



REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT ELDORET

CIVIL SUIT NO. 61 OF 2004

ELTEX SACCO LIMITED.....PLAINTIFF

VERSUS

RIFT VALLEY TEXTILES LTD (Under Receivership).....DEFENDANT

RAPHAEL MASINDE.....DEFENDANT

JUDGMENT

1. **ELTEX SACCO LIMITED** (the plaintiff) has by an amended plaint dated 9th May, 2009 filed this suit seeking: -

a. Judgement against the defendants jointly and severally in the sum of Kshs 5,535,471/20cts

b. Costs of the suit and interest.

2. The plaintiff is a registered co-operative society which caters for the general welfare of the employees of **RIFT VALLEY TEXTILES LTD** (Under Receivership) (the defendant). To facilitate the process, members were required to make financial contributions to the scheme run by the plaintiff, which contributions would yield the savings from which emerging members' welfare matters would be addressed. The plaintiff relied on the 1st defendant to collect members' contributions as it had custody of the members' payroll, thus was in position to easily debit members salary accounts, and remit the cash collected to the plaintiff. The plaintiff claims that the 1st defendant deducted a total sum of Kshs 5,535,471/20cts from its members, but failed to remit the same to the plaintiff. Although these amounts were deducted during the pre-receivership period, it remained due and outstanding even after being placed under receivership, where **RAPHAEL MASINDE** (the 2nd defendant) was appointed the Receiver Manager. It is the plaintiff's case that the 2nd defendant was under an obligation to account for, and remit the money to it.

3. The defendants deny that such an arrangement ever existed or that the 1st defendant's employees were members of the plaintiff. It is also denied that any deductions were made from the employees for purposes of being remitted to the plaintiff, or that it is holding the sum claimed whether secured or unsecured. This court is urged to dismiss the claim on grounds that it has no basis

4. Pw1 (**JOHN CHRIS OTIENO**) who was appointed as the liquidator for of **Eltex Cooperative Society** (plaintiff) testified that the plaintiff was placed in liquidation on 30th December, 2005 vide a gazette notice dated 2nd June, 2006. The appointment was to last for one year but the same was extended for another year. He produced the appointment letters as Pexbt 1 and 2 respectively. He testified that the plaintiffs raised their money through contributions made by the members through their employer by check off system for onward transmission to the plaintiffs. After an inquiry was conducted by the **MINISTRY OF COOPERATIVE SOCIETY**, it was established that **RIVATEX** owed the plaintiff **Kshs. 2,320,400/-** after receivership. He further confirmed that the amount of Kshs. 5,535,421 is still owing to the plaintiff from the defendant, and was a pre receivership debt. That the debt was not incurred by **the Receiver of Rivatex**, but the directors of the company.

5. **DW1 (RAPHAEL MARIUS MOGIRE MASINDE)** testified that the 1st deft was not doing well, and on 21st May 1998, he was appointed a **RECEIVER MANAGER FOR RIFT VALLEY TEXTILES Limited** by Coopers and Lybrand who were the debenture holders. He managed the company for 11 years, while trying to realize the assets, for purposes of paying the accrued debts, and explained that when he took over the management of the company, he prepared a list of assets, liabilities debentures and statement of accounts. He found that **on debentures the secured creditors were owed Kshs. 340,342,734, which were classified in the TRUST DEED as: Category 1 - The Local Traders creditors who were owed Kshs. 160,988,667/15 cents, Category 2 - Foreign Trade Creditors were owed Kshs. 24,657,189 while Category 3 were the unsecured creditors loanees who included ICDC, INTERNATIONAL FINANCE CORPORATION, DEG, SIFIDA, IDB, DBK LTD, EAST AFRICAN DEVELOPMENT BANK LTD who were owed a total of Kshs. 883,697,280/-**

6. The 2nd defendant pointed out that **ELTEX SACCO** fell under local trade creditors who were not secured, and the amount owing to them

was **Kshs. 5,545,471/20 cts was therefore an unsecured debt.** As a Receiver Manager, so as to meet the debts, he sold the assets of the company to raise funds to pay secured creditors, and managed to raise **Kshs. 307,588,155/=**. He was supposed to pay the secured creditors first and if any money remained, it would then be paid to the unsecured creditors.

