



IN THE HIGH COURT OF KENYA AT NAIROBI

MILIMANI LAW COURTS

COMMERCIAL AND TAX DIVISION

CORAM: D. S. MAJANJA J.

COMM CASE NO. E071 OF 2021

CONSOLIDATED WITH

MISC CIVIL APPLICATION NO. E1308 OF 2020

BETWEEN

TREVOR SAWAYA NDWIGA1ST PLAINTIFF

IAN NYAGAH NDWIGA2ND PLAINTIFF

JUDITA WARUE NDWIGA 3RD PLAINTIFF

BRYAN KEVIN MUREITHI4TH PLAINTIFF

VICTORIA WANENE NDWIGAH 5TH PLAINTIFF

LISA MUMBI NDWIGA 6TH PLAINTIFF

AND

MERIDIAN ACCEPTANCES LIMITED 1ST DEFENDANT

REGISTRAR OF COMPANIES2ND DEFENDANT

AND

EDUARDO HERNANDEZ CIRIZA1ST INTERESTED PARTY

JOAN HERNANDEZ CIRIZA2ND INTERESTED PARTY

PALOMA MOSOQUERA CIRIZA3RD INTERESTED PARTY

JAMES NDWIGAH MUCHUNGU4TH INTERESTED PARTY

JUDGMENT

Introduction and Background

1. This matter concerns the affairs of the 1st Defendant, a limited liability company undertaking the business of rendering financial services within Nairobi County (“the Company”). It was incorporated in 2007 with the following shareholders:

	NAME	NATIONALITY	SHARES
1	JAMES NDWIGAH MUCHUNGUH	KENYAN	398193
2	GONZALO HERNANDEZ CIRIZA	SPAIN	881915
3	PALOMA MOSQUERA CIRIZA	SPAIN	159651
4	EDUARDO HERNANDEZ CIRIZA	SPAIN	679652
5	JOAN HERNANDEZ CIRIZA	SPAIN	218089

2. It is not in dispute that Gonzalo Hernandez Ciriza died on 15th January 2018.

3. This suit has been consolidated with the application filed by the interested parties against the Company and 4th interested party as the dispute involves the management of the Company and accusations by the parties against each other.

4. The 1st, 2nd and 3rd interested parties, as shareholders in the Company, filed an application against the Respondent and the 4th interested party, **Misc. Application No. E1308 of 2020** seeking protection against oppressive conduct and leave to commence a derivative action, inter alia, under **section 780** of the **Companies Act, 2015** seeking an order:

[2] THAT leave be and is hereby granted to the Applicants to commence a derivative claim in respect of the acts of omission involving negligence, default, breach of duty and breach of trust by the 1st Respondent, a Director of Meridian Acceptances Limited, 2nd nominal respondent herein and its former Managing Director.

5. The application is supported by the deposition of Eduardo Hernandez Ciriza sworn on 17th December 2020. It is opposed by the affidavit of James Ndwigah Muchungu sworn on 15th January 2021.

6. The gravamen of the Interested Parties' complaint is that James Ndwigah Muchungu was the Managing Director of the Company until his services were terminated on 2nd December 2020 following acts of negligence, default and breach of the trust committed by him. The Board of Directors decided to recruit a new managing director. Instead of leaving, the Applicants accuse Mr Muchungu of the taking over the Company offices, locking the offices and removing the signage and failing to renew the lease of one of the Company's premises. They also accuse him of incapacitating the Company's ICT system thereby preventing staff from performing their duties. This, the Applicants claim, has caused the Company to default in its tax obligations causing Kenya Revenue Authority to issue agency notices and that the Company has failed to conduct its annual audit and file the necessary returns for the year 2020. The applicants believe that Mr Muchungu is diverting the assets of the Company to his own personal and family business.

7. In his response, Mr Muchungu denies that allegations against him. He states that it is the Applicants who have attempted at various times to forcefully take over the Company business. He impugns the alleged meeting of the Board of Directors removing him and denies that that Company has removed him from his position as Managing Director. He states that he has been performing his duties in the position diligently and submits that the Applicants have not made out a case for the grant of the orders sought.

