REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

COMMERCIAL & ADMIRALTY DIVISION

MILIMANI LAW COURTS

HCCC NO. 119 OF 2014

TROPICAL FOODS INTERNATIONAL LIMITED...............................1ST PLAINTIFF

JAMES KIMONYE…………………………………………………2ND PLAINTIFF

Versus

THE EASTERN AND SOUTHERN AFRICA TRADE AND

DEVELOPMENT BANK (PTA BANK)………………....................1ST DEFENDANT

CORFU INVESTMENTS LIMITED ……………….......…………2ND DEFENDANT

RULING

Stay and referral to arbitration

[1] The application before me is a Chamber Summons dated 28th April, 2014 and is made by the 1st Defendant's (hereafter ''the Applicant"). It is expressed to be brought under Section 6 of the Arbitration Act, 1995, rules 2 and 8 of the Arbitration rules, 1997, Sections 1A and B and 3 of the Civil Procedure Act and all the enabling provisions of the law. The Applicant is asking the Court to stay the proceedings between the 1st plaintiff and the 1st defendant herein and refer it to arbitration. It also asks for costs of the application.

[2] The application is supported by the Supporting Affidavit sworn on 28th April, 2014 by David Mulira the Senior Legal officer of the 1st defendant. The application does not concern the 2nd defendant as he accordingly notified the court through the advocate that they will not take part in the application. The 1st plaintiff has not filed any affidavit and therefore acknowledges the facts as stated in the supporting affidavit. It has however filed Grounds of Opposition dated 14th May, 2014.

The 1st Defendant's submissions

[3] The 1st Defendant submitted that the relevant facts are agreed and the only dispute is as to the legal implications of those relevant facts. These facts are : The 1st plaintiff and the applicant (jointly referred to as "the parties") executed a facility Agreement dated 8th December, 1998 pursuant to which the Applicant agreed to advance to the 1st plaintiff a trade finance loan in the sum of US$250,000/=. On consideration thereof, the Facility Agreement provided that the 1st plaintiff would provide the following securities.

i. A first legal mortgage/charges over title No. Komothai/Igi.652 registered in the name of one Francis Muhia Mutugu; title No. Aboguchi/katheri/1959 registered in the name of one James Kamonye; and title No. Ex-Lewa Settlement Scheme/6 registered in the name of one John Gituma.
ii. An assignment in favour of the 1st defendant of receivables; and
iii. Personal Guarantees by the Directors of the 1st plaintiff for the repayment of the Facility, payment of interest and other charges thereon.

[4] The 1st plaintiff provided the securities aforesaid and procured the guarantors, including the 2nd plaintiff. The charges were registered under Kenya law and were therefore subject to the laws of Kenya. The Facility Agreement contained an arbitration clause that embodied both a choice of law and choice of forum at Article XIV in the following terms:

> ***"DISPUTES AND ARBITRATION"***
> ***This agreement shall be governed by and construed in accordance with the laws of England. Any dispute or difference which may arise between the parties hereto under this Agreement which shall not have been settled by mutual agreement of the parties shall be finally settled under the rules of Conciliation and Arbitration of the International Chamber of Commerce by one or more arbitrators of the International Chamber of Commerce by one or more arbitrator appointed in accordance with the said Rules. The Arbitration award shall be final and binding on both parties."***

[5] It is therefore evident that the Facility Agreement provided for a choice of law and choice of forum being the Laws of England and Arbitration under the Rules of the International Chamber of Commerce respectively. Sometimes in October, 2001 a dispute arose under the facility aforesaid and the 1st defendant herein filed suit before the Honourable court being Nairobi High Court Civil Suit No. 1534 of 2001 claiming general damages and special damages against the 1st Defendant herein for breach of contract. The parties in the said suit purported to alter the terms of the arbitration clause aforesaid by way of consent recorded on 1st November, 2001 before Honourable Justice Mwera (as he then was) to the effect that the court would appoint an arbitrator in default of agreement by the parties. However, this consent was set aside by this Honourable Court as confirmed by the Court of Appeal in Civil Appeal No. 253 of 2002.

