REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA

AT NAIROBI

(MILIMANI LAW COURTS)

CIVIL APPEALS 913 & 930 OF 2003

1. **SHAH MUNGE & PARTNERS LIMITED**
2. **FRANKLIN KARIUKI KIRIGIA**
3. **ARTHUR RUNYENJE NAMU**
4. **JOHN PAUL MUNGE**
5. **PAUL ANTHONY SPENCE ……APPELLANTS**

V E R S U S

THE CAPITAL MARKETS AUTHORITY ……..……..RESPONDENT

JUDGMENT OF KASANGO, J

By agreement of the three of us Judges, I will deal in my judgment with the issue of sanctions as imposed upon the Appellants by the **Capital Markets Tribunal** (hereinafter called the **Tribunal**).

These are second appeals from the disciplinary action taken against the Appellants by the **Capital Markets Authority** (hereinafter called the **Authority**) under the **Capital Markets Act, Cap. 485A** (hereinafter called the **Act**). The first appeals were to the Tribunal under **section 35 (1)** of the Act. Under **subsection (2)** of the same section, the Tribunal may affirm or, after affording the Authority an opportunity of being heard, set aside the Authority's decision. And under **section 35A (16)** of the Act, upon appeal the Tribunal may:-

"**(a) confirm, set aside or vary the order or decision in question;**

(b) exercise any of the powers which could have been exercised by the Authority or any of its committees in the proceedings in connection with which the appeal is brought; or

(c) make such other order, including an order for costs, as it may deem just".

The Tribunal had imposed the following sanctions and orders against the Appellants:-

1. It suspended the 1st Appellant, SHAH MUNGE & PARTNERS LIMITED, from rendering services as a stockbroker (including trading at the Nairobi Stock Exchange) for a period of 30 days with effect from 18th October, 2002.

2. It imposed a penalty of KShs. 1.5 million upon the 1st Appellant, the same to be paid to the Capital Markets Authority Investor Compensation Fund as required by the Act.

3. It ordered that all the then directors of the 1st Appellant, that is the 2nd Appellant (FRANKLIN KARIUKI KIRIGIA), the 3rd Appellant (ARTHUR RUNYENJE NAMU), the 4th Appellant (JOHN PAUL MUNGE) and the 5th Appellant (PAUL ANTHONY SPENCE), do take responsibility for the 1st Appellant's violations of the Act, and therefore be ineligible for directorship in the 1st Appellant, or in any other licensee of the Authority and listed companies, for a period of one year.

4. The Authority further ordered that the lifting of the suspension of the 1st Appellant's license as a stockbroker be subject to full compliance with the requirements of the Act and the Capital Markets (Licensing Requirements) (General) Regulations, 2002, including the appointment of new directors and chief executive officer acceptable to the Authority, and the fulfillment of the first three sanctions.

The Tribunal, after hearing the appeals, which hearing was in the nature of a re-hearing, not a mere review of the evidence taken by the Authority and the conclusions it had reached, set aside the penalty of KShs. 1.5 million imposed upon the 1st Appellant for being unlawful. It also varied the other sanctions/orders imposed by the Authority as follows:-

1. It ordered that the license of the 1st Appellant issued to it by the Authority under the Act be suspended for 3 years with effect from 18th October, 2002.

2. The Tribunal also ordered that the directors of the company, that is the 2nd, 3rd, 4th and 5th Appellants, be ineligible for directorship or any other position of management or control of any licensee of the Authority for a period of 5 years from 18th October, 2002.

3. Finally, the Tribunal ordered that the issuance of a license to the 1st Appellant after serving the suspension imposed be subject to full compliance with the requirements of the Act, including all subsidiary legislation thereunder.

