



REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

MILIMANI LAW COURTS

COMMERCIAL & ADMIRALTY DIVISION

CIVIL CASE NO.159 OF 2018

JAMES NDUNGU GETHENJI.....APPLICANT

VERSUS

FREDRICK GITAHU GETHENJI.....1ST DEFENDANT

ARI FARM LIMITED.....2ND DEFENDANT

AND

WAGEMA LIMITED.....INTERESTED PARTY

RULING

(1) Before this court is the Notice of Motion dated 25th April 2018 and filed on even date in which the Plaintiff seeks the following Orders:-

“(1) SPENT

(2) THAT leave do issue to the Plaintiff/ Applicant to prosecute and proceed with the derivative suit filed herewith against the Defendants.

(3) THAT a temporary injunction do issue restraining the 1st and 2nd Defendants, their agents, servants or any other person under their instruction, consent, authority and control from selling, charging, disposing, letting, leasing or in any other manner whatsoever dealing with all those properties known as L.R NO.3862/2(I.R NO.108886), L.R 27776 (I.R NO. 31950/12). And L.R. NO.3861/19 all situated in Kitusuru and any other assets of the Interested Party pending hearing and determination of this application.

(4) THAT a temporary injunction do issue restraining the 1st and 2nd Defendants, their agents, servants or any other person under their instruction, consent, authority and control from selling, charging, disposing, letting, leasing or in any other manner whatsoever dealing with all those properties known as L.R No.3862/2(I.R NO.108886), L.R 27776(IR NO.31950/12, and L.R.NO. 3861/18 all situated in Kitusuru and any other assets of the Interested Party pending hearing and determination of this suit.

(5) THAT pending the hearing and determination of this suit a mandatory injunction do issue compelling the 1st and 2nd Defendants to render a true account of all rental and other income derived from its operations on the Interested Party's properties known as L.R.No.3862/2(I.R.NO.108886),L.R 27776(IR.NO.31950/12, and L.R. NO. 3861/19 all situated in Kitusuru, and other assets of the Interested Party.

(6) THAT pending the hearing and determination of this suit a mandatory injunction do issue compelling the 1st and 2nd Defendant to deposit in court all rental and other income derived and received from its operations on the Interested Party properties known as L.R No.3862/2(I.R NO. 108886), L.R 27776 (IR NO.31950/ 12, and L.R.NO. 3861/19 all situated in Kitusuru and other assets of the Interested Party.

(7) THAT pending the hearing and determination of this suit a temporary injunction do issue restraining the 1st Defendant

from dealing in any manner whatsoever with all the monies held in the Interested Party's STANDARD CHARTERED BANK KENYATTA AVENUE BRANCH A/C NO. 0102023006700.

(8) THAT the Plaintiff be indemnified by the Interested Party for all the expenses reasonably incurred in respect of prosecuting the suit herein.

(9) THAT this Honourable court be pleased to grant leave to the Plaintiff to serve summons and all other court documents by way of email.

(10) THAT costs of this application be provided for.

The application which was supported by the affidavit of **JAMES NDUNGU GETHENJI**, (the Plaintiff herein) sworn on **25th April 2018** and Further Affidavit sworn on **6th May 2018**.

(2) The application was opposed by the 1st and 2nd Defendants through the Replying Affidavit sworn on **18th May 2018** by **FREDRICK GITAHU GETHENJI** (the 1st Defendant herein). The Interested Party **WAGEMA LIMITED** also filed in opposition to the application a Replying Affidavit sworn on **18th May 2018** by **HILDA WANGARI GETHENJI** a Director and shareholder of the Interested Party.

The court directed that the matter be disposed by way of written submissions. The Applicant filed his written submissions on **5th July 2018**, whilst the Defendants and the Interested Party filed their submissions on **17th September 2018**.