8. While the Interested Parties' application was pending, the Plaintiffs filed a suit against the Company and the Registrar of Companies. The Plaintiffs state that they are shareholders of the Company following resolution by the Company on 11th December 2020 as evidenced by the CR 12 dated 23rd December 2020 as follows:

	NAME	NATIONALITY	SHARES
1	TREVOR SAWAYA NDWIGA	KENYAN	50000
2	IAN NYAGAH NDWIGA	KENYAN	50000
3	JUDITA WARUE NDWIGA	KENYAN	50000
4	BYRAN KEVIN MUREITHI	KENYAN	50000
5	VICTORIA WANENE NDWIGAH	KENYAN	50000
6	LISA MUMBI NDWIGAH	KENYAN	50000
7	JAMES NDWIGAH MUCHUNGUH	KENYAN	98193

8	GONZALO HERNANDEZ CIRIZA	SPAIN	881915
9	PALOMA MOSQUERA CIRIZA	SPAIN	159651
10	EDUARDO HERNANDEZ CIRIZA	SPAIN	679652
11	JOAN HERNANDEZ CIRIZA	SPAIN	218089

9. The thrust of the Plaintiffs' case is that some directors, who are intent on taking over the operations and business of the Company, made fraudulent representations to the Registrar of Companies alleging that they are not shareholders and directors of the Company and purported to remove them from register of shareholders and directors without any basis in law or due process.

10. The Registrar of Companies did remove the Plaintiffs as shareholders and directors of the Company as shown in the CR 12 dated 23rd December 2020 and issued a fresh CR-12 dated 11th January 2021 reverting the Company shareholding to the original position of shareholders and directors.

11. The Plaintiffs' alleged that the other directors, called a Special General Meeting on 5th February 2021 to discuss, inter alia, change of management of the Company, their removal and other critical issues concerning the running of the Company without the required 21-day notice. Thus, the Plaintiffs seek, inter alia, the following reliefs:

(a) *A declaration that the plaintiffs are bona fide shareholders and directors of the 1st Defendant Company and holding the shares set out in the company's list of directors and shareholders issues by the Registrar of Companies, the 2nd Defendant, on the 23rd December 2020 and entitled to participate in all company's meetings including the Special General Meeting scheduled for the 5th February 2021.*

(b) *A declaration that the removal of the Plaintiffs by the 2nd defendant from the 1st defendant's register of members and directors is unlawful, irregular and otherwise null and void ab ignition and that any meetings held without prior notice to them are unlawful and any resolution made thereon invalid.*

(c) *A mandatory injunction compelling the 2nd defendant to reinstate the plaintiffs to the 1st defendant's register and list of directors and shareholders and further that the defendants be restrained from interfering with the same forthwith.*

12. Together with the Plaintiff, the Plaintiffs filed an application under **Order 40 rule 1** of the **Civil Procedure Rules** seeking to restrain the Special General Meeting.

13. During the interlocutory proceedings, I suggested to the parties that from the totality of the pleadings and depositions, the dispute concerned the shareholding and management of the Company. On 2nd March 2021, I directed that, "*the directors of the Company as per the CR 12 dated 11th January 2021 to hold a meeting to resolve the issue of transfer of shares and shareholding in accordance with the Articles of Association.*" Because of the dispute as to shareholding, the meeting failed to reach the intended objective because the shareholding of the Company remains a sticking point. On the other hand, one of the ways to resolve the 1st, 2nd and 3rd Interested Parties' application for permission to commence a derivative action is to place the matter before the shareholders.

14. Following my suggestion, the parties agreed that based on the material before the court, the court should first resolve whether the Plaintiffs are lawful shareholders. It is not in dispute that that the Plaintiffs are the spouse and children of James Ndwigah Muchungu who transferred his 300,000 ordinary shares to them in equal shares as set out in the CR 12 issued by the Registrar of Companies on 23rd December 2020.

