



REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA

AT NAIROBI

MILIMANI COMMERCIAL & TAX DIVISION

CIVIL CASE NO. E028 OF 2021

MOHAMEDIN MOHAMED 1ST PLAINTIFF

HISH COMPANY LTD 2ND PLAINTIFF

VERSUS

IBRAHIM ISMAIL ISAAK 1ST DEFENDANT

YUSSUF ADAN HUSSEIN 2ND DEFENDANT

RULING

1. This is a ruling on the Notice of Motion dated 30/12/2020. It is brought under *sections 238 and 239 of the Companies Act, The Companies (General) Regulations 2015, Order 51 Rule 1 of the Civil Procedure Rules and sections 1A, 2B, 3 and 3A of the Civil Procedure Act and Article 159(2) of the Constitution of Kenya.*

2. The Motion seeks orders, *inter alia*, that: -

“ ” ii) *THAT the applicant be granted permission to continue the Derivative Claim seeking relief on behalf of Hish Company Ltd in respect of the acts and omissions by the Respondents, involving negligence, default, breach of duty and breach of trust in their capacity as directors of Hish Company Ltd on such terms as the Honourable Court considers fit.*

iii) *THAT pending the hearing and determination of this Application a temporary injunction do issue restraining the defendants, their servants, agents and/or employees from selling, alienating, transferring, charging, disposing, removing or in any way manner whatsoever dealing with the assets of the 2nd Plaintiff company.*

iv) *THAT pending the hearing and determination of this suit a temporary injunction do issue restraining the defendants, their servants, agents and/or employees from selling, alienating, transferring, charging, disposing, removing or in any manner whatsoever dealing with the assets of the 2nd Plaintiff company pending the hearing and determination of this Application.*

v) *THAT pending the hearing and determination of the derivative claim, the Respondents be compelled to produce the books of records, banking slips, audited financial accounts, bank statements of the 2nd Plaintiff company in their custody from 2015 up to date.*

vi) *THAT this Honourable Court be pleased to issue orders restraining the Board of intimidating and threatening the 1st Plaintiff/Applicant.*

vii) *THAT costs of this Application be provided for”.*

3. The application was supported by the affidavit of **Mohamedin Mohamed** sworn on 30/12/2020. The basis of the application is that the 2nd applicant is a Company established under the **Companies Act 2015** for purposes of doing business of excavation and supply of quarry stones and products in Kenya (hereinafter “the company”). That the 1st applicant is a minority shareholder thereon holding 100 shares out of 1000 shares.

4. On the other hand, the 1st and 2nd defendant are directors and majority shareholders holding 400 and 500 shares, respectively out of 1000 shares in the company. They are in charge of the daily operations and management of the company.

5. It was contended that the company had undertaken and completed several projects. However, the defendants have failed to convene a general meeting of the company since 2018. Neither have they declared any profit or paid any dividends. They have also not submitted financial accounts to the shareholders for accountability and good management purposes.

6. There are allegations of impropriety on the part of the defendants including fraudulently pocketing monies belonging to the company. They have also closed the business of the company and hired out its equipment thereby prejudicing the shareholders.

7. Although the defendants were served, they never filed any documents in opposition to the application.

8. The Court has considered the deposition on record as well as the written submissions dated 1/02/2021. This is an application for permission to continue a derivative suit. In **Ghelani Metals Limited & 3 others v Elesh Ghelani Natwarlal & another [2017] Eklr**, the court explained: -

“Derivative actions are the pillars of corporate litigation. As I understand it, a derivative action is a mechanism which allows shareholder(s) to litigate on behalf of the corporation often against an insider (whether a director, majority shareholder or other officer) or a third party, whose action has allegedly injured the corporation. The action is designed as a tool of accountability to ensure redress is obtained against all wrongdoers, in the form of a representative suit filed by a shareholder on behalf of the corporation: see Wallersteiner v Moir (No.2) [1975] 1 All ER 849, 38.

