject to the penalties prescribed under the Tax Procedures Act, 2015.

The Finance Bill, 2022

Notably, the Finance Bill, 2022 proposes to overhaul the above framework for CbC Reporting. The Finance Bill 2022 proposes to introduce CbC Report filing requirements for an ultimate parent entity (**UPE**) and a constituent entity of an MNE with gross annual turnover of above Kenya Shillings Ninety-Five Billion (KES 95 Billion). A UPE is required to file a CbC Report not later than twelve (12) months after the last day of the reporting fiscal year of the MNE group.

The CbC Reports should contain information relating to each entity's tax residence, the group aggregate information relating to the amount of revenue, profit or loss before income tax, income tax paid/accrued, capital, number of employees, and tangible assets (other than cash and cash equivalent), for each jurisdiction where the group has a taxable presence.

The Finance Bill, 2022 further proposes to introduce master file and local file filing requirements for UPEs and constituent entities of MNEs with gross turnover of above Kenya Shillings Ninety-Five Billion (KES 95 Billion). The master file and local files should be filed not later than six (6) months after the last day of the reporting financial year of the MNE. The master file should contain information about the MNE group, including but not limited to information about its financial activities, assets, and each entity's contribution - while the local file shall include information about the MNE´s entities that are resident in Kenya. This measure is in line with the BEPS Action 13 Final Report, that requires MNEs to file a three-tiered transfer pricing documentation i.e., master file, local file and CbC Reports, with tax authorities in countries where they have taxable presence.

KRA is poised to derive several benefits from the new tax requirements. To begin with, KRA will be able to use the CbC Reports to make high-level assessments of an MNE's transfer pricing and BEPS risk, including assessing potential non-conformity to transfer pricing rules by members of the MNE group. KRA will also be in a position to use the information from the CbC Reports for economic and statistical analysis. Further, as Kenya is a signatory to the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, it is also expected that KRA will use the information in the CbC Reports to exchange relevant information with other countries and gain visibility of additional tax risks beyond our borders.

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According to the BEPS Action 13 Final Report and the draft Regulations, KRA cannot use the information contained the CbC Reports to make transfer pricing adjustments, however, it may use the CbC Reports as a basis to make further enquiries into an MNE's affairs. Accordingly, the information in the CbC Report cannot be used, by itself, to reassess a taxpayer's income, or as conclusive proof of the appropriateness of the transfer prices within an MNE. KRA is also mandated to preserve the confidentiality of the information contained in the CbC Reports, which is crucial as some of the information shared is sensitive and can have market implications should it be accessed by unauthorised parties.

For MNEs, the proposed introduction of a turnover threshold of Kenya Shillings Ninety-Five Billion (KES 95 Billion), which is in line with the Seven Hundred and Fifty Million Euros (€750 Million) set out by the OECD, is a welcome move since MNEs that do not meet the global threshold will not be required to file the three-tiered transfer pricing documentation in Kenya. The main implications of the CbC Reporting requirements for MNEs that meet the set threshold are the increased transfer pricing compliance and transparency on their business affairs.

As the information disclosed in the CbC Reports will provide KRA with an avenue to make extended enquiries into the MNEs' operations, the affected MNEs will thus encounter increased compliance costs arising from additional reporting and filing obligations. To ease this burden, MNEs that meet the reporting threshold must prepare for the annual filing of CbC Reports by assessing how to collate the required information from different sources in a timely manner.

The MNEs should consider, for instance, digitizing their data and introducing tools to easily collate the required information, particularly since the CbC Reports are to be filed electronically. Moreover, given that the principal purpose of CbC Reports is for KRA to enhance its transfer pricing risk assessment capacity, MNEs should consider reviewing the CbC Reports before filing the same so as to ensure their alignment with the group's transfer pricing policies. Any inconsistencies between the two is likely be flagged as indicators of tax risks.

Upfront Review

Beyond compliance, affected MNEs need to take a closer look at how the information to be provided can be interpreted. This requires an upfront review of the CbC Reports to determine how the CbC Reporting data such as global allocation of profits could be perceived by tax authorities. MNEs should thus put together a strategy and systems before the first CbC Report filing period to enable them to discharge their obligations in a timely, accurate and efficient manner, thereby avoiding the attendant penalties.

Conclusion

Kenya is progressively implementing the minimum standards set out in BEPS Action 13 that seeks to address tax revenue leakages caused by transfer pricing. MNEs should therefore consider assessing their compliance with the proposed amendments and international best practices relating to BEPS in line with Kenya's implementation of the same. A proactive approach by MNEs to transfer pricing compliance would enable them to effectively implement necessary changes and reduce their tax exposures.

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