Timba & another v Housing Finance Company of Kenya & another (Commercial Suit 660 of 2002) [2023] KEHC 20008 (KLR) (Commercial and Tax) (10 July 2023) (Judgment)

Neutral citation: [2023] KEHC 20008 (KLR)

REPUBLIC OF KENYA

IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)

COMMERCIAL AND TAX

COMMERCIAL SUIT 660 OF 2002

FG MUGAMBI, J

JULY 10, 2023

BETWEEN

SAMUEL O. TIMBA ..... 1ST PLAINTIFF

LYDIA NYAMBONYI ..... 2ND PLAINTIFF

AND

HOUSING FINANCE COMPANY OF KENYA ..... 1ST DEFENDANT

JOSEPH KARIUKI WANYUGI ..... 2ND DEFENDANT

JUDGMENT

Introduction And Background

1. The plaintiffs are husband and wife. They instituted this suit vide a plaint dated 28th May 2007 which was amended on 21st March 2007 and further amended on 24th July 2019. The plaint sought the following reliefs;

    i. A permanent injunction restraining the 1st and 2nd defendant and each of them whether by themselves, their appointed agents, servants or agents or employees from further transferring, leasing, charging. alienating. disposing and/or otherwise howsoever interfering with all that property known as Land Reference Number 36/111/948 Nairobi.

    ii. All further registration or change on registration in the ownership, leasing. subleasing, allotment, user, occupation or possession or in any kind of right, title or interest in all that parcel of land known as Land Reference Number 36/1 11/948 NAIROBI with any Land Registry, Government department

and all other registration authorities be and is hereby prohibited until further orders of this Honourable Court.

iii. A permanent injunction restraining the 2nd Defendant whether by himself, servants. employees and/or agents from taking possession, occupying collecting or demanding rent or other benefits of whatsoever nature and/or from evicting or otherwise howsoever interfering with the Plaintiffs' peaceful occupation and possession of all that property known as Land Reference Number 36/11 1/948 NAIROBI.

iv. A declaration that the sale and subsequent transfer and registration of the suit property to the 2nd Defendant is fraudulent, unlawful, illegal, null and void and that the Transfer registered on 17th January 2007 in favour of the 2nd Defendant be and is hereby nullified and/or cancelled.

v. A declaration that the offer to advance and the charge document and all subsequent dealings between the Plaintiffs and the 1st Defendant were procured through fraud and or deceit and hence null and void ab initio.

vi. A declaration that the Plaintiffs' equity of redemption was clogged and fettered and neither was the 1st Defendant entitled to the excessive monies demanded in that the same are illegal, oppressive, contrary to public policy and constitute a breach and variation of the Mortgage Contract, the *Central Bank of Kenya Act* and the *Banking Act*.

vii. An order directing the 1st Defendant to prepare and/or render a true, proper and accurate account of all the financial dealing conducted in the Plaintiffs' Mortgage Account No. 600-XXXXXXX from 1995 to date be taken.

viii. General damages for fraud.

ix. Such other consequential relief as this Honourable Court may deem fit and just to grant.

x. Costs of this suit together with interest thereon at court rates.

The Plaintiffs' Case

2. The genesis of this suit was a mortgage facility of Kshs. 3,600,000/= that the plaintiffs obtained from the 1st defendant, on 27th September 1995. The purpose of the facility was the purchase of a property known as L.R. No. 36/111/948 Eastleigh Nairobi (the suit property) consisting of a block of 17 single room flats and 12 two-bedroom flats which the plaintiffs rented out.

3. The terms of the loan were that the plaintiffs would repay the loan at an interest rate of 29% per annum on the principal loan. It was repayable over a period of 10 years with monthly instalments of Kshs. 92,250/=. According to the plaintiffs, parties had also agreed that no variation of interest would be made by the 1st defendant without informing the plaintiffs and that the 1st defendant would only charge maximum interest rates as approved by the Central Bank and other applicable statutory provisions.

4. The plaintiffs allege that during the pendency of the facility, the 1st defendant without issuing a statutory notice appointed a receiver to take over the running and management of the suit property. Although the receivership was later revoked, the sum of Kshs. 3,000,000/= which the receiver had collected over the 2 years that he was managing the property remained unaccounted for.

