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Case Action:	Order
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Advocates:	-
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REPUBLIC OF KENYA

COURT OF APPEAL, AT KISUMU

CIVIL APPLICATION NO NAI 116 OF 1985

Madhupaper International Limited

versus

Kerr

(application from the High Court at Nairobi, O'Connor J, Civil Suit 3438 of 1985) December 16, 1985, Kneller, Nyarangi JJA & Gachuhi Ag JA delivered the following

Order of the Court.

Madhupaper International Limited, the company, manufacturers cartons, tissues and lavatory paper in the industrial area of Nairobi. Kerr and Cahill, the receivers and managers of the company are partners in the Nairobi firm of accountants, Peat Warwick, Mitchell and Company, and were appointed by the Kenya Commercial Bank Limited, the Bank, and its subsidiary, the Kenya Commercial Finance Company Limited, KCFC, a finance institution within the Banking Act (cap 488).

The company, according to its plaint and affidavits, imports a large amount of the raw materials for its business and to do this it has to use large amounts of foreign exchange. The National Bank of Kenya, the National, was its banker until 1981. The company's executive chairman, Mr Macharia, decided about 1980 it would save foreign exchange, create jobs for 800 Kenyans and expand production (and profits) if it used the wood and water of Kenya to make the pulp it devoured and regurgitated paper in all its forms. The Bank and KCFC were interested and ready to help from 1981 provided the company replaced the National with the Bank and KCFC as its 'bankers' which it did.

The Bank and KCFC took part between 1981 and October 1983 with the company when there were meetings with government departments to appraise and approve the company's plans to finance the pulp plant at Thika and to persuade banks in Europe and the International Finance Corporation, IFC, to lend the company the funds the new plant needed. They produced something they called a 'feasibility plan' for it.

In return, the Bank asked the company to replace the Kshs 15 million form the Industrial Development Bank, IDB, with a loan of Kshs 12 million from KCFC. The repayment of the loan from KCFC was secured by debentures for Kshs 9 million and Kshs 3 million dated July 3, 1981 and December 7, 1981 respectively. The Bank allowed the company to have an overdraft of Kshs 9 million which was later raised to Kshs 30 million and the repayment of these was secured by two debentures of December 7, 1981 and October 17, 1983 for those sums.

In October 1983 the Bank and KCFC asked the company to repay its overdraft as soon as possible. The company promised to do so with a loan IFC had promised it and IFC agreed in December 1984 that is how the loan should be used. The company and IFC agreement was settled on July 30, 1985 and the Bank and KCFC knew of this and against asked the company to repay the amounts secured by the debentures. They made the demand on October 11, 1985 and gave the company a month to repay Kshs 50,308,881.55.

The month did not elapse, however because on October 25, 1985 unsettled by an article in the Weekly Review suggesting the company was in financial trouble the Bank and KCFC gave Mr Macharia half an hour to repay the sum or suggest some reassuring way of doing so which he did not do and so they appointed the receivers and managers who took possession of the company's industrial area premises and undertaking.

The company gave notice of its intention to sue the receivers, the Bank and KCFC, and did so by a plaint filed three days later which was the beginning of Nairobi High Court Civil Suit 3435 of 1985.

The company's prayers in the plaint are for:-

(1) a declaration that the Bank and KCFC were not entitled to demand payment of the money secured by the debentures before IFC released the loan to the company;

(2) a declaration that the appointment of the receivers is null and void and that each is a trespasser on the company's premises;

(3) an injunction to restrain the receivers from breaching the implied conditions of the debentures;

(4) a perpetual injunction to restrain the defendants from interfering with the company's management of its business;

(5) general damages; and

(6) costs.

