REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

CIVIL CASE NO 918 OF 1999

HOUSING FINANCE COMPANY OF KENYA LIMITED.....PLAINTIFF

VERSUS

PALM HOMES LIMITED .....1ST DEFENDANT

MOHAMED ALI MADHANI .....2 ND DEFENDANT

PULIN SHAH.....3RD DEFENDANT

JUDGMENT

The plaintiff in this suit claims a sum of Kshs 10,762,978.88 and interest at the rate of 29% per annum from the three defendants jointly and severally. The interest is claimed from 17th February 1999.

The first defendant is a corporate entity while the second and third defendants are individual male adults. By an instrument made in writing on 25th August 1997, the plaintiff agreed to offer the first defendant the sum of Kshs 13,300,000/= upon the terms and conditions contained in the said instrument and the first defendant accepted the plaintiff's offer. As a security for the loan, the first defendant executed a charge mentioning properties known as LR NO 2951/274; LR NO 2951/275 and LR NO 2951/276, Farasi Lane, Lower Kabete Nairobi, in favour of the plaintiff. The first defendant said that the properties belonged to it.

On the other hand, the second and third defendants who were said to be Co-Directors of the first defendant acted as sureties to the first defendant and guaranteed the repayment, to the plaintiff, of the principal sum, interest and other monies which may at any time be outstanding on the account of the first defendant. To that effect the second and third defendants gave the plaintiff their written personal guarantee that they will be personally responsible for the loan.

The first defendant failed to repay the loan as agreed and has continued in the said default. The second and third defendants are said to have also failed to honour their guarantee and their obligations as sureties under the mortgage contract, and failed to pay the plaintiff the outstanding sum as sureties for the first defendant. As a result, the plaintiff in exercise of its statutory power of sale over the charged properties advertised the sale of the properties by public auction, and sold the properties in a public auction held on 17th February 1999 for Kshs 9,000,000/= leaving a shortfall of Kshs 10,762,978.88 as at that date. That shortfall is the sum of money the plaintiff is now claiming from the defendants in this suit. Since it is the first defendant who was to be served with a statutory notice, and that defendant is not complaining, the complaint of the second defendant on the issue of a notice has no basis and I will not take my time on that complaint.

The first and third defendants have not cared to defend themselves and as a result judgment has already

been entered against them as prayed in the plaint.

It is the second defendant who filed his defence and is defending himself in these proceedings before me. The plaintiff's application for summary judgment against the second defendant was dismissed by my learned brother Kasanga Mulwa, J on 14th March 2000. In his amended defence dated 21st January 2000 and filed on 24th January 2000, the second defendant raises five issues in his defence. Firstly, he says that he was only a nominee of the third defendant and not a substantive director of the first defendant. He avers that at the time of entering into the loan arrangement set out in paragraph five of the plaint, the plaintiff was duly notified in writing by the second defendant that the second defendant was merely a nominee and an agent of the third defendant and that it was agreed with the plaintiff that the second defendant would execute the documents pursuant to the said arrangement only as a nominee director and/or agent and that no personal liability would attach. He avers further that it was only after receiving representation from the plaintiff in that respect that he executed the purported guarantee. The second defendant, therefore, disclaims personal liability in respect of the loan; and alternatively and without prejudice to the foregoing, contends that if there was any personal liability attaching to him with respect to the said arrangements, such liability would only be such as would attach to a disclosed agent of a disclosed principal and puts the plaintiff to a strict proof of allegations to the contrary.

Secondly, the second defendant raises the issue of estoppel stating that the plaintiff having been made aware of the second defendant's role as an agent of the third defendant in the matter right from the beginning and having acknowledged and/or approbated that position, the plaintiff is now estoppel from attaching personal liability to the second defendant.

Thirdly the second defendant raises the issue of lack of consideration stating that his purported guarantee was void *ab initio* for lack of consideration.

Fourthly the second defendant raises the issue of the Plainitff's failure to pursue its remedies against the first defendant, as the principal borrower, on its default, timely and with diligence. He claims that, that led to accumulation of interest on the first defendant's account. He avers that by that conduct on the part of the plaintiff, the second defendant's purported guarantee was discharged. He further avers that the purported guarantee was also discharged following the plaintiff's failure to adhere or stick to the conditions precedent to which the purported guarantee was issued.

Fifthly the second defendant raises the issue of under value. He alleges that the plaintiff sold the charged properties at gross under value and further failed to exercise due care in the sale of the said properties resulting in the shortfall referred to therein. He contends that had the plaintiff exercised due care in sale of the said properties, it would have recovered in full and without any shortfall.

On the basis of those issues, it is the second defendant's case and he contends that the plaintiff does not have any cause of action against him and that the amount claimed, Ksh 10,762,978.88, or any other sum, in the plaint is not due from him and, therefore, the plaintiff's suit against the second defendant herein be dismissed. The plaintiff does not agree.

Briefly, what I have set out above is the position on each side. Mr Ahmednasir appeared for the plaintiff while Mr Herit Sheth appeared for the second defendant. Subsequent to the taking of evidence in this suit, Mr Ahmednasir and Mr Herit Sheth filed their respective written submissions which give me the impression that the two advocates concentrated on the issue of the liability of the second defendant as a guarantor and or nominee/agent under a guarantee he entered into starting with the loan application letter dated 27th June 1997. I will take what they have said into account and I am very grateful. While I will discuss all the five issues raised in the case as stated above, the sequence of handling those issues will not necessarily follow the sequence in which I have mentioned them. This is because of the way I propose to conclude this judgment. Accordingly, I will start with the issue of estoppel.

I do not find any dispute between the parties as to whether the plaintiff on one part and the defendants on the other, executed a charge dated 25th August, 1997 under which the first defendant was advanced the sum of Ksh 13,300,000/=. But it is from the execution of that charge that the estoppel the second

defendant is relying upon emanates. He says that at that time the plaintiff was made aware of the role the second defendant was playing as an agent of the third defendant and that the plaintiff acknowledged that role, the plaintiff or its then lawyer M/s AGN Kamau and Kimani Advocates, agreeing that the second defendant was to execute the charge as a nominee of the third defendant, and that no personal liability was to be attached to the second defendant. He explained that the representation he refers to in paragraph four of his amended defence is the response he got to his letter dated 24th July 1997. He said that by that response the plaintiff accepted him to sign documents as a nominee or agent of the third defendant.

Although the second defendant produced his letter dated 24th July 1997 as exhibit 2, he did not produce, in the evidence, the Response to that letter. The plaintiff was expecting the second defendant to sign the documents as a Director of the first defendant and the second defendant subsequently signed those documents as a Director of the first defendant and I have no evidence before me to show that once the second defendant wrote the letter dated 24th July 1997, the plaintiff accepted that the second defendant signs the documents as a nominee or agent of the third defendant. Indeed in his letter dated 1st August 1997 the second defendant said he had signed the documents as

> "Director Only."

The letter is Defence Exhibit 3, and indeed the second defendant's signatures on the relevant charge documents, plaintiff Exhibit 6, confirm that the second defendant signed the documents as one of the two Directors of the first defendant and not as a nominee or agent. If the second defendant was relying on his alleged telephone conversation with a Mr Maina of M/s AGN Kamau and Kimani Advocates to contradict that clear documentary evidence, the second defendant should have, at least, called Mr Maina to give evidence.