5. The plaintiffs obtained injunctive orders against the 1st defendant but sometime around 15th December 2006 they learnt that the 1st defendant was in the process of disposing off the suit property in order to realize loan arrears from their account, of an alleged Kshs. 19,680,284.95.

6. The plaintiffs instructed the Interest Rates Advisory Center (IRAC) to investigate the mortgage rates and amount owing. The findings by IRAC confirmed that the 1st defendant had been charging excessive rates beyond what was allowed by the Central Bank of Kenya, that the total sum collected by the receiver was never credited to the plaintiffs' account and that the amount owing as at 31st January 2007 should have been Kshs. 4,526,399.45 and not Kshs. 19,680,284.95. The plaintiffs therefore faulted the 1st defendant for acting illegally, unreasonably and in breach of its duty of care by charging illegal interest rates.

7. The plaintiffs also took issue with the 1st respondent for illegally selling the suit property by private treaty for a sum of Kshs. 9,000,000/= contrary to the market value of Kshs. 18,000,000/=. An independent valuation of the suit property commissioned by the plaintiffs dated 26th February 2007 indicated that the market value for the property was Kshs 17,425,000/=.

8. In order to prove their case, the plaintiffs called the 1st plaintiff, their independent valuer and a managing consultant with IRAC to testify.

The 1st Defendant's Case

9. The 1st defendant filed a statement of defence, a further statement of defence and further further statement of defence dated 2nd October 2019 denying the claim by the plaintiffs. It further relied on the witness testimony given by a Manager working at the Debt Management Unit at the bank.

10. The gist of the 1st defendant's case was that clause 3(a) of the mortgage instrument expressly gave it the right to vary interest rates and that failure to advice the plaintiff of the same would not affect recovery of the outstanding loan. The 1st defendant therefore confirmed that the rate of interest applied on the facility was in line with the provisions of the mortgage.

11. Although the 1st defendant admitted appointing a receiver when the plaintiffs defaulted in making the required payments, it noted that the plaintiffs interfered with the receiver and stopped him from accessing the suit property and collecting rent. On this account, the 1st defendant revoked the appointment of the receiver.

12. The 1st defendant further denied that the receiver had collected any rent from the suit property throughout the period of receivership. As a result of the frustrated receivership, the 1st defendant issued statutory notices of sale dated 28th September 2001 and 8th March 2005 and exercised its statutory power of sale through private treaty.

The 2 nd Defendant's Case

13. The 2nd defendant filed an amended statement of defence and counterclaim dated 20th July 2009. He also testified in court and confirmed that he had learnt of the sale of the suit property from advertisements and offered to buy it. He confirmed having entered into a sale agreement with the 1st defendant on 21st December 2006 where it was agreed that the property would be sold for Kshs. 9,000,000/=. Upon payment of the sum required the suit property was transferred to him.

14. He was therefore categorical that any dispute between the plaintiffs and the 1st defendant on interest rates was not relevant to him since he had purchased the suit property legally and at a reasonable market

price. The property was registered on 17th January 2007 and he acquired good title which was protected under the Government Lands Act and Indian Transfer of Property Act.

15. The 2nd defendant took issue with the plaintiffs for refusing to hand over the suit property to him and prayed for judgment by way of a counterclaim, against the plaintiffs seeking the following prayers: -

    i. An eviction order,

    ii. Mesne profit, the quantum thereof to be determined by this Honourable Court on the basis pleaded here above, together with interest at court rates from 17th January 2007, to the date when the 2nd defendant became the registered owner of the suit premises,

    iii. Costs and interest,

    iv. Any other relief this Honourable court would deem fit to grant.

Issues For Determination

16. I do not propose to rehash the witness testimonies as these were along the lines set out in the pleadings which I have summarized. I shall only refer to aspects of the evidence and submissions filed by the respective parties, where necessary, either to point out to a dispute or to clarify a point.

17. I have otherwise carefully considered the pleadings, evidence on record and rival submissions as well as authorities cited by all sides in support of their respective arguments. A substantial part of the facts are not contested. For the avoidance of doubt, I find that the following issues arise for determination: -

    i. Whether the 1st defendant lawfully exercised its statutory power of sale;

    ii. Whether the interest levied on the mortgage was illegal, unconscionable and higher than allowed by the law;

    iii. Whether the 2nd defendant was a *bona fide* purchaser for value;

    iv. Whether the plaintiffs and the 2nd defendant are therefore entitled to the prayers in the plaint and in the counterclaim.