The company's bases for these prayers in the plaint are that:-

a) the Bank promised to help the company with its Thika plan until it was executed;

b) by virtue of the debentures the Bank and KCFC are mortgagees and under a duty to make a valid demand of payment of the moneys secured by the debentures;

c) the Bank could not make such a valid demand until the Thika factory was in full production. alternatively: d) the Bank and KCFC were estopped in law from insisting on their rights under the debentures;

e) they had waived those rights; f) they were in breach of their contracts and acting mala fides in making their demands;

g) their demands were null and void for uncertainty so their appointment of the receivers was unlawful; and

h) the receiver were trespassers.

No appearance or written statement of defence has been filed by the receivers, Bank or KCFC. They have been tied up with the company's next steps in this matter. It filed with its plaint a summons in chambers under Order XXXIX rules 1-3 of the Civil Procedure Rules supported by an affidavit of Mr Macharia asking the High Court for an interlocutory injunction restraining the Bank and KCFC their servants and agents from:

i) interfering with its business;

ii) taking possession of its undertaking; and

iii) putting it under receivership until the suit was determined

The receivers, Bank and KCFC replied with affidavits of October 30, and November 5, 1985 of Mr Muthundo, the Manager of the Bank's City Centre Branch, and Mr Muraya, the Chief Manager of its Marketing and Credit Division. These called for another from Mr Macharia and from Mr Mathundo. Together with their exhibits, all these affidavits came to two hundred and eighty two foolscap pages.

The summons came before Mr Justice O'Connor who dismissed it with costs on the higher scale on November 15, 1985.

He observed that the plaint's prayers included one that the receivers should be removed and the company's directors be at liberty to operate the company until the IFC loan was released to it which is when the Bank and KCFC will be repaid in full what the company owes them. He was, however, concerned with whether or not the company should have the interlocutory injunction and he did not have to decide the issues in the suit. He reminded himself of the tests propounded by Spry, JA (as he then was) in Giella v Casssman Brown & Co Ltd, [1973] EA 358, 360E. Following upon them, he required the company to persuade him to exercise his discretion and to do so by proving its case on the balance of probabilities.

He would not dismiss the application, he continued, only on the grounds that a prima facie case with a probability of success had not been established. (We assume that by that the learned judge meant he found a prima facie case with a probability of success had not been established). He found that the company could be adequately compensated in damages by the Bank and KCFC if the company succeeded in proving its claims in the trial of the action. The damages were quantifiable and the Bank and KCFC had the assets to cover them. He refused to take into account the government's policy which was bent on encouraging Kenyan businesses because it was extraneous to the issues in the summons. Had he done so, he thought that the appointment of the receivers did not mean the Thika plan was doomed. The receivers were bound by clause 13 in each debenture as an agent of the company to act in its best interests. The company's directors could still find other sources from which to pay off the Bank and KCFC and have the receivers removed. The receivers were in, the company's assets were large and it employed many people. The balance of convenience, in his view, tilted in favour of letting the receivers remain. He advised the advocates for the parties to get on with the pleadings and then appear before him for early hearing dates for the trial.

The company's next move was to ask for an interim injunction pending the determination of its appeal from his ruling but the learned judge declared he saw:

"no grounds for granting an injunction that would manifestly result in an order directly contrary to the ruling I have just delivered. The application should be made to the appeal court."

The reasoning of the learned judge was, with respect, incorrect. He was referred to Erinford Properties Ltd v Cheshire County Council, [1974] 2 All ER 443 in which Mr Justice Megarry held that where a judge dismissed an application for interlocutory injunction he has jurisdiction to grant the unsuccessful applicant an injunction pending an appeal against the dismissal. It is unnecessary for him to apply to the Court of Appeal for it. There is no inconsistency in doing so. The purpose of granting one having just refused to do it is to prevent the decision of the Court of Appeal being nugatory should it reverse the

judge below, which sometimes happens.

In Erinford's case the unsuccessful applicant moved ex parte for the injunction pending the appeal which Megarry, J granted for six days and then heard it inter partes . It was submitted that he had no jurisdiction to let it go forth because he was functus officio quoad the injunction. He could not sit on appeal from his own refusal to grant one. Nothing new had occurred so how could it be right to allow what had a minute before been disallowed"

The applicant's reply was that the trial judge had jurisdiction to preserve the subject matter of the dispute until the appeal was concluded. He knew all along the relevant facts and law. It was speedier and more convenient to deal with it at the end of the main motion (or, in Kenya, summons). A judge can under the Rules of court grant a stay of execution pending an appeal.

