REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT

MILIMANI COMMERCIAL COURTS, NAIROBI

HCCC 524 OF 2004

AFFORDABLE HOMES AFRICA LIMITED……..PLAINTIFF

V E R SUS

HENDERSON ……..…1ST DEFENDANT

SUPERIOR HOMES (KENYA)LTD……..2ND DEFENDANT

MICHAEL KLESH…….3RD DEFENDANT

R U L I N G

In the application before the court, the plaintiff/applicant seeks injunction orders against the defendants. The application is brought by way of a chamber summons dated 28th September, 2004 and expressed to be brought under O.XXXIX Rules 2, 2A and 9 of the Civil Procedure Rules and section 3A of the Civil Procedure Act, and the inherent powers of the court.

To that application, the defendants, through their counsel, filed notice of a preliminary objection on the 6th October, 2004. It was this objection which was heard before me on 7th October, 2004. The objection is based on the grounds thatwww.

(a) The suit is bad in law and incompetent and the same ought to be struck out with costs.

(b) The verifying affidavit is incurably defective and incompetent and consequently the same ought to be struck out.

(c) The supporting affidavit of Seth Steven Okuthe is inadmissible in law and the same should be expunged from the record.

(d) The application is incompetent and bad in law and the same ought to be struck out.

(e) Other grounds and reasons as may be adduced at the hearing thereof.

During the oral canvassing of the preliminary objection, Mr. Angima appeared for the defendant/applicant while Mr. Oluoch- Olunya appeared for the plaintiff/repsondent. Mr. Angima argued that authority to institute court proceedings in the name of the company is vested in the board of directors, or should be effected through a resolution of the shareholders in a general meeting. He therefore submitted that it was improper for one director to file a suit in the company's name without such authority. As there was no such authority in the instant case, he maintained, the suit was improperly filed and therefore incompetent.

He then referred the court to paragraphs 3 and 4 of the replying affidavit of IAN HENDERSON and also paragraph 4 of the supporting affidavit sworn by RAYMOND H. CHISHOLM. The averment by Mr. Henderson to the effect that no resolution was passed authorizing the institution of the suit had not been contraverted. Counsel further argued that no resolution of the Board of Directors or shareholders at a general meeting had been exhibited, and thereupon submitted that in those circumstances, the action brought by one of the directors without authority was incompetent and ought to be struck out. He then referred the court to T**RADE BANK LTD.**(In liquidation) v. **L.Z. ENGINEERING CONSTRUCTION LTD. & ORS**, Civil Appeal (application) No. 14 of 1998, **BUGERERE COFFEE GROWERS LTD. v. SEBADUKA & ANOR**. [1970] E.A. 147 and also **JOHN SHAW AND SONS (SALFORD) LTD. v. SHAW** [1935] K.B. 113

Mr. Angima also submitted that if the company did not authorize the suit, then the verifying affidavit is incompetent for lack of authority. The same argument applies to the two supporting affidavits, and for this reason they are equally invalid. He therefore submitted that the suit, as instituted, cannot stand but ought to be struck out with costs.

The application is opposed. In his response, Mr. Oluoch-Olunya for the plaintiff argued that it was not disputed that Mr. Raymond Chisholm holds 75% of the shares in the company which constitutes not just a simple majority but a special majority. By virtue of this fact, counsel submitted, the company would be entitled to commence action at the instance of such a shareholder. He then referred the court to **EAST AFRICA GENERAL INSURANCE CO. LTD. v. EAST AFRICA GENERAL INSURANCE CO. LTD**. [2201] 1 E.A. 31 and submitted that even though the court could stay an action to allow a meeting to be held, if you have a majority, it is not necessary to go back to a general meeting and necessarily get a resolution. In that case, the court need not make any further inquiry. He further submitted that it was not practicable to obtain this resolution as the cause of action is against one of the directors of the company who is in breach of his fiduciary duties to the company, and the remedy sought is to restrain him from proceeding with his breach of duty to the company. Any general meeting would have to be called by at least 21 days notice. Counsel then referred to paragraph 1171 at page 875 of Volume 7 (2) of Halsbury's Laws of England, 14th Edition, 1996 Reissue and submitted that it was not open to the director/respondent to raise the issue of lack of a resolution. He also referred to **TRADE BANK LTD. v. L.Z.ENGINEERING CONSTRUCTION LTD. & ORS.** (Supra) and also **RAI & ORS v. RAI & ORS**. [2002] E.A. 537 and submitted that the remedy being sought herein is an equitable remedy. Consequently, he further submitted, the court has very wide ranging discretionary powers to look into the matter and allow the suit to be continued without a board resolution. In so doing the court should exercise its discretion judicially.

In reply, Mr. Angima submitted that although an action may be brought by a majority even where the directors object, they must call a meeting first. In the instant case, however, no meeting was called and therefore even a majority cannot avail themselves of that option. Secondly, the proposition by the respondent to this objection that a majority does not need to pass a resolution is not supported by any authority. He has also not sought the matter to be stood over to facilitate a meeting of the shareholders, but instead has said that there need not be further investigation as the director who came to court is a majority shareholder. Finally, counsel submitted that a practical difficulty, e.g. the giving of 21 days notice before a meeting can be held, is not a good reason for not obtaining a resolution. He thereupon urged that the action be struck out and that the advocates who instituted it pay the costs personally.