Until 2015, in Kenya, the common law guided derivative actions in Kenya.

With the advent of the Act, the law fundamentally changed. The requirement to fall under the exceptions to the rule in Foss v Harbottle was replaced with judicial discretion to grant permission to continue a derivative action. Judicial approval of the action is what now counts and such approval is based on broad judicial discretion and sound judgment without limit but with statutory guidance”.

9. Derivative claims now have their foundation in statute under **sections 238-241 of the Company’s Act**. These provide as follows: -

“1) In this Part, "derivative claim" means proceedings by a member of a company—

(a) in respect of a cause of action vested in the company; and

(b) seeking relief on behalf of the company.

(2) A derivative claim may be brought only—

(a) under this Part; or

(b) in accordance with an order of the Court in proceedings for protection of members against unfair prejudice brought under this Act.

(3) A derivative claim under this Part may be brought only in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director of the company.

...”.

17. It is clear from the Act that, the Court must first satisfy itself that there is a prima facie case on any of the causes of action set out under **section 238(3) of the Act**. If the evidence adduced in support of the application do not disclose a case for the giving of permission, the application is for dismissal. The importance of judicial approval under the Act, is therefore to screen out frivolous claims. The court will only allow meritorious claims to be litigated as derivative suits. In this regard, an applicant needs to establish, through evidence, that he has a prima facie case without the need to show that it will succeed.

19. At the second stage, the court will put into consideration statutory provisions and factors which ordinarily guide judicial discretion, albeit in the realm of derivative action. In view of the clear provisions of **Part XI of the Act**, the court determines applications for permission in exercise of discretion.

20. In **Isaiah Waweru Njumi & 2 Others –v- Muturi Ndungu [2016] Eklr**, the court set out some of the factors to be considered in such an application thus: -

“(a) Whether the Plaintiff has pleaded particularized facts which plausibly reveal a cause of action against the proposed defendants. If the pleaded cause of action is against the directors, the pleaded facts must be sufficiently particularized to create a reasonable doubt whether the board of directors’ challenged actions or omissions deserve protection under the business judgment rule in determining whether they breached their duty of care or loyalty;

(b) Whether the Plaintiff has made any effort to bring about the action the Plaintiff desires from the directors or from the shareholders. Our Courts have developed this into a demand or futility requirement where a Plaintiff is required to either demonstrate that they made a demand on the board of directors or such a demand is excused;

(c) Whether the Plaintiff fairly and adequately represents the interests of the shareholders similarly situated or the corporation. Hence, a shareholder seeking to bring a derivative suit in order to pursue a personal vendetta or private claim should not be granted leave. In the American case of *Recchion v Kirby* 637 F. Supp. 1309 (W.D. Pa. 1986), for example, the Court declined to let a derivative lawsuit proceed where there was evidence that it was brought for use as leverage in plaintiff's personal lawsuit;

(d) Whether the Plaintiff is acting in good faith;

(e) Whether the action taken by the Plaintiff is consistent with one of a faithful director acting in adherence to the duty to promote the success of the company would take;

(f) The extent to which the action complained against – if the complaint is one of lack of authority by the shareholders or the company – is likely to be authorized or ratified by the company in the future; and

(g) Whether the cause of action contemplated is one that the Plaintiff could bring directly as opposed to a derivative action”.

21. The foregoing then are the broad principles to be applied in considering applications for permission. In the present case, the plaintiff allege that he has fastidiously raised the issues he would like addressed in this derivative suit with the directors and management but the same has not been resolved. The 1st applicant has particularized five claims against the defendants. These are: -

a) Unapproved lending of company assets, and subsequent lack of accounting for funds received as rent. There is prima facie evidence that the defendants have, without the approval of the shareholders lent the company's equipment to a third party and the monies not accounted for.

b) Unapproved financial borrowing and subsequent misappropriation of the same. It has been contended that the defendants had borrowed Kshs. 9,185,000/= from various investors without the authority of the shareholders contrary to **section 155(1) of the Act**. This led to the filing of a claim against the company, *to wit*, **Civil Case No. MCCCMMMSU/190/2020**.

c) Failure to pay Employee salaries leading to the grounding of operations of the company. The strikes and other threats to the company led the 1st plaintiff to pledge his vehicle to settle employees' salaries.

d) Failure to submit Financial Accounts of the company since 2015.

e) Failure to hold Shareholders' Meetings since 2018.