Megarry, J granted the intended injunction pending appeal which the applicant sought on the principle that:

"when a party is appealing, exercising his undoubted right of appeal, the court ought to see that the appeal if successful is not nugatory."

Which was what Cotton, LJ enunciated in the leading judgment in Wilson v Church (No 2) [1879], 12 Ch D 454 and 458 dealing with an appeal from the Court of Appeal to the House of Lords and Pennycuick, J applied in Orion Property Trust Ltd v Ducane Court Ltd, [1962] 3 All ER 466 even though the action in the High Court had wholly failed and the appeal was to the Court of Appeal from it.

It is preferable for the High Court to deal with such an application, in any event, not so much as to protect this court from a sudden inconvenient dislocation of its lists but more because this court would have the distinct advantage of seeing what the judge made of it. The learned judges of the High Court should take note of this concurrent jurisdiction which the two courts have and exercise theirs.

There are cases, however, where it would be wrong to grant an injunction pending appeal. These would include where the appeal is frivolous or to grant it would inflict greater hardship than it would avoid. And there will be others which was have not experienced yet.

Three days after Mr Justice O'Connor's ruling the company filed an appeal from them in the High Court and an ex parte motion on notice under rule 5(2) of the Court of Appeal Rules with a certificate of urgency.

The motion was for the orders until the appeal is dealt with which the High Court refused and the certificate claimed the company would lose a Kshs 400 million factory and plant in Nairobi and its cherished Thika scheme which is likely to cost Kshs 950 million. The receivers could and might sell the factory at once. They could not and would not continue the delicate negotiations with the government for the loans from foreign financers. The company's Nairobi business was unique and the Thika one would be. So, if they were erased no amount of damages would be adequate compensation.

The ex parte motion set out twelve grounds for holding that Mr Justice O'Connor erred when he refused the main application. It was supported by an affidavit of Mr Macharia. The material before the judge and his ruling were added. We were denied his notes of the submissions of Mr Kuria for the company and Mr Le Pelley for the receivers, Bank and KCFC, probably because of lack of time to prepare them.

We heard the motion ex parte on November 19, 1985 because among other things the certificate of

urgency and Mr Macharia's affidavit led us to believe not a moment should be lost if the company were not to lose its Nairobi factory and business. We granted it the same day without giving reasons which is a wise and usual course to adopt if the matter is to be ventilated inter partes as it was on November 22, 25, 27, 28 and 29. Each side filed more affidavits before November 22 and KCFC briefed Mr Oraro to appear for it. There was a Saturday and Sunday separating November 22 and 25 which we hoped might help the parties to negotiate a settlement on terms that secured the Bank's and KCFC's loan repayments. After November 29, this court went on circuit to Kisumu so the ex parte injunction modified by consent on November 22 was extended until today again in the belief that the company would find the Kshs 51 million the Bank and KCFC demanded or have made such satisfactory arrangements for its payment that it would be necessary for the receivers to re-enter and because it requires some time for the reasons for an order to be composed since we do not have any court shorthand writers.

It took a little time to persuade the advocates that under rule 5(2)(b) the court has its own jurisdiction to grant an injunction pending an appeal since February 8, 1984 when it was provided for by clause 3 of the Court of Appeal (Amendment) Rules 1984 (L N 18 of 1984). The conditions in the amendment rule for the exercise of it are that a notice of appeal has been lodged in accordance with rule 74 and that if it is granted it will be so on such terms as the court may think just. It is a matter for this court's discretion according to the rule. It is exercised judicially and not in whimsical or arbitrary fashion.