Otherwise as things remain, I go by the documentary evidence before me and, therefore, reject the second defendant's claim for estoppel against the plaintiff.

It now becomes convenient to move to the issue of a nominee. There are two aspects to this issue. One aspect is whether the second defendant was a nominee guarantor and, therefore, not liable to honour the guarantee. The second aspect is whether the second defendant was a nominee director and, therefore, a nominee guarantor also not liable to honour the guarantee. The second aspect covers the first aspect but it is better to handle the two aspects separately to fit in the written submissions before me.

Starting with the first aspect, that is whether the second defendant was a nominee guarantor and, therefore, not liable to honour the guarantee, there is no dispute that the second defendant signed a guarantee. Both sides rely on a loan application letter dated 27th June 1997 which they agree was signed by the second defendant together with the third defendant. They were both applying for a loan to be granted by the plaintiff to the first defendant.

After that letter the plaintiff responded offering the loan applied for and one of the conditions of the offer stated as follows:

> "The offer is subject to M/s Pulin Shah and Mohamed Ali Madhani to join in the security documents as guarantors."

That condition did not say that Mr. Mohamed Ali Madhani was to join in the security documents as a nominee guarantor and the second defendant also says that as security for the said loan, the plaintiff required that the directors of the first defendant sign personal guarantees in addition to the properties offered by the first defendant as securities for the said loan.

In order to comply with that condition in the plaintiff's offer for the loan, the second defendant voluntarily together with the third defendant signed a guarantee which stated as follows:

> "With reference to the above loan facility applied by the Palm Homes Limited for Kshs 15.0 millin (fifteen million only) we the directors of the company we jointly and severally guarantee

the palm homes limited for the loan."

After signing the above document, the second and third defendants and the plaintiff subsequently executed a mortgage Deed dated 28th August 1997 containing paragraph C in the recital stating that one of the terms upon which the plaintiff had agreed to advance the loan to the first defendant was that the Second and third defendants had to guarantee the repayment to the plaintiff of the sum so advanced and any interest and any other money outstanding in case the first defendant defaults.

The mortgage Deed further contained paragraph 15 which is to the effect that the second and third defendants, as sureties, were to repay the plaintiff the principle sum and interest, fines and others once the principal borrower defaulted in making any repayment. Once that default occurred, the second and third defendants were to assume the role of the principal debtor/ borrower at the election of the plaintiff.

Those are clear terms: the condition in the plaintiff's offer; the guarantee signed; and the mortgage Deed executed. None of them shows that the plaintiff was looking at the second defendant as a nominee or agent of the third defendant who was himself present and throughout acting together with the second defendant. Evidence suggests that it is the second defendant who was unilaterally trying to make himself look like a nominee or agent by adding the word "nominee" against his signature in the application for the loan and in the guarantee and by preparing and singing what he calls "a Declaration of Trust". No credible evidence that he got the approval or the agreement of the plaintiff to add the word "nominee" against his signature or to prepare the so called Declaration of Trust. Of course the declaration had been prepared prior to the loan transaction and sent to the third defendant only. Subsequently the second and third defendants were involved in the loan transaction with the plaintiff in their capacities as directors of the first defendant.

If the application for the loan as well as the guarantee, despite the condition in the offer requiring M/s Pulin Shah and Mohamed Ali Madhani to jointly sign a guarantee, create doubt as to the capacity in which the second defendant signed those two documents because of the presence of the word "nominee" against the signature of the second defendant, there is the more important evidence of the second defendant's signatures in the mortgage Deed which have no word "nominee." That mortgage Deed is a contract between the plaintiff on one part and the defendants on the other part, drawn in clear and unambiguous terms needing no parole evidence to explain or clarify. The parole evidence the second defendant has adduced before me to persuade me that he was a "nominee" or "agent" of the third defendant or anyone else and, therefore, not liable, under the guarantee, to pay the loan after the first defendant has defaulted in paying that loan is not acceptable. In fact the veracity of that evidence becomes more doubtful when the second defendant, a senior member of the legal profession and an advocate of many years standing, tells the Court that he had signed the mortgage document without reading it. In those circumstances and looking at the background of this case, the credibility in the second defendant's parole evidence, even if that evidence were to be accepted as admissible, is, to my mind, not there.

Otherwise a part from the veracity or the credibility of the parole evidence the second defendant has adduced, I follow and uphold the law on parole evidence as stated in the following passages starting with the case of *Jacobs –v- Batavio and General Plantations Limited,* (1924) 1 Ch D 287 at page 295 last paragraph where it is stated:

> "It is firmly established as a rule of law that parol evidence cannot be admitted to add to, vary or contradict a deed or other written instrument. Accordingly, it has been held that (except in cases of fraud or rectification and except, in certain circumstances, as a defence in actions for specific performance) parol evidence will not be admitted to prove that some particular term, which had been verbally agreed upon, had been omitted (by design or otherwise) from a written instrument constituting a valid and operative contract between the parties."

Halsbury's Laws of England, Vol 12, 4th Edition 1975 at page 612 paragraph 1478 shows that the parole evidence rule applies to all forms of evidence outside the contract itself, not merely oral evidence. Quoted in *Robin –v- Gervon Berger Association Limited And Others* (1986) *The Weekly Law Reports* 16th May

526 at page 530 it is stated:

> "Where the intention of the parties has been reduced to writing, it is in general, not permissible to adduce extrinsic evidence, whether oral or contained in writings such as instructions, draft, articles, conditions of sale or preliminary agreements, either to show that intention or to contradict, vary, add to the terms of the document --- Extrinsic evidence cannot be received in order to prove the object with which a document is executed, or that the intention of the parties was other than appearing on the face of the instrument."

Accordingly I reject what has been advanced by the second defendant in attempting to explain why he signed the documents as he did *inter alia*, that he was promised that no liabilities will follow him, that the plaintiff wanted his signature as a formality, that he did sign the documents as a "nominee" director, that counsel for the plaintiff informed him that his signature was required just for a formality, that he was acting as a disclosed agent for a disclosed principal.

In that respect, I hold that the mortgage Deed speaks sufficiently. But to make this point double stronger, let me look briefly at the Memorandum of Association and the Articles of Association of the first defendant because those were the documents under which the mortgage Deed and the loan transaction in general come to be there. I am thus moving from the first aspect to the second aspect of the issue of a "nominee." A nominee as opposed to a substantive director.

It has been shown that the second defendant was not a nominee guarantor. This second aspect of the issue "nominee" will attempt to show whether the second defendant was a nominee director and, therefore, a nominee guarantor. This being a larger aspect than the aspect of nominee guarantor which I have been discussing, what I have been saying about the nominee guarantor is relevant. But I will add some remarks.

The second defendant’s involvement in this matter did not start with the letter dated 27th June 1997. It started with the formation of the first defendant.

It is the second defendant’s case that although the Companies Act does not make provisions for the concept of nominee directors and although that concept is not even known to the Kenyan Jurisprudence and that not withstanding the mandatory need for advocates to observe professional ethics, it is common practice in the Commercial Sector in Kenya for an advocate acting for a single person who wishes to incorporate a company in Kenya, to give the advocate’s name as a Second director with the single person for the sole purpose of satisfying the legal requirement as to the minimum number of directors necessary to incorporate a company.

