REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

CIVIL CASE NO 703 OF 1983

HOECHST EAST AFRICA LIMITED.....PLAINTIFF

VERSUS

KISUMU COTTON MILLS LIMITED.....DEFENDANT

(IN RECEIVERSHIP)

RULING

October 4, 1983, **Cockar J** delivered the following Ruling.

As per the agreed statement of facts the plaintiff had at all material times supplied goods to Kisumu Cotton Mills (called Kicomi) under a contract between the two which included a clause within section 21 of the Sale of Goods Act (cap 31) (hereinafter referred to as the clause) which was effective between these parties to reserve to the plaintiff the ownership of the goods until the plaintiff was paid. The clause is in the following terms:

> **"The goods shall become the property of the Buyer only after he has settled all his obligations arising from the mutual business relations and has completed payment for the goods supplied. Buyer shall collaborate in any measures Seller may take to protect his proprietary rights in the delivered goods. If a third party should try to assert or substantiate rights in the goods, Buyer shall inform Seller immediately.**
>
> **Until the Buyer has paid all sums due by it to the Seller, the Seller reserves the right of disposal of the goods supplied to the Buyer in accordance with this condition and ownership thereof does not pass to the Buyer and the Buyer has no power to charge the goods or to create any security over them. Until payment in full as aforesaid the Buyer will store the goods in such a way that they are clearly shown to be the property of the Seller and the Buyer will not give contrary information to anyone: and in the event of the Buyer creating or having created any general charge on its asset the Buyer will forthwith on the creation of the general charge or on receiving possession of any goods supplied in accordance with this condition (whichever may be the later) notify the Seller of such general charge and also notify the holder thereof this reservation the right of disposal of such goods.**
>
> **If the Buyer makes new objects from the goods or in any way mixes the goods with other objects or materials these new objects or mixtures are owned by the Seller in the same way as the goods and on the same terms.**
>
> **Until payment in full as aforesaid the Buyer shall hold the goods as Trustee for the Seller.**

Nevertheless the Buyer may sell the goods to third parties in the normal course of the Buyer's business but shall do so only as agent for the Seller and shall hold the proceeds of all sales of the goods in trust for the Seller and to account therefor as requested.

If and whenever the Buyer is in default of payment for any goods supplied to him by the Seller or commits any breach of the foregoing conditions the Seller may forthwith rescind all or any of its contracts for sale to the Buyer in respect of which payments are still outstanding and stop delivery or as the case may be resume possession of the goods the subject thereof without... prejudice to any claim for compensation or other remedy that may be available to the Seller in respect of such default or breach".

The Standard Bank Ltd (the Bank) to whom Kicomi had given a debenture charging all its assets eventually appointed the defendants as receivers and managers of Kicomi, when the Bank's floating charge crystallised over the assets of the Kicomi which assets included certain products of the plaintiff still in possession of Kicomi and were still unpaid for (hereinafter referred to as the goods).

At no time prior to the appointment did the Bank know that the plaintiff was doing business with Kicomi upon terms which reserved ownership of goods as set out earlier.

The application is for the determination of the following questions.

1. Is the reservation of ownership of the plaintiff effective to oust the charge given by Kicomi to Bank?

2. Alternatively was the appointment of receivers and the consequent crystallisation of the floating charge of the Bank effective to charge to the Bank the goods bought by Kicomi from the plaintiff notwithstanding that they had not been paid for?

Mr. Le-Pelley for the Bank claimed that irrespective of the terms of the clause, under the provisions of section 26(2) of the Sale of Goods Act, cap 31 Laws of Kenya (hereinafter referred to as the Act) and in consequence of the crystallisation of the debenture which the Bank held over the assets of Kicomi (including the goods) the right of the receivers appointed by the Bank over the goods superseded that of the plaintiffs. He relied on two decisions of Chanan Singh J in *GAS Weingut v Leslie* [1967] EA 480, and *BASF AG v Grindlays Bank International (Kenya) Ltd & another* [1976] KLR 235. He also referred to *Worcester Works Finance Vs Cooden Engineering* [1972] 1 QB 120.

Section 26 (2) of the Act reads as follows:-

"Where a person having bought or agreed to buy goods obtains, with the consent of the seller, possession of the goods or the documents of title to the goods, the delivery or transfer by that person, or by a mercantile agent acting for him, of the goods or documents of title, under any sale, pledge or other disposition thereof, to any person receiving them in good faith and without notice of any lien or other right of the original seller in respect of the goods shall have the same effect as if the person making the delivery or transfer were a mercantile agent in possession of the goods or documents of title with the consent of the owner."

