



P&L Consulting Company Limited v Scribe Services Registrars & 2 others (Commercial Case E244 of 2019) [2024] KEHC 14372 (KLR) (Commercial and Tax) (20 November 2024) (Judgment)

Neutral citation: [2024] KEHC 14372 (KLR)

REPUBLIC OF KENYA
IN THE HIGH COURT AT NAIROBI (MILIMANI COMMERCIAL COURTS)
COMMERCIAL AND TAX
COMMERCIAL CASE E244 OF 2019
A MABEYA, J
NOVEMBER 20, 2024

BETWEEN

P&L CONSULTING COMPANY LIMITED PLAINTIFF

AND

SCRIBE SERVICES REGISTRARS 1ST DEFENDANT

DIANA GICHAGA 2ND DEFENDANT

MARGARET GICHAGA 3RD DEFENDANT

JUDGMENT

1. This suit was instituted by the plaintiff against the defendants vide a plaint dated 12/8/2019. The plaintiff sought judgment against the defendants for the reconstruction of the plaintiff company; that the 2nd and 3rd defendant do exit the plaintiff and hand over and transfer the shares of the plaintiff to the plaintiff; that the 2nd and 3rd defendant do pay for the shares issued and retained by them at the market rate; that the 2nd and 3rd defendant do release to the plaintiff all the files and documents belonging to the plaintiff company.
2. There were also prayers for compensation for loss suffered by the plaintiff as well as general damages for breach of fiduciary duty.
3. The plaintiff alleged that it was owned and managed by Mercy Sonia Randa and Mwalo Owiti, who was later replaced by the 2nd defendant, Diana Gichaga. In 2014, Diana nominated her mother, Margaret Gichaga, to hold the shares. That in 2016, the members made resolutions to return the company to its original proprietor, Mercy Sonia Randa.
4. The parties agreed that the remaining director and the 2nd defendant would split off the plaintiff's business into two separate entities owned independently. They devised two approaches for the



- demerger: a legal approach and a good faith approach. The legal approach required the 2nd and 3rd defendant to exit the company after reimbursing the plaintiff for any amounts owed. The good faith approach involved the 2nd and 3rd defendant exiting the company and relinquishing their shares while migrating with their clients, staff, assets, and liabilities to form a new entity, potentially called private equity support.
5. The 2nd defendant opted for the good faith approach and it was agreed that, the existing director would move to a new office of her choice with a request for an audit to be conducted. An audit was carried out by Messrs Clyde & Associates in April 2017.
 6. The plaintiff further alleged that despite the agreements and resolutions, the 2nd defendant, in collusion with the 1st defendant, allegedly reneged on many agreements and selectively chose how to exit the plaintiff company. As a result, the plaintiff suffered losses due to unpaid employee arrears, accrued debts from unpaid tax obligations, withholding of transfer documents that hindered the plaintiff's operations and missed opportunities.
 7. It was further alleged that the 1st defendant's breaches included refusing to follow instructions and undertaking unlawful and procedural changes to the plaintiff. It further illegally retained the plaintiff's files and necessary documents. The plaintiff expressed concerns that the defendants might make changes or alter *the constitution* of the plaintiff company without its consent.
 8. The defendants defended the suit vide a joint statement of defence dated 1/10/2019. The 2nd defendant acknowledged being a former director, while the 3rd defendant was a current shareholder of the plaintiff. The 2nd defendant denied that her shares, held in trust by the 3rd defendant, were unpaid. It was contended that the costs had been offset by various expenses shared with Mercy Randa, the remaining director of the plaintiff.
 9. It was claimed that the 2nd defendant joined the plaintiff company as a shareholder in 2013 and nominated her mother, the 3rd defendant, to hold 49% of the shares on her behalf. The plaintiff was said to have agreed to this arrangement and duly executed the transfer forms. A board resolution was passed to facilitate the transition of clients from the business line the 2nd defendant started to the new firm. That the 2nd defendant would transfer her shares to the remaining shareholder, Mercy Randa, under the condition that the latter would have no further claims against her.
 10. The 2nd defendant and the 1st defendant (the company secretary and auditor), alleged that it was against company law to require a shareholder to transfer his/her shares to another shareholder while at the same time demanding payment for those shares. The dispute arose when the 2nd defendant was asked to pay the plaintiff company an amount equivalent to 49% of her shareholding upon her exit, which she refused. She was informed that her shareholding had a negative value of Kshs 14,444,265/24, while the other director's 51% was valued at Kshs 14,181,411/70.
 11. The defendants contended that the memorandum of association did not contain any provision allowing for a shareholder to be legally compelled to transfer her shares to remaining shareholders and at the same time requiring payment therefor. The 2nd defendant stated that some clients she had brought to the company still remained with the plaintiff. Additionally, the 3rd defendant had signed the share transfer forms but was awaiting an undertaking that the existing director would have no claims against the 2nd defendant.
 12. The defendants therefore prayed for the plaintiff's suit to be dismissed with costs and the existing director Randa be directed to execute the necessary undertakings to enable closure of the matter.