Although such an advocate is described in the new Commercial Company’s documents as a director, the second defendant explains, the advocate is never really a director of the company but a mere nominee or agent of the single client as the advocate, in reality, has no share in the incorporated company and, therefore, no business interest in the affairs of the commercial company other than his only interest as an advocate for the single person sole beneficiary as well as being an advocate for the now incorporated new company.

In other words the one or more shares that may be attributed to the Advocate as a director of the company are not real shares or shares contributed by the Advocate. They are sham shares put down to deceive the eye of the law so that the new company is incorporated – when in reality the company should not be incorporated under the law.

That being the position, in this matter the second defendant as the advocate for the third defendant who was forming and incorporating the first defendant, the second defendant was named as a second director of the first defendant and a holder of one share out of the 1000 shares in the first defendant. The third defendant was said to hold 999 shares. Not only that but the second defendant was described in and signed the Memorandum of Association, and the Articles of Association as a director of the first defendant. As such a director, the second defendant assumed the title of a director and could assume no

other title in those two important documents which constituted the basis of the incorporation of the first defendant to whom a Certificate of Incorporation number C 66651 produced as plaintiff exhibit number 3 was issued on 30th August 1995 by the Registrar of Companies under the provisions of the Companies Act (Cap.486 Laws of Kenya). The title "nominee" or "agent" is, therefore, not seen anywhere in those two important documents which are the only ones that brought the first defendant and keep the first defendant into lawful existence. They were prepared and registered by none other than the second defendant himself who made sure they were in the form and terms, not only acceptable before the eye of the law symbolized by the Registrar of Companies, but also beneficial to the first defendant – and its directors.

To-day, probably because the second defendant is faced with this suit, he is telling this court that he is only a nominee with no interest and no benefit in the first defendant, the third defendant being the sole beneficiary. Tomorrow, when this suit is out of the way, the court may perhaps hear the same second defendant saying that he is a substantive director in the first defendant and that, therefore, the third defendant is not the sole beneficiary from the first defendant as the second defendant must fully benefit as a director in terms of the Memorandum of Association and Articles of Association of the first defendant. An act of a shrewd architect who strategically places himself in a position from which he can benefit from both sides as the situation suits him.

While the Memorandum of Association says very little about directors of the first defendant, see what the Articles of Association says at page 16 the first paragraph under the heading "DIRECTORS". It states:

> "Until otherwise determined the number of Directors shall not be less than two and not more than seven. The names of the First Directors shall be determined in Writing by the subscribers of the Memorandum of Association or a majority of them and until such determination the signatories to the to the Memorandum of Association shall be the First Directors."

It be noted that the second and third defendants are the only signatories to the Memorandum of Association and the only subscribers of the Memorandum of Association. The concluding words of the quotation just above are: they "shall be the First Directors". It is mandatory.

In the second paragraph under the heading DIRECTORS it is provided that each Director

> “shall have power to nominate any person to act as alternate director in his place during his absence from Kenya or in ability to act as such director, and at his discretion to remove such alternate director by notice in writing to the Company ...”

That is the only situation in which a person who is a director of the first defendant may not act as such a director. There will be an alternate director doing everything as a director in the place of the director who nominated him and in such a situation, the director who nominated him would not be there to act either as a director also or as anything else including "nominee" or agent – and there is nothing in those two paragraphs on page 16 under the heading "DIRECTOR" to suggest that one director can or has the power to act as a "nominee" or "agent" of another director when both are present in Kenya or have the ability to act as both the second and third defendants were doing in the instant case.When both directors are present in Kenya or both of them have the ability to act then no nomination takes place under the second paragraph under the heading "DIRECTOR" on page 16 and it would seem that no director would appoint another director under this paragraph.

That is the only paragraph using the word "nominate" in so far as the replacement of a director is concerned. That word "nominate" is changed to the word "appointment" in the middle of the same paragraph and the person so nominated or appointed becomes a director for all practical purposes— so that he never acts as a nominee or agent at anytime.

The other paragraph, which provides for the replacement of a director is the last paragraph on page 17. But that paragraph does not use the word "nominate’. It uses the word "appoint" or "appointment." The provisions in this paragraph come into play in a situation different from the one obtaining when paragraph

two under the heading DIRECTORS on page 16 is used.

Under the last paragraph on page 17, the alternate director is appointed for the purpose of acting at meetings only and the director to be represented need not be out of Kenya or be having inability to act as a director. The paragraph says:

> "Any Director may in writing appoint any person, who is approved by the majority of the Directors, to be his alternate to act in his place at any meeting of the Directors at which he is unable to be present. Every such alternate shall be entitled to notice of meetings of the Directors and to attend and vote thereat as a Director when the person appointing him is not personally present, and where he is a Director to have a separate vote on behalf of the director he is representing in addition to his own vote. A Director may at any time in writing revoke the appointment of an alternate appointed by him. Every such alternate shall be an officer of the company and shall not be deemed to be the agent of the Director appointing him."

Going back to page 16 there is a heading "MANAGING DIRECTOR", under which it is provided that the Managing Director be appointed by directors of the first defendant. Each director participates in such an appointment in his capacity as a director only. It is the directors who determine the terms and conditions of service of the Managing Director they have appointed and every director does that as a director and not as a "nominee" or "agent".

As to the power of the first defendant to borrow, it is stated in the first paragraph on page 17 that:

> "The Directors may exercise all the powers of the Company to borrow money and to mortgage or charge its undertaking, property and uncalled capital or any part thereof and to issue debentures, debenture stock and other securities whether outright or as security for any debt, liability or obligation of the company or of any third party."

Here again, like in the case of the appointment of a Managing Director, each Director whether alternate or not exercises the power of the Company to borrow money and to mortgage or charge property etc, as stated above, in each director's own right as a director of the company, the first defendant. There cannot, therefore, be a question of one of the directors acting as a "nominee" or "agent" of either the Company or the other director – worse still when the other director is also there acting at the same time in his own right as a director of the same Company like the second and third defendants were doing here when they were signing documents relating to the mortgage in question in this suit.

It seems to me that a director can only act as an alternate for a fellow director under the provisions of the last paragraph on page 17 and that is only for the purpose of acting at meetings of directors which the director, appointing the other an alternate, is not personally present.

In other words, and pursuant to the Articles of Association of the first defendant herein, once a person has lawfully become a director of the first defendant under the provisions of the Companies Act, that person remains a director and only acts as such a director unless and until he nominates an alternate director to act in his place on the ground that he is out of Kenya or he is under an inability to act as a director or he is unable to attend a specified meeting of directors or unless and until he resigns his office as a director or becomes of unsound mind or becomes prohibited from being a director by reason of any order made under section 189 of the Companies Act or becomes bankrupt or makes any arrangement with his creditors generally. See page 17 under the heading

> "DISQUALIFICATION OF DIRECTORS"

The above being the position I do not see how the second defendant could properly and lawfully claim to be a "nominee" or "agent" of the third defendant and then proceed to properly and lawfully execute a Declaration of Trust (2nd D Exh 1); the mortgagee Application Form (P Exh 1) and Director's Personal Guarantee letter dated 6th March 1997 (P Exh 5) all as a "nominee", some of those documents having properly described him as a director only for him to hand write after his signature, the word "nominee".

