REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

MILIMANI LAW COURTS

COMMERCIAL AND TAX DIVISION

CORAM: D. S. MAJANJA J.

CIVIL APPEAL NO. 12 OF 2019

BETWEEN

RED GEMS INVESTMENT GROUP LIMITED.....APPELLANT

AND

IRENE CHEPKOECH CHUMO.....RESPONDENT

(*Being an appeal from the Judgment and Decree of Hon. E. Wanjala, RM dated 11th February 2019 at the Magistrates Court at Nairobi in Civil Case No. 855 of 2017*)

JUDGMENT

1. The appellant appeals against the judgment and decree of the trial court where the learned trial magistrate held as follows:

> *I agree with the plaintiff that based on clause 20 of the agreement dated 29.6.2016 that the agreed interest rate was 13% from the date of default till payment in full, the defendant is in default of over 27 months at an interest rate of 13% per month which translates to Kshs. 130,000/- per month which makes a total of Kshs. 3,510,000/- as at the date of writing this judgment, clearly the amount is over and above the Principal sum of Kshs. 1,000,000/- and I find that section 44A of the Banking Act applies to this suit. I agree with the defendant that indeed the 13% per month interest rate as a must as it is contractual but is unconscionable and in the circumstances and from the defendant's submissions she argues that the court interest rates should apply in the case before me. However, since the defendant deprived the plaintiff the use of the money, I will award interest on the principal sum of Kshs. 1,000,000/- at court rates from the date of default and that is September 2016 till payment in full …..…*

2. The appellant's case against the findings I have set out about, is outlined in the memorandum of appeal dated 7th March 2019 and its advocates' written and oral submissions. The thrust of that case is that the trial magistrate erred in law by holding that 13% interest per month charged by the appellant for money borrowed by the respondent was unconscionable yet it was the agreed rate of interest in the loan agreement between the parties dated 29th June 2016 ("the Agreement").

3. The appellant contended that in awarding interest at court rates, the trial court erred by determining an issue that was not pleaded in the defence. In addition, the appellant complained that the trial magistrate erred in finding that the provisions of **section 44A** of the ***Banking Act (Chapter 488 of the Laws of Kenya)*** applied to the transaction between the parties notwithstanding that the appellant is not a banking institution. The appellant further complained that the trial magistrate erred by finding that the respondent was to pay interest on the default amount at court rates and not the agreed rate of interest. The circumstances, the appellant added that the court also erred by re-writing the agreement between the parties.

4. The respondent opposed the appeal on the basis of her advocates' written and oral submissions. Her position was that the rate of interest charged by the appellant was unconscionable in the circumstances and that the trial magistrate came to the correct conclusion in the judgment. The respondent argued that the issue of unfairness of the interest rate was pleaded in the statement of defence and in the event it was not, it was matter that was left to the court for determination thus the trial court was right in making such a finding. The respondent also argued that **section 44A** of the ***Banking Act*** which limits the interest rate charged by banks was applicable to the appellant as it was carrying on the business of banking by, inter alia, lending money to members of the public. The respondent maintained that the trial magistrate come to the correct conclusion based on the facts of the case.

5. In dealing with the issues raised by the parties, it is important to recall the general principle governing the exercise of this court's appellate jurisdiction. It is that the first appellate court is required to reconsider the evidence, evaluate it and draw its own conclusions making an allowance for the fact that it neither heard nor saw the witnesses testify (see ***Selle v Associated Motor Boat Company Ltd*** **[1968] E.A. 123, 126**).

6. The underlying facts of the dispute are not contested. In addition, the respondent did not cross-appeal against the findings and ultimately the judgment of the trial court hence the only for determination revolves around the application of interest on the principal amount. Under the Agreement, the appellant lent the respondent Kshs. 1,000,000/- attracting interest at 13% per month. It was also agreed that the money would be paid back within 3 months from the date of execution. Clause 20 of the Agreement stated as follows:

> *Interest under this Agreement for the purpose of any legal and/or recovery proceedings shall be thirteen (13 %) per month from the date of default until payment in full.*

As a result of the respondent's default, the appellant claimed Kshs. 1,000,000/- together with interest at 13% per month from 30th September 2016.