13. At the trial, PW1 Mercy S. Randa adopted her witness statement dated 30/4/2020 as evidence in chief and produced the bundle of documents dated 12/8/2019 as Pexh1. She testified that the 2nd and 3rd defendant did not pay for the shares in the plaintiff and the 2nd defendant had benefited from 2014 to December 2016 as directors. That the valuation dated 24/1/2017 showed that the value of the 2nd defendant's shares was negative Kshs 14,444,265/24. That the company secretary, having been appointed by the plaintiff, was present throughout and he was instructed to conclude the separation and restructure of the plaintiff company.
14. The company secretary did not act as directed as he only retired the 2nd defendant as director but did not reconstitute the shareholding. The memorandum and articles did not allow for a sole director. That the company secretary held all the registration documents for profit and loss consulting and the registration documents for affiliate marketing. That she was unable to file taxes and not complied with beneficial owner regulations. That the company secretary owed the company a duty of care.
15. In cross-examination, she testified that the 1st defendant did not follow the given instructions. That the 2nd defendant resigned as director without due process, which was a violation of the memorandum of association. She admitted that there were discussions regarding her giving an undertaking that she would not seek payment from the 2nd defendant until the process was finalized, but she could not recall whether her advocate provided such an undertaking.
16. When she received notes from the company secretary, they indicated that the process was silent on compensation. She stated that the splitting of revenue and expenses was a consensus among the directors and the transfer of shares was not completed.
17. She further told the Court that the company did not owe the 1st defendant any fees, as he had stopped taking instructions from the plaintiff.
18. PW2, Mr. Clyde Mototso, is a registered and practicing member of the Institute of Certified Public Accountants of Kenya. He was appointed as the auditor for the profit and loss account. He confirmed that all shareholders were present at the meeting where the specific approach was decided.
19. In cross-examination, he admitted that there was a meeting where it was resolved that the 2nd defendant would receive compensation for part of the business being hived off. However, he noted that the resolution produced at page 25 of Pexh1 did not include the issues of valuation and compensation.
20. DW1 was Bernard Kirago Kamau, the company secretary. He testified that the first step was addressing the resignation of the former director and preparing a share transfer form. That however, the 2nd defendant did not release the transfer forms as she was waiting for an undertaking from Pw1. That was simply awaiting payment and noted that there were no instructions regarding who would assume the role of the 2nd director according to the memorandum of association.
21. In cross-examination, he confirmed his involvement in the restructuring, including assisting in the establishment of a different company and facilitating the director's resignation. When asked about the resignation of one director and leaving only one behind, he stated that he acted based on instructions from the client.
22. DW2 Diana Gichaga adopted her witness statement dated 3/2/2020 as her evidence. She testified that she was an executive director and shareholder but she chose to leave the business to the plaintiff. That she was to leave with her clients and leave the company at nil value. There was no agreement for payment for the shares. The company had corporate liability and its debts could not be passed individually to the directors.