BACKGROUND

(3) The parties in this suit are all members of one family. **Hilda Wangari Gethenji** is the mother of **James Ndungu Gethenji** (the Plaintiff) and **Fredrick Gitahi Gethenji** (the 1st Defendant. The three together with another brother **ROBERT MEREKIA GETHENJI** are all directors/shareholders in **Wagema Limited**, the Interested Party holding shares as follows:

(i) Hilda Wangari Gethenji - 125 shares

(ii) Robert Merekia Gethenji - 125 shares

(iii) Fredrick Gitatu Gethenji - 125 shares

(iv) James Ndungu Gethenji - 125 shares

The patriarch of the family **Joseph Augustine Gethenji** passed away on **3rd June 1997**. The Interested Party was incorporated in 1972 and its business includes purchasing and holding investments. The company is the registered owner of

- **L.R No.3862/2(IR NO.108886)**,

- **L.R 27776 (IR NO.31950/12) and**

- **L.R.NO.3861/19**

which properties are all situated in the Kitisuru area of Nairobi.

(4) The Plaintiff avers that sometime in the year 2009 the Company passed a resolution to suspend all commercial activities on its properties. That notwithstanding this resolution the 1st Defendant together with her wife one "**Winnie Gitahi**" incorporated a new company called **ARI LIMITED** (the 2nd Defendant herein). They proceeded to fence off and lease out one acre of the Company premises to third parties, thereby realizing profits from the rent collected. The Plaintiff contends that such profit ought to have accrued to the company. The Plaintiff further avers that from January 2017, the 1st Defendant irregularly and without authority alienated several acres of **LR NO.3862/2** situated in Kitisuru, where he caused to be erected a chain link fence, several greenhouses, a borehole and other structures and embarked on commercial activity by conducting organic farming on several acres of property belonging to the company. He alleges that the 1st Defendant is marketing and selling produce derived from the said farming activities without any legal authority from the company and to the detriment of the other shareholders.

(5) The Plaintiff goes on to aver that the 1st and 2nd Defendants have been collecting rents from unauthorized structures erected on land belonging to the company, and has failed to give any account of the sums collected nor remitted the income so derived to the company. The Plaintiff contends that the actions of the 1st Defendant amount to a breach of duty and breach of trust of his position as director and shareholder of the company. That the unauthorized actions of the 1st Defendant has resulted in misappropriation and depletion of company property and has denied the company its right to derive benefit from its own properties. Finally the Plaintiff avers that despite the 1st and 2nd Defendants being asked to vacate company property, they have adamantly refused and/or declined to do so.

(6) On his part the 1st Defendant denies any wrong doing. He concedes that he and his wife did form the Company **Ari Limited** the 2nd Defendant to carry out organic farming in greenhouses built on two acres of land on LR No.3862/2, which farming activity had been ongoing

for about two years. The 1st Defendant avers that this farming was undertaken with the full knowledge and consent of all the other shareholders of the company and that in any event the Plaintiff had not raised any issue when these activities commenced.

(7) **Hilda Wangari Gethenji** a director/shareholder in the Company and mother to the Plaintiff and 1st Defendant swore an affidavit for the company in support of the 1st Defendant and in opposition to the present application. She avers that prior to 2017, she had leased about ½ acre of **LR 3862** to one **Agnes Maganyo** who was carrying out organic farming on the land and none of her sons objected to this activity. It was only after 7 years when the said **Agnes Maganyo** left the site that the 1st Defendant and his wife took over the organic farming under the name of the **Ari Farm Ltd** (the 2nd Defendant). It is averred that this farming activity was fully approved by herself and **Robert Marekia Gathenji**, one of her other sons who is also a Shareholder/Director of the company.

(8) **Hilda Wangari Gethenji** further avers that the 3 properties owned by the company have had rental rooms with tenants in occupation for the past ten years. These were staff quarters which had been erected when the company was engaged in flower farming. The said rooms were later rented out to tenants and she avers that the 1st Defendant collects the rent and accounts to her for the same.

(9) The said **Hilda Gethenji** denies that a resolution was passed in 2009 suspending all commercial activity on company land and avers that the company is currently constructing a residential estate comprising 55 houses known as “**Kihingo Village**” on **L.R 27754** which was hived off from **L.R 3862**. It is also denied that the 1st Defendant is the sole signatory of the company’s bank account held at Standard Chartered Bank as **Hilda Gethenji** avers that **both** herself and the 1st Defendant are signatories to that account. She asks that the present application be dismissed with costs.

