REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA

AT NAIROBI

MICHAEL OYUGI)
TOM OTUCH)
PATRICK NDUNG'U)
PETER KIRAI)

Civil Case 1908 of 2001

(Suing on their own behalf and on behalf of 178 ex-employees)
of Industrial Plant (E.A) Limited) ……..PLAINTIFFS

VERSUS

INDUSTRIAL PLANT (E.A.) LIMITED (in receivership)1STDEFENDANT

GRAHAM SILCOCK ……..2ND DEFENDANT

J U D G M E N T

1. THE PLEADINGS

The plaint herein was dated and filed on 7th November, 2001. The plaintiffswere suing in their personal capacities and also in a representative capacity, onbehalf of the 178 ex-employees of the 1st defendant who had been declared redundant. Representative action had been allowed by the Court on 19th July, 2001 in Miscellaneous Application No. 233 of 2001.

The Plaintiffs pleaded that they were at all material times entitled to remain in the employ of the 1st defendant company. They averred that on or about 1st March, 2001 the 2nd defendant had declared them redundant, and such action was wrongful, and in violation of the conditions for declaring redundancy as provided for under the Regulation of Wages and Conditions of Employment Act (Cap.229). They state that the declaration of redundancy by the 2nd defendant had been done Michael Oyugi & 181 others v Industrial Plant (EA) Limited (in receivership) & another [20061 eKLR without proper notice, and in contravention of the agreement reached between the parties.

The plaintiffs pray that this Court do direct the defendants to comply with the redundancy provisions of the Employment Act (Cap. 226), of theRegulation of Wages and Conditions of Employment Act (Cap. 229), and of the various regulations made under these statutes, and the express and implied terms of the applicable employment agreements.

The plaintiffs assert that by reason of the acts of the defendants, they (theplaintiffs) have been deprived of the benefits they would otherwise have earned, as well as all other entitlements such as

redundancy payment, notice of termination (three months), severance pay (16 days for each completed year of service), cash remunerations for accumulated annual paid leave, travel allowance, overtime allowance, refund of deductions (save for statutory deductions).

The plaintiffs pray for: (i) Payment of all entitlements due; (ii) general

damages; (iii) Costs of this suit, and (iv) interests.

The defendants' joint statement of defence dated 8th January, 2002 was filed on 10th January, 2002.

The 2"d defendant pleaded that he had no ***locus standi*** in this matter as he had no contracts with the plaintiffs or any other employees of 1st defendant, but had at all material times been an agent of the 1st defendant appointed under a debenture, bearing no personal liability. The 2nd defendant stated that he would rely on his Deed of Appointment, and would raise preliminary objections to the suit being brought against him. It is asserted that the 1st defendant ought to be sued in its own name, as it continues to exist in its corporate status. Without prejudice to that statement, the defendants assert, all the workers of the 1st defendant had been duly informed when the company was placed in receivership, that heir contracts of employment were not to be adopted by the receiver; and no formal contract had been entered into with the workers, during the period of receivership. The defendants pleaded that the termination of employment at that time of receivership was effected within the terms of the Employment Act (Cap. 226), and payment in lieu of notice was made to each plaintiff in person. The defendants state that any other benefits which the plaintiffs had earned as at the date of receivership, formed part of the unsecured claims as against the 1st defendant, and the same may be pursued in terms of the provisions of the Companies

The defendants stated the essence of a debenture, which, they assert, accorded protection against the claims in this suit: once a receiver is appointed, the debenture crystallizes over the company's assets; and consequently, all other creditors' claims become subordinate to the claims of the debenture holders.

2. THE PLANTIFFS' CASE: IS IT WRONGFUL TO TERMINATE

EMPLOYMENT CONTRACTS DUE TO INSOLVENCY?

This case first came up for hearing before me on 20th January, 2004 when learned counsel Mr. Shiluli represented the plaintiffs, while learned counsel Mr. Namachanja represented the defendants.

In his introductory address, Mr. Shiluli stated that the dispute was between 185 plaintiffs, on the one hand, and their employer (1st defendant) and a receiver (2nd defendant) on the other hand. The plaintiffs had been employed in various capacities, had served diligently, and had been entitled to varying levels of compensation. The plaintiffs had been served with letters terminating their employment, and then the receiver took over as manager. Several months later their employment was terminated, being paid for only the period they had worked following the notice of termination conveyed in separate letters. So the plaintiffs were now seeking payment to them of their entitlements and dues, general damages, costs, interests.

PW1 was Peter Kirai Gachomba, who was sworn and gave his evidence on 20th January, 2004. He testified that he had been a welder with the 1st defendant company; his employment began in 1963; he worked until 1979 when the 1st defendant was acquired by another company by the name Airduct, though it still retained its original name; the witness received the employer's letter, dated 14th August, 1979, which assured him that the share re-structuring which had taken place, would not affect his status in service. The said letter of 14th August, 1979 was marked plaintiffs exhibit No.