In the end he executes the mortgage document (P Exh 6) as a director and his Company, the first defendant, gets the loan applied for the second defendant to come to this court, after default in repayment of the loan, to claim that he was not a director. Forget use of the word "substantive". All that should be looked for is the word “Director”.

Where is evidence of the second defendant’s disqualification as a director in accordance with the Articles of Association of the first defendant? The second defendant has not claimed he became disqualified.

Then since he is using the word "nominee" from the word "nominate" used in the second paragraph under the heading "DIRECTOR" at page 16 of the first defendant’s Articles of Association, where is the evidence of his nomination by the third defendant? I have none.

If the nomination the second defendant claims was done under the provisions of the last paragraph on page 17 of the Articles of Association, then apart from the fact that the second defendant has failed to adduce evidence as pointed out in the previous paragraph, he should also have shown how such an appointment as an alternate, and not nominee, director gave him power to sign the documents he signed indicating he was a nominee when all that, that appointment could give him was for him to act at meetings of directors only, and while there, to act as a director only. Such an appointment could not give him authority to sign the type of documents he signed, the documents about which I do not have evidence to show were being signed as part of proceedings at any meeting of directors of the first defendant’– as stipulated under the provisions of the last paragraph on page 17 of the Articles of Association.

The second defendant is a person who, together with the third defendant, signed the Memorandum of Association as well as the Articles of Association on 16th August 1995. As a result they had the first defendant incorporated under the Companies Act on 30th August 1995 and on the same day the second defendant signed his Declaration of Trust (2nd D Exh 1).

I have no evidence to show the signed declaration was sent to the Registrar of Companies for any purpose. I have no evidence as to the persons to whom that declaration was sent and for what purpose. It purports to benefit the third defendant as the second defendant is declaring in that document that he holds his one share in the first defendant Company upon trust for the third defendant.

That having been done, in February, March 1997 the second defendant was signing the first defendant’s loan application to the plaintiff and the subsequent guarantee respectively as a director in accordance with the provisions of the afore quoted paragraph one page 17 of the first defendant’s Articles of Association but indicating at the end of his signature the word "nominee". He ended up signing the mortgage Document (P Exh. 6) as a director of the first defendant, the mortgage document having ended with the following words before the two directors of the first defendant signed it:

> "We Pulin H Shah and Mohamed Ali Madhani the Directors of the Borrower who witnessed the Affixing hereto of the common Seal of the Borrower have read and had explained to us the above sections and confirm that we understand the same".

The mortgage document contains paragraph 15 under which the Second and third defendants, as sureties, jointly and severally convenanted with the plaintiff to pay the loan if the first defendant was in default. The document contains other binding clauses. Even if the second defendant did not read them, he is deemed to have read them.

The second defendant has ignored all that on the basis that no liability attaches on him because he is not a director of the first defendant and that all that he did in connection with the loan in question in this matter, he did it in his capacity as a "nominee" or "agent" of the third defendant.

From what I have been saying, I cannot agree with that defence. I rejected parole evidence adduced to explain and clarify clear and unambiguous documentary evidence before the Court. This is a court of law and the law must apply as the Court should not allow the rule of the jungle to replace the rule of law. That being my position, I should not and cannot ignore, like the second defendant is doing, what the first

defendant's Memorandum of Association as well as the Articles of Association are saying as to who the directors of the first defendant are and what their powers and duties are. I should not and cannot ignore, like the second defendant is doing, the fact that the first defendant is an incorporated Company under the Companies Act on the basis of the first defendant's Memorandum of Association and Articles of Association and that those documents were drawn by the second defendant who subsequently caused the incorporation to be effected. I should not and cannot ignore, like the second defendant is doing, the fact that the second defendant signed the mortgage agreement between the plaintiff and the first defendant as a director of the first defendant thereby binding not only the first defendant but also himself to repay the loan the subject matter of the said mortgage agreement.

I find that the first defendant is a lawfully incorporated company, under the Companies Act, with two directors one of them being the second defendant whose claim for being a mere "nominee" or "agent" of the third defendant is based on evidence which is not only inadequate and unacceptable on facts, but also unsupportable professionally, ethically and legally. He could never be a "nominee" or an "agent" for the ever present, able and co-working third defendant when in reality and in law he, the second defendant, was a director of the first defendant. When therefore the second defendant purported, without the support of legal provisions, to execute the Loan Application Form, and the Guarantee as a "nominee", he never became a "nominee" or "agent". He remained a director, as once you are a director under the Memorandum of Association and Articles of Association of the first defendant, you remain a director, and in law therefore those forms were signed by a director and not by a "nominee" or "agent" and the word "nominee" appearing on those forms is of no legal effect. Similarly the Declaration of Trust is of no legal effect.

The second defendant is now seeking the protection of the Court through an order stating that he is not liable. I hold that he who deceives the eye of the law deserves no protection of the law to that deceit.

Accordingly I reject the second defendant's claim that he was a "nominee" or an "agent" for the third defendant in this matter. I find that he was, has been and still is a director of the first defendant under the Companies Act and that, therefore, personal liability to pay the loan under the guarantee attaches upon the second defendant.

Moving to the issue of the guarantee or surety given by the second defendant being void *ab initio* for lack of consideration, the argument seems to be that the loan which was given by the plaintiff to the first defendant did not go to the second defendant personally. He did not personally receive that money to personally benefit from it.

That may be so but unless the two co-directors of the first defendant formed a company in the name of the first defendant in order to obtain a loan from a financial institution to share the money individually without that money benefiting the first defendant commercially, I do not see the basis of the second defendant's complaint. It is because in that loan transaction, it was clear the borrower was the first defendant. That was the legal person to receive and use the money. The money was not expected to go to individual directors or share holders of the first defendant for their personal use. No part of that money was expected to be freely dished out to any such individuals for their personal use. That money or any part of it was not, therefore, consideration due to the second defendant personally as a director or share holder of the first defendant, or as an ordinary individual.

But in law, the second defendant, as a director of the first defendant, had to sign a guarantee to repay that money in case the first defendant defaulted in repaying the loan. The plaintiff had to get satisfactory security for the repayment of the loan in order for the plaintiff to release the money to the first defendant. It was a large sum of money Kshs 15,000,000/=. I am told Kshs 13,300,000/= was subsequently offered and accepted. The sum remained large and following the acceptance, there is no dispute that the money was given by the plaintiff and received by the first defendant. That was the consideration as the first defendant, a mere company, had to act through its two directors who accepted and went a head to guarantee the loan. I do not see how the second defendant expected to gain over and above that consideration and his evidence does not support his claim on this issue.

Accordingly his claim that the guarantee or surety given by him is void *ab initio* for lack of consideration is hereby rejected.

I now turn to the last and vexing issue of the value and price of the security the first defendant gave to the plaintiff in this matter. The security as already stated was property which contained three separate plots in one compound and these were known as LR No 2951/274; LR No 2951/275 and LR No 2951/276; Farasi Lane, Lower Kabete, Nairobi.

