



REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

COMMERCIAL AND TAX DIVISION

HCCC NO. E286 OF 2019

HARJINDER SINGH RIHALPLAINTIFF

VERSUS

JASWINDER SINGH RIHAL.....DEFENDANT

RULING

1. This ruling is in respect to two applications, namely;

a) The application dated 9th September 2019 (hereinafter “**the 1st Application**”) wherein the plaintiff/applicant seeks orders to restrain the defendant, his agents, workers, relatives or anyone acting on his behalf from acting on behalf of the company known as GURBAKSONS KENYA LIMITED or interfering with the affairs of the said company including managing collecting rent from LR No. 25407 or in any manner whatsoever. The plaintiff also seeks orders directing the defendant to produce accounts for the management of the company rental incomes and other payments.

b) The application dated 12th February 2020 (hereinafter “**the 2nd Application**”) wherein the plaintiff/applicant seeks orders for leave to continue the present suit as a derivative action pursuant to Section 238 and 239 of the Companies Act (hereinafter “**the Act**”).

2. The 1st application is supported by the plaintiff’s affidavit and is premised on the grounds that the plaintiff, the defendant and others incorporated a company known as **Gurbaksons Kenya Limited** under Memorandum and Articles of Association with shareholding as follows: -

i. Mohinder Kaur Rihal- 12499

ii. Jaswinder Singh Rihal – 1

iii. Gurjinder Singh Rihal – 1

iv. Harjinder Singh Rihal – 2499

Total - 15000

3. The plaintiff states that the nominal share capital of the company is Kshs 300,000/- divided into 5000 ordinary shares of Kshs 20/- each but that the defendant has moved unilaterally and without the authority of the company in breach of fiduciary duties and transferred the shares in the company as follows: -

1. Gurjinder Kaur Rihal – 1

2. Harjinder Singh Rihal – 2499

3. Jaswinder Singh-12500

4. It is the plaintiff’s case that the defendant has committed acts of fraud by operating the company’s bank accounts in a manner that is detrimental to the company and that the has refused to hand over the company’s seal, statutes and other property in his possession thus exposing the company to loss and damage.

5. The defendant opposed the 1st application through the replying affidavit dated 27th September 2019 wherein he states that the application is fatally defective as the applicant did not seek leave to file a derivative suit on behalf of the company as required under Section 239 of the Companies Act.

6. He states that the total issued share at the death of the late **Amrik Singh Rihal** of 15000 remains intact to date and that there has been no allotment of shares as alleged by the plaintiff. He states that **Mohinder Kaur Rihal**, who is their mother and who is still alive voluntarily transferred her 12,499 shares to him thus increasing his shareholding to 12,500 shares but that he has since re-transferred the said shares back to her.

7. He further states that the applicant is not a director of the company and that the orders sought have the effect of paralyzing the operations of the company which is managed by its Board of Directors as shown in the Companies records.

8. He adds that the applicant, who is his brother, is pursuing a vendetta against him as he has filed a similar application over the company in the Family Division being Succession Cause No. 1476 of 2016 which is pending ruling. He denies any involvement with the management of the business of the company.

9. The 2nd application is supported by the applicant's affidavit and is premised on similar grounds as the first application including the ground that the defendant attempted to reverse the illegal transfer of 12,500 shares to himself by retransferring 12,000 shares to her mother, **Rihal Mohinder Kaur**, but retained 499 in contravention of the Company's Articles of Association.

10. The defendant opposed the 2nd application through the Grounds of Opposition dated 19th February 2019 wherein he raises similar grounds to those listed in the replying affidavit in response to the 1st application.

11. The applications were canvassed together by way of written submissions which I have carefully considered. The main issue for determination is whether the plaintiff can commence a derivative suit without the leave of the court and if such leave, can be obtained after the commencement of the suit.

12. It was not in dispute that the plaintiff filed the plaint herein dated 9th September 2019 seeking the following order against the Defendant; -

a) A permanent injunction be issued against the defendant, his servants, workers, relatives or anyone acting on his behalf from purporting to act on behalf of the company GURBAKSONS KENYA LIMITED or interfering with the affairs of the company or acting as a director of shareholder forthwith.

b) The defendant be ordered to provide detailed accounts of the company since 2002 to date.

c) Costs of the suit.