Whether the 1st defendant lawfully exercised its statutory power of sale;

18. Clause 9(a) of the mortgage instrument entered into by the parties provides that the powers of sale and appointment of receivers conferred by Section 69 to 69G inclusive of the *Indian Transfer of Property Act 1882* shall apply to this mortgage.

19. Section 69A of the repealed Indian Transfer of Property Act 1882 provided thus;

> A mortgagee shall not exercise the mortgagee's statutory power of sale unless and until-notice requiring payment of the mortgage-money has been served on the mortgagor or one of two or more mortgagors, and default has been made in payment of the mortgage-money, or of part thereof, for three months after such service; or some interest under the mortgage is in arrear and unpaid for two months after becoming due;

20. Of relevance is the decision of the Court of Appeal in the case of *Trust Bank Limited vs Eros Chemists Ltd*. (2000) 2 E.A. at page 550. The Court addressed its mind to what constitutes a valid notice under section 69A of I.T.P.A. 1882 of India and held that;

> "... there is a mandatory requirement that a statutory right to sell will not arise unless and until three months' notice is given. We consider that the provision as to the length of the notice is a positive and obligatory one, failing obedience to it, a notice is not valid".

21. The evidence before the court indicates that a statutory notice was sent to the plaintiffs on 8th March 2005 by registered mail. A certificate of posting dated 11th March 2005 was also produced by the 1st defendant. The property was sold on December 2006. I therefore find no difficulty holding that the relevant statutory notices had been served on the plaintiffs. I disagree with their submission that they were not served.

22. Even prior to this, another statutory notice dated 28th September 2001 had also been sent by registered mail. Several demands for the outstanding amount had been made by the bank to the plaintiffs and the plaintiffs had made offers to make good the outstanding amounts. It is therefore not in dispute that the plaintiffs were aware of their default status.

23. The plaintiffs admit at paragraph 18 of their submissions that in fact the amount that was due to the bank should have been Kshs. 9,010,323.52 as opposed to Kshs. 19,680,284.90. It was open to the plaintiffs to pay up what they believed was due to the 1st defendant from their calculations, and then bring their claim against the Bank rather than stop payment altogether. On this account I therefore find that the bank was within its rights to exercise its statutory power of sale.

Whether The Interest Levied On The Mortgage Was Illegal, Unconscionable And Higher Than Allowed By The Law;

24. It is a matter of public knowledge that in the years between 1991 and 1997 Kenya implemented interest rate caps to respond to concerns raised by the public regarding the high cost of credit. During the periods in which a limit was set by statute, financial institutions were required to keep their lending interest rates within the prescribed statutory regulated limits and a failure to do so was unlawful. The applicable law with respect to regulation of interest rates in September 1995, was section 39 of the *Central Bank of Kenya Act* (CBK Act). It provided that:-

> The bank may from time to time to time acting in consultation with the minister determine and publish the maximum and minimum rates of interest which specified banks or specified financial institutions may pay for deposits and charge for loans or advances.

25. From the testimony given by the IRAC, at the time the parties were getting into the contract, the maximum rate of interest permitted and prescribed by law was 19% per annum. The 1st defendant did not deny charging 10% beyond the allowed interest rate but states in its defence that the plaintiffs had accepted this rate as per the mortgage agreement that parties had executed. In fact, the plaintiffs admitted that clause 3(a) of the mortgage agreement provided that the 1st defendant could vary the interest rates without notice to the plaintiffs. The 1st respondent therefore asked that the court should not rewrite a contract that parties had negotiated.

26. It is now well settled, considering a wide spectrum of judicial pronouncements, that courts will not interfere with contracts entered into by two consenting parties unless the terms are on the face of it are illegal, unconscionable, oppressive and fraudulent. This is in keeping with the need to balance between

the sanctity of contracts but at the same time recognizing the ever-existing reality that parties may not always negotiate from equal footing.

27. In such cases the court will interfere where the terms amount to unjust enrichment at the expense of desperate borrowers. It is certainly the duty of this court to release such parties from a bad bargain. This position was espoused in *Danson Muriuki Kihara Vs Johnson Kabungo* (2017) eKLR to the extent that

> " It is clear that the Court can interfere even where parties have agreed on a rate of interest as long as it is shown that the rate is illegal, unconscionable or fraudulent".