At a public auction sale conducted on 17th February 1999 all those three plots were sold at the price of Ksh 9,000,000/= leaving a shortfall of Ksh 10,762,978.88 which the plaintiff is claiming in this suit against the defendants.

At the time the loan in question here was being negotiated in May 1997 that security was valued by the plaintiff's own Ag Chief Valuer at Kshs 20,000,000/=. By that time the parties were negotiating a loan of Ksh 15,000,000/=. The value of Ksh 20,000,000/= was market value. That same valuation which has been produced as plaintiff Exhibit11, gave the mortgage value of the security as Ksh 19,000,000/= and the Investment value as Ksh 6,000,000/=.

The valuation Report which is dated 26th May 1997 and was prepared by the plaintiff's Ag Chief Valuer notes that only one of the three plots is developed with a residential house. That is plot Number 274. The other two were empty and Mr Baldip Singh Rihal, a Surveyor valuer and Urban Management Consultant who gave evidence as DW 2 held the view that the figure Kshs 6,000,000/= Investment Value must have been derived from the income of the one house development on the security without taking into account the potential for development on the other two plots. He did not like use of the term "Investment Value", claiming that the term does not exist in the terminology of his profession. Instead, what exists is the term "Investment method"

That does not agree with what the plaintiff's Legal Officer, Jane Wabuda Mwanunda who gave evidence as PW 1, said in her evidence. According to her, the figure Kshs 6,000,000/= investment value was for all the three plots and not for one plot only.

The two witnesses were merely interpreting plaintiff exhibit 11 as read together with plaintiff exhibits 14 and 15 as neither of the witnesses was involved in the matter at the time of the auction sale. However one of them is a professional valuer of long and varied experiences in that field while the other one is not even a valuer. She is a lawyer in the commercial field.

But that not withstanding, it is worthy noting that the plaintiff's own Chief Valuer made the following remarks in plaintiff Exhibit 11, the first valuation report in this matter, concerning the location of the security:

> "A preferred location where capital values are on the rise."

That is only one of the favourable remarks made by the Ag Chief Valuer in that report which also talks of the potentiality to develop maisonettes.

As already stated, a loan of Ksh 13,300,00/= was offered, and accepted against that security. That was in August 1997 when the relevant charge or mortgage was executed by the parties and, was registered at the relevant land registry. Since the mortgage value of the security was Ksh 19,000,000/ =, the plaintiff's loan of Ksh 13,300,000/= must have been reasonably and very well secured. The normal practice, according to the evidence, is that a financial institution exercising due caution would lend up to 80% of the mortgage value of the security. As that 80% in this matter was Ksh 15,000,000/=, a loan of Ksh 13,300,000/= was more than adequately covered by the security the first defendant gave to the plaintiff.

The first defendant, after receiving the loan, fell into arrears and by 6th October 1998 the amount of the outstanding loan together with interest had risen up to Ksh 15,666,148.30. As a result the plaintiff had instructed auctioneers, first M/s Watts Enterprises and later M/s Valley Auctioneers to sell the security.

The amount was rising so that by the time the security was sold, the total loan balance was Ksh 19,762,987.28 while the mortgage value of the security had also risen to Ksh 20,000,000/=.

Evidence is that the mortgage value of a security for a loan is normally 10% to 15% below the market value of that security and that when the mortgage value of the security in this suit was given as Ksh 19,000,000/ = the market value would be around Ksh 21 to 22 million although it was cautiously given as Ksh 20 million. It follows that when by 17th September 1998 the mortgage value of the security was Ksh 20,000,000/=, the market value was higher than Ksh 22,00,000/=. The Forced Market Value would be what the market would be selling at the time of the auction sale. Mr BS Rihal described it as the rock bottom. It is the minimum that, in the valuer's opinion, a seller should be able to fetch on the market. The one on which a lender should determine his reserve price.

The security was first advertised for public auction sale in December 1998. At that time the market value of the security was not given but the mortgage value was shown to have risen to Ksh 20,000,000/= and a reserve price of Ksh 20,000,000/= was put up. It is not clear what happened as the security was not sold.

Thereafter the second advertised public auction of the security was scheduled for 17th February 1999. This time again no body seems to have cared about the market value. The mortgage value was retained at Kshs 20,000,000/= and the plaintiff claims to have instructed the Auctioneers that the reserve price was Kshs 20,000,000/= subject to a minimum price of Shs 6,000,000/=. The last figure appears to have been based on the sum for the Investment Value found on the last page of the valuation Report, plaintiff Exhibit 11 dated 26th May 1997. While the plaintiff claims that that instruction causes no confusion, it is the Second defendant's case that that instruction is confusing. In any case there is no credible evidence that the plaintiff instructed the Auctioneer as to the reserve price before the security was on 17th February 1999 sold at Kshs 9,000,000/=.

Valley Auctioneers sold the security after they had claimed that the security had been vandalized. Evidence from the plaintiff's Legal Officer is that there were three valuations up to the time the security was sold, the first valuation having been the one dated 26th May 1997 in plaintiff's Exhibit No. 11 and that the last one was given on 17th February 1999. Another one had been done on 17th September 1998 when the mortgage value of the security was given as Kshs 20,000,000/= and the Investment Value retained at Kshs 6,000,000/=. By then it was said the property was due for sale by Public Auction on 17th February 1999. Both plaintiff exhibit 14 and exhibit 15 talk of the date of the last valuation as 17th September 1998. Exhibit 15 was written on 2nd December 1998 and the two exhibits are both internal memos in the plaintiff's office from the Mortgage Manager to the Managing Director through the Chief Manager Advances. While exhibit 15 recommended a reserve price of Kshs 20,000,000/= without more, exhibit 14 gave a reserve price of Kshs 20,000,000/= subject to a minimum price of Kshs 6,000,000/= and the Auctioneer who gave evidence as PW 2, Mr Samuel Mutahi Gathogo, told the court he acted on instruction to sell the security having been given a reserve price of Kshs 9,000,000/=. He said he sold the security at Kshs 9,000,000/= to the highest of the three bidders participating.

This is the Auctioneer who had claimed the security had been vandalized. He told the Court that before making that claim, he had visited the security on 15th December 1998. He found the security had been abandoned for about two years and had therefore been vandalized and most of the structures inside such as tiles, bath tabs, had been removed. He claimed he saw cracks on the wall and that electrical gudgets were not in the kitchen. He concluded that generally the whole house was not habitable. He told the court he had not been given any valuation report and he did not talk of having seen plaintiff Exhibits 11, 14 and 15 or 17. Obviously he was talking about the one residential house on plot LR No 2951/274.

After Mr SM Gathogo's report that the security had been vandalized, the plaintiff's Ag Chief Valuer, a University Graduate Valuer, visited the security again and according to the plaintiff's Legal Officer's evidence, the security had not been vandalized. She produced plaintiff Exhibit 17, another internal memo, this time, dated 17th February 1999 from the Ag. Chief Valuer to the Mortgage Manager. It states:

> "Further to your memo of 6th February, 1999, we have now inspected the above referenced property and report as hereunder:-

(1) The only improvement against this Composite security is on parcel 2951/274 and the same is under care-taker service with one person in the main House and another in the Domestic Staff Quarters.

