



REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA

AT NAIROBI (NAIROBI LAW COURTS)

**BANKRUPTCY & WINDING-UP 9 OF 1978**

**KHOSHALS LTD.....APPLICANT**

**VERSUS**

**TANNERIES OF KENYA LTD.....RESPONDENT**

**RULING**

This is an application by way of chamber summons under s 224 of the Companies Act (Cap 486) and rules 5(2) and 7(2) of the Companies (Winding up) Rules.

Tanneries of Kenya Ltd (to which I shall refer as the company) on a petition presented by a creditor on 20<sup>th</sup> June 1978 was ordered to be wound up by the High Court on 6<sup>th</sup> July, 1978.

By a Legal Charge of the same date the company purported to charge a piece of land situate at Athi River in Machakos District L.R 337/613 of which it was registered proprietor as lessee from the Kenya Government in favour of the applicant Queensway Trustee Ltd. The charge was presented for registration on 10<sup>th</sup> July, 1978.

The Official Receiver who was appointed Liquidator acting on behalf of the company agreed to the sale of this land to Twentsche Overseas Trading Co (Technical) Ltd free from all incumbrances at the price of Kshs 3,500,00 and a conveyance was subsequently executed. The Liquidator doubted the validity of the charge in favour of the applicant and it was left open in the Agreement for sale for either the applicant or the Liquidator to apply to the Court for directions under s 224 of the Companies Act.

The Liquidator contends that as the charge was created after the commencement of the winding-up proceedings it is void under s 224.

On 21<sup>st</sup> July, 1976, a Debentur Trust Deed had been made by the company and the applicant in which the applicant was appointed trustee for debenture stock-holders who had advanced Kshs 1,600,000 to the company. The Trust Deed was issued to secure this sum and interest thereon. It was agreed that for the purpose of perfecting the charge contained therein the company would execute a first legal mortgage or charge in favour of the trustee. The charge in question was originally prepared for execution in September, 1977. Delay in registration of the charge was due, the applicant says, to the failure of the company to pay the necessary land rent with the result that the debenture – holders at a meeting held in February 1978 agreed to pay the land rent to enable the charge to be registered. The delay according to the applicant was not prompted by any intention on the part of the applicant was not prompted by any intention on the part of the applicant to preserve the credit of the company or prevent the destruction

thereof and both the Company and the applicant claim to have acted completely in good faith throughout the transaction.

The applicant accordingly seeks an order that the Charge created under the Trust Deed be treated by all concerned as valid security for the sum of Kshs 1,600,000/- and interest intended to be thereby secured and also for payment of the costs of this application.

The Deputy Official Receiver contends that the charge is void ab initio. In an affidavit he states that a receiver and manager having been appointed by the debenture holders on 5<sup>th</sup> July, 1978, the directors of the company had no power in law on 6<sup>th</sup> July, 1978 to execute the charge. Indeed the liquidator continues, they had no power to do so after 20<sup>th</sup> June, 1978, the date on which the winding-up was deemed to have commenced (s 226 (2) of the Companies Act).

Moreover by virtue of the provisions of section 32 as read with section 20 of the Registration of Titles Act (Cap 281) the charge was totally ineffective to pass any interest, either legal or equitable in the land until its registration on 10<sup>th</sup> July, 1978, by which time the winding-up had commenced.

Under 2 312 of the Companies Act any charge created by a company within 6 months before the presentation of a winding-up petition is deemed a fraudulent preference of its creditors and to be void. A fortiori, the Liquidator contends, a charge created after the commencement of winding-up proceedings.

Mr Kwach who appeared for the applicant, apart from submitting that no fraudulent preference could be inferred since the charge was made in fulfillment of a prior obligation and was merely perfecting the charge contained in the debenture trust deed which had been registered under the Companies Act, did not dispute these contentions of the liquidator.

The charge is clearly void. The question now is – do I have discretion under 224 of the Companies Act to order otherwise?

S 224 provides\_

“In a winding up by the court, any disposition of the property of the company, including things in action, and any transfer of shares, or alteration in the status of the members of the company, made after the commencement of the winding up, shall, unless the court otherwise orders, be void.”