28. Likewise, in *Kenya Commercial Finance Company Ltd –vs- Ngeny & Another* (2002) 1 KLR it was stated that:

> " The court will not interfere where parties have contracted on arms – length basis. However, by its equitable jurisdiction this court will set aside any bargain which is harsh, unconscionable and oppressive or where having agreed to certain terms and conditions thereafter imposes additional terms upon the other party. Equity can intervene to relieve that party of such conditions."

29. This court associates with the foregoing pronouncements and holds that any interest charged beyond what was required by law at the time of executing the contract was unlawful and illegal and cannot be validated by an agreement between the parties. It is absurd that the 1st defendant appears to be saying that parties had agreed on an illegality and therefore the court should not interfere. The 1st defendant cites the case of *Francis Joseph Kamau v HFCK* (2014) eKLR which actually espouses this same principal.

30. Even after committing the illegality, the Bank went further to vary the interest rates at liberty without notice to the plaintiffs. In its defense, the 1st defendant stated that the mortgage agreement allowed it to do so but that time and again, it would send notices of interest variation to the plaintiffs. No evidence was provided in support of this. It also emerged that there was an element of penalty interest that was chargeable on the outstanding loan. The exact percentage was not disclosed to the plaintiffs but would be charged as 'other interest'.

31. Again, there are numerous judicial pronouncements on the issue. I concur with the court in the case of *Margaret Njeri Muiruri vs Bank of Baroda (Kenya) Limited* [2014] eKLR that even where a lending institution has a written clause permitting it to charge different rates of interest that discretion was not absolute. The discretion on the 1st respondent in the present case was not completely unfettered. It is indeed objectionable that a lender can vary interest to its benefit, without any recourse to or passing such information to the borrower, especially where such interest is illegal.

32. The plaintiffs produced a report from the IRAC detailing the over charge in interest rates. I note that the Bank did not controvert the findings of IRAC. It is such interest rates that led to the three-times-plus amount demanded by the bank, in disregard to the in duplum rule as provided for under section 44 of the *Banking Act*.

33. Having said this, I find that the interest rates charged by the 1st defendant on the facility were not only illegal. They were unconscionable and unreasonable for the reasons that I have given.

Whether The 2nd Defendant Was A *bona fide* Purchaser For Value;

34. The plaintiffs aver that the suit property was sold by the 1st respondent to the 2nd respondent at an undervalue. In order to prove this, the plaintiffs commissioned their own valuation which was

presented before the court. The report dated 26th February 2007 returned an open market value of Kshs. 17,425,000/= against the valuation by the bank carried out on 17th November 2006 which placed the suit property at an open market value of Kshs. 9,000,000/=.

35. I note that the two valuations were carried out just months apart. I am also conscious of the fact that having a counter valuation report is not sufficient reason to find that a sale was conducted at an undervalue as was held in *Zum Zum Investments Limited v Habib Bank Limited* (2014) eKLR. I would further concur with the finding in *Palmy Company Limited v Consolidated Bank of Kenya Limited* (2014) eKLR that: -

> " The Court needs cogent evidence and material in order to say that prima facie, there has been an undervaluation of the suit property which is an infringement of Section 97 (2) of the *Land Act* by the Defendant as to entitle the Court to call for an explanation or rebuttal from the Defendant. That approach is necessary to prevent defaulters from filing valuation reports with value way beyond the open market value just to obtain an injunction."

36. The 1st respondent made great effort in discrediting the report presented by the plaintiffs, including the fact that the witness was not the maker of the report. The defendants also attacked the qualifications of the witness.

37. In a curious turn of events, the record shows that the 1st defendant wrote to the plaintiffs on 14th November 2006 informing them that the suit property had been revalued to Kshs. 18,545,000/= as a result of which the 1st defendant went on to demand additional insurance premiums from the plaintiffs. It is not clear why there would be such a huge discrepancy in value of a property in an exercise carried out just days apart, even if the valuation report was for a different purpose.

38. More importantly, the 1st defendant has not denied the contents of this letter and has not demonstrated why the court should disregard the letter, since the valuation was commissioned by the bank. The figures presented in the letter are closer to the figures that the plaintiffs' valuer presented.