1. The witness' terms and conditions of service did not change. He continued to work for the 1st defendant until February, 2001 when he received a letter from his employer (plaintiffs' exhibit No. 2) dated 9th February, 2001. This was a letter of termination of service, and at that time the witness was paid Kshs.11,579/= (last payslip plaintiff's exhibit No.3). The witness averred that he would have been entitled, at the time of termination of employment, to a payment of Kshs. 900,090/=. He testified that he

had worked for the 1st defendant for a period of 37 years and 6 months, as is acknowledged in a certificate of service made by the 1st defendant, dated 11th January, 2001(plaintiff's exhibit No. 4).

On cross-examination, the witness averred that he had no contract of employment with the 2nd defendant. He testified that while he did not believe his employment could not have been terminated, he was entitled to payment of dues, for the period he had worked.

Learned counsel drew the witness' attention to the termination letter which he had received from the defendant dated 9th February, 2001 (plaintiff's exhibit No 2). The letter reads, in part, as follows:

> *"You are aware that Mr. J.S Ward and myself were appointed joint receivers and managers of [Industrial Plant] on 26th September, 2000 by Stanbic Bank under the power of debentures dated 16th March, 1995, 19th August, 1997 and 17th March 1999 held by Stanbic Bank Kenya Limited.*
>
> *`In my capacity as Agent of the company and without personal liability, I regret to advise you that the company is no longer in a position to make payments to you for services rendered under its contract of employment with you. I regret therefore that there is no alternative but to terminate your services with immediate effect.*
>
> *"Furthermore, as a consequence of the company's insolvency, it is not in a position to pay to you the amounts owed in respect of'your employment prior to the appointment of the receivers, including notice pay and severance pay.*
>
> *These will remain unpaid at this stage and will form part of your unsecured*
>
> *claim against the company.*
>
> *"You will be paid for the days worked between 26th September, 2000 and 9th February, 2001, net of'statutory deductions. Accrued leave for this duration will also be paid to you ".*

When the content of the above letter was put to the witness he remarked that the letter had not stated why other benefits were not being paid to him. He did not think the company had no money and so could not pay his dues. But he testified that he had no knowledge of the company's financial strength.

The witness averred that upon receipt of the termination letter he had no choice but to leave employment; he did not communicate back to the management; he and others, instead, resorted to the Ministry of Labour for a possible solution. The Ministry invited the company's management who, however, failed to attend at a scheduled meeting.

On re-examination, the witness said although he had been paid for his last four months of employment, he had not known how the payment was calculated. He was dissatisfied with the termination of his employment.

PW2, James Ngugi Gathura, was sworn and gave his evidence on 15th June, 2004. He testified that he had been employed by the 1st defendant as an accounts clerk in 1968, and remained in employment for 32 years ending on 28th February, 2001. He was one of 182 employees of the 1st defendant whose service was terminated at the same time.

The witness testified that the 1st defendant had operated on an overdraft with a bank, and although this facility was being serviced the bank had been dissatisfied with the mode of such service; servicing had not been prompt, for the reason that the company was involved in large-scale projects in respect of which turn around time was invariably slow; accessing work by the company was also slow; and liquidity problems were the consequence. The company had an overdraft facility of about Kshs. 170 million with Stanbic Bank (K) Ltd.

According to PW2, the 1st defendant had many projects running; the work force was strong and experienced; the workers did not stand to blame for any shortfalls in the company's business targets; and there was no reason to terminate the employment of the plaintiffs. The workers, apprehending imminent loss of employment, had used their trade union to seek accommodation with the employer; but the employer did not accord them an opportunity to address their concerns. In the end, the plaintiffs' employment was terminated, without notice.

Following the termination of their employment, the plaintiffs took up the matter with the Engineering Workers Union; they also visited the Ministry of Labour; but there was no solution, and this necessitated the filing of suit.

The witness said he was owed by the defendant Ksh.5,477, 697/=, and that the total amount owing to all the plaintiffs was Ksh.30,684,7211=.

On cross-examination, the witness testified that while he had a contract of employment with the 1st defendant, there was no contract between him and the 2nd defendant. He did know, as he testified, that the 1st defendant had been placed under receivership by Stanbic Bank (K) Ltd. and that the receivers had taken possession of the company's premises. He averred that he, like the other plaintiffs, had been given only four months' payment at the time of termination of employment.

PW3, Patrick Mungai Ndung'u testified that he had worked for the 1stdefendant for a period of five years, during which he had taken no leave. His employment was terminated by the receivers on 7th February, 2001 and he was paid for the seven days that he worked in that month. He expressed surprise that the letter terminating his employment had come from "a stranger". He said the employer had accorded him no hearing prior to the termination of employment. His salary per month had been Kshs.10,300, and in addition he had received a housing allowance. He had worked as a fitter, and handled mechanical works involving metal. He testified that he was owed Kshs.87,000/= at the time his employment was terminated. He believed the 1st defendant has lots of work to be done, at the time his employment was terminated.