7. The respondent admitted the Agreement but contended that the appellant's director, Paula Njuguna (PW 1), was aware that the money was invested in a mining business as agreed between the parties and that the suit was brought in bad faith owing to the conflict of interest as the said Paula Njuguna is the one who drafted the agreement, expected a cut from the proceeds of the mining venture. The respondent also contended that should she be ordered to make payment then, *"all monies initially remitted by the defendant must be noted and put into consideration."* In addition, the respondent challenged the agreement on the ground that it was not executed in accordance with the law.

8. At the hearing, PW 1 testified on behalf of the appellant while the respondent (DW 1) testified on her own behalf and after considering the evidence and submissions, the trial magistrate reached the conclusion that I have outlined in the opening paragraph of this judgment.

9. From the parties' submissions, there two broad issues for determination. The first is whether the trial court was entitled to vary the interest rate agreed upon by the parties in the Agreement and if so, under what circumstances.

10. On the first issue I do not think there is much controversy as the matter has been settled by various decisions of the Court of Appeal cited by the appellant. At the heart of this issue are two principles. First, the freedom of contracting parties to voluntarily enter agreements and determine the terms thereof. Second, the duty of the court to relieve parties of onerous and unconscionable obligations imposed by such agreement in certain circumstances. The appellant placed emphasis on the former principle by citing several decisions of our courts. For example, in ***National Bank of Kenya Limited v Pipeplastic Samkolit (K) Limited & Another,*** **Civil Appeal No. 35 of 1999 [2001] eKLR**, the Court of Appeal expressed the view that:

> *A Court of law cannot re-write a contract between the parties. The parties are bound by the terms of their contract, unless coercion, fraud or undue influence are pleaded and proved.* [Emphasis mine]

11. The general principle is that parties are bound by their agreement and the court will not intervene unless, coercion, fraud, undue influence or other facts that may vitiate such an agreement are pleaded and proved. I therefore agree with the respondent that in a proper case the court may vitiate a contract where the terms are unfair or unduly harsh. This point was emphasized by the Court of Appeal in ***Margaret Margaret Njeri Muiruri v Bank of Baroda (Kenya) Limited*** **NRB CA Civil Appeal No. 282 of 2004 [2014] eKLR** where it observed that:

> *36. Nevertheless, courts have never been shy to interfere with or refuse to enforce contracts which are unconscionable, unfair or oppressive due to procedural abuse during formation of the contract, or due to contract terms that are unreasonably favourable to one party and would preclude meaningful choice for the other party. An unconscionable contract is one that is extremely unfair. Substantive unconscionability is that which results from actual contract terms that are unduly harsh, commercially unreasonable, and grossly unfair given the existing circumstances of the case (See Black's Law Dictionary, 9th Edition, Gardner, Ed.).*

12. This brings me to the point raised by the appellant that the respondent did not plead any ground for vitiating the interest rate clause in the Agreement. As stated in ***National Bank of Kenya Limited v Pipeplastic Samkolit (K) Limited & Another*** **(Supra)** such grounds must be pleaded and proved. The requirement that a defendant must plead a specific ground of defence is not an idle one. The Court of Appeal considered this issue in ***Nizar Virani t/a Kisumu Beach Resort v Phoenix of East Africa Assurance Company Ltd*** **KSM CA Civil Appeal No. 88 of 2002 [2004] eKLR** where it observed as follows;

> *Firstly, there is no denying that there were no particulars supplied in the defence pleading under* ***Order VI rule 8(1) (of the Civil Procedure Rules)*** *which requires in mandatory terms that:*
>
> *Every pleading shall contain the necessary particulars of any claim defence or other matter pleaded including, without prejudice to the generality of the foregoing: –*
>
> > *(a) particulars of any … fraud … on which the party relies.*
> >
> > *(b) Where a party pleading alleges ... fraudulent intention … particulars of the facts on which the party relies.*
>
> *In the absence of such pleading, the insurer is not at liberty to agitate the allegation of fraud or fraudulent intention. Fraud is a serious quasi–criminal imputation and it requires more than proof on a balance of probability though not beyond reasonable doubt. Sufficient notice and particulars must therefore be supplied to the party charged for rebuttal of such allegation.*