[6] On 26th October, 2009 the 1st plaintiff acting pursuant to the terms of the Facility Agreement referred the matter to Arbitration under the auspices of the International Chamber of Commerce ("the ICC") claiming delayed disbursements and loss of revenue and profits. Consequently, the terms of the Arbitration were set out and agreed upon by the parties. The ICC upon receipt of the Terms of Reference which were agreed and executed by the 1st plaintiff and the Applicant indicated the advance costs payable by the parties and reserved the right to amend the same in accordance with the pleadings. However, the 1st plaintiff failed to pay its portion of the advance costs and the claims were considered as withdrawn under Article 30(4) of the rules of the International Court of Arbitration. Consequently, the proceedings before the Arbitrator were deemed to have been withdrawn pursuant to the applicable rules and the ICC refunded to the 1st defendant its portion of the Advance Arbitration costs it had paid, upon which the arbitration proceedings were terminated.

[7] Following the termination of the Arbitration proceedings as aforesaid, the 1st Defendant served a notice of default on the 1st plaintiff and all the guarantors including the 2nd plaintiff herein, calling for the payment of the outstanding amount in the sum of US$ 449,948.66 as at 30th June, 2013, being the amount advanced together with the interest accrued thereon. The 1st plaintiff failed, refused and/or neglected to respond to the said demand and did not pay the amount due to the 1st Defendant. In the meantime one of the Guarantors offered to purchase the debt in the sum of Kshs. 20,000,000/= in full settlement of the debt on condition that the debt is assigned to the 2nd defendant herein. The 1st defendant accepted the same and upon full settlement on the terms agreed upon, transferred all its interests under the Facility Agreement and the securities thereunder to the 2nd defendant.

On The Guarantee

[7] The Applicant cited the following passages in ***Halsbury's Laws of England***, **4th Ed** that**:**

Para 101

" A guarantee, being merely an accessory contract, does not, even when under seal, cause a merger with it of the principal debtor's simple contract debt to which it relates……

Para 103

"although sometimes bound by the same instrument as his surety, the principal debtor is not a party to the surety's contract to be answerable to the contract; there is not necessarily any privity between the surety and the principal debtor; they do not constitute one person in law, and are not as such jointly liable to the creditor, with whom alone the surety contracts."

[8] It also cited the case of **Nairobi Mamba Village v National Bank of Kenya (2002) I EA 197**, a property had been charged to the Defendant by Muturi Investments Limited, a limited liability company, in its capacity as guarantor of a loan advanced by the Defendant to the plaintiff. The plaintiff brought a claim together with an application challenging the exercise of the statutory power of sale in accordance with the terms of the charge. The defendant raised a preliminary objection to the application on the ground that in the absence of the relationship of chargor and chargee between the plaintiff and the defendant, the former lacked the legal standing to seek relief. The court held that;

"…. For what is in dispute is not the ownership or possession of the charged property but the contractual rights of the parties under the loan agreements and the contract of charge. Whereas the plaintiff can….. legitimately complain of the alleged breaches of the loan agreements and seek other reliefs in connection therewith, he cannot properly seek to restrain the chargee from selling the charged property for the reason that the intended sale is pursuant to the exercise of the contractual and statutory powers of the charge which were expressly or impliedly contained in the contract of charge to which the plaintiff is not party."

[9] Drawing from the above authorities, the Applicant submitted that, not only does the Facility Agreement between the 1st plaintiff and the 1st defendant constitute a separate contract from the Guarantee but the 1st plaintiff is also not a party to the contract of charge between the 2nd plaintiff and the 1st defendant. Accordingly, the 1st plaintiff is not a party to matters arising from the transfer of the charge to the 2nd defendant herein. The 1st Defendant the plaintiffs' ground (c) of their Grounds of Opposition identifies the central issue to these proceedings to be the transfer of charge to a 3rd party which issue, the 1st defendant humbly submitted arose from the Guarantee

and the consequent charge to which as already illustrated above, the 1st plaintiff is not a party. In any event, the 1st plaintiff has failed to disclose any cause of action, if at all, against either the 1st or the 2nd defendant. Therefore, the 1st plaintiff is not a necessary party to the central issue in these proceedings.