The **background** to these appeals has been set out in the judgment of Waweru, J which I have had the advantage of reading in draft. That judgment deals with the issue of the **disciplinary jurisdiction** of the Authority under the Act. I fully agree with the conclusions reached by the learned Judge on that issue. The judgment of Waweru, J also touches upon the Tribunal's **jurisdiction to impose sanctions upon the directors of a limited liability company that is a licensed stockbroker under the Act**. I respectfully agree with the conclusions of Waweru, J on this issue. My judgment deals only with the particular sanctions as imposed upon each Appellant.

I have also had the advantage of reading in draft the judgment of Kubo, J which deals with issues of **procedure of the Authority when conducting inquiries and exercising other related powers under the Act**. I respectfully agree with the learned Judge in all the conclusions that he has reached, and I have nothing useful to add in that regard.

The grounds of appeal that touch on sanctions are numerous and repetitive in Appeal No. 913 of 2003. They include **grounds 58 to 62, grounds 64 to 92** and **grounds 94 to 99**. Apart from the issue of the Tribunal's **jurisdiction to impose the sanctions** (which the judgment of Waweru, J has dealt with), the **legality** of the sanctions is also challenged. Issues raised on legality include:-

1. That the Tribunal was in error in suspending the directors of the 1st Appellant from being

directors thereof or of any other licensee for 5 years.

2. That the term "**officer'** of a licensee cannot apply to a director.

3. That the directors ought not to be held accountable in respect of violations of the Act, and rules and regulations made thereunder, by the 1st Appellant on account of the separate corporate personality of the 1st Appellant.

I have considered the submissions of the learned counsels appearing on these issues, including the authorities cited. I will consider the issues in turn.

1. <u>Suspension of the 2nd to 5th Appellants</u>

Under **section 29(1) (b)** of the Act, it is the discretion of the Authority to accept or refuse to accept a director of an applicant for a license. If a director is removed from directorship of a suspended licensee, whether or not to approve such director for directorship of another licensee during suspension of the first licensee lies with the Authority. It cannot be a proper interpretation of **section 33(2)(b)** and section 29(1) (b) of the Act that, though a director be removed from the directorship of one licensee, the Authority would be bound to accept such person as a director of another licensee. That would be absurd, and the law does not tolerate absurdities!

It must be clarified here that the rights of a director under the **Companies Act, Cap. 486** are not affected in any way. Only his rights under the **Capital Markets Act** are. The legislative intent of section 29(1) (b) obviously is to ensure that only such persons as the Authority may approve are allowed to be directors of a licensee so as not to defeat the objectives of the Act as set out in the preamble thereof.

2. <u>Is the term</u> "officer" **<u>applicable to a director?</u>**

Under **section 2** of the Act, the term "director" has the meaning assigned to it in the Companies Act. That meaning is to be found in section 2 of that Act and is:-

'"**director"** includes any person occupying the position of director by whatever name called'.

In the same section,

'"**officer"** in relation to an association or a body corporate, includes a director, manager or secretary'.

It is thus clear that a director is indeed an officer of the company. In any event, under **section 37** of the Capital Markets Act, the Act takes precedence over any other law where there is a conflict between the provisions of the Act and any other law. The violations by the Appellants that the Tribunal was concerned with were those under the Act, not under the Companies Act or the common law.

3. Are the 2nd to 5th Appellants saved by the separate <u>corporate entity of the 1st Appellant?</u>

The sanctions imposed upon the 1st Appellant were not so imposed upon it as a *persona* under the Companies Act. They were imposed pursuant to the provisions of the Capital Markets Act against a licensee under that Act, and pursuant to powers conferred under the Act. A licensee under the Act need not be a corporate entity; it could be a person *sole*. The corporate structure of the 1st Appellant is thus absolutely irrelevant to the application of the provisions of the Act. We are concerned only with the provisions of the Act, not whether the corporate veil of the 1st Appellant was lifted (which it was not) in imposing sanctions against its directors. In short, this is not a company law matter under the Companies Act. Removal of the directors was under **section 33A (1) (c)** as read with section **33A (2) (b)** of the Capital Markets Act. The removal was not under the Companies Act, or under the articles of association of the 1st Appellant. Issues of negligence under common law or the provisions of company law as such were thus not relevant or germane to the matter before the Authority or Tribunal.