13. Concurrently with the plaint, the plaintiff also filed the 1st application and thereafter, the 2nd application wherein, as a reaction to the short fall in the first application, he seeks leave to continue the suit as a derivative action.

14. The plaintiff submitted on the principles governing the conditions to be fulfilled by a plaintiff who wishes to succeed in an action for a derivative suit as contained in Sections 238 and 239 of the Act. For this submissions, the plaintiff relied on the decision in **Joseph Munyoki Nzioka v Raindrops Limited and 3 Others** [2019] eKLR wherein it was held: -

i. He must be a member of the company.

ii. The proceedings must be in respect to a cause of action vested in the company.

iii. The applicant must seek leave to act on behalf of the company.

iv. The proceedings must be for protection of members against unfair prejudice brought under the Companies Act; and

v. The proceedings are in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default breach of duty or breach of trust by a director of the company.

15. The plaintiff further expounded on the reasons informing the filing of the suit in his capacity as a minority shareholder in the company.

16. On his part, the defendant submitted that there is no provision in the Act allowing a party to commence a derivative suit without the leave of court and later seek such leave retrospectively. For this argument, the defendant relied on the decision in **Nilkunj Ratilal Dodhia v Shashikant Mepa Shah & 5 Others** [2018] eKLR where the court held: -

“19. Part XI of the Companies Act is dedicated to provisions on Derivative Actions. It mainstreams the concept of a Derivative Claim into Statute. An enduring feature of a Derivative Claim is that it can only be commenced or continued with the express sanction of the court.”

17. Reference was also made to the decision in *Ghelani Metals Limited & 3 Others v Elesh Ghelani Natwarlal & Another* [2017] eKLR where Onguto J. held: -

“44. Statutory procedure is now the exclusive method of pursuing derivative claims. The Act sets out what sorts of company claims may be pursued and is also explicit that derivative claims may be pursued under the Act.

The Judge further broke down the derivative suits into a two-stage process. He stated that: -

45. There appears, in my view, to exist a two stage process. The court must first satisfy itself that there is a prima facie case on any of the causes of action noted under Section 238(3) of the Act provides that the application for permission will be dismissed if the evidence adduced in support “do not disclose a case” for giving permission. The essence of judicial approval under the Act is to screen out frivolous claims. The court is only to allow meritorious claims. All that the applicant need to establish, through evidence, is a prima facie case without the need to show that it will succeed.

46. The second stage entails a consideration of statutory provisions and factors which ordinarily guide judicial discretion albeit in the realm of derivative action.”

18. Sections 238 and 239 of the act stipulates as follows: -

238. (1) In this Part, "derivative claim" means proceedings by a member of a company —

(a) in respect of a cause of action vested in the company; and

(b) seeking relief on behalf of the company.

(2) A derivative claim may be brought only —

(a) under this Part; or

(b) in accordance with an order of the Court in proceedings for protection of members against unfair prejudice brought under this Act.

(3) A derivative claim under this Part may be brought only in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director of the company.

(4) A derivative claim may be brought against the director or another person, or both.

(5) It is immaterial whether the cause of action arose before or after the person seeking to bring or continue the derivative claim became a member of the company.

(6) For the purposes of this Part-

(a) "director" includes a former director;

(b) a reference to a member of a company includes a person who is not a member but to whom shares in the company have been transferred or transmitted by operation of law.”

239. (1) In order to continue a derivative claim brought under this Part by a member, the member has to apply to the Court for permission to continue it.

(2) If satisfied that the application and the evidence adduced by the applicant in support of it do not disclose a case for giving permission, the Court-

(a) shall dismiss the application; and

(b) may make any consequential order it considers appropriate.

(3) If the application is not dismissed under subsection (2), the Court-

(a) may give directions as to the evidence to be provided by the company; and

(b) may ' adjourn the proceedings to enable the evidence to be obtained.

(4) On hearing the application, the Court may-

(a) give permission to continue the claim on such terms as it considers appropriate;

(b) refuse permission and dismiss the claim; or

(c) adjourn the proceedings on the application and give such directions as it considers appropriate.”