25. These allegations have not been denied or controverted. They are particularized and if proved, could lead to findings against the defendants for the benefit the company. This is to say that, the claims could plausibly succeed if not rebutted or demonstrated to be false. They raise a *prima facie* case at least warranting for the case to proceed to trial. They disclose a plausible cause of action.

26. Further, the Court is satisfied that the circumstances surrounding this application do not reveal any of the negating factors which would lead to the disqualification of the applicants as either acting in bad faith or as pursuing private claims and filing this suit merely for nuisance.

27. In the premises, I find that the applicants have pleaded sufficient material to permit the derivative suit to proceed. Leave is, therefore, hereby granted.

28. The next issue is whether the plaintiffs have established a case for preliminary reliefs sought. The conditions for the grant of an interlocutory injunction are well settled as set out in ***Giella v Cassman Brown and co ltd 1973 E.A 360*** and ***Mrao v First American Bank of Kenya Ltd and 2 others 2003 KLR 125***.

29. These are that, an applicant must establish a prima facie case with a probability of success, that unless injunctive orders are granted he will suffer irreparable harm which would not be adequately compensated for by damages and that if the court is doubt, it will decide the matter on a balance of convenience.

30. On prima facie case, the allegations made in the affidavit have not been rebutted. They are arguable. The Court is satisfied that on the material on record, the matters raised are at least arguable.

31. On irreparable harm, in ***Halsbury's Laws of England, 3rd Edition volume 21, paragraph 739 page 352*** the writer observes: -

“Injury which is substantial and could never be adequately remedied or atoned for by damages, not injury which cannot possibly be repaired and the fact that the plaintiff may have a right to recover damages is no objection to the exercise of the jurisdiction by grant of injunction, if his rights cannot be adequately protected or vindicated by damages. Even where the injury is capable of compensation in damages, an injunction may be granted, if the injury in respect of which relief is sought is likely to destroy the subjected matter in question.”

32. The applicants have submitted that if the injunctive orders sought are not granted, they will suffer financial mismanagement, waste and loss of assets of the company, lack of prudent and diligent governance of the company and loss of funds. Those are damages that may not be compensatable.

33. The Court keeps in mind the contention by the applicants that the defendants had at some point become unreachable and only resurfaced in January, 2021. The Court is also alive to the fact that the excavator belonging to the company is currently engaged in business with **Tinaba Construction Company Limited**, which the applicants submitted is currently undertaking business in Sudan.

34. In this regard, this Court is called upon to balance between preservation of company assets, and the need to promote continuity of business for the company. It must bear in mind the financial status of the company and the need to keep it afloat to enable it meet its expenses such as payment of salaries.

35. To this Court's mind, it appears that the balance of convenience lies in granting the orders sought. The 1st applicant is a minority shareholder who is at a greater disadvantage as compared to the defendants. The latter have also been unreachable on some occasions, leaving the 1st applicant to deal with the financial burdens of the company.

36. The defendants are also at a greater advantage as they have borrowing power and have allegedly abused it on occasion. There is also a case against the defendants where it has been alleged that they have failed to enter their defence. In this case, the defendants did not oppose the application. In the premises, I find that the balance of convenience lies with the applicants.

37. Accordingly, I allow the application as prayed.

DATED and **DELIVERED** at Nairobi this 6th day of May, 2021.

A. MABEYA, FCI Arb

JUDGE