A look at the relevant portions of the Tribunal's award reveals that the decision to impose sanctions upon the 2nd, 3rd and 4th Appellants was not lightly reached. It was painstakingly arrived at. There was close scrutiny of the role of each of the three directors in the transaction between the 1st Appellant and NSSF. The Tribunal found as a matter of fact that each of the 2nd, 3rd and 4th Appellants had signed cheques in withdrawal or transfer to unknown destinations of the NSSF funds banked in the 1st Appellant's office account contrary to the rules or regulations then applicable. Each of those three directors was found, as a matter of fact, to have caused the 1st Appellant to contravene provisions of the Act, rules and regulations made thereunder. The withdrawals completely depleted the NSSF funds, all KShs. 251,505,500/00 of it! It all disappeared, and at the time of hearing the appeals, not a cent of it had been recovered. The money was banked in a bank (**Euro Bank**) in which the Tribunal found, as a matter of fact, the 4th Appellant, JOHN PAUL MUNGE, was also a director and shareholder. It was publicly known, and the 2nd, 3rd and 4th Appellants surely must have known, that the bank was experiencing grave financial problems. The pilfering of the NSSF funds (and this was without doubt theft) contributed to the deterioration of the financial stability of the 1st Appellant.

Under **section 33A (2) (b)** of the Act, a director of a licensee can be removed if:-

- **he has caused or contributed to any contravention of the Act, or regulations made thereunder by the licensee; or**

- **if he has caused or contributed to any deterioration in the financial stability of the licensed person; or**

- **he has been guilty of conduct detrimental to the interests of investors.**

The 2nd, 3rd and 4th Appellants clearly met these thresholds. The sanctions imposed upon them by the Tribunal were lawful. They were also manifestly deserved. Their appeals against the sanctions are without merit, and ought to be dismissed.

I can find fault only with the way the Tribunal dealt with the 5th Appellant, PAUL ANTHONY SPENCE. The Tribunal appeared to accept that this Appellant was totally in the dark as to what was happening in respect to the transaction between the 1st Appellant and NSSF. It is common ground that the Act (and the rules and regulations made thereunder) does not impose strict liability upon directors of a licensed person. There are specific actions or defaults under the Act that will constitute culpability.

The 5th Appellant was a non-executive director of the 1st Appellant. He testified before the Authority and the Tribunal by affidavit that as a non-executive director since 26th April, 1991 he had taken absolutely no part in the day-to-day operations and administration of the 1st Appellant, and had been neither aware of nor privy to the business and/or transactions of the 1st Appellant. He further deponed that he had no knowledge whatsoever of the transaction between the 1st Appellant and the NSSF. He was not challenged on these assertions. How then could he be accused of having sat back and watched with a "**see no evil, hear no evil"** approach? How could he have reported to the Authority violations of the Act, rules and regulations that he was not even aware of?

I hold that the Tribunal erred in respect to the 5th Appellant. In effect it held him strictly liable contrary to the provisions of the Act where strict liability is not provided for. His appeal as far as the sanctions imposed upon him are concerned ought to be allowed. With regard to his costs, I note that his challenges on jurisdiction and procedure have been disallowed by Waweru and Kubo, JJ (and I have already respectfully agreed with the learned Judges in this regard). So, his appeal has only partly succeeded. I therefore propose that the 5th Appellant and the Respondent in Appeal No. 930 of 2003 do bear their own costs of that appeal.

Waweru, J has proposed that the appeals of the 1st, 2nd, 3rd and 4th Appellants be dismissed in their

entirety with costs to the Respondent. I agree.

DATED, SIGNED AND DELIVERED AT NAIROBI THIS 14TH DAY OF MAY 2009

MARY KASANGO

J U D G E