[10] The Applicant contended that the matters being raised in the Plaint by the 1st Plaintiff and the 2nd Plaintiff are distinct as explained below:

a. The 1st plaintiff is disputing the conclusion of the arbitration proceedings before the International Chamber of Commerce which arises from the Facility Agreement and the exercise of the 1st Defendant's rights under the said facility.
b. On the other hand, the 2nd plaintiff's dispute is in respect of a guarantee as secured by a charge registered under Kenya laws and the consequent assignment of the said charge to the 2nd defendant and which the 1st defendant does not object to being determined by this court but only as between the 2nd plaintiff and the 1st and 2nd defendants.

[11] In addition to the above, the securities under the guarantees were in the form of legal charges which were registered under Kenyan law and as such the law applicable to them is the Laws of Kenya. On the other hand, the law and forum of settling disputes arising from the Facility Agreement as between the 1st plaintiff and the Applicant was settled by the Court of Appeal in **Tropical Foods Limited v The eastern and Southern African Trade and Development Bank (PTA Bank), (2007) eKLR** where it upheld the finding of this honourable court, Mwera J (as he then was) as follows:-

> ***"The parties had clearly and in mandatory terms bound themselves to adopt the laws of England as the substantive law but more importantly to resolve their disputes before the International Chamber of Commerce. They had chosen a foreign monetary unit in which to deal and it is no doubt that PTA Bank is a regional institution. So in general, the parties saw their dealings as being governed by international as opposed to national arbitration."***

[12] According to the 1st defendant, since the decision of the Court of Appeal determined the issues as to the forum and the substantive law applicable to disputes and/or matters arising out of the Facility Agreement between the 1st Plaintiff and the 1st defendant, those issues are res judicata.

On stay pending arbitration

[13] Section 6(1) of the Arbitration Act provides that, a court before which proceedings are brought in a matter which is the subject of an arbitration agreement shall, if a party so applies not later than the time when that party enters appearance or otherwise acknowledges the claim against which the stay of proceedings is sought, stay the proceedings and refer the parties to arbitration. In the case of **Paczy v Hoendler and another (1981) 1 Llyods Rep 302 CA,** it was held that the court must grant a mandatory stay where there is a non-domestic arbitration agreement unless it is satisfied that either the arbitration agreement is null and void, inoperative or incapable of being performed. The 1st defendant respectfully submitted that based on the decision of the Court of Appeal in the case of **Tropical Foods Limited v The Eastern and Southern African Trade and Development Bank (PTA Bank)** aforesaid, the Facility Agreement entered into by the 1st plaintiff and the 1st defendant contained a valid and operative non-domestic arbitration agreement and consequently the grant of stay is mandatory.

[14] The 1ST Defendant relied on the case of **Construction Engineering & Builders (Kenya Ltd v Municipal Council of Kisumu, the Court of appeal** which approved and followed the

following dictum of Lord parker of Waddington in the case of **Bristol Corporation v John Aird & Co. (1913) AC 241 (HL (E):**

> ***" I do not think it is advisable that any d o but should be thrown upon what I personally know to be the practice of the courts below, and in particular of the Chancery Division, with regard to exercising their discretion under the Arbitration Act. It is, I know, a common thing to stay an action as to one mater in dispute and at the same time to allow it to proceed as to another, notwithstanding that both matters are within the reference; and I think it is obviously a desirable course in many cases, for this reason, that very often the matters subject to the reference include both the question of the true matters of detail, and it maybe of account. Everybody knows that with regard to the construction of an agreement it is absolutely useless to stay the action, stated; therefore it is more convenient on a question of construction to allow the action to proceed; and at the same time with regard to accounts and matters of detail to allow the arbitration to proceed."***

The Court of Appeal accordingly held that it is a common thing to stay an action as to one matter in dispute and at the same time to allow it to proceed as to another.

[15] The plaintiffs aver at paragraph 11 of the plaint that the arbitration process did not continue to the end and therefore any of the parties is at liberty to re-commence the process. It is uncontested that the reason for the withdrawal of the Arbitration filed before the International Chamber of Commerce was the 1st Plaintiff's failure to pay advance costs. In the case of **BDMS Limited v Rafael Advance Defence Systems (2014) EWHC 451 (Comm),** the High Court held that a failure by the respondent to pay its share of the ICC Advance on costs did not amount to a repudiatory breach of the arbitration agreement entitling the claimant to bring the claim in court and that arbitration remained the right forum.