15. The issue placed before the court for determination is whether such a transfer requires the sanction and approval of all the directors of the Company and if so, whether such approval was issued by the directors. The parties filed written submissions in support of their respective positions.

16. In order to resolve the issue, I shall set out the relevant part of the Articles of Association ("the Articles") to be found at pages 9, 10 and 11. I note however that the Articles do not flow in a numerical order. The Articles under the heading TRANSFER OF SHARES are Article 5 which has sub- Article (a), (c), (d), (e), (f) and (g) followed by Articles 7, 8 and 9 which provide as follows:

Article 5

(a) *Subject to the provisions of Article 8 hereof, no shares in the company shall be transferred unless and until the rights of pre-emption hereinafter conferred shall have been exhausted.*

(c) *Every member who desires to transfer any share or shares (hereinafter called "the vendor") shall give to the Company notice in writing of such desire (hereinafter called "the transfer notice"). Subject as hereafter mentioned, a transfer notice shall constitute the Company the Vendor's agent for the same of the share or shares specified therein (hereinafter "the said shares") to the Members*

other than the Vendor at a price agreed upon by the Vendor and Directors or, in case of difference, at the price which the auditor of the Company for the time being shall by writing under his hand, certify to be in his opinion the fair value of thereof as between a willing seller and willing buyer. A transfer notice may contain a provision that, unless all the shares comprised herein are sold by the Company pursuant to Article, none shall be sold and any such provision shall be binding on the company.

(e) -----

(f) -----

(g) -----

Article 8

The rights of pre-emption hereinbefore conferred in Article 5 shall not apply to;

(a) Any transfer approved in writing by all members.

(b) Any transfer by a member to the spouse, child or remoter issue, brother, sister or parent of the member.

(c) -----

(d) -----

(e)-----

(f) -----

Article 9 (b)

The directors may decline to register: -

(a) Transfer of any shares on which the Company has a lien;

(b) Transfer of any share to a person of whom they do not approve, and

(c) Transfer of any share the registration of which would cause the number of members to exceed the maximum permitted by Regulation 2 of Part II of Table A;

Provided that the provisions of paragraph (b) of this Article shall not apply to any transfer made pursuant to Article 5 of 7 thereof. Regulation 3 of Part II of Table A shall not apply.

Submissions

17. The Plaintiffs submit that the Company's Articles of Association ("the Articles") allow the shareholders to freely transfer their shares to spouses, children and other persons within that degree of consanguinity, without the interference and approval of the other directors and shareholders.

18. The Plaintiffs submit that the Interested Parties' objection to these transfers is not based on any specific provision of the Articles and neither is it justified by any particular concern or prejudice demonstrated by the Defendants but made for the sake of actively pushing for the removal of Mr Muchungu as the Managing Director and has nothing to do with the Plaintiffs in this matter. The Plaintiffs urge the court to adopt a literal construction of the letter and wording of the Articles and allow the transfer of shares to the Plaintiffs as already made by the said Mr Muchungu.

19. The Company in its submissions takes the position that the transfer of shares by Mr Muchungu was valid and lawful for all purposes and that there is no basis in law for the object made by Interested Parties to the transfer and registration thereof. Counsel for the Company also submits that there is no pleading by way of defence or counterclaim that has been made by the Interested Parties to set aside and invalidate the transfer which was effected and registered by the 2nd Defendant as evidenced by the CR 12 made on 23rd December 2020 hence the court does not have any jurisdiction to adjudicate on or invalidate on matters that have no basis on the pleadings.