(2) The property has not been vandalized at all. What, however, has happened is that the borrowers were undertaking some minor improvement works to the kitchen and on ensuit extension to the master Bedroom. These works have been abandoned at fittings with sink in place, but no glazed tiles around it; WC suite on site, but not fixed; windows frames fixed, but not glazed.

(3) We have recognized and provided for the above position, since noticing that the works sort of stalled. The sums advised are, therefore, in order for this 1.5 Acre property off Lower Kabete Road."

This report is what the plaintiff's Legal Officer is calling the third valuation – and it was her evidence that the Ag Chief Valuer did not talk of any reduction in the value of the security. In that respect his last sentence is worthy a special note. He said

"The sums advised are, therefore, in order for this 1.5 Acre property off Lower Kabete Road."

The Ag Chief Valuer was talking of "The sums advised" in previous valuation reports the one dated 17th September 1998 having put the mortgageValue at Ksh 20,000,000/= up from Ksh 19,000,000/= which was in the first valuation report. As can be seen at page 58 or folio 61 otherwise marked 61 of the plaintiff's bundle of documents filed in this case file, Ksh 20,000,000/= was given as "mortgage/market value" of the security. plaintiff Exhibits 14 and 15 say that that figure in that valuation report was for mortgage value. No market value was specified and by 2nd December 1998, therefore, M/s Watts Enterprises, the plaintiff's Auctioneers then handling the Public Auction Sale scheduled for that date were advised by the plaintiff's Assistant Mortgage Manager, through plaintiff Exhibit 16 that the reserve price was Ksh 20,000,000/= suggesting that the market value and even the mortgage value of that security were in December 1998 higher than they were on 17th September 1998 and more higher than they were in May 1997. Yet only two months later, in February 1999 the same security was sold at a price less than 50% of the original mortgage value given in May 1997.

It was the plaintiff's Mortgage Manager, and not the Ag Chief Valuer, who recommended through plaintiff exhibit 15 dated 2nd December 1998 that the reserve price was Ksh 20,000,000/= and proceeded to advise through plaintiff Exhibit 14 dated 16th February 1999 that the reserve price was Ksh 20,000,000/=.

"subject to a minimum price of Ksh 6,000,000/=."

Evidence is that the sum of Ksh 6,000,000/= is investment value. In plaintiff exhibits 14 and 15 the Mortgage Manager is quoting "minute No. 3298 (d) of SMC" which state:-

"Agreed i) That in future the Chief Valuer would put for consideration as the reserve price, investment value where the property has rental value.

ii) That where the debt is higher than the reserve price, the Auctioneer would be given the amount of the debt so that he is in the picture as to the debt required to be recovered.

iii)That where it was not possible to let the property, i.e. properties in rural areas, then the mortgage value would be put forward by the Chief Valuer for consideration as the reserve price."

I have evidence that the Ag Chief Valuer gave figures. But I have no evidence that he suggested any of those figures to be a reserve price. The evidence I have shows action by the Mortgage Manager. But from that evidence while plaintiff Exhibit 14 shows that a reserve price of Ksh 20,000,000/= was set, Mr SM Gathogo of Valley Auctioneers told the court he was given a reserve price of Ksh 9,000,000/=. Since the

figure he says he was given was less than the debt, Mr. Gathogo should have told the court that he was given the amount of the debt also. On the contrary, he said he was not given the amount of the debt. There was no compliance with clause (ii) of the contents of plaintiff Exhibits 14 and 15 I have just quoted above.

It would appear, from what happened, that the plaintiff applied clause (i) out of the three clauses 1 have quoted above and therefore in practice used what the plaintiff termed "Investment Value" as the reserve price while in theory the plaintiff was telling the world through Exhibit 14 that the reserve price was Ksh 20,000,000/= and the plaintiff's Legal Officer has told this court that the reserve price was somewhere between Ksh 20,000,000/= and Ksh 6,000,000/=. That explains why the plaintiff accepted the price of Ksh 9.000,000/= from the Public Auction sale. That also explains why the plaintiff may not have cared to inform Mr. Gathogo that the debt was standing at Ksh 19,762,978.88. That may explain why the plaintiff did not think it was necessary for Mr Gathogo to have a Valuation Report on the property he was to sell. Perhaps the plaintiff thought it was better for the Auctioneer who was not a professional valuer, to rely on his own claim that the property had been abandoned, and the house there vandalized to the extent of not being habitable. Indeed that is the knowledge the Auctioneer relied upon as there is no evidence that the Auctioneer, Mr Gathogo, saw plaintiff Exhibits 11,15,14,16 and 17. Exhibit 17, the Ag Chief Valuer's report, to the effect that the security had not been abandoned and vandalized and that the house therein was habitable was written on the day of the auction sale and there is no evidence that that report ever reached Mr Gathogo before the auction sale or even anytime.

In those circumstances, I do not see how I can accept the word of Mr Gathogo that he was given a reserve price of Ksh 9,000,000/=. Moreover, looking at the three clauses at the bottom of plaintiff Exhibits 14 and 15, and it appearing that the Mortgage Manager was applying clause (i) when he set a reserve price of Ksh 20,000,000/= subject to a minimum price of Ksh 6,000,000/=, a question arises as to what justification was there for choosing clause (i). From that clause, Investment Value is given where property has a rental value. Concerning the security here, evidence is clear that only one of the three plots had a rental residential house. That being the position, and with all due respect to the plaintiff's Legal Officer, Jane Wabuda Mwanunda, it is reasonable to agree with what DW 2 Mr BS Rihal says that the figure Ksh 6,000,000/= Investment Value must have been derived from the income of the one house development on the security without taking into account the potential for development on the other two plots.

Having agreed with that opinion, I do not see why development on one plot should over shadow the situation on the other two undeveloped plots. In the circumstances, I hold the view that it is clause (iii) rather than clause (i) which should have applied on the basis of the number of plots either developed or undeveloped. The mortgage value of the security would therefore have been given as the reserve price without additional phrases confusing the issue and the figure should have been simply stated to be Ksh20,000,000/= without more.

From what happened therefore, what I find is a Public auction sale conducted by an Auctioneer who had no information about the amount of the debt owed by the defendants to the plaintiff; no information about the value of the security he was to sell; no information about the reserve price and not bothered about a reserve price; playing the role of a valuer yet he was no professional valuer; and left alone and free, perhaps because of his 14 years auctioneers experience, to act on his own erroneous information and conclusions – his ideas of abandonment, vandalism and uninhabitability of the security having been left uncorrected, with the results of his action, as the auctioneer of the security, being readily accepted by the plaintiff as the plaintiff planned the next move again to jump over onto the necks of the defendants, this time, for more money to satisfy the debt on the basis that the proceeds of the auction sale left a short fall.

The second defendant is saying: No. Even if I am liable to pay the debt, what the plaintiff is doing is unfair, harsh, oppressive and a contradiction. A contradiction because the plaintiff having circulated internal memos stating clearly that the mortgage value and the reserve price of the security was Ksh 20,000,000/=, gave no such information to the Auctioneer who was left free to sell the security at less than 50% of the mortgage value and the reserve price. It is in the evidence of the plaintiff itself that there had been three valuations, the second one on 17th February 1999, each having raised the mortgage value to no less than Ksh 20,000,000/= from the first Valuation which had put it at Ksh 19,000,000/= and there

being no evidence of a dramatic slump to have lowered the higher value by more than 50% on the date of the auction sale which was also the date of the third valuation on 17th February 1999. There was no evidence of any slump affecting the value of the security at the time of the auction sale to contradict the valuation given by the Ag Chief Valuer on the same date through plaintiff Exhibit 17.