[16] The 1st defendant further submits that, quite apart from being contractually bound by the Arbitration Clause, Article 159(2) (c) of the Constitution of Kenya obligates the court to promote alternative forms of dispute resolution including arbitration as a principle of justice. On this see the case of **Hausram Limited v Nairobi City County (2013) eKLR,** this Honourable court held that:-

> ***" I am aware of the belief that Article 159(2) (c) of the constitution 2010 is expressed in mandatory terms and this court is under a duty to promote alternative forms of dispute resolution. This is all the more so when the parties themselves have chosen the forum as is the case herein."***

[17] The plaintiff's main ground of opposition is that the issues raises in the current proceedings involve other parties who were not parties to the Facility Agreement which contained an arbitration clause. In the book of ***Russel on Arbitration*****, Twenty-first Edition, Sweet & Maxwell:** London **(1997)**, David St. John Sutton, John Kendell and Judith Gill aptly state that there is no longer any scope for the court refusing stay of proceedings on the ground that third parties are involved and that it would be preferable for the dispute to be dealt with by one tribunal (i.e. the court) in order to avoid the possibility of inconsistent decisions. From the authorities cited, the 1st plaintiff is in contravention of the constitution, the Arbitration Act and the contractual obligations of the 1st plaintiff and the 1st defendant. For the reasons set out hereinabove, the 1st Defendant humbly prays that the will allow the application dated 28th April, 2014 with costs.

The 1st Plaintiff opposed stay of proceedings

[18] The 1st Plaintiff submitted that the application by the 1st Defendant is to stay proceedings as between the 1st plaintiff and the 1st defendant and that the dispute to be referred to arbitration. According to the 1st Plaintiff, the relevant proceedings as in the plaint and Notice of Motion dated

24th March, 2014 relate to a temporary injunction to restrain the defendants by themselves or agents or otherwise howsoever and however, from exercising their statutory power of sale pursuant to a charge entered between the plaintiff and the 1st defendant dated 8th December 1998 and the subsequent transfer thereof dated 10th January 2014. What is relevant is that; a) The defendants allegedly transferred a charge dated 8th December, 1998 between the 2nd plaintiff and the 1st defendant to the 2nd defendant; it was illegal and un-procedural as it was without consent and occasioned the 2nd plaintiff prejudice. The alleged transfer is dated 10th January, 2014; b) The defendants have never issued any notice to the 1st plaintiff statutorily notifying the 1st plaintiff of the need to exercise powers of sale thereof; c) There exists a dispute between the 1st plaintiff and the 1st defendant as envisaged in the Facility Agreement entered thereof dated 8th December, 1998 implying that any resolutions thereof should have been referred to arbitration. The 1st defendant failed and/or neglected to do so and instead opt to pursue an illegal process of assignment of some of the charges registered in support of the Facility Agreement; d) Further no prayer in the plaint is exclusively relevant to the application herein; and moreover an application for stay does not in any way mean that the suit is struck out. The suit is only stayed.

[19] The 1st Plaintiff gave an account on the genesis of the proceedings in court to be that; on 10th January, 2014 the 2nd plaintiff was served with a statutory notice by the 2nd Defendant allegedly for non-payment of US$449,948.66 (as at 30th June, 2013). Both plaintiffs had never dealt with the 2nd Defendant whatsoever. The statutory notice was to the effect that the 2nd Plaintiff's Land, number Abothuguchi/Katheri/1959 that had been charged to the 1st defendant vide charge dated 8th December, 1998 will be sold by the 2nd defendant, to recover money allegedly owed. A transfer of charge was annexed to the notice allegedly transferring the 8th December 1998 charge from the 1st Defendant to the 2nd defendant. Neither the 1st nor the 2nd plaintiff was aware of the said transfer. A complete stranger to the transaction was purporting to enforce its alleged rights; hence, the plaintiffs herein filed the present proceedings against the "stranger" and the 1st defendant- the chargee on the charge dated 8th December, 1998.