20. It is the Company's position that the Company has not passed any resolution rejecting or invalidating the transfer of shares by Mr Muchungu to the Plaintiffs and as the Company has not made any such resolution, there is no basis for the court to set aside a valid disposition. Further, its position is that Article 8(b) excludes the application of pre-emption rights to transfer of shares to the members of the family and that Article 9(b) requiring approval of directors is expressly excluded on a transfer of shares made under Article 8(b). Counsel for the Company submits that the Company is owned by two families; the Ndwiwa and the Hernandez families and in drawing up the Articles they expressed the intention that isolate disposition of shares and other interests in the Company within the respective families to the extent of excluding pre-emptive rights and directors' approvals from transfer of shares from member to spouse or children. The Company therefore submits that the court in interpreting the Articles should give effect to the intention of the parties and decline to intervene in the disposition

of shares by a member to his spouse and children.

21. The Interested Parties' position is that a reading of Article 5 and Article 9(b) give the directors power to decline to register transfer of shares to a person they do not approve of. The Interested Parties submit that from a literal reading of Article 9(b), before a shareholder exercises its pre-emptive right, it must notify the directors of the Company of the intended transfer as to enable the directors to register the transfer of shares as it is only the directors who have the mandate to register share transfers of a company. They contend that Mr Muchungu did not inform them, as majority directors/shareholders of the purported transfer of shares hence he did not comply with the memorandum and Articles. They further submit that by dint of Article 9(b) there are two mandatory pre-requisites by the Directors before approval of any transfer of shares that being: first, a notice issued to the Directors of the intended transfer and second, the transfer has to be registered by the Company.

22. The Interested Parties submit that transfer of shares is exclusively provided for under Article 5 and that it is mandatory under Article 5(c) for every member who desires to transfer any share(s) to give to the Company notice in writing. They add that ownership of a company is a preserve of the directors/shareholders and as such any issue regarding transfer of ownership cannot be done without notice. The Interested Parties rely on **section 497(1)** of the **Companies Act** which provides that the Company may register shares only if proper documents of transfer have been delivered to it.

23. The Interested Parties submit that the pre-emptive rights created under the Articles does not derogate the existence of the rules of procedure laid down in the **Companies Act** and the Company's Articles of Association. In sum, the Interested Parties maintain that the purported transfer of shares by Mr Muchungu was irregular and illegal as he did not give notice to the Interested Parties and that registration was done contrary to Articles of Association as well as the **Companies Act**.

24. As regards the meeting held on 11th December 2020, the Interested Parties contend that it does not meet the requirements set out in the **Companies Act**. Further, the meeting did not comply with Article 15(a) in terms of quorum and consent and that the 21-day notice stipulated by **section 281** of **Companies Act** was not met as it was sent out to persons who were not members of the Company. Consequently, they urge, the meeting held on 11th December 2020 and the resolution passed are a nullity.

25. Counsel for the 2nd Defendant submitted that the transfer of shares in the company must comply with the provisions of the **Companies Act** as well as the preemption rights as set out in the Articles of Association of the company. He also submitted that the meeting convened on 11th December 2020 and any such resultant resolutions must comply with the pre-emption rights, the requirement to issue share transfer notices, notice to convene a meeting in the right manner and time frames as well quorum threshold including the requirement on the minimum number of directors.

Analysis and Determination

26. From the pleadings and submissions, the main issue for determination is whether the transfer of shares from Mr. Muchungu to the Plaintiffs was valid. As the 2nd Defendant submits, the issue for consideration concerns the allotment and transfer of shares and the appointment of directors in a company and the procedures for calling meetings of the company.

27. The applicable law for allotment, transfer of shares and appointment of directors in a company is found in the **Companies Act** and the Articles of Association which ordinarily governs the relationship between members of a company. The general rule is that private companies may freely transfer their shares unless articles explicitly restrict the manner of transfer. Counsel for the 2nd Defendant cited the *dictum* of Lord Greene MR in **Re Smith and Fawcett Ltd [1942] Ch. 304,306** that;

The shareholder has such prima facie right, and that right is not to be cut down by uncertain language or doubtful implications. The right, if it is to be cut down, must be cut down with satisfactory clarity. It certainly does not mean that articles, if appropriately framed cannot be allowed to cut down the right of transfer to any extent which the articles on their true construction permit.