The witness had been the secretary to the company's branch of the Kenya Engineering Workers Union, and resort was made to this union when the employment contracts were terminated. Through this channel, the plaintiffs met with the District Labour Officer in charge of the Industrial Area, in Nairobi. The defendants were not represented at any of the several meetings which were arranged at the labour office.

On cross-examination, the witness said he had no contract with the second defendant, he did not know how the receiver came to be at the company premises; the letter of termination of employment was signed by the receiver.

PW4 was Peter Oloo Oduor who he testified that he had been employed by Airduct Engineering Company in 1977 as a fitter and welder, but later there was a merger between that company and the 1st defendant, and in 1980 the merger was completed by physical integration. He averred that receivers had taken possession of the company's premises in 2000. the receivers later addressed the workers and indicated that a sum of Kshs.4000/= would be paid to each worker as termination pay, and the workers would then leave employment. At the time the receivers came in, there was an on-going project, and to complete this, the receivers retained the workers until February, 2001 when they were discharged. The workers were asked to report at a counter where each was served with a termination letter, a certificate of service, and pay for the first seven days of February, 2001.

The witness testified that the plaintiffs, upon being served with the termination letters, had sought help from the trade union and from the Labour Office, but to no avail, and hence the filing of this suit. He averred that termination of employment was effected without notice; the plaintiffs were not paid their benefits; even the Kshs,4000/= which had been promised, was not paid.

On cross-examination, the witness said he had first worked with Airduct Engineering, a small

company which later acquired the 1St defendant, and from 1993 the two companies became one single entity; Airduct Engineering ceased to exist, as such. He testified that the receivers announced to the workers, on 26th September, 2000 that they, that receivers, had been sent by the Bank to take over the management of the 1st defendant. The witness did not know the circumstances in which the receivers had come to take over the 1St defendant Company. He said he had had a contract of employment with the 1St defendant; but it is the receivers who terminated his

employment, through formal notice.

3. THE DEFENDANTS' CASE: DO RECEIVER- MANAGERS

HAVE A DUTY TO MAINTAIN EMPLOYMENT CONTRACT

The plaintiffs' case having closed, DWI, Graham James Silcock was sworn and gave his evidence on 22nd June,2005. He testified that, before his retirement, he worked with Price Waterhouse and was involved in the insolvency management of the 1St defendant. He had been appointed as a receiver of Industrial Plant by deed of appointment dated 26th September, 2000. He had been appointed by Stanbic Bank (K) Ltd and his appointment related to a series of debentures. The debenture deed had defined the role of the receivers and had vested in them numerous powers and duties; they had been empowered to operate the business, to safeguard the assets, to sell the assets etc. The witness testified that the business had lost as much as KSh.123 million during the year ended December, 1999; then in the following nine months, before the appointment of the receiver, the company lost another KShs.25milion. The directors had made substantial borrowings from banks KShs.185million from Stanbic Bank; KShs.120million from Banque Indosuez; KShs.40million from Diamond Trust (K) Ltd. The directors had established a steel rolling mill, but this business proved non-viable. In the light of the existing business situation, the receiver wrote a letter to the Ministry of Labour, on 18th January, 2001. the letter reads, in part, as follows;

"Mr. J.S. Ward and [Mr. G. Silcock] were appointed receivers and managers by Stanbic Bank Kenya Ltd. on 26t September.2000. "The company has incurred substantial losses and continues after the receivership appointment to operate at a loss.

"Therefore it is necessary to notify you of an intention to terminate

the contracts of employment of all employees."

Thereafter it became necessary to close the business, and the receiver managers sent out letters of termination of employment to the employees. The witness indicated in the termination letters that the company would remain indebted to

employees but this would be company liability in respect of which the receiver had no personal liability. The witness advised the employees that their dues would now form part of the unsecured claims against the company. He testified that although he had been sued as receiver, he had no liability to the company's creditors including the employees. He asked that the Court do dismiss the claim being made against him. In his belief, the plaintiffs' claim was valid as against the company, but not as against the receiver. He testified that the company had not, at the moment, any source of revenue which was not part of the prior charge by Stanbic Bank (K) Ltd. The

employees were protected only up to the limit of Kshs.4000/=, and any other claim by them would be unsecured.

On cross-examination, the witness testified that he had since 1971, been

involved in receivership functions in Kenya, and when he was appointed a receiver in the instant case, he had been moved by the intent to operate the business, and to make it profitable. For that reason, he had not shut down the business immediately. He continued with existing contracts. At the end of the existing

contracts, he found it necessary to shut down the business. The witness said he had not been put off by the existing borrowing situation in the company. As the company "was so specialized, manufacturing stainless steel for breweries and dairies", it would have been important to secure strategic partnerships to enhance the company's access to new money. This, however, was not a successful endeavour, and so it became necessary to shut down.