23. That upon valuation of the company, it was established that there was a negative value. That she refused to sign the proposal on the way forward since she was required to make payments. That she asked her co shareholder for an undertaking which was not given. That there was nothing produced to show the liabilities payable by members and employees and there were no tax liabilities.
24. In cross examination, she stated that the company benefits shareholders. That shares are equity and not assets nor liabilities. There was no request to pay for the shares. She drew benefits from the work she did in between 2013 to 2016. She disputed the audit report.
25. The plaintiff submitted that the issue before Court was one of corporate governance and thus invited the Court to intervene and protect the plaintiff. That the 2nd defendant had established the plaintiff's business without taking heed of the loss occasioned to the plaintiff before the reconstruction and demerger as the business had been held in abeyance.
26. That the 2nd and 3rd defendant took advantage of the demerger to benefit from the business and in turn incapacitated the plaintiff as it could not proceed as a going concern. That the defendants colluded to reconstruct the plaintiff contrary to the memorandum of association of the company and the law on reconstruction of companies.
27. It was further submitted that the parties were enjoined to act in the best interest of the company in accordance with the law and the memorandum and articles of association. That the 2nd defendant was well aware of her responsibility and pending liabilities that survived her resignation.
28. It was submitted that the directors were responsible for the oversight of the audit process and since none of the other directors asked questions at the time, they are estopped from doing so when they are called upon to make payments. That the defendants had breached their duty to the plaintiff company. The 2nd defendant was under an obligation to exercise reasonableness in making decisions as a director for the benefit of the company.
29. With respect to the company secretary, counsel submitted that he was responsible for the efficient administration of the company with respect to ensuring compliance with statutory regulation requirements. That the 1st defendant placed the plaintiff in a position of extreme non-compliance with the law. That removing the 2nd defendant as a director was in conflict with the company's articles of association.
30. Further, that the 1st defendant's continued holding the plaintiff's files and the company details as lien for unpaid fees was an afterthought. That he never raised an invoice with the plaintiff prior to the court case. That the 1st defendant did not perform any service to the plaintiff for him to claim a lien. That the 1st defendant's move to refuse to release the documents paralyzed the financial activities of the plaintiff and in turn caused it loss and damage.
31. For the defendants, it was submitted that where a wrong is done to the company, the proper plaintiff would be the company itself and not individual shareholders. That the 2nd and 3rd defendant had not committed any wrong against the plaintiff and the existing director ought to have instituted the suit in her name and on behalf of the company.
32. On whether there was a breach of the demerger agreement, counsel submitted that the demerger agreement was never written and no document existed to prove that fact. That the parties did not document the process and methodology concerning the good faith approach. That the valuation report was not binding as it was an opinion of the auditors. It was the defendant's submissions that the demerger agreement was not signed by anyone and therefore there was no breach of that agreement.



33. Counsel submitted that the 2nd and 3rd defendant had no obligations or liabilities to the plaintiff and the same were not captured in the board resolutions of 9/12/2016. That there was no valuation done of the plaintiff when the shares were allotted to the 2nd defendant and the plaintiff was dormant and business had not picked. That it was unusual for a company to have both a negative and positive shareholder equity and it was fair to have the liabilities of the company ascertained and divided pursuant to the shares unpaid for by the shareholders.
34. It was submitted that one could not be compelled to pay for shareholding that had a negative value and therefore the 2nd and 3rd defendant did not have any outstanding obligations to the company. Counsel submitted that the plaintiff failed to specifically plead the losses and damages incurred as a result of the defendant's breach. He urged that the suit be dismissed.
35. I have carefully considered the pleadings and the submissions on record. The main issue is whether the plaintiff has established its case for grant of the orders sought.
36. It is uncontested that the issue between the parties emanated from the decision for demerger and for the shareholders to go separate ways. The Court was informed through the testimony of PW1 that the parties had narrowed down to two models which they called the strict legal approach and the good faith approach.
37. That the good faith approach was agreed by a resolution made at a meeting of 9/12/2016. It entailed the exit of the 2nd and 3rd defendant from the company by relinquishing their shares while migrating with their staff, clients as well as liabilities to form a new entity.
38. A disagreement arose when the 2nd and 3rd defendant were not agreeable to this model and made a condition that they would only comply if Pw1 gave an undertaking to the effect that the 2nd defendant would not be subjected to any payments. The 2nd defendant with the facilitation of the company secretary, the 1st defendant, was removed as a director a move that threatened the status of the company since the articles of association and the repealed Companies Act made it mandatory for a company to have at least two directors. The 1st defendant was accused of refusing to hand over the company files and compromising the status of the company.
39. On the first issue, the defendants, through their submissions have challenged the competency of the suit. According to them, the suit should not be a derivative claim since no loss has been occasioned to the plaintiff. The defendants submitted that PW1 ought to have instituted the suit in her name.
40. Derivative claims are vested under section 228 of the Companies Act 2015. The threshold being that the claim is brought by a member of the company with respect to a cause of action vested in the company and seeking relief on behalf of the company. These proceedings are brought in respect of a cause of action arising from alleged breach of duty and trust by a director of the company. For that reason, I find the suit to be competent. This position was upheld by the Court in the ruling made on 27/5/2019 where the Court granted leave for the suit to continue as is.
41. The next issue is the demerger and reconstruction of the company. The Court notes that the core of the dispute emanates from the shareholder's decision to demerger the company for purposes of reconstruction.
42. On the one hand, there is the plaintiff through its director PW1 apportioning blame on the defendants for sabotaging the process of reconstruction through failure to surrender shares, pay the requisite payments and surrender of documents. On the other hand, the defendants agreed that the 2nd defendant and PW1 Mercy Randa consented to spin off the business through the good faith approach,