28. The parties agree that the Articles allow a director to transfer shares to their spouse or children. The point of departure is whether notice to the other directors is required before such a transfer is effected under Article 5(c). This calls for an interpretation of the Articles which must be read as a whole. In **Stothers v William Steward (Holdings) Ltd [1994] 2 BCLE 226, 273** cited by counsel for the 2nd Defendant, Gibson LJ observed that:

[T]he articles, including the regulations of Table A incorporated into the articles, must be construed together and effect given, so far as possible, to every provision; it is only if the express articles are inconsistent with the incorporated regulations of Table A that the former will override the latter.

29. Transfer of shares is provided for under Articles 7, 8 and 9 of the Articles. Article 5(a) provides for the general rule that no shares in the Company shall be transferred until pre-emption rights have been exhausted. By use of the phrase, "*Subject to the provisions of Article 8 hereof*" implies that that Article 8 provides the exception to the general rule which is underscored by the opening phrase, "*The rights of pre-emption hereinabove conferred in Article 5 shall not apply*".

30. Does a member who wishes to transfer shares to members of his family require to give notice? The requirement for notice is to be found in Article 5(c). By referring to, "*rights of pre-emption hereinafter conferred shall have been exhausted...*" Article 5(c) deals exclusively with pre-emption rights and not any other forms of transfers. This is buttressed and underpinned by Article 8 which refers to, "*The rights of pre-emption hereinbefore conferred in Article 5*" In other words, the clause after Article 5(a) sets out how pre-emptive rights are exercised. I therefore find and hold that a member who wishes to transfer his shares in accordance with Article 8(b) does not require to give notice in the manner provided for in Article 5(c). It is for this reason that I also hold that the other requirements in Article 5 including consideration do not apply to a transfer by a member to a family member.

31. I also hold that the right of a member to transfer shares to the spouse, child or remoter issues, brother, sister or parent is a free standing and an unconditional right by reason of Article 8(b) but is subject to Article 9(a) under which the directors may decline to register a transfer of any share to a person of whom they do not approve. The proviso to Article 9 states that:

Provided that the provisions of paragraph (b) of this Article shall not apply to any transfer made pursuant to Article 5 of 7 thereof. Regulation 3 of Part II of Table A shall not apply. [Emphasis mine]

As I have held, Article 5 only provides and establishes the general rule on pre-emptive rights and it is only the “Article 5 of 7” that is excluded by the proviso to Article 9. Had the authors intended that the Article 8(a) be excluded from the purview of the directors’ approval, nothing would have been easier than for the provision to Article 9 to state that, “*this Article shall not apply to any transfer made pursuant to Article 8(a) thereof*”. Although Counsel for the Company submitted that intention of the shareholders was that transfer of shares within the family was to be immunized from directors’ actions, such intention must be given effect by the terms of the Articles of Association. The court cannot violate the clear language of the Articles in order to give effect to an intention that is not supported by the clear words of the Articles.

32. But the fact that the member has made a transfer of shares to his relatives under Article 5(b) is not in itself complete. The Interested Parties correctly point out that it is the responsibility of the Company to register the transfer by reasons of **section 497** of the **Companies Act** which provides:

497(1) A company may register a transfer of shares or debentures of the Company only if a proper document of transfer has been delivered to it.

(2) Except as provided by subsection (3), a purported registration of a transfer of shares or debentures in contravention of subsection (1) is void.

(3) Subsection (1) does not affect a power of the company to register as a shareholder or debenture holder a person to whom the right to any shares in or debentures of the company has been transmitted by operation of law.

33. It follows therefore that even when notice is not given to the Company of any transfer, the transfer must in any case be presented to the Company for registration. Further, under Article 9(b), such transfer must be approved by the Company. From the totality of the evidence, the transfer of shares by Mr Muchungu to the family members was not presented to the Company for approval. In view of the findings I have made, the transfer was proper to the extent that Mr Muchungu was not required to give notice of it under Article 5 but the transfer had to be placed before the Directors for approval or otherwise in accordance with Article 9.