[20] The connection between these proceedings and the facility agreement dated 8th December, 1998 is important. The 1st defendant should be clear to the court that:

a. The current proceedings are related and indeed flow from the facilities agreement of 8th December, 1998.
b. The fact that there are other parties involved does not alter the terms of the facilities agreement as far as the arbitration term is concerned.
c. The rights of the other parties are not prejudiced whatsoever.
d. The interest of justice is best served in which direction.

[21] The 1st plaintiff filed four grounds of opposition; namely;

a. The issues raised in the current proceedings involve other parties who were not parties to the Facility Agreement which referred disputes to arbitration and hence the matter cannot be referred to arbitration between some parties without prejudicing their case.
b. For the correct position to be clarified and all relevant issued be presented and argued before the court even as between the parties who were not involved directly in the Facility Agreement, it is imperative that the 1st plaintiff and the 1st defendant do continue being parties in the current proceedings. They are therefore necessary parties to the current proceedings.
c. The central issue to the current proceedings involves transfer of charge to a 3rd party. This issue and the parties involved cannot be referred to arbitration. The cause of action and the parties clearly are not governed by the arbitration clause in the facility agreement which is basically a background documents in the current proceedings.
d. The circumstances and issued that led to the proceedings herein and the parties involved cannot

allow the invocation of the doctrine of res judicata. Moreover if indeed the doctrine of res judicata were applicable then the proceedings between the 1st plaintiff and the 1st defendant would be terminated and not stayed.

[22] Based on the brief background information about the matter, the Plaintiffs submitted that the application herein is most undeserving because the issue at hand is an illegal transfer of a charge between the 2nd plaintiff and the 1st defendant to a 3rd party 'stranger'. All these parties were never parties to the facilities agreement that speaks about arbitration. The invocation of the arbitration clause should be between the 1st plaintiff and the 1st defendant only. In the circumstances the Facilities Agreement has been largely altered by the subsequent entry of the other parties and their rights. These rights must now be addressed before the honourable court. The 1st Defendant, by asking this matter to be stayed and referred to arbitration is in effect asking the Court to abdicate its constitutional responsibility over the disputes herein. Ironically, the party now invoking the arbitration clause has ignored the fact that before transferring the charge the matter should have been referred to arbitration. The arbitration agreement is a background document to the claim in court and hence not the central issue. Secondly, the two are necessary parties to the current proceedings. Therefore, staying proceedings against the parties herein and against each other will make it very difficult for the other parties to unravel the issues and meet the ends of justice. Thirdly, the doctrine of res judicata cannot apply here as the claim in Nairobi High Court Civil Suit NO. 1534 of 2001 arose directly from the Facilities Agreement and was governed by the arbitration clause; the current issues are much more removed from the said Facilities Agreement and hence not governed by the arbitration clause and/or the Facilities Agreement.

[23] In response to the Applicant's submissions, the Plaintiffs stated that:- a) The arbitration between the 1st plaintiff and 1st defendant failed to proceed because BOTH parties did not raise the required advance costs. In fact the 1st defendant was the most reluctant in effecting the payments. Moreover that issue is irrelevant in the current matter since the Arbitration then concerned the Facilities Agreement and the parties thereto. Although the 1st defendant alleges that: ***"...following the termination of the arbitration proceedings..., the 1st defendant served a notice of default on the 1st plaintiff…",*** there is no evidence of such notice which has been produced-however, this neither validates an illegal transfer of a charge nor makes the issues in this suit part of the issues in the Facilities Agreement as to make this suit to be stayed and referred to arbitration. Finally, the Plaintiffs submitted that Article 159 2(d) of the Constitution demands that ***"justice shall be administered without undue regard to procedural technicalities."*** The issue before court is simple. Could the Defendants transfer a charge in the manner that they did and remain legal and enforceable? The request for referral is a side show to and unconnected to this suit and should be declined. Therefore, the application should be dismissed with costs.