7. He sold the following:

- a) **Residential Estate A to MOI UNIVERSITY PENSION SCHEME for Kshs 14,000,000/-**
- b) **Estate B to MOI UNIVERSITY PENSION SCHEME at Ksh 71,555,600/-**
- c) **Estate C to MOI UNIVERSITY PENSION SCHEME at Kshs 13,555,555/-**
- d) **Motor vehicles and tractors sold at different prices, but realizing a total of Kshs 3,477,000/-**
- e) **Factory premises to MOI UNIVERSITY PENSION SCHEME at Kshs 205,000,000/-**

8. The sales did not raise enough money to pay the even the secured creditors, leaving a shortfall of Kshs 32,342,734/- so there was no money left to pay the unsecured creditors who included **ELTEX SACCO** as they were not priority creditors. The debt owed to Eltex arose before his appointment as a receiver and that he does not have money in his personal capacity to pay Eltex Sacco.

9. On cross examination, he admitted that there was a resolution clause in the trust deed considering all the debenture holders. Further, that he classified unsecured traders within three categories based on the trust deed and on information given by the directors. He explained that there was a consolation clause consolidating all the Debenture holders.

10. He confirmed the debt owed to Eltex Sacco amounting to Kshs. 5,535,471/20cts. He also confirmed that the former management used to deduct monies from the employees before the company was placed under receivership but was never remitted. That the information was given by Eltex officials and it is true that the deductions were from the workers' pay-slips.

11. In their submissions, the plaintiff stated that they were able to provide evidence to show that it had members who employees of the 1st defendant and that the sum of Kshs. 5,535,471.20 was deducted from these employees as their contribution to the scheme run by the plaintiff.

12. That the question on whether the plaintiff's claim should be rejected on application of the rules of priority in settling claims upon insolvency of a corporate body does not find foundation in the statement of defence filed.

13. The defendant concedes in its submissions that in compliance with the agreement between the plaintiff and its members, it made payroll deductions from the plaintiff's members for onward remittance to the plaintiff. However, in 1998, the 1st defendant became insolvent, resulting in the appointment of the 2nd defendant as the Receiver Manager. The 1st defendant contends that it could not pay any monies to its debtors, until the Receiver Manager realized all its assets, before embarking on payments of debts, in the order of preference. The Receiver Manager was able to realize the assets and paid the secured debtors, although the sums realized were not enough to fully settle the secured creditors. Consequently, the 1st defendant is unable to remit the sum outstanding.

14. It is not denied that there was an obligation on the part of the 1st defendant to make deductions and remit the same to the plaintiff. However, the argument is that from the appointment deed dated 15/6/1998, the 2nd defendant was appointed as a Receiver Manager by the debenture holders (secured creditors) of the 1st defendant, when the 1st defendant became insolvent. That this meant that the 2nd defendant was an agent of the secured creditors of the 1st defendant and as such his primary obligation was to look after the interests of his principals (i.e. the secured creditors).

15. The 1st defendant ceased to be in existence after it was wound up by the receiver manager upon realization of its assets and part settling of the secured creditors debts a total sum of Kshs1,422,910,698/15cts, (One billion. Four hundred and twenty-two million nine hundred and ten thousands, six hundreds and ninety-eight shillings and fifteen cents) which included

- 3 secured creditors who were owed Kshs 340,342,734/-
- 173 unsecured local creditors who were owed Kshs. 160,988,676/15cts
- 33 unsecured foreign trade creditors who were owed Kshs. 24,657,189/-
- 8 unsecured creditors (loanees) who were owed Kshs 883,697,280/-
- 2 preferential creditors who were owed Kshs. 13,224,819/-

— apparently, the plaintiff was not one of the secured creditors.

16. The defendants argue that at the time of the 2nd defendant's appointment, the alleged debt had already accrued and therefore cannot be held liable on account of debts that had already accrued before the appointment.