34. Having reached this conclusion, it is not necessary to decide whether in fact the meeting on 11th December 2020 resulting in the Plaintiff being appointed as directors of the Company was valid. Unless and until the share transfers are approved by the directors as required by Article 9(b), the Plaintiffs could not become shareholders and directors of the Company.

35. Before I conclude the matter, the Company contested the jurisdiction of this court to grant relief in favour of the Interested Parties as there was no defence and counterclaim requesting the court to annul the transfer of shares by Mr Muchungu to his spouse and children. It is worth noting that even if I decline to interfere with the transfer and the registration of the Plaintiffs as shareholders and directors of the Company which had been done on 23rd December 2020, the same process was reversed by the 2nd Defendant as evidenced by the CR 12 dated 11th January 2021 after the office realized that the Interested Parties had lodged a caveat on 12th December 2020. These changes which now show that the shareholding reverts to the original shareholders and directors is the action that the Plaintiffs seeks to set aside and in deciding whether or not to set aside the decision of the 2nd Defendant, the court must address itself to the totality of circumstances that led to the transfer of shares and appointment of the Plaintiffs as directors.

36. Further, the Plaintiffs, in their submissions, agreed that the singular issue for resolution is, “*whether or not the approval of directors was required for a shareholder to transfer his shares to a spouse and his or her children.*” I have proceeded therefore on the basis of the parties’ agreement and on the basis that facts, as is evident, are not disputed. Further the matter concerns an interpretation of the Company Articles of Association which will resolve the entire suit that is why this decision is a judgment.

Conclusion and Disposition

37. Since I have resolved the question agreed for resolution, the question remains what relief should I grant to the parties.

38. In **HC Misc. E1308 of 2021**, the Interested Parties sought permission to commence a derivative action on behalf of the Company against the 4th Interested Party. As I indicated to the parties during the proceedings, all the matters complained of can be resolved by a meeting of the shareholders. Further, it is clear from the shareholding that although the largest shareholder is deceased, the Interested Parties hold 45% of shares as opposed to 16% held by Mr Muchungu hence they cannot be termed as minority shareholders who are oppressed. The Notice of Motion dated 17th December 2020 is therefore dismissed.

39. Turning to the suit by the Plaintiffs, I have now held that under the Articles of Association, the directors have the power to decline registration of any transfer of shares to a members’ relatives. The members of the Company also have a right to amend the Articles of Association if they so wish. The matter is in the hands of the Company and the members may call General or Special Meeting in that regard.

40. Having reached the above determination, no purpose will be served by proceeding further with the suit as the issue in contention has been determined by an authoritative interpretation of the Articles by the court. Having done so, the members may proceed to resolve their issue in accordance with the Article of Association.

41. In view of the nature of the matter, I do not propose to award costs as this would merely aggravate the already hostile relationship between the parties who must work together.

42. In light of the aforesaid, I now grant the following reliefs:

(a) The Notice of Motion dated 17th December 2020 filed in HC Misc. E1308 of 2020 is hereby dismissed.

(b) A declaration be and is hereby issued that under Article 9(b) of the Company Articles of Association, the directors may decline to register a transfer to a person of whom they do not approve including a transfer of shares made under Article 8(b) being a transfer by a member to a spouse, child or remoter issue, brother, sister or parent of the member.

(c) There shall be no order as to costs in the matter.

DATED AND DELIVERED AT NAIROBI THIS 13TH DAY OF AUGUST 2021.

D. S. MAJANJA

JUDGE

Court Assistant: Mr M. Onyango

Ms Munyua instructed by Ngonyo Munya and Company Advocates for the Plaintiffs

Mr Njenga instructed by Muchoki Kangatta Njenga and Company Advocates for the 1st Defendant.

Mr Odhiambo, Advocate instructed by the Business Registration Service for the 2nd Defendant.

Mr Otieno instructed by Brian Otieno and Company Advocates for the 1st, 2nd and 3rd Interested Parties.