- no process or methodology was agreed upon. The defendants argued that no documentation was signed to facilitate the transfer.
43. From the record, it is clear that the parties did not come up with a demerger agreement to bring into effect the terms and conditions of the demerger. The plaintiff relied on the resolution of 9/6/2016. In its submissions, the plaintiff invoked the duomatic principle which states that in the absence of a formal agreement, a company is bound by the unanimous agreement of the members.
 44. The Duomatic principle is a common law principle to the effect that anything that the shareholders of a company can do by formal resolution in a general meeting, can also be done by them informally if all of them assent to it.
 45. In *Re Duomatic Ltd* [1969] 2 CH 365, Buckley J held at pg 373C: -

“Where it can be shown that all shareholders who have a right to attend and vote at a general meeting of the company assent to some matter which a general meeting of the company could carry into effect, that assent is as binding as a resolution in general meeting would be.”
 46. In the present matter, it is evident from the resolution dated 9/6/2016 that the parties assented to the process of demerger. This was evident in the correspondence between the parties and the resolution was duly signed by the parties. Consequent thereto, the operations of the company stalled and the 2nd defendant was subsequently removed as a director.
 47. In this regard, the defendants cannot contend that there was no agreement with respect to the demerger. Their actions at the time spoke to the contrary. As to whether the duomatic principle was applicable the Court finds in the affirmative. The parties clearly agreed to the course of action through their collective conduct. By their actions and correspondence, they effectively demonstrated their consent to the demerger. The defendants cannot therefore claim that they had no obligation in relation to the demerger process.
 48. The next issue is with respect to how the demerger would affect the rights and obligations of the parties with respect to any financial obligations. An arrangement for reconstruction is basically a contract that parties are free to decide on the terms and conditions as well as consideration to be paid. This is why a valuation is important in order to ascertain the financial position that is the value of the company at the stage demerger.
 49. In the present case, a valuation was conducted and the defendants argued that the valuation report failed to capture or compute the value of the plaintiff as at the time of separation. The defendants argued that it would be fair to have the liabilities of the company ascertained from shares unpaid for by the shareholders.
 50. The company is a company limited by shares. In this regard, the assets and liabilities of the company should be apportioned based on the company's shareholding structure. As a company limited by shares, the allocation of the company's assets and liabilities during a demerger or restructuring process must reflect the proportionate interests of the shareholders in the company. This means that each shareholder's entitlement to the assets and liabilities of the company, post-demerger, will be determined by their respective shareholding percentages, unless otherwise agreed upon in the demerger plan.
 51. Upon reviewing the record, the Court finds that the proportionate allocation of assets and liabilities in this case is not clear. Furthermore, the valuation report has been contested, raising doubts about the fairness and accuracy of the apportionment of the company's assets and liabilities. The absence of a