ANALYSIS AND DETERMINATION

(10) It is always very unfortunate when family disputes spillover into the arena of the Courts. In such a case where all the Directors/Shareholders of the company are members of the same family, it would have been desirable for parties to reach an out of court settlement. Be that as it may, the matter is now before the court which must render a decision on the same.

(11) I have carefully considered the rival submissions filed by the parties in this suit, the authorities cited therein as well as the relevant law. There is only one issue for determination, that is whether leave should be granted to the Plaintiff to proceed with a derivative suit against the Defendants. **Blacks Law Dictionary 10th Edition** defines a derivative suit/action in the following manner:-

“ A suit by a beneficiary of a fiduciary to enforce a right belonging to the fiduciary, especially a suit asserted by a shareholder on the corporation’s behalf against a third party (usually a corporate officer) because of the corporations failure to take some action against a third party.”

In Kenya the provisions concerning derivative actions are to be found in **Section 238 to Section 242 of the Companies Act, 2015**. Section 239, 240 and 241 are all material to the present application

In order to determine the present application two considerations must come into play;-

- (i) Has the Applicant established a prima facie case to warrant the orders sought?
- (ii) Is the application brought in good faith?

(i) Prima Facie Case

(12) Section 241(2) of the **Companies Act 2015** provides as follows:-

“(2) In considering whether to give permission, the Court shall take into account the following considerations:-

- (a) whether the member is acting in good faith in seeking to continue the claim:**
- (b) the importance that a person acting in accordance with Section 143 would attach to continuing it.**
- (c) if the cause of action results from an act or omission that is yet to occur whether the act or omission could be and in the circumstances would be likely to be:-**
 - (i) Authorized by the Company before it occurs; or**
 - (ii) Ratified by the Company after it occurs;**
- (d) If the cause of action arises from an act or omission that has already occurred - whether the act or omission could be and in the circumstances would be likely to be ratified by the company.**
- (e) Whether the company has decided not to pursue the claim.**

(f) Whether the act or omission in respect of which the claim is brought gives rise to a cause of action that the member could pursue in the members' own right rather than on behalf of the company.

(3) In deciding whether to give permission, the court shall have particular regard to any evidence before it as to the views of members of the company who have no personal interest/direct or indirect in the matter.

(13) The general rule as established in the case of **FOSS –VS- HARBOTTLE 67 All ER 189** is that in any action in which a wrong is alleged to have been done to a company, the proper claimant is the company itself. However there are several important exceptions to this general rule and one such exception is a “**derivative action**” which allows a minority shareholder to bring a claim on behalf of the company.

(14) The Court of Appeal in Kenya in **GRACE WANJIRU MUNYINYI & Another –VS- GIDEON WAWERU GITHUNGURI & 5 others 2011 eKLR** summarized the principle in **FOSS –VS- Harbottle** as well as its exception in the following words.....

“The classic definition of the rule in *Foss Vs Harbottle* is stated in the judgment of Jenkin LJ in *Edwards Vs Halliwell* [1950] 2 ALL ER 1064 at 1066 as follows. (1) The proper plaintiff in an action in respect of a wrong alleged to be done to a corporation is, prima facie, the corporation (2) where the alleged wrong is a transaction which might be made binding on the corporation and on all its members by a simple majority of the members, no individual member of the corporation is allowed to maintain an action in respect of that matter, because, if the majority confirms the transaction, *caditquaetstio*; or, if the simple majority challenges the transaction, there is no valid reason why the company should not sue. (3) There is no room for the operation of the rule if the alleged wrong is *ultra vires* the corporation, because the majority shareholders cannot confirm the transaction. (4) There is also no room for the operation of the rule if the transaction complained of could be validly sanctioned only by a special resolution or the like because a simple majority cannot confront a transaction which requires the concurrence of a greater majority. (5) There is an exception to the rule where what has been done amounts to fraud and the wrongdoers are themselves in control of the company. In this case the rule is relaxed in favour of the aggrieved minority, who are allowed to bring a minority shareholders action on behalf of themselves and all others. The reason for this is that, if they were denied that right, their grievance could never reach the court because the wrongdoers themselves, being in control, would not allow the company to sue.”