Mr Satish Gautama who appeared for the liquidator submitted that a legal charge or mortgage is not a disposition and referred to s 312 of the Act where the expression used is “transfer, conveyance, mortgage, charge, delivery of goods, payment, execution or other act relating to property”. The term is defined neither in the Companies Act nor in the Interpretation and General Provisions Act (Cap 2). It is defined in the Registered Land Act (Cap 300) as meaning “any act by a proprietor whereby his rights in or over his land, lease or charge are affected, but does not include an agreement to transfer, lease or charge.” In the Trusts of Land Act (Cap 290) it is defined to include a mortgage and charge. Mr Gautama referred me to no authority for so restricting the meaning of the term. In Re Steane’s (Bournemouth) Ltd [1950] 1 All E R 21, an application under s 227 of the Companies Act, 1948 which corresponded to s 224 of the Kenyan Act a debenture issued by the directors between the presentation of the petition and the order was confirmed by the Court. I am of the opinion that the term “disposition” should be given a liberal construction and that it includes a legal charge and mortgage.

I have discretion under s 224 to make the order sought but only I think if the only reasons for the charge being void is that it was made after the commencement of the winding-up. The section does not give the Court power to validate a disposition which is void for other reasons. In the present case the disposition was void ab initio because by the time it was made a receiver and manager had been appointed by debenture-holders and the directors no longer had authority to execute it.

In case I am wrong however I shall proceed to consider the arguments put forward for and against the

exercise of my discretion in the applicant's favour.

With regard to the factors to be taken into account in exercising my discretion Mr Kwach invited my invitation to the following passage from the judgment of Vaisey J in Re Steane's (Bournemouth) Ltd at page 25.

“But the view which I take of my duty under the section (shared to the best of my belief by Roxburgh J) is that each case must be dealt with on its own facts and particular circumstances (special regard being had to the question of the good faith and honest intention – of the persons concerned) and that the court is free to act according to the judge's opinion of what would be just and fair in each case.”

Mr Kwach submitted that the applicant should have the benefit of the Court's discretion unless the charge constituted a fraudulent preference. The principal document was the debenture trust deed which was registered under the provisions of 296 of the Companies Act. Thus any prudent person dealing with the company would know of its existence. The company executed the charge in fulfilment of its obligation under this deed to perfect the charge contained therein. There was no intention of constituting fraudulent preference.

Mr Gautama referred to the facts set out in the liquidator's affidavit, namely that when the charge was executed and registered the company was hopelessly insolvent having incurred losses amounting to Shs 5,977,011/-. The total amount realized from the sale of the charge property was Shs 3,500,000/-. The total liability of the company in respect of its unsecured creditors amounted to Shs 4,347,370/- and if the applicant were to be treated as a secured creditor for Shs 1,600,000/- the balance available for distribution among the unsecured creditors would be only Shs 670,000.

Mr Gautama submitted that no reasonable excuse had been put forward for the failure to execute and register the mortgage which had been prepared in September 1977 long before the winding up commenced. After the resolution of the debenture-holders in February 1978 to pay the land rent they had delayed until July. The delay must have been deliberate and must have affected the position of creditors who would be unaware of the premise to execute a charge. In the absence of any charge registered at the Land Titles Registry they would be entitled to assume that there was no encumbrance on the title.

As I understand s 224 the Court has discretion to uphold all proper transactions entered into after the commencement of the winding-up. Such transactions might for example include dispositions of property made by a branch in ignorance of the presentation of a winding – up petition or transactions to enable a company to continue to carry out its contracts. In this case however no adequate reason has been given for the delay of 2 years between execution of the debenture trust deed and the execution and registration of the mortgage in favour of the applicant. The delay affected the credit – worthiness of the company and unsecured creditors may well have been misled by the absence of this encumbrance in the title to the land. It leads to suspicion that the delay was at least partially deliberate with a view to protecting the credit of the company. It would not in my view be just and fair to the unsecured creditors to treat the charge as valid.

I should not therefore be disposed to exercise my discretion in favour of the applicant. The application is dismissed with costs.

**Dated and delivered at Nairobi this October 16, 1980.**

**A.H SIMPSON**

**JUDGE**