19. In the instant case, I note that the derivative suit was filed without the leave of the court which is an anomaly that the plaintiff seeks to ‘regularize’ through the second application.

20. My finding is that from a simple reading of the provisions of Section 238 and 239 of the Act and the dictum in the above cited cases, it is a requirement that leave may be obtained before the filing of derivative suit so as to enable the court, at the preliminary stage of the leave application, to screen the case and satisfy itself that there is a prima facie and meritorious case worthy of its leave/permission before the case can be filed.

21. Courts have however held that leave may be obtained to continue with a suit that has already been filed. This is the finding that was made by the Court of Appeal in *Amin Manji & 2 Others v Altaf Abdulrasul Dadani & Another* [2015] eKLR where the Court of Appeal held as follows: -

“Leave of the court shall be obtained before filing of a derivative suit but may also be obtained to continue with the suit once filed. On this the court was right in adopting the exposition of the treatise “Minority shareholders”; Law, Practice and Procedure” by Joffe that “there is no approved pre-action protocol in relation to the derivative action” and that after the claim form has been issued, the claimant is required to make an application which must be supported with written evidence for permission to continue with the claim”. It is our view that at whatever stage leave is sought, the crucial requirement is for the applicant to establish a prima facie case demonstrating that he has locus standi to institute such an action, the company is entitled to the intended relief and the action falls within any of the exceptions of the rule in Foss vs Harbottle.” (emphasis added).

22. From the above cited decision, it is clear that the court has the discretion to grant leave to continue the suit herein as a derivative claim depending on whether or not the case meets the exceptions to the rule in *Foss v Harbottle* [1843] 2 Hare 461.

a. The court discussed the exceptions to the rule in *Foss v Harbottle* (supra) in derivative actions in *Grace Wanjiru Munyinyi and Another v Gideon Waweru Githunguri and 5 Others* [2011] eKLR as follows:

“There is also another remedy arising from the English Legal precedent on corporate law which continues to apply in Kenya more than 160 years since it was decided: Foss vs Harbottle (supra). As stated earlier, in any action in which a wrong is alleged to have been done to a company, the proper claimant is the company itself. This is the rule in Foss v Harbottle. But there are four exceptions to that rule which appear in the leading case itself but also in subsequent decisions on the subject.

Firstly, where the directors or a majority use their control of the company to paper over actions which would be ultra vires the company or illegal.

Secondly, if some special voting procedure would be necessary under the company’s constitution or under the company’s Act, it would defeat both if they could be side stepped by ordinary resolutions of a simple majority, and no redress for aggrieved minorities were to be allowed (Edwards v Halliwell [1950] 2 ALL ER 1064, Thirdly, where there is invasion of individual rights, such as voting rights (Pender vs Lushington [1887] 6 ch D 70. Fourthly, where a fraud on the minority is being committed. In all those cases, a “derivative action” could be brought before the court on behalf of the company where the wrongdoer is in control of the company or by the shareholder where his personal rights are violated.”

23. In *Pender v Lushington* [1877] 6 ch D 70 Jeseel MR amplified an additional exception to the rule in *Foss v Harbottle* (supra) and stated as follows: -

“But there is another ground on which the action may be maintained. This is an action by Mr. Pender for himself. He is a member of the company, and whether he votes with the majority or the minority and he is entitled to have his vote recorded – an individual right in respect of which he has a right to sue. That has nothing to do with the question like that raised in Foss vs Harbottle and that line of cases. He has a right to say, “whether I vote in the majority or minority, you shall record my vote, as that is a right of property belonging to my interest in this company, and if you refuse to record my vote I will institute legal proceedings against you to compel you” what is the answer to such an action? It seems to me, it can be maintained as a matter of substance, and that there is no technical difficulty in maintaining it.”

24. The question which also arises is whether the plaintiff, as a minority shareholder, can bring a derivative suit in the name of the company.

25. The answer to the above question is to the positive as can be seen in the decision in *Sultan Hashem Lalji & 2 Others v Ahmed Hasham Lalji & 4 Others* [2014] eKLR wherein it was held: -

“It is the minority shareholders that are availed the protection by the exceptions since generally majority shareholders exercise power of the company and control its affairs”.