The charge in this matter was registered under the Indian Transfer of Property Act. The notice to sell the property was therefore given under S 69 A of that Act. A question is whether there are provisions like section 77 of the Registered Land Act (Cap 300 Laws of Kenya) which imposes a duty on the chargee to act in good faith and have regard to the interests of the chargor.

In other words, what duty is cast on a mortgagee or chargee in the exercise of his power of sale in so far as it relates to the value of the property? Views are not unanimous but generally it can be said that the mortgagor is not completely ignored although banks may like him to be ignored completely. In England, for example, where the application of the Registered Land Act or the Indian Transfer of Property Act is not found, *Halsbury's Laws of England*, 4th Edition, Vol 32 Paragraph 276 has this to say:

> "If the mortgagor seeks relief promptly, a sale will beset aside if there is fraud or if the price is so low as to be in itself evidence of fraud, but not on the grounds of undervalue alone, and still less if the mortgagor has in some degree sanctioned the proceedings leading up to the sale."

Lord Denning MR, pointed out in *Standard Chartered Bank vs Walker* [1982] 3 All ER 938 that that Law is set out in *Cuckmere Brick Co Ltd Vs Mutual Finance Ltd* [1972] 2 All ER 633 where it is stated:

> "A mortgagee was not a trustee of the power of sale for the morgagor and, where there was a conflict of interests, he was entitled to give preference to his own over those of the mortgagor, in particular in deciding on the timing of the sale; in exercising the power of sale, however, the mortgagee was not merely under a duty to act in good faith i.e. honestly and without reckless disregard for the mortgagor's interest, but also to take reasonable care to obtain whatever was the true market value of the mortgaged property at the moment he chose to sell it."

Explaining that passage, Lord Denning said

> : "If a mortgagee enters into possession and realizes a mortgaged property it is his duty to use reasonable care to obtain the best possible price which the circumstances of the case permit. He owes this duty not only to himself (to clear off as much of the debt as he can) but also to the mortgagor so as to reduce the balance owing as much as possible ---. There are several dicta to the effect that the mortgagee can choose his own time for the sale, but I do not think this means that he can sell at the worst possible time. It is at least arguable that, in choosing the time, he must exercise a reasonable degree of care."

That is a higher duty than had been placed upon the mortgagee by court decisions in earlier cases such as *Reliance Permanent Building Society vs Harwood Stamper* (1944) 3 Ch 362.

That position of the law in England does not seem to be different from what the Court of Appeal in Kenya said in *Kenya Commercial Bank Ltd vs James Osebe* (1982-88) 1 KAR 48. In that case the trial judge had held:

> "that although there was no evidence of fraud or bad faith, or that the conduct of the auction was irregular or improper, that none the less the interests of the respondent as chargor were not taken into consideration and that the bank was careless, negligent and reckless."

Regarding that holding, the Kenya Court of Appeal, through the leading judgment of Hancox, then Ag JA, stated:

> "Had it not been for the point of jurisdiction to award damages, the judge in my view delivered a very good judgment, fully sensitive to the rights of the parties and to the issues before him: and, as

> I have said, his mind was never directed to this question, (meaning the question of jurisdiction) as it should have been. The bank's conduct has to my mind been shown in a most unmeritorious light, and the judge's finding that it did not have sufficient regard to the chargor's interests on the sale is certainly arguable."

That clearly shows that had there not been the question of jurisdiction, which had not even been raised and canvassed in the High Court, that appeal was going to be dismissed. It was allowed because of lack of jurisdiction, the court having awarded damages in an originating summons and the quotation above from Hancox Ag JA may be said to be *obiter dicta*, which, in practical terms, it is not because had there not been the technicality of lack of jurisdiction, that purportedly *obiter dicta* was the *ratio decidendi* – in that case.

Facts of that case, in brief, were that the respondent borrowed Shs 30,000/ = from the appellant bank, Kenya Commercial Bank Limited, and executed a charge over his property at Kisii. He fell into arrears with his repayments and the bank exercised its statutory power of sale by public auction at which the property realized Ksh 20,000,000/=. This was sufficient to discharge the respondent's indebtedness at that time March 1980 of only Ksh 8027/20. In September 1980 the property was valued at Ksh 160,000/ = and in April 1981, the purchaser at the auction sold it for Kshs 180,000/ =. The second purchaser charged it to the same bank in May 1981 for Ksh 200,000/=. The respondent chargor took out an originating summons to declare against the bank and the first purchaser whether the sale was fair and just, and if not, to set aside the sale allowing him to repay to the bank the Ksh 20,000,000/= obtained at the auction. The trial judge held that although there was no evidence of fraud or bad faith, or that the conduct of the auction was irregular or improper, that nonetheless the interests of the respondent as chargor were not taken into consideration and that the bank was careless, negligent and reckless. He did not set aside the sale but awarded Ksh 180,000/= damages to the respondent the chargor. The Bank, the Chargee, appealed – resulting into the decision of Hancox Ag JA referred to above.

The position is that the decision of the learned trial judge, Aganyanya Ag J. as he then was, as approved by the Court of Appeal, expressed the Law in Kenya. It be noted that there need not be evidence of fraud, and the learned trial judge in the *Kenya Commercial Bank Case* included evidence of bad faith. That evidence need not be there and Lord Denning did not include the word "fraud" or the words "bad faith" in the passage quoted here from him. Instead he said the mortgagee has a "duty to use reasonable care" The mortgee "owes that duty not only to himself but also to the mortgagor so as to reduce the balance owing as much as possible."

That "duty to use reasonable care" existed in the case before me and I need not look for evidence of fraud as the evidence before me justifies my adoption of the statement from *Kenya Commercial Bank Limited vs. James Osebe* that

> "although there was no evidence of fraud or bad faith, or that the conduct of the auction was irregular or improper, none the less the interests of the" second defendant "as chargor were not taken into consideration and that – the bank was careless, negligent and reckless."

I add what Hancox, then Ag JA said that

> "The bank's conduct has --- been shown in an unmeritorious light."

And that

> "To say that all the bank was required to do was virtually to recover its own outstanding debt is an attitude which" I, like him, find "not only unrealistic, but also harsh, oppressive and uncompromising."

I would therefore, with all due respect, not subscribe to the views, like those expressed in the dissenting judgment of Apaloo JA as he then was in the case of *Mbuthia vs Jimba Credit Corporation Limited and Another* in Civil Appeal No 111 of 1986 where the learned Judge of Appeal supported Schoefield J who

had handled the case in the High Court stating:

> "The mortgagee of course, sells primarily for his own benefit. The object of the sale is to realize the security and recover the money he has lent. He is entitled to think of himself first. He must not ignore the mortgagor but the whole purpose of the sale, is to get his money back."