Seeing, therefore, we were not sitting on appeal from Mr Justice O'Connor, and for less were we dealing with the intended appeal, and cannot deal with the trial, much of what was put before us in documents, authorities and submissions can be left on one side without injustice though it might appear ungracious to the herculean labours of the parties' advocates.

The test we have to apply to this particular application to this court is whether or not the company has made out its claim for an injunction to preserve its property until the appeal is heard" Or is it an application which ought to fail because the appeal is frivolous or it would be worse for the company if the injunction went forth or for any other reason" We do not forget that if this court's discretion is not exercised in favour of the company the receivers re-enter and the powers of the directors are stifled which may or may not affect any litigation thereafter in which the company is involved though curiously enough none of the advocates mentioned this one way or the other.

The company's property from its own standpoint is the business, plant, premises and goodwill at Nairobi and the plans and agreement for the extension in Thika. There is no support for the suggestion that the Nairobi lot will be disposed of by the receivers who will wish to recover their remuneration and expenses and the Kshs 51 million for the Bank and KCFC and leave. Any proposed sale will have to be after three months notice to the company.

The Thika extension is another matter. This depends on loans from the IFC and foreign bankers and the purchase of machinery from foreign firms and although it seems true that none of these loans would be made to the company if the receivers were in control of it there were agreements for these loans to be made soon for the extension and the repayment of the Kshs 51 million to the Bank and KCFC seek.

The Thika project also depends, we were told, on the help of the Treasury and various departments that deal with land, forests, water, employment of labour, customs duties and taxes. In fact without that help it does not survive. There was no affidavit from anyone with authority to make it stating all that help is forthcoming.

The next matter of fact we have to consider carefully is the financial health of the parties today. There has been no suggestion that that of the Bank and KCFC is anything but robust. We need not be detained

long by the suggestion that if the company succeeded to proving its claim to the injunction(s) it sought and did not get then the damages would be more than the Bank and KCFC could meet because we do not accept they would be astronomical as the company's optimism leads it to believe. But look at the company's state of affairs. There is a judgment of September 5, 1985 in Nairobi High Court Civil Suit 2170 of 1984 for over Kshs 1,700,000 in favour of Bunzl Pulp & Paper (Sales) Ltd against it which does not seem to have been met yet. We were told that the re-entry of the receivers would attract the culturine descent of its other creditors. There has been no compromise or repayment within the last month and a half of the Kshs 51 million or any of it demanded by the Bank and KCFC. One receiver estimates its liabilities, secured and unsecured, at about Kshs 163 million on October 25, 1985 and its fixed assets in the company's unaudited balance sheet for December 1984 are valued at Kshs 216 million but whether or not they would realize this in a sale is another matter. The same receiver's approximate balance sheet for the company for October 25, 1985 puts the net assets of all sorts at only Kshs 56 million.

The company, when it is not worrying about those who will file suits against it for what it owes them, asserts that it is buoyant and has fixed assets in Nairobi of Kshs 400 million and the Thika enterprise is worth Kshs 900 million and so forth. The receiver notes that the 1983 professional valuation of the Nairobi fixed assets on the basis of gross replacement cost put them at Kshs 340 million and with adjustment to valuation and depreciation gives them a book value of Kshs 216 million at the end of 1984. He puts the Thika assets at nil in the approximate balance sheet because they are intangible. The company recorded it as valued at Kshs 10 million in the books of account on December 31, 1984. And Mr Munene, the finance manager of the company, declares the receiver's figures are inaccurate and those of its auditors in its draft financial statement for mid- 1984 are correct. The company's assets were really worth Kshs 316 million in February 1984 and Kshs 293 million in October 1985.

All this, without holding where the truth lies, fails to persuade us that the company's undertaking in damages is acceptable now.