After hearing the rival submissions of both counsel, I am constrained to observe that this is basically a case of a company against one of its directors for the alleged breach of a fiduciary duty. Directors owe their fiduciary duties to the company. In the event of any breach of those duties, therefore, the company and the company alone, is the only proper plaintiff that can sue to redress the wrong. This was the decision in the case of **FOSS v. HARBOTTLE** (1843) 2 Hare 461, one of the landmark cases in corporate management.

As an artificial person, however, a company can only take decisions through the agency of its organs, which are primarily the board of directors or the general meeting of its shareholders. One of these should therefore authorize the use of the company's name in litigation so that the company can properly come to

court and enforce a breach of a director's duty. As to which of these two organs should give the necessary sanction depends, in the case of registered companies, entirely on the construction of the company's articles of association. In **AUTOMATIC SELF-CLEANSING FILTER SYNDICATE v. CUNINGHAME** [1906] ch.34, C.A., it was held that where a company's powers of management are, by the articles, vested in the board of directors, the general meeting cannot interfere in the exercise of those powers. It is therefore necessary to examine a particular company's articles of association to ascertain wherein lies the power to manage the company's affairs, for therein also lies the power to sanction the commencement of court actions in the name of the company.

A re-visit of the plaintiff company's articles of association shows from the very outset that article 1 thereof states-

> **"The regulations contained in Table A in the First Schedule to the Act shall not apply to the Company."**

This means that the Articles of Association registered by the plaintiff company are a self contained code of regulations for the company, and operate to the exclusion of the provisions of Table A altogether. Consequently, the plaintiff company will stand and/or fall by those articles unless and until they are altered.

With regard to the powers and duties of its board of directors, article 94 of the plaintiff's articles of association is in the following words-

> **"The business of the company shall be managed by the Board which… may exercise all such powers of the company as are not by the Act or by these Articles required to be exercised by the company in general meeting…"**

This article is substantially identical with article 80 of Table A in the First Schedule of the Act and will therefore receive the same judicial interpretation as the said article 80. From **QUIN & AXTENS Ltd v. SALMON** [1909] AC 442 HL and subsequent cases, it seems to be well settled that where the formula in article 80 is employed, the general meeting cannot interfere with a decision of the board of directors unless they are acting contrary to the provisions of the Companies Act or the company's articles of association. This view was adopted in **SHAW & SONS (SALFORD) LTD. v. SHAW** [1935] 2 K.B. 113, C.A in which Lord Justice Greer reiterated, at page 134 –

> **"…If powers of management are vested in the directors, they and they alone can exercise these powers…"**

Since article 94 of the plaintiff's articles of association is in pari material with article 80 of Table A, it follows that the power to manage the plaintiff company's affairs is vested in its board of directors and they alone should authorize the commencement of court proceedings in the company's name.

It is common ground that in the instant suit, there was no authority from the Board Directors to institute this suit. In paragraphs 3 and 4 of his replying affidavit, the first defendant, Mr. Ian Henderson, avers-

> **"3. That I am a director of the plaintiff company herein and I swear of my own personal knowledge that prior to the institution of this suit, no meeting of the board of directors was held and consequently no resolution was passed authorizing the firm of Oluoch-Olunya & Company, Advocates to institute this suit in the name of the Company.**
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> **4. That I am advised by my said advocates, which advice I hold to be true, that both the verifying affidavit and the supporting affidavit are incompetent as the same were sworn by the said Raymond Hugh Chisholm without the authority of the company."**

These averments have not been controverted in any way. As if to confirm that there was indeed no resolution of the board, Mr. Chisholm says in paragraph 3 of his verifying affidavit-

"That I have instructed the firm of Oluoch- Olunya & Co. Advocates to institute this suit on our behalf and to conduct proceedings thereof."

Clearly, it was Mr. Chisholm, the managing director and principal shareholder of the plaintiff company who gave instructions for commencement of this suit in the company's name rather than the company itself. In so doing, the managing director usurped the powers of the board, and that is irregular. In the case of **SHAW & SONS (SALFORD) LTD. v. SHAW** (supra) , Greer L.J. said in relation to this aspect of the law-

"A company is an entity distinct from its shareholders and its directors."

Even a majority shareholder therefore, is not and cannot purport to be the company. His votes alone may ensure the passing of an ordinary resolution, or even a special resolution, which would constitute an act of the company. But until then, the company cannot be said to have acted in a particular manner merely because that is the intention of the majority shareholder. His wishes remain wishes unless and until they are translated into an act of the company by an appropriate resolution at an appropriate forum.

Counsel for the plaintiff submitted that since the managing director holds 75% of the company's share capital, the court need not make further enquiry. I agree with counsel for the defendant that no authority was cited for such a proposition. Indeed, with respect, so to hold would set a very dangerous precedent as it would amount to relegating the company to the status of an alias for the majority shareholder. Such a view was rejected in **SALOMON & CO.LTD. v. SALOMON** [1897] A.C. 22 H.L., which is the very foundation of modern company law. If such a view were to hold sway, there would be nothing to prevent a majority shareholder from getting up any morning and undertaking all manner of actions in the company's name with an utter contempt to the interests of the other shareholders. Even if the minority are certain to be out voted, it is their right to vote.

The upshot of these considerations is that in the absence of a board resolution sanctioning the commencement of this action by the company, the company is not before the court at all. For that reason, the preliminary objection succeeds and the action must be struck out with costs, such costs to be borne by the advocates for the plaintiff.

Dated and delivered at Nairobi this 27th day of October 2004

L. NJAGI

JUDGE