The rule in *Foss Vs Harbottle* still stands in Kenya. The exception to the rule referred to above may be taken advantage of by minority shareholders if they can show fraud but they cannot do so by way of a petition. They can only do so as plaintiffs in a derivative action.”

Section 239(2) of the **Companies Act** requires that the court do refuse such applications where no prima facie case has been established. Therefore at this stage the court must consider two things. Firstly whether the Applicant has disclosed a prima facie case and secondly whether there has been an act of omission by one or more of the directors of the company within the meaning of Section 283 of the Act.

(15) In the case of **ISIAH WAWERU NGUMI & 2 others –VS- MUTURI NDUNGU, 2016 eKLR, Hon Justice Joel Ngugi** set out the factors which the court ought to consider in determining whether or not a prima facie case meriting leave has been established, as follows:-

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 efforts 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 Vs 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 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 complainant 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 as a direct as opposed to a derivative action”.

(16) I note that in the present case the Applicant is a minority voice in the company. The other two directors are clearly in agreement and the court has heard nothing at all from **Robert Marekia Gethenji** (the 4th Director/ Shareholder).

The Plaintiff herein has raised at least two particularized claims which he would like to have addressed in a derivative suit. One is the

question of failure or refusal to remit monies owed to the company by the 1st and 2nd Defendants and secondly mismanagement of company finances through the opaque behavior of the directors who have the mandate to operate the company account. The Plaintiff has demonstrated that he did raise these issues through letters written to the company (**Annexures JNG 6 and JNG 7**) to no avail. Similarly efforts to call for a meeting of the directors did not bear any fruit. All these disclose a plausible cause of action or in other words establish a prima facie case. Derivative actions are a remedy for minority shareholders against oppression. Aside from **“Robert Marekia Gethenji”** whom the court has not heard from it is obvious that the 1st Defendant and his mother **Hilda Gethenji** both sit on the same side of the fence over the issues raised. Based on the foregoing, I am indeed satisfied that the Applicant has pleaded sufficient material to permit the derivative suit to proceed.

GOOD FAITH PRINCIPLE

(17) The **“good faith”** requirement was designed to prevent proceedings of this nature being brought for selfish reasons that would further the purposes of the Applicant himself rather than the good of the company. **Section 241(2)** of the **Companies Act 2015**, obliges a court considering an application for leave to bring a derivative suit to take into account.

“(a) whether the member (applicant) is acting in good faith in seeking to continue the claim.”

However the mere fact that a shareholder stands to derive some benefit from the derivative claim will not automatically disqualify him from leave. The court must be satisfied that the main advantage of such derivative suit will flow to the company and any minor benefits that may accrue to the applicant are permissible.

(18) This **“good faith”** test is best encapsulated in the Australian case of **LESINI & others – VS – WESTRIP HOLDINGS LTD & others [2009] EWHC 2526** in which it was stated:-

“If the [Plaintiff] brings a derivative claim for the benefit of the company, he will not be disqualified from doing so if there are other benefits which he will derive from the claim.”

Generally speaking where the court is satisfied that a prima facie case has been made out it would be difficult to show that the Applicant for leave does not honestly believe that the company has a cause of action with a reasonable prospect of success.

(19) In this case the Defendants have averred that the Applicant’s motivation for seeking leave is the personal vendetta he has against the other family members. However these averments remain mere allegations and are not sufficient to demonstrate that the Applicant in this case has no motive other than bad faith.

CONCLUSION

(20) Based therefore upon the foregoing, I am satisfied that the present application for leave to continue claim this as a derivative suit has merit. Accordingly I do grant Prayer (2) and (3) of this application. I however decline to grant prayer (9) for service of summons by email. Summons will be served upon all parties in the normal manner.

Dated and Delivered in **Nairobi** this **1st** day of **March** 2019

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Justice Maureen A. Odera