When the witness was appointed by deed to be the receiver manager on behalf of Stanbic Bank (K) Ltd, he found that the position of the company's indebtedness attributable to Banque Indosuez was being operated through Stanbic Bank (K) Ltd. Indosuez had at the time, already called in its guarantee, and so the company's debt to Indosuez was already crystallized. The same was true also for the company's indebtedness to Diamond Trust; and thus the company was under attack by three secured lenders.

The witness, upon being appointed receiver manager, conducted an appraisal of the company's state of affairs, and reported to Stanbic Bank (K) Ltd. The report showed that directors of the company denied that many of the assets did belong to the company; the directors insisted that these were not subject to the control of the witness as receiver manager. There was an ownership dispute, with these directors maintaining that the witness had no power to make use of certain machines. This, however, is not the factor which led the witness to close the business; he had dealt with the dispute by asking the protesting directors to come forward with a new partner, to buy those assets which were not in dispute.

The witness testified that at the time of his appointment, there were existing contacts, which were yielding a positive contribution. There were also potential contracts which could have been profitable even though they entailed risks. Such potential contracts could not be taken up, due to the hostility of the directors, and also owing to the fact that the receiver lacked financial resources to undertake new projects. It proved impossible to obtain bonds for the performance of new contracts. Had the receiver, in those circumstances, engaged in such new contracts, he would have been personal liability in respect of the same.

The witness testified that when the receivers sold the company's assets, the proceeds covered no more than the costs of receivership. Many assets had been taken out of the control of the receivers. Stanbic Bank (K) Ltd. had also apparently sold some property, obtaining payments in the order of Kshs. 2 1 milion.

The witness testified that it was entirely reasonable to terminate the plaintiffs'

contracts of employment, in February 2001, because in company law, a receiver

becomes personally liable under contracts unless he repudiates the same. In his view the company could not possibly have remained a float, even if he had not shut down the business: as there were numbers of creditors claiming against the company, its assets would, by now, have been dissipated in litigation and other dispute resolution procedures.

4. WAS THE RECEIVER ENJOINED TO RUN THE BUSINESS? BY CLOSING DOWN, WAS HE IN BREACH OF THE LAW?- SUBMISSIONS FOR THE PLAINTIFFS.

Learned counsel Mr. Kuloba presented submissions for the plaintiffs, on 23rd November, 2005. These were based on written submissions filed on 22nd July, 2005.

The plaintiffs' position was that the 2nd defendant had violated their employment contracts with the 1st defendant; that it is the 2nd defendant who declared the plaintiffs redundant as employees. It is contended that the 2nd defendant, after declaring redundancy, had been in breach of the laws relating to employment the Employment Act (Cap.226) and the Regulation of Wages and Conditions of Employment Act (Cap 229). It was contended that the 2nd defendant had refused to pay to the plaintiffs their employment dues; and that "by the acts of the 2nd defendant, the plaintiffs have been unlawfully deprived of all benefits that they are entitled to under the contract of employment with the 1st defendant, full redundancy pay..... , notice,severance pay at the rate of

16 days for each completed year of service, travel allowances and other allowances as agreed to between themselves and their former employer, the first defendant".

It was contended that the 2nd defendant has also violated the contractual

benefits agreement which had been arrived at between the plaintiffs' trade union (the Kenya Engineering Workers Union) and the 1st defendant: by that agreement the plaintiffs were to receive a further 8% increment to their wages, housing allowances, leave allowance, travelling allowance and others. All these elements, counsel submitted, were to be taken into account during terminations.

Upon those premises, learned counsel made the inferential statement:"Therefore, this suit is brought by the plaintiffs as a result of the 2"d defendants violation of all their entitlements while acting in disregard of the law as a receiver".

Learned counsel, however, did not make submissions on the specific principles of law which, in these circumstances, would guide a receiver. Suppose the receiver was not a receiver but a purchaser.- would he have the duty to render all the claimed benefits to the plaintiffs? Does the company, for the purpose of fulfilling employment contract claims, continue to bear its responsibilities in the same manner, whether the company passes on to new shareholders or to a receiver manager? This is an important point of law which should have been canvassed by counsel.

Mr. Kuloba blames the 2nd defendant in particular, for the alleged violation to the plaintiffs' legal rights. The reason: "had the 2'"d defendant not ... come and interfered with the smooth running of the Pt defendant company's activities, they would still be in employment as per their contracts with the 1st defendant". This is, with respect, a very conjectural argument. As the plaintiffs did not dispute the fact of the 1st defendant's very substantial indebtedness, they cannot very well maintain that such a company would always remain in business. Secondly, learned counsel's contention runs against the principle contained in the law of debentures. Debentures constitute the core capital upon which a company's business operations are founded.