Mr. Ransley for the plaintiff's sought to disagree with the said two judgments of Chanan Singh J and relied on an English Court of Appeal decision in *Aluminium Industries Vassen BV v Romalpa Aluminium Ltd* [1976] 1QB 210. I must point out that of the above cases that were cited the facts in the two Kenya cases that is in *Weingut's* case and *BASF* case, and in the *Romalpa* case were on all fours with the present case in that in each of these cases the agreement of the sale of goods contained a clause similar to the one in this case reserving in the plaintiff (or the original seller) the ownership of the goods, and the eventual appointment of a receiver and the crystallization of the debenture by the debenture-holder. In the two Kenya cases the goods were still in possession of the buyer. In *Romalpa's* case, however, a part of the goods after manufacture had been sold to a 3rd party and the question of the right of the original seller over the proceeds of sale to the 3rd party as against the debenture-holder was also considered together

with the right to the part of the goods still held by the borrower-company.

In the *Rolmalpa* case the relevant section – the English section 25(2) being exactly the same as our section 26(2), was not even touched upon. According to Mr. Le-Pelley the reason for this omission must have been that something additional must have happened such as perhaps the debenture-holder had notice of the clause prior to the execution of the debenture to nullify the debenture holder's rights under the relevant subsection. Mr. Le-Pelley contended that the *Romalpa* case was not an authority on section 26 (2) of our Act because it was not dealt with therein. Mr. Ransley's argument was that in *Romalpa's case,* the English section 25(2) was not discussed at all for the simple reason that the clause had created a fiduciary relationship between the plaintiff (the original seller) and the buyer which was analogous to that of a bailor and bailee or of a trustee and beneficiary which over-rode section 25(2) and made it inapplicable. Mr. Le-Pelley had also stressed the words "as between those parties" used in paragraph 2 of the agreed statement of facts the relevant portion whereof reads as follows:

> "2. The contract between the plaintiff and Kicomi contained a clause which was effective as between those parties to reserve to the plaintiff the ownership of the goods until…"

I do not find any significance in the use of these words. The contracts of sale in case of both the Kenya cases and the *Romalpa case* all contained the same clause which was effective between the original seller and the buyer. Yet although in the Kenya cases the clause has been held ineffective against a receiver appointed by the debenture holder in consequence of the provisions of section 26(2) of the Act, in the *Romalpa case* in consequence of the existence of the clause the claim of the original seller over the goods was held to be in priority to the secured and unsecured creditors of the buyer.

Having carefully considered the two Kenya cases and the arguments put forward by both the learned advocates, to my mind, the essential questions to be decided are whether there was a disposition of the goods and if so then in consequence of such disposition whether or not a transfer or delivery of the goods took place. It is also clear from sub-section 2 that such transfer or delivery must be both of a physical and voluntary nature. So that question also, if necessary, will have to be considered.

As to what constituted disposition Mr. Le-Pelley quoted Lord Denning in *Worcester Works Finance Ltd v Cooden Engineering Company Limited*, a court of appeal case, 1 QBD 1972, 1, wherein on page 218 he has said as follows:-

> "To my mind the word "disposition" is a very wide word. In "*Carter Vs Carter* (1896) 1 Ch 62, 67, Sterling, J said that it extends "to all acts by which a new interest (legal or equitable) in the property is effectually created.
>
> That was under an entirely different statute, but I would apply that wide meaning in this section."

The section under review in the above quotation was section 25(1) of the English Sale of Goods Act, 1893, which is similar to section 26(1) of our Act.

I accept the meaning of the word "disposition" as expounded above. But in sub-section (2) (as in sub-section (1)) the disposition is to be accompanied or followed by an actual physical act of receiving possession of the goods by or physical delivery or transfer of possession of the goods to the 3rd party that is the debenture holder in this case.

Mr. Ransley, disagreeing with the judgment of Chanan Singh J, said that the learned judge had held that physical delivery had taken place by the fact that the charge had crystallized and that a receiver had been appointed. But Mr. Ransley argued the receiver was appointed as an agent of Kicomi and as such the possession of goods never changed hands.

In this case there is no doubt that there has been a disposition of the goods in consequence of the crystallisation of debenture in favour of the bank. The question then left is whether or not a delivery or transfer of goods to the Bank took place together with the crystallisation. As far as the delivery of goods

is concerned, Mr. Le-Pelley for the defendants/receivers conceded in his letter Ref No 4/23689/1 of July 29, 1983 (in file) that there had been no delivery of the goods to the Bank. He, however, maintained that a "transfer" within the section had taken place as he explained in his said letter as follows:-

> It is our argument that there has been a "Transfer" within the section. This is dealt with by Chanan Singh, J Supra at page 484 A and the transfer was effected by the crystallization of the charge over the goods on the appointment of the receiver.
>
> This is the only way there can be a "transfer" of the "disposition" that is to say the charge created. It is submitted that this is implicit in Chanan Singh J's judgment."

The case referred to in the above letter was *G.A.S Weingut v Leslie* [1967] EA 480.

Earlier in his address Mr. Le-Pelley while particularly stressing what the learned judge had said in his judgment in passages 'C', 'D', 'E''F' and'G' on page 484 of *Weingut's* case, had said that the debenture or charge had created a legal interest in the goods. Thus in this case a legal interest in the goods created by the charge was transferred to the bank by way of the debenture documents. Transfer therefore had taken place. In *Weingut's* case the learned judge had said as follows on page 484-:A.