13. In ***Abdulkadir Shariff Abdirahim & Another v Awo Shariff Mohammed T/A A. S. Mohammed Investments*** **NRB CA Civil Appeal No. 1 of 2008 [2014] eKLR**, the Court of Appeal extensively discussed the role of pleadings and held that special grounds of defence are required to be specifically pleaded. It quoted, with approval, the learned authors of ***Bullen and Leake and Jacob's Precedents of Pleadings***, **Sweet & Maxwell, 12th Ed., page 6-7** which states that:

> *These requirements operate to compel the defendant, who intended to raise a special ground of defence or to raise an affirmative case to destroy any claim of the plaintiff, to plead specifically the matter he relies on for such purpose. The effect of the rule is for reasons of practice and justice and convenience, to require the defendant to tell his opponent what he is going to the court to prove. Thus, when a contract, promise, or agreement is alleged in the statement of claim, a bare denial by the defendant will be construed only as a denial in fact of the express contract, promise or agreement alleged or of the matters of fact from which the same may be implied by law, and not as a denial of the legality or sufficiency in law of such contract, promise or agreement. It is, therefore, often not enough for the defendant to deny an allegation in the statement of claim; he must go further and dispute its validity in law or set up some affirmative case of his own in answer to it. Accordingly, the defendant has the duty to state any special defence or any new fact on which he will rely at the trial, as otherwise a plaintiff may legitimately complain that he has been taken by surprise.*

14. I therefore find that the respondent ought to have pleaded specifically the grounds upon which it claimed that the interest rate of 13% per month was unconscionable to enable the appellant respond appropriately. As those grounds were not pleaded, it was not open for the court to consider the issues raised on that account.

15. That is not the end of the matter as the respondent contended the general rule on pleading is ameliorated by the rule in ***Odd Jobs v Mubia*** **[1970] EA 476.** The principle was succinctly set out by Law JA., who held as follows:

> *On the point that a court has no jurisdiction to decree on an issue which has not been pleaded, the attitude adopted by this Court is not as strict as appears to be that of Courts in India. In East Africa the position is that a Court may allow evidence to be called and may base its decision on an unpleaded issue if it appears from the cause followed at the trial that the unpleaded issue has in fact been left to the court for decision...*

16. The question for resolution is whether the issue of interest rates was raised by the parties in the course of proceedings and left to the court for determination in line with the rule in ***Odd Jobs v Mubia*** **(Supra)**. I have studied the respondent's witness statement which she adopted as the evidence in chief and it does not raise any issue about the interest charged being unconscionable. Further, the counsel for the respondent did not raise the same issue when he cross-examined PW 1. It is only in the final written submissions before the trial court that counsel for the respondent submitted that the interest pleaded by the appellant was unconscionable and unfair. The totality of the proceedings does not support the conclusion that the issue of unfairness of the interest rate was raised in the statement of defence and testimony of both witnesses. There is no evidence that the appellant acquiesced to the issue being dealt with by the court in a manner that this court can come to the conclusion that parties left the matter for the court's resolution. I therefore find and hold that the issue whether the interest was unconscionable and unfair was not pleaded and was not left to the court by the parties for determination.

17. Since the issue grounds upon which the interest rate clause could be vitiated were not pleaded, it was improper for the trial magistrate to proceed on an examination of the provisions of the ***Banking Act*** as a basis for varying the agreed interest rate. The issue was not pleaded, it was not put to the witnesses and it only arose in the final submissions. I therefore find and hold that the trial magistrate erred in applying the provisions of the ***Banking Act*** in these circumstances. For this reason, I do not find it necessary to proceed with an examination of those provisions and their applicability to the Agreement.

18. For the reasons I have set out, I allow the appeal on the following terms:

(a) The rate of interest on the principal sum at court rates in the judgment before the subordinate court is set aside and substituted with a rate of interest at 13% per month from 30th September 2016 until payment in full.

(b) The appellant shall have costs of this appeal.

DATED and DELIVERED at NAIROBI this 1 9th day of SEPTEMBER 2019.

D. S. MAJANJA

JUDGE

Ms Mueni instructed by Henia Anzala and Associates Advocates for the appellant.

Ms Gesare instructed by Meritad Law Africa LLP Advocates for the respondent.