39. Since this correspondence was exchanged between the plaintiff and the 1st defendant, there is no evidence that the 2nd defendant would have known the actual value of the suit property. It is only unfortunate that the property was sold by way of private treaty and attracted only one bid. A public auction would have presented an opportunity for competitive bids which would have given a wider price indication. Is this sufficient to claim that the 2nd defendant was not a purchaser for value? I do not think so.

40. A *bona fide* purchaser for value has been described in the case of *Lawrence Mukiri Vs Attorney General & 4 Others* [2013] e KLR thus:-

> " ... A *bona fide* purchaser for value is a person who honestly intends to purchase the property offered for sale and does not intend to acquire it wrongly. For a purchaser to successfully rely on the *bona fide* doctrine, he must prove the following:
>
> i. He holds a certificate of Title.
>
> ii. He purchased the Property in good faith;
>
> iii. He had no knowledge of the fraud;
>
> iv. The vendors had apparent valid title;
>
> v. He purchased without notice of any fraud;

vi. He was not party to any fraud.

41. In addition to the purchase price of the suit property, the plaintiffs also allege fraud and collision on the part of the defendants, as the sale is further said to have taken place on a Sunday, which is not an official working day for the 1st defendant. I have looked at the documents on record and the explanation given by the defendants and I am satisfied that the date on the sale agreement, which falls on a Sunday, was indeed an inadvertent error. This is corroborated by the cheque made out to the bank by the 2nd defendant, which is said to bear the correct date of sale, which is not a Sunday.

42. Having previously stated that the sale was regular as the proper notices were sent out, I find that there has not been any evidence placed before court to show that there was fraud on the part of the 2nd defendant in acquiring the suit property. For these reasons, while I find that the 2nd defendant was a *bona fide* purchaser and in good faith, I do agree with the plaintiffs that the suit property was sold at an undervalue.

43. Having carefully considered all the issues, since the suit property has already been sold and transferred to the 2nd defendant, and further in light of section 99 of the *Land Act* which contemplates that damages are a remedy for any irregular sale, this court considers that the just orders would be for restitution to the plaintiff of what the 1st defendant denied them through an award of damages.

The 2nd Defendant's Counterclaim

44. Having so held, I must now decide whether the 2nd defendant is entitled to his counterclaim. Since I have already noted that the sale by the 1st respondent was regular and that property had already changed hands, the 2nd respondent is entitled to take possession of the property. Noting however that he benefited from the sale by paying way much less than the actual value of the property, I decline to award the mesne profits or interest as prayed. On the contrary, I find that the rent collected and held in a joint account pursuant to the orders of this Court, should be released to the plaintiffs.

45. For the avoidance of doubt, there are also other monies said to have been collected by the receiver/manager during the pendency of the alleged receivership. The plaintiff has not provided any evidence to prove that there was Ksh. 3,000,000/= collected by the receiver manager over a two-year period. There would therefore be no basis to make any order with regard to this allegation and I also find no basis to make the order for accounts, having made the findings which I am convinced are sufficient recompense to the parties.

Determination And Orders

46. This discussion then turns to the remedies that the parties deserve. The final orders of the Court are as follows: -

i. The court awards the plaintiff the amount of Kshs. 18,545,000/= which is the estimated value of the property at the time of sale, based on the insurance valuation last carried out on the property, less Kshs. 9,000,000/= being the actual amount received for the suit property.

ii. The court further awards the plaintiffs general damages assessed at Kshs. 2,000,000/= with interest thereon at court rates from the date of this judgment until payment in full.

iii. The rent amounts collected from the suit property and held in a joint interest account shall be released to the plaintiffs.

iv. For this reason and based on the finding that the 2nd defendant purchased the suit property at an undervalue, it would be wrong to allow the defendants to benefit from processes which do not inspire confidence in their transparency and as such, I reject the purchaser's counter-claim for mesne profits and interest. The prayer for eviction succeeds and as such the 2nd defendant shall be entitled to half of the costs from the plaintiff.

v. The Court is aware that the bank's case is that the plaintiffs are still indebted to it but the 2nd defendant has not made a counterclaim. Had it done so then the damages granted by the Court would first be applied towards offsetting the debt.

vi. The Plaintiff shall also have costs of the suit and half of the counterclaim.

DATED, SIGNED AND DELIVERED IN NAIROBI THIS 10TH DAY OF JULY, 2023.

F. MUGAMBI

JUDGE

Court Assistant: Ms. Lucy Wandiri.