The claims of the debenture holders have priority over other claims, during receivership. It has not been argued for the plaintiffs that the debenture holders had no right to appoint a receiver; and if they had that right, then the plaintiffs' claims would in law, and perforce, be relegated to secondary status in relation to the claims of the debenture holders. I think the testimony of DWI forms the strongest evidence on record: that the 1st defendant company had become so debt- ridden that it had no chance of survival. That must mean that, sooner or later, all employees of the 1st defendant would lose their jobs.

Learned counsel submitted that even assuming the business of the 1st defendant company was properly shut down, the employees were entitled to their dues in accordance with the contract of employment. He further urges: "It is only parties to a contract that can move to determine the same and not one who is not privy to it. [The] second defendant not being privy to the contract [which] the plaintiffs had with the 1st defendant, interfered with the same and has caused the plaintiffs untold misery". It is not clear, however, what legal point, or what cause of action is here in reference. Contract, it is well known, is a cause of action only to those privy to it. So, is there a new cause of action referred to as "stranger interfering with contract which binds the parties"? This has not been argued; and so the contention is, in my view, no more than a general grievance which hardly fits into the juristic templates.

Mr. Kuloba submitted that the appointment of a receiver manager was not properly done: because there was no "demand prior to [the] appointments"; "there is nothing before this Court to show that the defendants and more so the first defendant received a formal demand of payment of the outstanding debt from the debenture holder". Counsel argued that the requirement for such a demand was stated in an English case which however, he did not attempt to analyse ***Cripps (Pharmaceuticals) Ltd. V. Wickenden [1973]*** 1 WLR 944. Counsel urged that the appointment of receivers in that case was found to be "premature and not in the interests of the company nor its employees."

Learned Counsel cited Halsbury's Laws of England 4th ed , vol. 39 (para 805) to support the

proposition that a receiver may be liable in tort, as a trespasser, where his appointment is defective. I have read the said para.805, it states:

> ***"Prima facie a receiver appointed out of court, being an agent only, is not personally liable in respect of transactions properly entered into by him as a receiver. However, if a receiver gives his personal promise to pay a debt for which his principals may become liable, he is bound by the promise A receiver may be liable in tort as a trespasser wherethe appointment is defective ..."***

Mr Kuloba submitted that the appointment of the 2nd defendant as receiver was defective, and so he had become a trespasser and should be held liable to the plaintiffs. Learned counsel grounded the plaintiffs' prayers on a certain factual foundation which, in my view, had little evidence in support: firstly, that at the time the receiver was appointed, "the 1St defendant company was running a lucrative contract and had other pending contracts ... which would have fetched it approximately Kshs.886, 257,008 by the end of February 2001 "; and secondly, that the 2nd defendant asreceiver had been guided by the "intent to ground the company". Such a claim is set against the more detailed evidence led for the 2nd defendant, which is to the effect that the 1St defendant was shouldered with an almost suffocating debt burden which could not be disposed of in the normal course of business. Moreover, evidence was tendered for the defendants, that the receiver was unable to take on certain production contracts since the directors of the 1St defendant objected to the use of certain assets and equipment in the production process.

Which is the more cogent position, as a matter of law: that the receiver desisted from carrying on with certain contracts, and so caused the plaintiffs to forfeit their economic interests and attendant legal rights? Or that the debenture holders had rights crystallized in law, once the 1St defendant was overwhelmed by debt, to designate receivers with wide powers including the power to terminate the business? The claim of the plaintiffs, on a generous construction, could very well be linked to legitimate interests; but that of the debenture holders would, I belive, be founded on definite, accrued legal rights.

In learned counsel's submissions, the debenture holders did something improper, in appointing a receiver when their debts went unpaid. In the words of counsel, "reasonable opportunity was not accorded to the 1St defendant by the

debenture - holder acting [hand in- glove] with the 2nd defendant to see through its contracts..... " Counsel attempted to substantiate this hypothesis by a certain construction of the evidence of DW1: "[DW1]... clearly exhibited his lack of enthusiasm [in running the business]. This was revealed [in the] cross-examination when he stated that he feared making losses. [Yet] business is all about profits and

losses. One cannot enter a business without taking a risk."

I have had difficulty with such a construction, bearing in mind the basic principles relating to debenture holding. Debenture holders have committed their capital, to form the foundation for the life of the business. The debenture holders are, in return for their very substantial resource risk, accorded legal protection; they have a legal right to appoint a receiver when they are faced with grave risks of loss of their capital investment. So at that stage, their interests have priority over other claims especially claims founded on assumptions of continuing, buoyant business. I am not, therefore, in agreement with learned counsel's submission that the 2nd defendant, that's the receiver,

had acted as "a messenger of doom [towards] the 1st defendant and subsequently, [towards] the plaintiffs".