THE DETERMINATION

Issues

[24] The way the arguments herein have been presented really entangles the issues in wool. But the Court need not employ any high wit, for the issues are simple and easily discernible. The major one is whether the issues in controversy in this suit are disputes covered by the arbitration agreement as to be referred to arbitration. Four things are clear. One; there was a facility agreement for advance of money by the 1st Defendant to the 1st Plaintiff. Two; a guarantee was given by the directors of the 1st Plaintiff which obviously constitutes a separate agreement from a charge herein. Three; there were charges over several properties including the property belonging to the 2nd Defendant. And, four; there seems to have been a DEED OF ASSIGNMENT OF LOAN FACILITY dated 14th October, 2013 and a TRANSFER OF CHARGE dated 10th January, 2014; the transfer of charge was in respect of the property of the 2nd Plaintiff and was done by the 1st Defendant to the 2nd Defendant. The 2nd Defendant now seeks to exercise the statutory power of

sale on the transfer of charge.

[25] I have perused the plaint and it is clear this suit is challenging: 1) the transfer of charge by the 1st Defendant to the 2nd Defendant. The charge that was being transferred is the one dated 8th December, 1998 on the property of and granted by the 2nd Plaintiff to the 1st Defendant. 2) And, the purported exercise of the power of sale by the 2nd Defendant on the transfer of charge herein. The 2nd Plaintiff refers to 2nd Defendant as a stranger to the charge and who has no legal authority to exercise such power of sale over his property. In such circumstances, the exercise of a power of sale and any challenge thereto are matter governed by the domestic land laws and should be tried in court. Invariably, the issue of transfer of charge is inextricable to the challenge on the exercise of the statutory power of sale by the 2nd Defendant and so it becomes an integral aspect of the suit herein. The assignment of the loan facility is not the transfer of charge although it may be used in evidence in support of the transfer of charge. But the prospects of using the assignment of loan facility as a basis for a transfer in this case is a question of admission of evidence and I do not wish to discuss it at this stage. Therefore, the assignment of the loan facility as a substantive issue in dispute is a perfect candidate for the arbitral proceedings between the 1st Plaintiff and the 1st Defendant. But despite the possibility of a confluence of the issue as a substantive matter or evidentiary material for the arbitral tribunal and the court, respectively, the cause of action in this suit does not become the subject of the arbitral proceedings. I should add that, the issue on whether notice of default was served on the plaintiffs by the defendants becomes a matter for determination in this suit by the Court**.** Therefore, the overall impression I make out of the above analysis is that an order for injunction to restrain the chargee from exercising the power of sale herein can only be granted by court in Kenya. The Arbitral Tribunal will not have jurisdiction over the subject of this suit and will not be able to render a remedy on the claim by the 2nd Plaintiff against the 2nd Defendant. But, any issue which is strictly between the 1st Plaintiff and the 1st Defendant arising from the facility agreement will have to be determined by the arbitral tribunal consisting of one or more arbitrators of the International Chamber of Commerce in accordance with the arbitration agreement. To that extent, I agree with the 1st Defendant's submissions. In this case, however, there is nothing that is purely between the 1st Plaintiff and the 1st Defendant and which would impel the Court to stay the entire proceedings and refer the dispute to arbitration. In line with what I have stated above, the 1st Plaintiff and the 1st Defendant are necessary parties in this suit in order to enable the Court to determine all the issues in controversy completely and effectually.

[26] In saying these things foregoing, the court is aware of the eminent literally works of David St. John Sutton, John Kendell and Judith Gill in ***Russel on Arbitration*****, (supra)** and the decisions of the Court of Appeal on the subject of stay under section 6 of the Arbitration Act**.** But the decision of the Court in refusing to stay these proceedings is not based on the ground that third parties are involved and that it would be preferable for the dispute to be dealt with by one forum (i.e. the court) in order to avoid the possibility of inconsistent decisions, rather it is based on the fact that the substance of the suit is not a dispute under the arbitration agreement but quite separate from it and which is an issue outside the jurisdiction of the arbitral tribunal. I should, however, be understood well, that, since the arbitral proceedings did not result into a final award which would have such finality in law of res judicata, thus, the dispute between the 1st Plaintiff and the 1st Defendant is not res judicata even in most generous sense of the law. I agree with the submissions of 1st Plaintiff and the 1st Defendant that they would still refer any dispute between them which they fail to mutually agree on to arbitration for resolution.

[27] The upshot is that I decline to stay this suit. I dismiss the application dated 28th April, 2014. Costs shall be in the cause.

Dated, signed and delivered in court at Nairobi this 6th day of November 2014

F. GIKONYO

<u>JUDGE</u>