- formal demerger agreement aggravates these concerns, as there is no clear framework in place to guide the distribution of the company's obligations and assets post-demerger.
52. Further, the resolution dated 9/6/2016, while indicating some agreement between the parties, failed to clearly outline the parties' respective obligations as it was supposed to. That notwithstanding, the Court finds that the 2nd and 3rd defendant cannot escape the obligations bestowed upon them as shareholders in the event of the demerger. If there are any liabilities or assets the same is binding on them based on the shares they hold. Valuation of the Company as at June, 2016 should be undertaken to settle this fact.
53. The other issue is whether the defendants were in breach of the fiduciary duties to the plaintiff. Black's Law Dictionary (11th Ed.) at p.770 defines "fiduciary" as someone who is required to act for the benefit of another person on all matters within the scope of their relationship; one who owes to another, duties of good faith, loyalty, due care and disclosure.
54. In Gower's Principles of Modern Company Law (4th edn.) at p. 571 states that: -
- “... In truth, directors are agents of the company rather than trustees of it or its property. But as agents, they stand in a fiduciary relationship to their principal, the company. The duty of good faith which this fiduciary relationship imposes are virtually identical with those imposed on trustees and to this extent, the description “trustee” still has validity. The duties of directors can conveniently be discussed under two heads: (a) fiduciary duties of loyalty and good faith (analogous to the duties of trustee's *stricto sensu*) and (b) duties of care and skill.” (See “Fiduciary Relationships” (1962) C.L.J. 69 and 91963) C.L.J. 119 and “The Director as Trustee” (1967) C.L.J. 83).
55. The plaintiff submitted that the defendants breached their fiduciary duties to the plaintiff by acting in ways that were contrary to the best interests of the company. Specifically, the plaintiff contended that the 2nd defendant's exit from the company was to her sole benefit and this action amounted to a breach of fiduciary duty. That the 1st defendant withheld crucial documents belonging to the plaintiff thereby crippling its operations.
56. The Court has carefully reviewed the evidence on record and finds that the 2nd defendant's exit from the company constitutes a breach of the duty of care and the duty to act in good faith for the benefit of the company. The duty of care requires directors to act with the level of care, skill and diligence that is reasonably expected of someone in their position.
57. The 2nd defendant's exit from the company was executed in a manner that appears to have favored her own interests to the detriment of the company. This is because, the articles of association of the company stipulated that the company should be run by a minimum of two directors. Therefore, any decision relating to the resignation or exit of a director should have been made in a manner that respected the legal and operational requirements of the company.
58. By failing to act in the company's best interests and ensuring that the company remained compliant with its own governance rules, the 2nd defendant violated the duty of care that she owed to the company and its shareholders. A failure to ensure that the company continues to meet its corporate governance requirements is a failure to fulfil the duty to act in good faith as well.
59. With respect to the 1st defendant, the Court finds that withholding crucial company documents constitutes a breach of fiduciary duty owed to the company. This was not just a failure to act in the company's best interest, but a direct violation of the trust placed on him. Company documents,



including financial records, corporate agreements and other important legal papers, are the property of the company and are vital for the management and operation of the business.

60. By withholding such documents, the 1st defendant failed in his duty to act in the best interests of the company, which includes ensuring that the company's records are accessible and properly managed. The actions of both the 1st and 2nd defendant were meant to incapacitate the plaintiff and they succeeded in doing so. Their actions were actuated by malice. They set to sabotage plaintiff's operations which they succeeded in achieving.
61. No issue of lien can arise as the same was never raised before the filing of the suit. No demand was ever made or invoice raised at the time that was unsettled for a claim of lien to arise. Therefore, the claim of holding the documents as lien fails.
62. Further, the company secretary was well aware of the legal obligations regarding the resignation of the 2nd defendant. He knew of his key role in ensuring that the company complies with its legal obligations, including the formalities surrounding the resignation of a director. It is clear from the evidence on record, that the 1st defendant, as company secretary, failed to address the matter appropriately and allowed the 2nd defendant's resignation to proceed without ensuring compliance with the company's articles of association and relevant legal requirements. On the face of it, the Court finds that the 1st defendant may have taken sides with the 2nd defendant thereby compromising his ability to fulfill his duties impartially and in the best interest of the company. The two were in collusion with each other to undermine the plaintiff.
63. In view of the foregoing, the Court finds that the plaintiff has proved its case on a balance of probability and enters judgment against the defendants, jointly and severally, as follows: -
 - a. The parties are hereby directed to complete the demerger and reconstruction of the plaintiff in a manner that clearly assigns obligations with respect to the assets and liabilities of the company. The allocation of these obligations must be proportionate to the shares held by each party.
 - b. To achieve (a) above, the parties to agree on a valuer who should value the plaintiff as at 9/6/2016 setting out the assets and liabilities of the company accordingly within 45 days of this Judgment.
 - c. The 1st defendant is hereby directed to release to the plaintiff within 14 days of this judgment, all the documents belonging to the plaintiff company.
 - d. The defendants are hereby found to have been in breach of their fiduciary duties to the plaintiff.
 - e. General damages of Kshs. 1 million plus interest from the date of this judgment.
 - f. The costs of the suit will be borne by the defendants jointly and severally.

It is so decreed.

DATED AND DELIVERED AT NAIROBI THIS 20TH DAY OF NOVEMBER, 2024.

A. MABEYA, FCI Arb

JUDGE