Although Mr. Kuloba raised the issue of lack of good faith on the part of the 2nd defendant as receiver, relying on the work by Sir Gavin Lightman and Gabriel Moss, entitled The law of Receivers and Administrators of Companies (London: Sweet & Maxwell, 2002) (pp.146-147), he did not draw the Courts attention to any specific legal doctrine on the point, nor did he attempt to relate his contention such squarely to any concrete evidence adduced by any of the plaintiffs' witnesses. Good faith, of course, is required of all persons acting in something like a trust or fiduciary position. Sir Gavin Lightman and Gabriel Moss have thus stated in their above cited work (p.147):

"Breach of the duty of good faith involves something more than negligence: it requires some dishonesty, or improper motive, someelement of bad faith, to be established. Reckless indifference to the rights or interests of others or shutting one's eyes deliberately to the consequences of one's actions may suffice to establish dishonesty or bad faith. In judging whether the mortgagee or receiver were acting in good faith in deciding how best to serve the interests of the mortgagee ...if the decision lay outside the range which the court thought might be arrived at by a reasonable commercial man, this might provide some evidence that the decision was not taken in good faith."

As learned counsel did not analyze the evidence led for the defendants in the context of the principles of law thus stated, I am, with respect, unable to agree with his contention that the 2nd defendant had acted in departure from the "duty to act in good faith and for proper purposes" in counsel's words.

Mr. Kuloba submitted that the 2nd defendant upon being appointed a receiver by the debenture holder, had stepped into the shoes of the company directors, and had consequently adopted the employees' contracts of employment, which he ought to have honoured in every respect. Counsel submitted that the termination of the employees' contracts amounted to wrongful dismissal, in respect of which the 2nd defendant should be required to pay damages.

5. IS A DULY APPOINTED RECEIVER PERSONALLY LIABLE?

WHAT IS TO BE DONE WITH REGARD TO UNSECURED CREDITORS? SUBMISSIONS FOR THE DEFENDANTS

Learned counsel Mr. Namachanja stated the pertinent issues in this dispute as

follow:

(i) Were the receivers validly appointed under valid debentures?

(ii) Is a validly appointed receiver personally liable for actions

authorized under the debenture?

(iii) What is the state of the law, as regards creditors not secured, in

receivership?

Learned counsel submitted that the receivers were duly appointed, in accordance with the law. They were appointed under debentures dated 16th March, 1995, 19th August , 1997 and 17th march,1999. These debentures were properly executed and were duly registered, and their validity has not been in dispute. These debentures secured the principal sum of KShs.300,000,000/= together with interest accruing. The debenture holders had the liberty to define the terms of reference of any person appointed to serve as receiver and manager. The appointment took place after the principal monies became payable, but the company failed to pay the same with interest.

Learned counsel relied on a passage in Gravin Lightman and Gabriel Moss, The Law of Receivers and Administrators of Companies (London: Sweet & Maxwell, 1986) (p.49):

"A receiver must be appointed in accordance with the terms of the debenture."

He noted that the 1995 and 1997 debentures, by their respective clause No. 18, had given power to Stanbic Bank (K) Ltd to appoint the receiver in writing, and the 1999 debenture gave the power to appoint a receiver by its clause No.20. The 1995 and 1997 debentures by their respective clause No.14 and the 1999 debenture by its clause No. 18, stated that the principal money and interest secured, immediately became payable without any demand or other notice of any kind if the amount payable was not paid on

the due date and such was the case herein. Counsel submitted that as the deed of appointment was done in writing, as required by the debentures, the receivers were validly appointed, under valid debentures. Consequently, Mr. Namachanja submitted, there was no need for a demand or a notice, prior to the appointment of receivers.

Learned counsel relied on Hubert Picarda's work, The law Relating to Receivers, Managers and Administrators 3d ed (London: Butterworths, 2000) to

demonstrate that no obligation had been placed on the debenture holders to lodge a

demand, or give notice before appointing receivers (pp. 78 - 79):

> ***"A moot point is whether a formal demand for payment of money due is a vital step in the procedure to be followed prior to the appointment of a receiver. Certainly there are dicta in Windsor Refrigerator Co. Ltd v. Branch Nominees Ltd. which suggest that before an appointment can be made there must be a demand, even though no such requirement was in fact specified in that case. And the Court of Appeal seems to have been prepared to import such a requirement.***
>
> ***But no persuasive reason has been suggested for importing a demand***
>
> ***as a prerequisite to the validity of an appointment. Of course express words may make a demand a crucial element in the appointment of a receiver. But in the absence of express words requiring a demand to be made the necessity of demand should not be implied.***
>
> ***"An example of a case where express words made it clear that a demand was de rigueur before a receiver could be appointed was Cripps (Pharmeceuticals) Ltd V. Wickenden (1973) WLR 944. There the debenture contained a clause making the money repayable on demand. Goff,J held that a demand was essential before the right to***
>
> ***appoint a receiver arose"***

Although learned counsel for the plaintiffs had also attempted to rely on the same case, I think the full picture thus emerging from the relevant passage is more in aid of the defendants' case. Mr. Namachanja remarked, I think quite properly, that the debentures in the instant case, by express words, state that no demand was necessary prior to the *appointment of receivers*. He concluded, I believe correctly, that the receivers were validly appointed under the debentures.