26. My finding is that as minority shareholder, the plaintiff is at a disadvantaged position since it is the majority shareholders who hold the veto power and are therefore unlikely to pass a resolution for the plaintiff to file a suit against them.

27. The defendant also took issue with the plaintiff's failure to enjoin the company to the suit and argued that this was a fatal omission on the plaintiff's part as the cause of action belongs to the company under Section 238(1) of the Act. The defendant relied on the decision in the case of *Ghelani Metals Limited & 3 Others Vs Elesh Ghelani Natwarlal & Another* [2017] eKLR where the learned Justice L. Onguto referred to the principle stipulated in *Foss v Harbottle* and *Rai & Others v Rai & Others* and stated: -

“39. The rule in Foss V Harbottle along with its exceptions held sway locally as well: See Rai & Others V Rai & Others [2002] 2 EA 537. A party seeking to ‘by-pass’ the company had, in limine, to show that he fell within the exceptions to the rule: See Murii & Another [1999] 1 EA 212.”

28. In the present case, having found that the plaintiff herein falls within the exceptions to the rule in *Foss v Harbottle*, I find that he is capable of proceeding with the suit on behalf of the company. I further find that failure to enjoin the company to the suit cannot in the circumstances of the case be said to be fatal as the company may still be enjoined as a party in the suit through an amendment, should it be deemed necessary.

29. For the above reasons, I find that the application for leave to continue the suit is merited and I therefore allow it with orders shall abide the outcome of the suit.

Injunction

30. The conditions for consideration in granting an injunction were settled in the case of *Giella v Cassman Brown & Company Limited* (1973) E A 358, where the court expressed itself on the conditions that a party must satisfy for the court to grant an interlocutory injunction as follows: -

"First, an applicant must show a prima facie case with a probability of success. Secondly, an interlocutory injunction will not normally be granted unless the applicant might otherwise suffer irreparable injury, which would not adequately be compensated by an award of damages. Thirdly, if the Court is in doubt, it will decide an application on the balance of convenience."

31. The test for granting of an interlocutory injunction was considered in the American *Cyanamid Co. v Ethicom Limited* (1975) A AER 504 where three elements were noted to be of great importance namely: -

i. There must be a serious/fair issue to be tried,

ii. Damages are not an adequate remedy,

iii. The balance of convenience lies in favour of granting or refusing the application.

32. The circumstances for consideration before granting a temporary injunction under **order 40 Rule 1 of the Civil Procedure Rules** requires a proof that any property in dispute in a suit is in a danger of being wasted, damaged or alienated by any party to the suit or wrongfully sold in execution of a decree or that the defendant threatens or intends to remove or dispose the property, the court is in such situation enjoined to grant a temporary injunction to restrain such acts. In the instant case,

33. In the instant case, the applicant seeks to restrain the defendant who is his own brother and Director of the Company, from interfering with the affairs of the company including the management of the Company's property and collection of rent. I note that even though the applicant accuses the defendant of acts of fraud in the management of the Company's bank accounts, not tangible evidence was presented to show that the Company had lost money or was about to lose money through such fraud. It was further not established that the loss, if any, to be suffered by the applicant was such that the defendant may not be able to pay and therefore irreparable.

34. I am therefore not satisfied that the applicant has made out a case for granting of orders of injunction sought or that it would be in the interest of the company to restrain the defendant from carrying out his mandate as a director of the said company.

35. In a nutshell, I am not satisfied that the 1st application meets the threshold of the conditions set for the granting of orders of injunction. I therefore dismiss the 1st application with orders that costs shall abide the outcome of the main suit.

Dated, signed and delivered via Microsoft Teams at Nairobi this 17th day of December 2020 in view of the declaration of measures restricting court operations due to Covid - 19 pandemic and in light of the directions issued by his Lordship, the Chief Justice on the 17th April 2020.

W. A. OKWANY

JUDGE

In the presence of:

Miss Munene for Koech for Defendant/Respondent

Court Assistant: Sylvia