17. Further that at the end of the realization process, the 2nd defendant had only managed Kshs. 307,588,155.00 against the outstanding debts of Kshs. 1,422,910,698.15, and that he made the payments in accordance with the provisions of the **Companies Act at section 302 which provides that;**

302. Costs of voluntary winding up All costs, charges and expenses properly incurred in the winding up, including the remuneration of the liquidator, shall be payable out of the assets of the company in priority to all other claims.,

Also the provisions of section 310 which is to the effect that:

310. Application of bankruptcy rules in winding up of insolvent companies In the winding up of an insolvent company the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors and to debts provable and to the valuation of annuities and future and contingent liabilities as are in force for the time being under the law of bankruptcy with respect to the estates of persons adjudged bankrupt, and all persons who in any such case would be entitled to prove for and receive dividends out of the assets of the company may come in under the winding up and make such claims against the company as they respectively are entitled to by virtue of this section.

As well as section 311

18. It is further contended that from the assets, the 2nd defendant was only able to recover a total of Kshs 307,588,155/- (Three hundred and seven million five hundred and eighty eight thousands, one hundred and fifty five) and taking into account the total sum of Kshs 13,224,819/- owed to the secured creditors, and the preferential creditors (i.e. fees for the Receiver Manager and employees' salaries) who rank in priority to all other claims, then all the other outstanding creditors including the plaintiffs could not be paid

29 The words of Jenkins LJ in *Re B Johnson & Co (Builders) Ltd*, [1955] 2 All ER 775 at page 790 are instructive:

“...whereas a receiver and manager for debenture-holders is a person appointed by the debenture-holders to whom the company has given powers of management pursuant to the contract of loan constituted by the debenture and as a condition of obtaining the loan, to enable him to preserve and realize the assets comprised in the security for the benefit of the debenture-holders ...The primary duty of the receiver is to the debenture-holders and not to the company. He is receiver and manager of the property of the company for the debenture-holders, not manager of the company. The company is entitled to any surplus assets remaining after the debenture debt has been discharged, and is entitled to proper accounts.”

19. As soon as the receivers complete their assignment, which may invariably include gathering in, managing and realizing the assets charged with a view to liquidating the secured creditors' debt, their involvement in the management of the company comes to an end and the control reverts to the directors of the company.

20. The receiver/manager is bound to settle pre-receivership debts. The receiver manager prepared a statement of accounts immediately upon his appointment in which he noted that the 1st defendant's debts stood at Kshs. 1, 422, 910,698.15 while the recovered assets amounted to Kshs. 307,588,155 was thus prudent to pay the debenture holders.

21. A secured creditor has rights over the property protected by the security agreement and statutory provisions where applicable. These rights take precedence over the administration and liquidation process in the sense that the holder of those rights is entitled to exercise them at any time.

22. The position is summarized in *Halsbury's Laws of England* (3rd Ed, Vol. 6) at para. 968 where the learned authors state as follows:

As a general rule, however, the holder of a debenture or debenture stock of a company has a charge or where the debenture stock is secured by a trust deed the trustees usually have a legal mortgage on specific assets of the company, and, if so, he or they can enforce the usual remedies of a legal or equitable mortgage against the company in the same manner as it were an individual. One of these rights is to have a sale of the property charged, either under the power given by the charge or by statute, or with the assistance of the court. If the company goes into liquidation, the rights of a secured creditor under his security are not prejudiced, and the liquidator cannot obtain an injunction to restrain a sale by the secured creditor except on the usual terms of paying the amount due, or, if it is not agreed, paying the amount claimed into court.

23. As regards the appointment of a receiver, the learned authors go further, at para. 969, to state that:

The power of the secured creditor to appoint a receiver under his security can be exercised after the company has gone into liquidation, and, where a receiver has been so appointed, the court will not, if the appointment is valid, displace the receiver by appointing the liquidator in his place.

24. The position of Eltex Sacco against the Company is that it is an unsecured creditor. It has no interest in the Company's property of secured in favor of secured creditors. The appointed receiver manager exercised his powers in accordance with the provisions of the law. The plaintiff ought to have pursued the previous directors of the company and not the receiver manager. Their suit is thus not merited and is dismissed. Each party shall bear its own costs

E-Delivered and dated this 8th day of July 2020 at Eldoret.

H.A. OMONDI

JUDGE

Mr. Mukhabane present for the defendants