Counsel submitted that a validly appointed receiver would not become personally liable for actions which have been authorized under a debenture. This is because a receiver is an agent of the company and so his actions bore the face only of the corporate body. The relevant principle is thus stated in Raymond Walton (ed), Kerr on the Law and Practice as to Receivers, 16th ed, (London: Sweet & Maxwell, 1983) (pp. 303 - 304):

> ***"Debentures and debenture trust deeds usually provide in express terms that the receiver is to be agent for the company, as in the case of the statutory power. Sometimes this provision is omitted and in such cases it may be inferred from the terms of the instrument that the receiver is agent for the debenture holders, as, for instance, where he is given the power to carry on the business or other powers largely in excess of those conferred on receivers by statute. When this is the case, the debenture holders will be themselves personally liable to persons dealing with the receiver, and also to the receiver for his***
>
> ***remuneration,"***

It had been expressly stated in clause No. 19 common to both the 1995 and 1997 debentures, and in clause No. 21 of the 1999 debenture, that the receivers

appointed were to be the agents of the company, which alone would be liable for acts of the receivers including "(g) to appoint dismiss and remove managers accountants workmen servants and agents upon such terms as to remuneration or otherwise as the receiver may determine".

Learned counsel submitted that as the plaintiffs were employees of Industrial Plant (E.A) Limited the 1st defendant a validly appointed receiver could not bear personal liability for having terminated their employment contracts. Counsel submitted that if the plaintiffs could prove that they had been wrongfully terminated in their employment, then only the company would be liable to them and in that case they would recover from the company's assets, as unsecured creditors. it was submitted that there was no basis for legal action against the 2nd defendant. In a recent decision of the High Court, Block Management Limited & Others vs. Njeu [2003] LLR 2489 Njagi, J had thus held:

"A receiver owes a duty of care to his debenture holder, a limited duty

of care to the company and a statutory duty of care to the preferential

creditors. He owes no duty to ordinary unsecured creditors..... "

On this principle, Mr. Namachanja submitted that the 2nd defendant had owed no duty of care to unsecured creditors such as the plaintiffs herein.

I have earlier queried the evidentiary basis upon which counsel for the plaintiffs contended that the company (1St defendant) had been poised for profitable enterprises, if only the receivers had been prudent enough to give a chance for new business ventures. Learned counsel for the defendants has challenged the plaintiffs' proposition on an issue of law. He submitted that the correct position in law, is that a debenture holder "can take whatever action ... available to it under the debenture, regardless of loss to the company or to unsecured creditors". This position is consistent with the Court of Appeal decision in Madhupaper International Limited vs. Paddy Kerr & Three Others, Civil Application No. Nai. 116 of 1985:

"The Bank ... maintains 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':

Counsel submitted that the plaintiffs could not be heard to claim that the receiver had acted improperly, in not undertaking alleged lucrative contract opportunities - because the receiver bears no duty of care toward unsecured creditors; and because the debenture holder owed no duty of care toward third parties.

Learned counsel submitted, I think on cogent grounds, that the suit against the 2nd defendant is misconceived and based on a mistake of law. Mr. Namachanja also made submissions on the position of an unsecured creditor, in conditions of receivership. He stated, quite correctly I believe, that the plaintiffs as unsecured creditors must rank well behind the debenture holder along with other unsecured creditors. By common clause No. 20 of the 1995 and 1977 debentures, as well as clause No. 22 of the 1999 debentures the receiver, after realizing the security shall apply the assets to the payment of his costs and expenses, to the payment of all principal moneys and interest due to the debenture-holders, and finally any surplus to the company and to any persons entitled thereto.

Counsel submitted that the plaintiffs, as unsecured creditors, are not preferential creditors. S. 95 of the Companies Act (Cap. 486) defines preferential creditors as those who are entitled by virtue of the provisions set out in Part VI of the Act, the relevant section being S. 311 whereunder the preferential payments are wages and *salaries for any service rendered to the Company during the four months ensuing since appointment of the receiver*. Since it is not in dispute that such payments were indeed made, counsel submitted, it followed that the claim in the suit is not in respect of the preferential payments

under the provisions of SS. 95 and 311 of the Companies Act (Cap.486).