The two learned judges were explaining the position of the mortgagee as they respectively perceived it from the case of *Reliance Permanent Building Society vs Harwood Stamper* as commented upon in *Halsbury's Laws of England 2nd Edition Vol 23* at page 435 and in *Coote on mortgages Vol 2, 9th Edition* page 917. But their explanation as quoted above is to the extreme as they stand on the proposition that a mortgagee is not a trustee of the mortgagor so that the mortgagor remains almost nothing thereby vindicating the position that in the area of a bank's rights against a debtor, Capitalism knows no neighbour. Capitalism which used to fight Communism flourishing on and cherishing the platform of religion and human rights seems to be saying to-day when communism is a toothless bulldog, that as between a chargor and chargee or between a debtor and creditor at the time the chargor or debtor is in arrears, you don't have to do to your neighbour as you would like him do to you. A Capitalist creditor bank, therefore, says a debtor is only a neighbour, physically or businesswise, when he is there solely in the interests of me the creditor. Otherwise the neighour ceases to be a neighbour as he becomes crushable to annihilation by the creditor, a foreigner to reasonable care or devoid of good faith and unmindful of the interests of the debtor, in order to recover arreas. It seems to me that it is in that light that the behaviour of the plaintiff in this suit can be explained.

If that be the position, there is a great need for legislation, not only like but also stronger than, section 77 (1), of the Registered Land Act, whose correct legal effect should not be watered down by biased capitalistic legal interpretation as is apparent in the case of *Mbuthia – vs – Jimba Credit Corporation Limited* (*Supra*) where Apaloo JA, as he then was, after approving what Schofield J said (*Supra*) added:

> "so the duty cast on a chargee by section 77 (1) that in the exercise of his power of sale, he shall act in good faith and have regard to the interests of the chargor is no more than a codification of the equitable principles articulated in *Halsbury's* and *Coote's on mortgages* and ascended to by equity Judges."

This is what section 77 (1) says in so far as it is material:

> "A chargee exercising his power of sale shall act in good faith and have regard to the interests of the chargor, ..."

Since the Indian Transfer of Property Act under which the charge herein was registered does not have similar provisions, that situation calls for courts of law to step in to see that a sense of justice is maintained as the neighbour needs to exist just as the credit bank or creditor does – need the existence. That means courts of law step in to apply equity.

In conclusion therefore, I should first state that I note that the authorities I have been discussing were cases where the plaintiffs wanted to set aside the public auction which had taken place. The plaintiffs wanted to prevent the resulting transfers of the properties sold. That is not what the second defendant wants in this suit. He is not challenging the auction sale. He is accepting it. It has taken place. His case is that the plaintiff "should be contented with that sale." The plaintiff should not come up in this suit to claim the shortfall from the second defendant.

Having noted that difference also note that the principles applicable in those cases are applicable in this suit before me. They apply to the facts in this suit. Those facts are that the plaintiff failed to pursue its remedies against the defendants on the first defendant's default, timely and with diligence which led to accumulation of interest in the first defendant's account so that the loan of Ksh 13,000,000/= which had been more than adequately secured by a security whose mortgage value then was Ksh 19,000,000/= and its 80% was Ksh 15,000,000/=, was left to accumulate to Ksh 19,762,978.88 at the time of the auction sale. Diligently and with reasonable care, the plaintiff should not have allowed the loan to pass the 80%

mark of the mortgage value of the security and if that level was passed, the plaintiff should not have allowed it to grow to the figures leading to this suit.

As a result of lack of diligence, lack of reasonable care or lack of good faith and of being mindful of the interests of the defendants, the plaintiff handled the subsequent public auction sale in a messy way allowing the Auctioneer to do what he wanted to do as to the sale price. The security then having a mortgage value of Ksh 20,000,000/= was sold at Ksh 9,000,000/=, no doubt being a gross under value of the security. Had the plaintiff had good faith and been mindful of the interests of the defendants or had the plaintiff exercised reasonable care in the sale of the security, even though he had allowed the debt to grow to where it was, the plaintiff would have recovered the debt in full and without any shortfall.

That security having been taken as adequate on account of that debt, I would have agreed with the contention of the second defendant and held that although I found that personal liability to pay the loan attaches on the second defendant, the plaintiff has not succeeded, in the circumstances of this case, in proving that the second defendant should pay the debt as I would have gone on to say that the second defendant's personal liability is discharged by the plaintiff's failure to act in good faith and failure to have regard to the interests of the second defendant or the plaintiff's failure to act with reasonable care in the realization and/or sale of the security resulting into a gross under value of the security to the level of less than 50%.

I have looked at the mortgage agreement in the light of the rest of the evidence and hold the view that a guarantor should only be called upon to honour his guarantee when there is default but the security is not being sold. If there is default and the security sold and there is a shortfall, the guarantor should only be called upon to honour his guarantee if the sale was done diligently and lawfully at a reasonable price, not being gross under value, taking into account the market value of the security, mortgage value of the security, the amount of the debt due and a proper reserve price. In other words, the sale should have been done in good faith taking the interests of the defendants in consideration or the sale should have been done with reasonable care. As that was not the position and I find that what the plaintiff has done and is doing in connection with this suit is, to use the words of Hancox, then Ag JA in the *Kenya Commercial Case*, unfair, unreaslistic, harsh, oppressive and uncompromising to the second defendant, I should have dismissed the plaintiff's suit against the second defendant. But being mindful that I am applying equity at this stage of this suit, I refrain from dismissing the plaintiff's suit and proceed to state as under:

> I am applying equity because the applicable law, the Indian Transfer of Property Act, does not have provisions, such as section 77 (1) of the Registered Land Act, to cover this situation. Some of the maxims of equity are that "Equity acts in *personam*." "Equity will not assist a volunteer." "He who comes into equity must come with clean hands."

In this suit I am talking of equity as it acts in the second defendant. He is come into equity tainted. He is come with unclean hands. Being an advocate, he prepared and signed the Memorandum of Association of the first defendant as a Director but came to this court to say he was not a director. He claimed he was a nominee. He prepared and signed the Articles of Association of the first defendant as Director but came to this court to say he was not a director. He claimed he was a nominee. He had the first defendant registered and incorporated under the Companies Act with himself as one of the two directors but came to this court to say the first defendant was so incorporated with him as a nominee. As a director of the first defendant he negotiated the loan in question in this matter and signed the relevant charge documents as a director but came to this court to say he was acting as a nominee. When Mr. Ahmednasir, counsel for the plaintiff, pinned him down on those facts, the second defendant conceded to the effect that he was doing that to deceive the eye of the law but surprisingly did not accept that any of those facts raised any ethical issue to him as a lawyer and an advocate of the High Court of Kenya.

Was the second defendant there to assist a friend swindle the plaintiff in this transaction where no effort was made to pay even the very first instalment?

The second defendant having deceived the eye of the law, the law has been blinded by that deceit and cannot see him to protect him. As a result, he has turned to equity. But equity says his hands are tainted.

Being a lawyer and a long experienced advocate with dirty hands, equity runs away leaving him unprotected, for this is the kind of game he wanted to play and I too leave him continue playing it.

Accordingly judgment be and is hereby entered against the second defendant as prayed in the plaint dated 13th July 1999.

Dated and delivered at Nairobi this 25th day of January, 2002

J.M KHAMONI

JUDGE