> "The word "transfer" seems to apply to documents of title but it can also apply to goods when conveyed by deed or an instrument in writing".

I am also quoting hereinunder the relevant portions of the same judgment from page 484 'B', 'C', 'D', 'E', 'F' and 'G'.

> **B.** "In the present case there was on the execution of the debenture neither a physical delivery nor a transfer by a written document. The debenture created merely a "charge" not a "mortgage" and there was no transfer of property in the goods.
>
> **C.** But 34 *Halsbury's laws* (3rd Edition), page 84, note (i), says: "It should also be noticed that it is not the contract that is made valid under this section, but the delivery or transfer under the contract."
>
> **D.** Thus, the mere execution of a debenture would not give the disponee the protection of section 26(2). I am of the opinion, however, that physical delivery under the terms of of the debenture would …….....
>
> **E.** It can be argued that a delivery or transfer, in order to come within section 26 (2), must be voluntary and for a consideration which is referable to that delivery or transfer, not for the satisfaction of, say, an antecedent debt. In the present case there was consideration which supported the charge but, as I have already stated, the charge itself is not within the section. Can the consideration for the charge be said to support the delivery at a later date?
>
> **F.** I think it can. The consideration supported not any particular term but all the terms of the contract in the debenture. One such term was that the goods could and would be taken over in a certain eventuality. When that eventuality happened the taking over was under the terms of, and for the consideration mentioned in, the contract.
>
> **G** . …..... I hold, therefore, that the giving of possession of goods under the terms of a debenture constitutes "delivery" under "other disposition" within the meaning of section 26(2) of Sale of Goods Act."

After carefully considering the judgment of the learned judge which he followed in his other judgment in the case of *Basfag v Grindlays Bank International (Kenya) Ltd and another*, I do not agree with Mr. Le-Pelley's submission that the learned judge found that the "transfer" was effected by crystallisation of the charge over the goods by the appointment of the receiver. Mr. Ransley has rightly pointed out that the

learned judge had found that a physical delivery of goods to the bank via the receiver had taken place. The following lines from the above quoted passages from his judgment are pertinent on this point:

> **C.“**Thus, the mere execution of a debenture would not give the disponee the protection of section 26(2). I am of the opinion, however, that physical delivery under the terms of the debenture would.”
>
> **E, F** “Can the consideration for the charge be said to support the delivery at a later date? I think it can. The consideration supported not any particular term but all the terms of the contract in the debenture. One such term was that the goods could and would be taken over in a certain eventuality. When that eventuality happened the taking over was under the terms of, and for the consideration mentioned in, the contract.”
>
> **G** “ I hold, therefore, that the giving of possession of goods under the terms of a debenture constitutes “delivery” under “other disposition” within the meaning of section 26(2) of the Sale of Goods Act.”

It is clear from the above that the learned judge did not make a finding that a transfer had been effected by a crystallisation of the charge over the goods. He found that a physical delivery of goods had take place.

To my mind whether the delivery or possession of goods passes over to the debenture holder at the time of crystallisation of the debenture depends on whether or not the receiver is appointed as an agent for the debenture holder. At no time when a debenture is executed and thereafter does the physical possession of goods pass into the hands of the debenture holder. The goods remain in possession of the borrower-company and in fact are constantly in transit under normal commercial transactions. On crystallization the receiver appointed by the debenture-holder takes over the running of the borrower company so as to dispose of its onus in order to satisfy debenture loan. The receiver now takes possession or delivery of the goods at that time in possession of the borrower company. If he is appointed as an agent of the debenture-holder then only can the goods be said to be transferred and or delivered into the possession of the latter. But if the receiver is appointed as an agent of the borrower-company then clearly no transfer and/or delivery of goods to the debenture-holder can be said to be made so as to satisfy section 26(2) of the Act.

In this case it has been conceded on behalf of the defendants/ respondents that the receiver was appointed as an agent of Kicomi and that no delivery of goods was ever made to the debenture-holder. I am also satisfied that no transfer of goods has taken place. As to what is the position now between the defendants/respondents as receivers for the debenture-holder, a secured creditor, as against the plaintiffs, the unpaid supplier of goods which were supplied subject to the clause, Mr. Ransley has very rightly pointed out the authority of *Romalpa’s* case, an English court of appeal decision, which held that in consequence of the provisions of the clause the supplier of unpaid goods had priority over other secured and unsecured creditors. The clause clearly intended and had created a fiduciary relationship in respect of the goods which was analogous to that of a trustee and beneficiary or an agent and bailee. Such a fiduciary relationship created a priority over secured and unsecured creditors.

Coming to the determination of the two questions posed in the originating summons the answer to the 1st question is that the reservation of ownership of the plaintiff/applicant in consequence of the provisions of the clause is effective to oust the charge given by Kicomi to the Bank. The answer to the 2nd question is in the negative.

The costs of the originating summons are awarded to the plaintiffs/applicants against the defendants/respondents.

Dated and delivered at Nairobi this 4th day of October , 1983.

A.M COCKAR

JUDGE