There are vehement denials by the Bank and KCFC officers that they asked the company to change its bankers. Nor did it commit itself to the Thika extension though it was at meetings between the company and other organizations in order to assess its future. It would, in our view, have been unwise of the Bank and KCFC to commit itself to such venture when so many loose ends remained untied. www.kenyalawreports.or.ke The Bank and KCFC had these debentures and appear to have waited for repayment of the loans and interests they secured by long periods and despite breaches of its obligations the company was given several deadlines to meet them which they were not bound to do. The half hour or so the company had in which to meet them on October 28 was probably in the circumstances unreasonable for the company had been led to believe it had until November 8 but that demand if invalid has been cured by the period that has since passed with no payment having been tendered up to this date.

A debenture of December 1, 1981 was an exhibit in the record. It was issued by the company under clause 3(t) of its Memorandum of Association and Article 22 of the company's Articles of Association and in pursuance of a resolution of its directors on some unrecorded date in 1981. It is for a maximum of Kshs 9 million. It was made between the company and the Bank and is a first fixed charge upon that amount of the assets of the company. Now the company knew of the terms of these debentures and accepted them on the advice of the its advocates.

Its terms are draconian. The Bank will advance to the company by loan by permitting it to overdraw its current or other accounts with the Bank or by giving it other financial accommodation from time to time in return for the company undertaking to repay all it owes the Bank on demand in writing. They include interest, commission, fees, charges and costs. During its continuance the Bank is the company's sole

banker and all sums the company receives in the course of its business must be paid by it into its account in the Bank whose costs for being the company's banker is a first charged on the company's assets and property. The principal moneys and interest secured became immediately payable and fall due to be discharged without demand under its clause 11 if, among other things, the company commits a breach of the covenants in the debenture. Receivers or managers may be appointed by the Bank once the principal moneys secured by the debenture becomes payable either by the lawful demand of the Bank or under the provision of clause 11. The Bank may from time to time remove them and appoint others in their stead (which some Banks are advised entitled them to do this if a court restrains the first ones from carrying out their duties) once the Bank has made its demand for payment of the moneys secured by the debenture or for any other reason becoming immediately payable the Bank is under no obligation to make any further advances or grant any further facility to the company. There are other clauses but those are enough to support what follows.

The Bank and KCFC maintain that under these debentures they are contractually entitled to appoint a receiver to protect their own interests including the right to take possession of the plant. It is correct law that a debenture holder which has this right is under no duty to refrain from exercising its rights because doing so might cause loss to the company or its unsecured creditors. See Cuckmere Brick Co Ltd v Mutual Finances Ltd [1971] Ch 949, 965; in Re Potters Oils Ltd 1985 Ch D Hoffman J, The Times November 26, 1985 so there could be no duty to refrain because the company is bent on building up another business which the debenture holder is sure is doomed to failure from the outset. The Bank asserts the principal moneys and interest secured became immediately payable and fall due to be discharged without demand under clause 11 when it discovered the company was in breach of its covenant in clause 6 in the debenture because it was no longer banking solely with the Bank. The fact that it was dishonouring the company's own cheque for its creditors did not affect this right. It had made its written demands under clause 11 from time to time and none had been met.

These receivers and managers were appointed not by the court or under the provisions of a statute under the debenture which are agreements between the parties interested in the property over which their appointment was made. They are not officers of the court. So for the purposes of this application for a temporary injunction the Company has failed to persuade us that on the balance of probabilities we should exercise our discretion in its favour and extend the ex parte one we granted, even its modified form, any further.

It has not shown that its undertaking in damages is acceptable in view of its creditors and its own financial straits. It was probably in breach of two covenants in the debenture. An unsatisfied judgment against it exposes it to execution or winding up proceedings which falls foul of another one (clause 11 (a). It did not have the money ready to be paid. See Cripps & Sons v Wickenden, [1973] 1 WLR 944. The Thika extension is not more than a distant prospect at the moment and may for various reasons be a mirage.

This is one of the cases, in our judgment, where it would be wrong to grant an injunction pending the appeal. It would probably inflict greater hardship than it would avoid.

The application is refused and the ex parte injunction lifted. We will now hear the advocates on the appropriate order for costs.

Delivered on **December 16, 1985**

Kneller, Nyarangi JJA & Gachuhi Ag JA

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