Learned counsel submitted that since the plaintiffs' claim for terminal benefits for wrongful termination of employment, would not fall under SS.95 and 311 of the Companies Act (Cap. 486), even were the suit to be successful a judgment entered against the 1st defendant would not elevate the plaintiffs to the status of secured creditors. In the Court of Appeal decision in Nyayo Bus Corporation vs. Firestone E.A (1969) Ltd. [1998] LLR 780 it was held:

> ***"Mr.Kipkorir advanced another argument, that is, that the respondent became a preferred creditor upon judgment being entered in its favour. A judgment debt, as opposed to a secured debt, [takes] nopriority. It remains an unsecured debt".***

Also relevant in that regard is the High Court's decision in Setright Kenya Ltd. vs. Kenya Co-operative Creameries Ltd. [1997] LLR 2074 (CCK). Ombija, J in that case remarked:

> ***"It was also Mr. Maingi's contention that the rights of the debentureholders take precedence over the judgment herein. In this regard, I was referred to Sections 95 and 311 of the Companies Act (Cap. 486)... I have analysed the said sections and in my considered view, the position taken by Mr. Maingi is the correct one in law':***

Learned Counsel submitted, quite correctly, with respect, that an unsecured creditor will only recover after the debenture- holder has recouped his principal amount aand interest. The unsecured creditor, therefore, can only recover from the surplus available. Counsel submitted that the plaintiffs cannot succeed against the 2nd defendant.

6. FINAL ANALYSIS, AND DECREE

There is no doubt that the 1st defendant had been operating on very substantial capital debts, thanks to the debenture holders. Although it has been contended for the plaintiffs that the 1st defendant did have considerable scope for strategic business arrangements which could possibly turn in much profit, it is not denied that the 1st defendant's debt commitments had not been met, and that it is in these circumstances that the 2nd defendant was brought in as receivers, under the terms of several debentures.

I have not been convinced by the plaintiffs that the debentures, in terms of form and content, were anything but proper, nor that these debentures did not lay out a clear framework of legal competence for the appointment of the receivers; nor that the debenture holders had not subsequently appointed receivers in writing as required; nor that the appointment of the receivers was not done within the law.

The upshot is that there are two main issues in dispute:

a. Was it right in law for the receivers to close the business, rather than pursue the strategic business opportunities in sight and thereby,

possibly, keep the enterprise running?

(ii) Even if the receivers had to shut down the business, was it right in

law for them not to meet the employees' contractual claims which had already accrued as against their employer, namely the 1st defendant?

It is clear from the authorities, notably Madhupaper International Ltd v Paddy Kerr & Three others, Civil Application No. Nai 116 of 1985; Nyayo Bus

Service Corporation v Firestone E. A (1969) Ltd. [1997] LL.R. 780 (CAK);

and R. Walton (ed), Kerr on the law and Practice as to Receivers, 16th ed

(London: Sweet & Maxwell, 1983) (88. 303-304), that receivers derive their terms of reference from the content of the debenture deed; and it is thus not right in law to maintain that receivers are always under duty to explore strategic business opportunities and to pursue the same; indeed if they did, they would be agents of the debenture holders who would in consequence bear liability for the legal incidents flowing from the new businesses undertaken. It is thus the

responsibility of the debenture holders to determine the content of the debenture deed, as well as the scope available to the receiver in respect of new business opportunities.

It follows, in my judgment, that there rested no legal duty upon the 2°d defendant herein, to keep the company's business afloat at all cost.

From the authorities, notably ***Block Management Limited & Others v Nje***u [2003] LL.R.2489; ***Madhupaper International Limited v. Paddy Kerr & Three Others,*** Civil Application No. Nai 116 of 1985; Nyayo Bus Service Corporation v. Firestone E. A. (1969) Ltd. [1998] LL.R.780 (CAK); and Setright Kenya Ltd. v. Kenya Co-operative Creameries Ltd. [1997] LL. R. 2074, it is clear that the receivers in this case, once appointed, had their primary responsibility to the secured creditors. The order of responsibility could not be reversed to obligate the receivers to preoccupy themselves with the interests, or indeed even the legal rights, of the plaintiffs. It is, I would add, not as though such legal rights were immaterial; but only that they were to take a secondary level of priority, and stood to be satisfied only after the secured claims had been met.

I have to hold, therefore, that the 2nd defendant had no legal liabilities towards the plaintiffs, and ought not to have been enjoined in the instant suit.

Now although the suit was filed against the two defendants, the plaintiffs' pleadings, evidence and submissions have been aimed squarely at the 2"d defendant alone. The effect is that in this suit, hardly any case has been made against the 1st defendant. It follows that no case has been made against either defendant. I will, therefore, dismiss the whole suit, with costs to the defendants.

Orders accordingly

DATED and DELIVERED at Nairobi this 10th day of February 2006.

J. B. OJWANG

JUDGE

Coram: Ojwang, J

Court Clerk: Mwangi

For the Plaintiffs: Mr. Shiluli; Mr. Mbugua; Mr. Kuloba instructed by M/s.

Khaminwa & Khaminwa Advocates.

For the Defendants: Mr. Namachanja, instructed by M/s. Walker Kontos Advocates.